Comparative Analysis of Disinvestment Policies in India and Other Emerging Economies

Abstract

The Indian economic framework immediately after independence followed a state-centred growth model. The government strictly regulated the entry of private entities into the market. This was detrimental to market competition leading to both government and private monopolies. Only a few business houses managed to thrive in an over-regulated environment, the ones that enjoyed a symbiotic relationship with the government. Nationalisations in the 1960s gave an ideological colour to the previous policy of command economy. Pro-poor tilt in distributional policies led to hostility towards private enterprises. State-led growth was not without its flaws. The paper examines the macroeconomic conditions which led the government to adopt disinvestment policies. Various policy changes since 1991 and their emphasis on disinvestment have been highlighted. Different approaches were followed by other governments based on a consideration of multiple factors. The disinvestment pattern for Air India was very different from the approach adopted for ONGC.

A comparison of the disinvestment policies of India post-1991 with other emerging economies is done. East Europe's shock therapy and Zambia's case were examined as useful lessons for the Indian disinvestment policies. United Kingdom's Private finance Initiative provided a useful experience in the adoption of these policies. This is because it was one of the first countries to privatize welfare services. Based on an international comparison, there were various institutional and political constraints in the implementation of disinvestment policies. Institutional constraints are related to the administrative inadequacies to cope up with the radical restructuring of the state led economy while political constraints refer to the ideological opposition to the entire process. Based on this analysis, various recommendations are provided to deal with these constraints. Improvement of valuation methods, joint ventures, employee-management buyouts and establishment of procurement agency are some of the recommendations.

Keywords: Strategic sale, public offer, disinvestment, non-core assets, employee-management buyouts

Introduction

Disinvestment refers to the process through which government sells minority stakes in Public Sector Undertakings (PSU) and various other assets owned by the government. The objective of disinvestment is to reduce the fiscal burden of the government and enhance efficiency of PSUs. Privatization, on the other hand refers to sale of majority stake of the government to private entities. India's first disinvestment was set up in 1996 during the tenure of Atal Behari Vajpayee under the chairmanship of GV Ramakrishna.

Naresh Chandra committee report[1] recommended the privatization of Air India. This was seconded by the recommendation of the Ministry of Corporate Affairs which called for partial privatization. This was due to the losses worth Rs. 1.74 billion in 1998-99. The government has sold a 76% stake in Air India Ltd., 100% stake in Air India Express Ltd and a 50% stake in Air India SATS Airport Services Pvt. Ltd.[2] Despite the merger of Air India and Indian Airlines, the losses did not stop accumulating. However, the disinvestment in Air India and other Public Sector Undertakings was never an easy policy decision because it involved a shift in ownership of a national symbol[3]. In contrast to the case of Air India, the disinvestment in Life Insurance Corporation (LIC) was a minority disinvestment. In this case, the majority of stakes shall remain with the government[4]. After the amendment of the LIC Act, the possibility of Foreign Direct Investment through Initial Public Offering was high[5].

After Economic reforms in 1991, successive governments have continued the policy of disinvestment or reducing government shares in Public Sector Undertakings. **Strategic disinvestment** refers to sale of

[1] Chandra , N. (2009). *Report of the CII taskforce on Corporate Governance .*

[2] Dhameja , N. (2018). *Air India Revival on JSTOR*. Jstor.org. https://www.jstor.org/stable/26536520?seq=14

[3] Mukherjee, A. (2021, October 11). *Air India's privatisation comes two decades late, but taxpayers should be relieved*. ThePrint; theprint. https://theprint.in/opinion/air-indias-privatisation-comes-two-decades-late-but-taxpayers-should-be-relieved/748881/

[4] Kumar, R. (2022). Disinvestment of Life Insurance Corporation of India. *Asian Journal of Management and Commerce*, *3*(2), 205–209. https://doi.org/10.22271/27084515.2022.v3.i2c.158

[5] Makol, S. (2021). Disinvestment of LIC: a strategic move of Indian government. *International Journal of Economic Perspectives*, *15*(1), 15–29. https://ijeponline.org/index.php/journal/article/view/2

a substantial portion of the government's stakes along with the transfer of managerial control to the acquiring company. Out of Rs. 4.2 Lakh crores raised from disinvestment in the last 10 years, 3.15 Lakh crores have been through the sale of minority stakes while only 70,000 crores have been raised through strategic transactions[6]. After 2010, the government has not been able to meet its disinvestment targets barring 2017-18 and 2018-19[7]. A case in point is not meeting its ambitious disinvestment target of 1.75 Lakh crore in 2021-22 despite the sale of Air India[8].

