The importance of public sector undertakings economics essay

ABSTRACT

Public sector undertakings (PSUs) are considered to be vital and crucial pillars for strengthening country's economy. The prime purpose of starting public sector enterprises was to fabricate infrastructure for economic growth and economic development. Since their birth PSUs have played an essential role in achieving the goal of economic development. Various factors such as deterioration of financial performance of PSUs, rising fiscal deficit forced Government to adopt a radically new approach towards the working of PSUs. The policy measure implemented involved Disinvestment of public sector undertakings (PSUs) . During the regime of P. V Narasimha Rao, entire new economic policy of Liberalisation, Privatisation, and Globalisation (LPG) was introduced in India in the year 1991. Dr Manmohan Singh was the finance minister who successfully implemented the policy of Liberalisation, Privatisation, Globalisation (LPG) into India. The goal of Disinvestment policy was as follows:

Improving the financial performance of PSUs.

Generating resources to reduce the fiscal deficit.

Promoting extensive public participation (including employees).

INTRODUCTION

Public sector undertakings (PSUs) are the companies established, maintained and controlled by the Central Government of India having 100% stake in it. In 1947 when India became independent, the country was confronting with a variety of socio-economic concerns which had to be resolved. India was mainly agriculture dependent economy with poor infrastructure facilities, no knowledge about investment, pathetic industrial base and low level of savings. There was wide difference in incomes of different people. The private sector neither had the necessary resources, trained managerial staff nor the ability to undertake risks involved in long term projects which forced the state government to intervene in all the sectors of economy. The type of problems faced by the country in all domains including economical, social obliged the Government of India to focus on public sector enterprises (PSEs) to empower self -dependent economic development. The holistic outline of public sector undertakings in India is heterogeneous mixture of service industries, manufacturing industries and infrastructural industries.

The basic objectives of starting public sector enterprises in India were as follows:

Generate employment opportunities.

Reduce gap between incomes of different people by redistribution of wages.

Promote rapid economic growth.

Improve essential infrastructure for economic development.

Support development of small and medium size enterprises (SMEs).

Central public sector units are widely diversified in products and services from steel manufacturing, instruments and machine tools, road transport, power generation, mineral mining, coal mining, manufacture of heavy machines, telecommunication equipment, equipments for thermal power station. Over the last five decades, huge investments have been done in public sector enterprises to expand their production, employ new emerging technologies. As on 31st March, 2005 there were 237 central public sector undertakings out of which 10 fall under the category of enterprise under construction, 144 are from field of manufacturing/producing goods and 83 under the head of enterprises providing services. From the Table-1 it is evident that initially at the commencement of First Five Year Plan, only Rs. 29 crore was the total investment for 5 enterprises. After gradually increasing the budget, at the commencement of Fifth Five Year Plan, the total investment reached whooping Rs. 6237 crore and the number of units became 122. By the end of the fifth Five year plan, total investment touched Rs. 15534 crore and the number of enterprises reached 169. From the data, it is quite clear that there has been increasing trend of investment from the commencement till the end of fifth five year plan, a rise of 149. 06 % is observed. Similarly a hike of 57. 70% in investment was examined from the start till the end of eighth five year plan. The investment made in public sector in 2005 was Rs. 3, 57, 849 , an increase of 2. 24 % from 2004. It can thus be concluded that there is increasing tendency towards investment made in the different five year plan.

TABLE 1:

DISINVESTMENT

The dictionary meaning of word " disinvestment" is opposite of investment. Investment means putting money into something with the hope to generate profits from it. So disinvestment means to pull out money from the investment. Initially central government had 100% stake in all the public sector enterprises, but due increasing fiscal deficit government is forced to sell 5 or 10 % stake to the public, thereby generating income for government spending. This way the government is losing full control over the corporations, but has no other option. Many times the government finds it very difficult to fulfil all the financial obligations of public sector enterprises, hence undergoes rigorous resource crisis. To bring back country's economy on right path, disinvestment formed an important part of structural reforms carried on by the government. The two most important reasons which favour disinvestment are as under:

Offer financial support to public sector undertakings (PSUs).

Develop effectiveness & efficiency of the public sector enterprises.

The resources raised from the sale of the stake of enterprises must be utilized for clearing past debts and thus reduce interest burden of government.

Principal goals for privatising the PSUs

The key objectives for privatising the PSUs are, as under:

Discharge huge amount of public resources blocked in non-strategic public sector enterprises & divert them towards more social issues like primary education, health and necessary infrastructure.

Decrease the public debt.

Encourage wider public participation by releasing shares in market.

Help the government reduce interest burden.

To facilitate the growth of the nation’s economy.

Freeing of tangible and intangible resources like labour blocked in maintaining public sector enterprises & reorganizing it towards high priority areas which have scare resources.

Some additional benefits from privatisation

The other advantages to be gained from privatisation are:

Disinvestment would picture the private firms towards more market discipline, compelling them to be more effective in their operations, working style. They would act in more responsibly and professional manner by responding to market forces at a greater pace. This would lead towards insertion of corporate governance into privatised companies releasing them from the government control.

Disinvestment would yield in fairer distribution of wealth among different individuals, as the shares of public sector enterprises would be offered to small investors and employees.

Disinvestment would have a great impact on capital markets, as the more stock inserted into market would bring in more liquidity allowing small investors with easier options to exit from market. It would result in forming more precise benchmarks for estimation of value, pricing.

Opening of vast portion of public sector for private participation would raise economic growth benefitting nation’s economy, employment prospects and tax collections in near future.

In many sectors like civil aviation, insurance, telecom, the introduction of private sector has brought in more customer satisfaction by delivering variety of products and services at cheaper rate and better quality. This even increased competition in the market. In case of civil aviation people were fed of Air-India's services and were demanding entry of private players into field of aviation.

The economic reforms along with the public sector reforms were mainly focussing on improving the effectiveness, efficiency & production output. Nowadays disinvestment, privatisation is grabbing everyone's attention as government is disinvesting stake in 5 to 6 companies every year. The government is planning to divest about 6 companies in year 2011. The New Industrial Policy states that a part of the Government stake in the public sector enterprises would be offered to various financial institutions, mutual funds (MF) and small investors in order to promote large public participation. In the current era of globalization, disinvestment would provide the motivation needed for the public sector corporations to make their mark in the list of top global companies. The Government of India formed a committee under the leadership of Shri V. Krishnamurthy to guide through the various characteristics of the process of disinvestment. It was Dr C Rangarajan's committee report's suggestions which resolved complex and complicated issues related to disinvestment. Similarly to a sports or a revenue department, an entire new department for disinvestment was formed which could solely focus on disinvestment issues, corporations which can be divested. During the NDA government rule, Shri Arun Shourie was the disinvestment minister. When UPA-1 regime started, disinvestment ministry had to be merged with finance ministry due to the mounting pressure from left parties (who are socialist attempting to reduce gap between rich & poor) who strongly opposed the formation of disinvestment ministry. Large number of corporation which were divested fell under the category of petroleum & oil exploration sector followed by metal, mining and minerals sector.

There are basically two approaches to the process of disinvestment:

First approach in which the PSU’s under the guidance of government issues fresh equity shares which can be brought by small retail investors, QIB’s, financial institution, Mutual funds.

Second approach in which the government sells it stake directly to the concerned public sector enterprises, interested retail investor, large financial institution.