India's command economy and need for disinvestment

Command economy

The pursuit of self-reliance was a determining factor in the socialist tilt of Indian economic policies. The Indian economy was marked by the 'Hindu Rate of Growth.' It was a shorthand for staggered growth rates due to the command economy and the central role played by the state in structuring the economy[9]. Public investment in non-critical sectors like hotels, real estate and restaurants led to the elimination of effective competition. Dreze and Sen (1999) pointed out state failure in terms of removing poverty, inequality and disease. They diagnosed excessive bureaucracy and state interventionism as the root cause of inefficiency of the economy. There were rent-seeking tendencies among politicians and bureaucrats[10]. The role of planning commission had been elevated to the status of a super-cabinet. It emphasized the socialist pattern of society which was associated with state

[6] Express News Service. (2023, December 26). *Disinvestment fetches over Rs 4.20 lakh cr in 10 years*. The New Indian Express; The New Indian Express. https://www.newindianexpress.com/business/2023/Dec/26/disinvestment-fetches-over-rs-420-lakh-crin-10-years-2645014.html

[7] PRS Legislative Research. (n.d.). *Vital Stats*. https://prsindia.org/policy/vital-stats/disinvestment-in-india

[8] Munjal, D. (2023). The status and proceeds of disinvestment. *The Hindu*. https://www.thehindu.com/business/Economy/explained-the-status-and-proceeds-of-disinvestment/article66485958.ece

[9] Virmani, A. (2004). *India's economic growth: From socialist rate of growth to Bharatiya rate of growth*. Www.econstor.eu. https://hdl.handle.net/10419/176144

[10] Das, R. (2001). The Political Economy of India. *New Political Economy*, *6*(1), 103–117. https://doi.org/10.1080/13563460020027786

ownership of productive assets[11]. The number of Central Public Undertakings rose from 5 in 1951-52 to 243 in 1998-99.

It was soon realized that the state did not have the institutional capacity and the economic resources to give effect to its socialist goals. To fulfil the twin developmental imperatives of building national power and rapid economic development involved a tacit developmental alliance with the industrial classes. By protecting from market volatility to the private sector, the state facilitated the process of converting these firms' narrow capitalist incentives into a powerful social force. The lack of industrial base and financial capital for the private sector, also called the **lumpiness problem**, was solved through the provision of state infrastructure to select private entities[12]. In the decade after independence, the 20 largest business houses in India controlled 30% of corporate assets. By 1976, this number had gone up to 65% [13].

Financial Position before 1991

The Gulf War and oil shock exacerbated India's balance of payments problem. India's foreign exchange reserves were only enough to last for 2 weeks. The Inflation rate had breached the 10% mark which is well above Reserve Bank of India's prescribed limits. The total investment in Central Public Sector enterprise was 99,315 crore. Out of the 244 CPSEs, 98 had accumulated losses in excess of 10,000 crore. The reason for loss-making was the inability of the government to transform the erstwhile sick industries into profitable enterprises[14]. A primary reason behind the decline of PSUs was the stagnation of investment. Investment in Public Sector Undertakings remained the same in 1976 and

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[11] Raghavulu, C. V. (1997). Economic Policy in India: From Centralised Planning to Liberalisation. *Indian Journal of Public Administration*, *43*(3), 473–490. https://doi.org/10.1177/0019556119970320

[12] Kaushik, S. K. (2010). India's Evolving Economic Model: *American Journal of Economics and Sociology*, *56*(1), 69–84. https://doi.org/10.1111/j.1536-7150.1997.tb03452.x

[13] Sharma , S. (2024). *FROM CENTRAL PLANNING TO MARKET REFORMS: INDIA'S POLITICAL ECONOMY IN COMPARATIVE PERSPECTIVE on JSTOR*. Jstor.org. https://www.jstor.org/stable/23263494?seq=

[14] Banerjee, S., Sane, R., Sharma, S., & Suresh, K. (2022). *History of disinvestment in India: 1991-2020.* https://nipfp.org.in/media/medialibrary/2022/03/WP_373_2022.pdf

1990 at around 8%. The logic underlying PSU's operation was that despite capital scarcity, there should be attempts to maximize employment. During the same period, employment increased from 6.6 lakhs to 22.2 lakhs[15].

The reason behind not divesting shares initially notwithstanding the poor economic performance was the politically ingrained notion of PSUs representing the public good while the private sector representing minority interests. Even sick PSUs were considered to have a welfare role insofar as they employed a massive number of workers. Due to the initial policy of balanced regional development, there was a deliberate attempt to locate PSUs in economically backward regions. The sale of stakes in PSUs is akin to sale of family silver which is why there are reservations coming from various stakeholders in the process of disinvestment[16]. The Air India employees union petitioned the Madras High Court to flag the ramifications of disinvestment of the airline. The employees enjoyed multiple benefits including job security until the age of 58 which made it an exception in the aviation industry with other airlines setting age limits on their cabin crew. Similarly, wage and service parity between men and women which was achieved through a long-standing legal battle was jeopardized. These are practical stakeholder-oriented grievances that slow down the process of disinvestment [17].

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[15] Santosh, S., & Das, K. (2023). *ISID Working Paper 264 Public Sector Performance in India and the Ongoing Contestation between Efficiency and Equity.* https://isid.org.in/wp-content/uploads/2023/05/WP264.pdf

[16] Katoch , R., & Bahri, S. (2023). *Winding Up of State Enterprises in India: A Case Study of Five Enterprises Under the Department of Heavy Industry.* Carnegie Endowment for International Peace. https://carnegieendowment.org/research/2023/09/winding-up-of-state-enterprises-in-india-a-case-study-of-five-enterprises-under-the-department-of-heavy-industry?lang=en

[17] Velayudhan, S. (2021). *Air India disinvestment: Madras HC grants interim relief to employees' union*. The Leaflet . https://theleaflet.in/air-india-disinvestment-madras-hc-grants-interim-relief-to-employees-union/

Evolution of disinvestment policies after 1991

The approach of NIP 1991

The shift towards disinvestment and privatization in the 1990s was underlined by the broader rolling back of the state from excessive involvement in the industrial sector. The overarching transformation was from a common economy to a market economy. By diluting the privileges of the PSUs, there was an aim of diversifying ownership of those enterprises. In this context, disinvestment refers to the broader policy goal of reducing government shares in PSUs. The New Industrial Policy (1991)[18] highlighted poor project management, over-manning, lack of technological upgradation and inadequate attention to R&D as major concerns faced by the CPSEs. It brought forth the need for the government to strengthen those enterprises which are essential for the survival of the economy and are high-priority sectors . The arrears reserved for PSUs came down from 17 before 1991 to 3 (Atomic Energy, minerals specified in schedule to atomic energy and railway) in 2002. It was projected that disinvestment will reduce public debt, transfer commercial risk and release money from non-strategic PSEs.

Following the New Industrial Policy 1991, the Department of Public Enterprises conducted a detailed review of 58 loss-making CPSEs. There were three plausible solutions or approaches which were laid down by DPE: revival, closure and privatization. Strategic sale, capital market, warehousing, reduction in equity, trade sale, asset sale, employee buyout, cross-sale and sale through demerger were the methodologies of disinvestment enunciated in the policy document[19]. A committee on disinvestment was formed in 1992 which made suggestions about the modus operandi for disinvestment.

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[18] Government of India. (1991). *STATEMENT ON INDUSTRIAL POLICY.* https://dpiit.gov.in/sites/default/files/IndustrialPolicyStatement_1991_15July2019.pdf

[19] Government of India . (2003). *Disinvestment: policy, procedures and progress .* https://xn--j2bim4e.xn--11b7cb3a6a.xn--h2brj9c/dipam_docs/strategicDisinvestment/Disinvestment_-_Policy,_Procedures_and_Progress_ebook2.pdf

In 1997, Government of India announced a package for the Navratnas which were profit-making with the aim of making them globally competitive[20]. The policy interventions were different for Navratnas and Miniratnas based on their financial performance. Oil and Natural Gas Videsh (ONGCV), Bharat Electronics Limited (BEL) and Hindustan Aeronautics Limited (HAL) were the prominent Navratnas. The Maharatna scheme was introduced in 2010 with a similar objective of enabling mega PSUs to become global giants by granting them more autonomy. However, empirical analysis reveals that Maharatnas also suffer from inefficiencies owing to excessive government intervention[21]. In 1999, a distinction was made between strategic and non-strategic sectors. For PSUs in non-strategic industries, government shares could drop below 26%. A new impetus was given to disinvestment policies by the first NDA government. A new department of disinvestment was set up under the Ministry of Finance. A new disinvestment commission was set up in 2001. The government sought to revive potentially viable firms, close down non-viable firms and emphasis on strategic deals. The government issued a policy document on disinvestment called 'Disinvestment: Policy and Procedures.'

Approaches

The Department of Investment and Public Assets Management (DIPAM) lays down the following modes of disinvestment: Public offer, strategic sale, buyback, sale to employees, Exchange Traded Funds and PSE to PSE sale. Strategic sale and Public offer are the principal means through which disinvestment policy is implemented. The method of sale is important because it impacts the price which the PSU raises. The assumption is that the value of PSUs will rise when given in private hands[22].

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[20] Arun, T. G., & Nixson, F. I. (2000). The Disinvestment of Public Sector Enterprises: The Indian Experience. *Oxford Development Studies*, *28*(1), 19–32. https://doi.org/10.1080/713688302

[21] Singh, K., & Sur, D. (2016). Profitability of Maharatna enterprises in India during the post-liberalisation era: a cross-sectional analysis. *International Journal of Management Concepts and Philosophy*, *9*(3), 239. https://doi.org/10.1504/ijmcp.2016.078310

[22] Mohan, T. R. (2021, February 10). *India's Privatisation Drive*. The India Forum. https://www.theindiaforum.in/article/india-s-privatisation-drive

Strategic Sale

Involves sale of a substantial portion of government shareholding in PSUs up to 50% along with transfer of managerial control[23]. Strategic sale as a strategy became prominent during the then Minister of Disinvestment, Arun Shourie's tenure. The process of strategic sale involves the expression of interest based on eligibility criteria and invitation of bids from shortlisted organisations. The highest bidder wins provided their bid is above a reserve price set by the government which is not known to the bidders. Efficiency is said to increase because the asset is being transferred to the highest bidder[24]. The sale of Air India is an archetype of strategic sale in India. The speculation of the Shipping Corporation of India's (SCI) sale raised its stock prices by 10%. The non-core assets of SCI were already demerged and listed on the stock market as SCI Land and Assets[25]

Public Offer

This approach has reduced the pressure on the government's budgetary allocation for capital-sensitive industries like banking. Good quality PSUs have always been well accepted by the market. It is being used as a platform by the government to monetize PSUs[26]. IPO is an offer of shares of an erstwhile unlisted company by the government to the public for the first time. **Further Public Offer** (FPO) is the offering of a listed PSU's shares to the public. To prevent lower proceeds for the government after valuation, 2 additional methods have been devised by the Securities and Exchange Board of India. This is through the Institutional Placement Programme and Offer for sales of shares through Stock exchange mechanism[27].

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[23] Comptroller and Auditor General of India . (2020). *Disinvestment Policy of Government of India*. https://cag.gov.in/uploads/download_audit_report/2020/CHAPTER%20III-061c1ab81b47ce6.63330903.pdf

[24] T. T. Ram Mohan. (2003). Strategic Sale versus Public Offer: Dispelling Myths. *Economic and Political Weekly*, *38*(28), 2969–2976. http://www.jstor.org/stable/4413780

[25] India Today. (2024, June 12). *Explained: Why Shipping Corporation of India shares surged over 7% today*. India Today; India Today. https://www.indiatoday.in/business/story/shipping-corporation-of-india-shares-surged-over-7-today-divestment-reports-2552166-2024-06-12

[26] Murugappan, A. (n.d.). *Disinvestments through Public Offers - The Road Ahead*. Retrieved September 14, 2024, from https://www.primedatabase.com/Article/dir-10ar17.pdf

[27] Sehgal, S., Kumar, M., & Gupta, P. (2014). Public Sector Disinvestment in India. *Global Journal of Emerging Market Economies*, *6*(2), 181–202. https://doi.org/10.1177/0974910114525539

Performance of erstwhile Public Sector Undertakings after disinvestment

Welfare and Benefits to employees

Global evidence confirms the negative relationship between disinvestment and employment. There was a general decline in the employment in PSUs but it was consistent with the overall decline in employment. Owing to inefficiencies resulting from overemployment, the government came out with a **Voluntary Retirement Scheme (VRS)** in 1988. The decline in employment was also linked to market structures. Overall decline in employment was higher in a competitive environment as compared to monopolistic enterprises. The average annual decline for the former sector was 8,000 while for the latter was 726. The real wages of the employees increased sharply in the post-reform period. PSUs were an important avenue for the representation of Scheduled Castes (SC) and Scheduled Tribes (ST) in organized employment. The share of SCs and STs in PSU employment had gone down by 3% between 1991 and 2003[28].

Performance of PSUs

Naib (2003)[29] conducted a study to compare the performance and efficiency ratios of PSUs before and after disinvestment. Significant improvements were found in dividend payout ratios and efficiency ratios. There is an increased profitability due to the transfer of control and cash flow rights from the government to the private sector[30]. Ghosh (2008)[31] compared the performance of Fully government-owned enterprises and partially government-owned organizations. However, there is contrasting evidence that shows that the performance of firms with higher levels of disinvestment is poor as compared to the performance of companies with more government holding. An empirical

[28] Mahajan, Shrikrishna. (2008). Disinvestment Policy and Its Impact on Employment In Public Sector : A Study. ETHOS. 1. 1-15.

[29] Naib, S. (2003). Partial Divestiture and Performance of Indian Public Sector Enterprises. Economic and Political Weekly. 38. 3088-3093. 10.2307/4413811.

[30] Mandiratta, P., & Bhalla, G. S. (2017). Pre and Post Disinvestment Performance Evaluation of Indian CPSEs. *Management and Labour Studies*, *42*(2), 120–134. https://doi.org/10.1177/0258042x17716601

[31] Mandiratta, P., & Bhalla, G. S. (2020). Disinvestment in Indian central public sector enterprises: a performance improvement measure. *Journal of Economic and Administrative Sciences*, *ahead-of-print*(ahead-of-print). https://doi.org/10.1108/jeas-02-2019-0023

analysis of three PSUs (MMTC Ltd., NMDC Ltd. and Hindustan Copper Ltd.) by Sridharan & Pradeepa (2021) reveals that the decline in performance of these companies was coincident with the decline in government shareholding. The reason behind their poor performance despite the change in ownership structure is that they have unsound business models and have accumulated huge losses.[32]

Case Studies in India

Indian Petrochemicals Corporation Limited (IPCL)

IPCL was set up in 1969 to provide raw materials for industries. The government disinvested 26% of its stake in the enterprise which was then taken up by Reliance Group. Reliance's bid of Rs. 231 a share was far ahead of those made by the next two competitors Indian Oil Corporation Limited (Rs. 128) and Nirma (Rs. 110). The reserve price was set to Rs. 131 based on the Discounted Cash Flow method. The disinvestment process was made favourable for the bidders when the Finance Ministry extended sovereign guarantee to IPCL on its World Bank loan of $100 million. It also withdrew Rs. 600 crore excise duty claim on IPCl. The erstwhile dependence of IPCl on Indian Oil Corporation Ltd (IOCL) will be eliminated as Reliance will use its own petroleum refineries for sourcing feedstock. This is a massive loss for IOCL as it supplied feedstock worth Rs. 100 crores to IPCL annually. High import duties on petrochemicals and increased prices of Polyethylene & Polypropylene have ensured that Reliance enjoys a monopoly in this sector[33].

Bharat Aluminium Co. Ltd. (BALCO)

It was set up in 1965 for the manufacture and sale of Aluminium and semi-fabricated products. In 2001, the government divested 51% share which was purchased by Sterlite Industries(Now Vedanta).

[32] Sridharan, Srividhya & Samanta, Pradeepta. (2021). A Critical Analysis of Disinvestment in Indian Public Sector Enterprises. The Empirical Economics Letters. 20. 13-28.

[33] Katakam, A. (2002). *Birth of a monopoly*. The Frontline Magazine. https://frontline.thehindu.com/other/article30245147.ece

There was a 'tag along right clause' in the agreement which implied that Sterlite would have to sell its shares for a discount of 25% if it desired to exit within the lock-in period of 3 years. The protective clause mentioned that if the strategic partner wished to exit within the lock-in period, the new purchasing entity could buy the remaining 49% of the government's share. However, this policy was taken to court by the employees of BALCO, the state of Chhattisgarh and some public individuals. The major contention of the disinvestment process was that it violated Schedule V of the constitution which gave tribals autonomy over their land. Since the announcement of disinvestment, the state government has increased the entry tax on bauxite from 10% to 50% so that the company cannot source their raw materials from within Chhattisgarh[34].

Comparative analysis of policies of other countries

Difference in Privatization Objectives

There is a difference in the objectives of disinvestment policies in developed and developing countries. In developed countries, the primary goal of disinvestment is to enhance economic efficiency. In developing countries, the policies are driven by additional motivations of poverty reduction and sustained economic development. However, the impact of disinvestment and privatization on poverty reduction has not been conclusively proven. The underlying assumption is that greater economic efficiency will lead to a reduction of poverty. Economic growth, distributional and poverty effects are important aspects in assessing the welfare impact of disinvestment [35]. One of the objectives of the Indian disinvestment policy was to redistribute proceeds to high-priority social sectors.

[34] Sridhar, V. (2001). *The Balco struggle*. The Frontline Magazine. https://frontline.thehindu.com/the-nation/article30250330.ece

[35] Parker, D., & Kirkpatrick, C. (2005). Privatisation in Developing Countries: A Review of the Evidence and the Policy Lessons. *Journal of Development Studies*, *41*(4), 513–541. https://doi.org/10.1080/00220380500092499

Evolution of disinvestment policies 1980s onwards

There were only a few state-owned enterprises in Sub-Saharan Africa that were subject to privatization between 1991 and 2001. The scope of disinvestment has been limited to small-scale manufacturing or industrial firms. The reason for the slow pace of disinvestment was the vested interests of the bureaucrats and industrialists. In Nigeria, the disinvestment programme led to short-term gains but it was abandoned in favour of mass commercialization policy. The nationalist inhibitions of forgoing ownership to foreign companies were problematic. In the late 1990s, the role of the World Bank and IMF in the reconstruction of economies led to the opening up of markets and diluting ownership structures. The weak fiscal position of state-owned enterprises led to a financial necessity of disinvestment. After a decade of hastened disinvestment, the 2008 financial crisis led to a stall in the process[36].

Sectoral Disinvestment and Macroeconomic Regulation

The long-term gains can only be realised if the mix of sectoral policies is appropriate. For potential competitive sectors, higher disinvestment would allow greater competitiveness. In Chile, the first stage of privatization was undertaken rapidly in an economically volatile environment without paying sufficient attention to the performance of different sectors. Consequently, many companies went bankrupt because they could not survive the competitive environment. Reforms like privatization can only be successful when they are preceded by macroeconomic reforms like stabilization, deregulation and liberalisation. In Sri Lanka, there were efforts made to formulate a telecommunications policy framework, the formation of a new legal entity before the introduction of the private sector. Privatization efforts are unlikely to be effective unless they are preceded by sectoral policy reforms[37].

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[36] Estrin, S., & Pelletier, A. (2018). Privatization in Developing Countries: What Are the Lessons of Recent Experience? *The World Bank Research Observer*, *33*(1), 65–102. https://doi.org/10.1093/wbro/lkx007

[37] Nankani, H. (1990). *Lessons of Privatization in Developing Countries.* https://www.elibrary.imf.org/downloadpdf/journals/022/0027/001/article-A014-en.pdf

OECD Privatization Report (2009)[38] lists the key elements of a regulatory framework: promoting transparency, articulation of division of responsibilities and highlighting the importance of competition. In developing countries, regulatory and political problems were aplenty during privatization. Another issue is with the stage of the value chain in which competition ought to be introduced. While the adoption of regulatory agencies has been present, their independence is questionable. Two metrics for measuring independence are the source of funding and leadership. Over 60% of agency heads in 22 African countries are appointed by the President which raises questions about the independence of the agency.

Restitution in East Europe

The process of restitution involves the transfer of ownership of an enterprise that was unjustly nationalized or acquired by the government. Along with ownership, property rights are also transferred to the erstwhile owners. Restitution was prominent in the Eastern European countries. These countries which were part of USSR adopted the soviet economy marked by nationalization. This policy unjustly divested the owners of the private enterprises of the proceeds of the enterprise's earnings. After the dissolution of the USSR, the policy of restitution was seen as an attempt at reprivatization. Symbolically, it was also a denouncement of the communist economy. In Czechoslovakia, direct restitution of property was attempted and compensation was provided in the scenario where it was not possible to directly restitute the erstwhile owners. The claimants were required to pay an additional amount in case of appreciation of property/assets. On the flip side, the government had to pay an extra amount on the occasion of deterioration of asset quality[39] .

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[38] Estrin, S., & Pelletier, A. (2015). *ECONOMIC AND PRIVATE SECTOR PROFESSIONAL EVIDENCE AND APPLIED KNOWLEDGE SERVICES TOPIC GUIDE Privatisation in developing countries: What are the lessons of experience?* https://assets.publishing.service.gov.uk/media/57a08977ed915d3cfd000264/Topic_Guide_Privatisation_Nov.pdf

[39] FISHER, L. M., & JAFFE, A. J. (2000). Restitution in transition countries. *Journal of Housing and the Built Environment*, *15*(3), 233–248. http://www.jstor.org/stable/41060010

Zambia's Privatization Agency

The Zambia Privatization Agency (ZPA) was an autonomous organization that was responsible for determining the process of disinvestment and the prices to be set for them. It was given significant powers to ensure that privatization can be carried out effectively. The first step in privatization was tranching or identification of a group of companies to be privatized in a period. The initial tranches were small companies to test the process of disinvestment. ZPA involves independent negotiators drawn from the public but are people of appreciable competence in matters of finance and business[40]. It is responsible for setting pre-qualification criteria for the selection of potential buyers. It undertakes independent valuation of assets and liabilities and ascertains the price for them. This helps in avoiding the undervaluation/overvaluation of SOEs due to market sale[41]. A report by World Bank studying the disinvestment impact in Zambia concludes that the programme has been successful in stalling the decline in turnover. The turnover of companies has increased in the two years following disinvestment[42].

United Kingdom's Private Finance Initiative

In the UK, disinvestment happened in distinct phases. The first phase of disinvestment involved disinvestment in firms that did not have any special characteristics. The second phase involved the sale of public utility industries like telephone, gas, water and electricity [43]. It is one of the few countries which has experimented with disinvestment in social welfare schemes. Social welfare has seen three kinds of privatization of production: through Non-profit organizations, private institutional care or

[40] Fundanga, C., & Mwaba, A. (n.d.). *Privatization of Public Enterprises in Zambia: An Evaluation of the Policies, Procedures and Experiences* . African Development Bank.

[41] Musambachime, M. (1999). *Privatisation of state-owned enterprises in Zambia: 1992-1998* . https://journals.co.za/doi/pdf/10.10520/AJA0304615X_140

[42] Serlemitsos, J., & Fusco, H. (2003). *ZAMBIA Post-Privatization Study*. World Bank. https://ieg.worldbankgroup.org/sites/default/files/Data/reports/zambia_wp_post_privatization.pdf

[43] Veljanovski, C. (1988). *Marquette Law Review Marquette Law Review Privatization in Britain -The Institutional and Constitutional Issues Privatization in Britain -The Institutional and Constitutional Issues INSTITUTIONAL CONSTITUTIONAL ISSUES.* https://scholarship.law.marquette.edu/cgi/viewcontent.cgi?article=1808&context=mulr

private domestic care [44]. The most popular form of disinvestment is Private Finance Initiative (PFI) which is a scheme under which private companies build new facilities and finance them. It is finally rented back to the government. Rather than paying the private player during the construction, the public sector pays a unitary charge using public money on the completion of the project [45].

The privatization policies were not without underlying political motives. It was seen as an attempt by the Conservatives to reverse the nationalizations done by the labour government. Disinvestment occurred through management and worker buyouts along with IPOs of select government enterprises. The government, headed by Thatcher began a sale of the state's housing stock (council housing) [46]. The right-to-buy campaigns resulted in the transfer of state housing to private ownership. In the health sector, authorities are required to subcontract services to private firms. Private options are subcontracted even if the costs per unit are higher.

Czechoslovakia's Voucher Privatization

More than 50% of the firms were privatized based on the book voucher method. It involved purchasing a voucher book with 1000 investment points for 1000 crowns. The voucher bookholders used the points to bid for shares of the companies that had been allocated for voucher distribution [47]. Before the bidding process, an individual had the opportunity to use some or all of their points to the **Investment Privatization Fund (IPF)**. At the beginning of the process, the public was given financial information about the enterprises for which bidding was to be done. If the bids did not exceed the supply of shares, the demands were met. The measures were surprisingly successful in the

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short run evidenced in the allocation of all shares and expenditure of all voucher points. The policy of large-scale privatization ensured that no individual or group gets a lion's share in any enterprise[48]. However, the benefits of voucher privatization did not last long. It was later realised that gradualism is a better approach to disinvestment and privatization rather than the shock therapy approach.

Failure of India's disinvestment process

National Monetization Pipeline (NMP)

The scheme aimed to raise $81 billion by leasing government core assets like roads, railways, telecom, oil and gas pipelines for a period of four years (FY 2022-2025). The aim is to monetize brownfield infrastructure assets. The reason for adopting monetization as a policy is the failure of the previous two policy measures to reduce government involvement in PSUs. Sale of majority shares in PSUs did not sustain for long due to political opposition. Public Private Partnership (PPP) models did not achieve the success imagined due to unsupportive government structures, zero- risk approach of the government and rigidity of contracts[49]. The monetization of non-core assets is being transferred from the Department of Investment and Public Asset Management (DIPAM) to the Department of Public Enterprises. The proceeds from this policy were supposed to be pumped into the **National Infrastructure Pipeline (NIP).** Road assets worth 1.6 lakh crore were projected to be the highest source of revenue. The techniques of monetization included Toll Operate Transfer (ToT) and Infrastructure Investment Trust [50].

48 Hanousek, J., & Kroch, E. A. (1995). The Two Waves of Voucher Privatization in the Czech Republic: A Model of Learning in Sequential Bidding. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.1545010

49 Ahluwalia , S. (2021). *A Rs 6 trillion National Monetisation Pipeline – Is it for real?* ORF India . https://www.orfonline.org/expert-speak/a-rs-6-trillion-national-monetisation-pipeline

50 The Hindu Bureau. (2021). *National Monetisation Pipeline | Here's the breakup of the govt's big privatisation push*. The Hindu. https://www.thehindu.com/business/Economy/national-monetisation-pipeline-heres-the-breakup-of-the-govts-big-privatisation-push/article36075874.ece

NMP failed in most ministries because of the lack of prior experience in the ministries and PSUs identified for monetization. Railways, which were set a monetization target of 1.6 trillion fell out of monetization for the same reason [51]. Another drawback of the policy was that it could finance not more than 5-6% of the investments in NIP. There is also some ambiguity regarding how the proceeds will be spent. There is no specific guidelines for how these proceeds will be used to finance infrastructure. Whether or not they will be used to pay pensions, salaries etc is also ambiguous. The policy document has not given much importance to the implementation plan . NMP is seen as an attempt to overcome the failures of the PPP model. While PPP models made private players a lot more circumspect, monetization will help them evade the procedural issues of PPP model i.e negotiations with the government, risk division etc[52] .

Implementation and Technical constraints

Disinvestment requires an administrative system to support the transition in ownership. The process of valuation of PSU assets is lengthy. It is fraught with concerns like undervaluation or overvaluation. Administrative capacity is required to design a rehabilitative plan for the recovery of PSUs and assessment of bids. There is a disconnect between the PSU valuations and operational performance. The BSE PSU index has underperformed the overall market. The reasons for the underperformance are frequent stake sales by the government and a fall in crude oil prices due to a decrease in demand following COVID-19 [53]. Selling small chunks of equity to the general public has not yielded financial results. Loss-making PSUs don't find buyers in the market because private players look for efficiency and strong business fundamentals. The asset valuation method is often unable to optimally estimate the valuation of an enterprise. This method often does not take into account non-core assets of an enterprise which might have an impact on its eventual valuation. The valuation tends to overlook

[51] Garg, S. (2024, July 11). *Completing Rs 6 Trillion Monetisation: Reality or Gimmickry?* TheQuint; The Quint. https://www.thequint.com/opinion/national-monetisation-pipeline-nmp-completing-rs-6-trillion-monetisation-reality-or-gimmickry

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intangible aspects of a company like goodwill, distributional network and consumer relationships. Due to non-consideration of these factors, the liquidation value of the PSU is greater than its intrinsic value.

Political constraints

There is an ambivalence about the transition towards privatization and disinvestment from the governing class. This is because the experience of privatization in the rest of the developing world was not as good as that of the developed world. The creation and exacerbation of inequalities was seen as a consequence of a move towards a corporate-driven economy. Private intervention was often equated with scams[54]. Party ideological positions also determine the intensity of the disinvestment policies. However, the policy of disinvestment is adopted by most governments regardless of the party's ideological position. The left parties which often represent the trade union interests are staunch opponents of the policy. Trade unions have consistently denied the need for introduction of private players in erstwhile government services. The reasons for opposition are: fear of loss of job security, post-retirement benefits and their ability to organise themselves.

There is also a moral conundrum associated with the disinvestment process. The PSUs are owned by the government which is in turn elected by the people. The *de facto* owners of the PSUs are the people. PSUs are run by managers (Agent 1) who are appointed by the ministries (Agent 2) on behalf of the citizens. This double agent problem makes them more susceptible to inefficiencies than private enterprises. The reason for inefficiency is that the incentive of one agent can clash with that of the other[55].

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Recommendations

Valuation

PSUs must be categorised based on their turnovers, industrial models and standards. This helps in distinguishing PSUs that have a lower return on investment in contrast to those that have a higher capacity to convert outstanding liabilities into potential assets. For instance, the top 10 profit-making PSUs are found in the energy and minerals sector. Such enterprises must have a higher valuation on account of their strategic importance and the value of non-core assets. Other PSUs such as Utkal Ashok Hotel Corporation and Broadcast Engineering Consultants India have low-cost non-core assets. They also operate in sectors in which private sector has a considerable footprint, they enjoy a comparative advantage over the PSUs.

There need to be multiple considerations to be taken into account while arriving at a reserve price. There needs to be a mechanism to take into account the value of non-core assets in order to arrive at a more accurate estimation of the enterprise's value. The asset valuation method must take into account the future economic benefits of an asset. The historical or replacement cost of an asset may not convey an appropriate picture of the potential of the asset[56]. Valuation in the UK follows an 'indicative price' approach in which the market value of current assets and their future projections were taken into account. The privatization of the water industry followed this approach. The historical earnings were adjusted to project their prospective returns[57].

Non-Equity Joint Ventures

There are two kinds of joint ventures: equity and non-equity forms. In India, the former has been more used than the latter. Government accepted the concept of Joint ventures in 1975 and evolved criteria for equity sharing between the two partners. The central government can jointly set up enterprises with private players wherein both share significant equities. The superiority of Joint ventures as compared to Government or private enterprises is that they allow for social control over

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[56] Chaudhary, V. K., & Singh, K. (n.d.) Sustainability of Public Sector Enterprises for Nation Building: An Assessment of Disinvestment Strategies in India.

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industry. Apart from the improvement in resource mobilization, Joint ventures can help in broadbasing entrepreneurship in India [58]. The Joint Venture between Suzuki Motors and the Government of India is a very successful model. Maruti Suzuki India Ltd. initially had the Indian government as its major shareholder. By 1992, Suzuki gained a 50% share in the venture. The Japanese industrial techniques of Kaizen combined with the vastness of the Indian market contributed to the success of the venture. The government sold its 27% stake in the venture in 2003 [59].

There are various forms of non-equity joint ventures: vertical integration and transfer of operations. In the first method, government and private enterprises can come together at different stages of the value chain. In this method, the ownership structure does not change. The government and private enterprises which are placed at different stages of the value chain come together to share proceeds. In the second model, the government retains ownership but the private entity manages the operations. This is similar to leasing operations to a private firm owing to their efficiency in managing operations. After the concession period, the management can continue to rest with the private entity or can be returned to the government [60].

Management Employee Buyout

A buyout refers to the transfer of ownership to a legal entity in which the significance of managers and employees is higher than that of the majority shareholders [61]. There are various kinds of buyouts: Manager buyout, Employee buyout and Management-Employee buyout (MEB). Buyouts may involve sale of whole enterprises, divestment of part of an enterprise and breakup of entire enterprises into parts. The introduction of insider equity ownership increases incentives for managers and employees to

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enhance their efficiency. The extension of ownership to employees through an **Employee Share Ownership Plan (ESOP)** or direct purchase converts employees from agents to principals. By becoming owners, employees and managers reinforce the vertical supervisory structure. MEBs mitigate the shortcomings faced by Employee buyout (EB) and Management buyout (MB) individually. Fragmented ownership in EB leads to conflicts in strategic decision making The costs of conflicts are higher if the employees are heterogeneous. MB will always represent the interests of the top managerial sections which are essentially in conflict with those of the employees. The managers have a vested interest in slowing down the process of promotion or keeping wages at an abysmally low price[62] .

Regulatory model

In India, apart from the Department of Investment and Public Asset Management and various disinvestment commissions, there are no regulatory agencies which oversee the entire process of disinvestment. There was only one disinvestment commission set up in 1996 which ceased to exist in 2004. In situations where the institutional capacity is weak, an independent regulatory agency is supplemented by contracting out certain regulatory functions. Policymakers can also get regulatory assistance from regional regulators or from other countries through bilateral agreements .

The 'agencification' of disinvestment is required because in most developing countries, procurement is a political process. There are two governance links in the disinvestment process introduced through the procurement agency. The link between the government and procurement body & link between the procurement agency and the service provider. This model ensures a clear separation of responsibility. The procurement agency is responsible for monitoring the technical aspects of bid submission, previous experience and revenue model [63].

[62] Chaplinsky, S., Niehaus, G., & Van de Gucht, L. (1998). Employee buyouts: causes, structure, and consequences. *Journal of Financial Economics*, *48*(3), 283–332. https://doi.org/10.1016/s0304-405x(98)00013-0

[63] Lieberherr, E., & Leiren, M. D. (2017). Privatization, outsourcing and public service objectives: An explorative analysis of two network industries. *Case Studies on Transport Policy*, *5*(4), 681–689. https://doi.org/10.1016/j.cstp.2017.07.007

In the Indian context, there needs to be an independent expert procurement body which evaluates bids and eligibility criterion for different sectors. The body, though centralised needs to have multiple wings which have specialisation in different sectors (telecom, energy, roadways etc). After receiving the bids, they would examine the submissions. Each wing will look at the previous projects of the bidders, the valuation of the projects and the sustainability of the project. This will help in deciding whether an enterprise is technically sound in order to handle large scale operations of a PSU. After the evaluation, the agency will submit the findings through a report to the government. The government will then proceed with the disinvcestment according to the recommendations.

Brazil Disinvestment Model

While traditional models of privatization involve sale of public assets, the Law of concessions in Brazil to pass those activities to the private sector which the private sector is better equipped to manage. There need to be different rules established for each sector in which concessions are to be granted through competitive bidding. Electric energy, telecommunications, transportation, highway construction, ports and airports, sanitation and potable water are the main sectors that will be covered under this law. Employees can participate in the disinvestment process. They can buy upto 10% of the company's capital and they will be offered shares at a 70% discounted price. The reason why the Brazilian model is an ideal model fr emerging economies because the process of disinvestment is accompanied by legislative changes through the law of concessions. The model also establishes a regulatory agency in order to oversee the entire process of privatization. The involvement of employees in the process of disinvestment also promises to increase employee motivation and productivity. Hence, the model contains most elements of a desirable disinvestment policy for a developing country[64].

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Conclusion

India's disinvestment policy was part of a larger framework in which the state was seen to be correcting its historical error of overinvolvement. There were multiple approaches which were adopted for the process of disinvestment ranging from strategic sale to public offering. The policies of disinvestment have had an impact on efficiency which has seen a major boost. However, it has been opposed by those who advocate for a weafrist role of state. The loss of employment and reduction in employment benefits has been opposed by various groups. The liquidation of PSUs has yielded returns but it has not reached its target apart from two years. There needs to be certain amends to the disinvestment policy in order to ensure a smooth transition form state owned enterprise to a jointly owned/ privately owned enterprises. Improvements in valuation methodologies can also play an important role in determining the financial performance of PSUs.

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