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CHANGING ENVIRONMENT FOR INDIAN PUBLIC SECTOR – ENTRY TO THE CAPITAL MARKET

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In today's liberalisation context, there is a very strong case for permitting the public enterprises to approach the capital market. However, it is important to note that disinvestment of public enterprise shares and the shares to be off-loaded would be determined by two factors, viz., the government's need for additional resources, and the availability of resources with the mutual funds for making investment in public enterprise shares. The authors have emphasised that a proper open policy for creating a conducive environment for the investors' confidence and protection is essential. There is also a note of caution that only those public enterprises should be selected for capital market entry which are efficient and economically viable.

I

Introduction

Public enterprises have been assigned a vital role in the Indian planning process. They have been regarded as an engine of economic development. The investments in these enterprises have dominated the economic scenario throughout the plan period. It is interesting to note that about 50 per cent of the public sector investments flowed to public enterprises during the 7th Plan period. It is also worthwhile to mention that in the gamut of public sector, the savings have remained positive in the case of public enterprises only. The departmental enterprises and administrative departments turned out to be a net drain on public savings. However, there is no denying the fact that even public enterprises fell short of the savings targets assigned to them during the 7th Plan period. Nonetheless, it must be noted that during the last 10 years between 1980-81 and 1989-90, there has been a perceptible increase in the generation of internal resources by Public Enterprises.

Th question about the size of the 8th Plan has undergone a number of twists and turns so much so that while we have had four changes between 1989 and 1991 in the government at the Centre, we have just been able to arrive at the finality about the size and initiation of the 8th Plan. It is now planned to aim at rate of economic growth of 5.6 per cent which would require an investment of Rs. 7,29,000 crores. The size of public sector would be about Rs. 3,60,000 crores which would measure to about 44 per cent of the total plan outlay.

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Although public enterprises have attained a 'commanding height' they have proved themselves to be a drain on the public exchequer. Public enterprises are facing severe criticism for their dismal performance. Some of the critics have gone to the extent of discarding the concept of public sector itself. The dismal performance and criticisms have, however, shadowed the positive role played by public enterprises in achieving social objectives. Whatever may the criticism, public enterprises shall continue to play their crucial role, though they would be under tremendous pressure for improving their performance.

The new industrial policy recently announced has resolved to review the portfolio of public sector investments with a view to focus the public sector on strategic, high-tech and essential infrastructure. The new policy has narrowed down the area reserved for public enterprises. The policy states that sick units would be referred to the BIFR; a part of the government's shareholding would be offered to mutual funds, financial institutions, general public and workers; the board of public sector companies would be made more professional and would be given greater powers; and there would be greater thrust on performance improvement through the MOU system; MOU signed between government and the public enterprise would be placed in the Parliament.

The Public Enterprises in India have not generated adequate internal surpluses because of their inadequate exposure to competition. The post tax-profits have declined from Rs. 3657.6 crores during 1989-90 to Rs. 2730.27 crores during 1990-91. The losses of loss-making enterprises have increased by 48.6 per cent. Out of 98 loss-making enterprises, 52 have been incurring losses continuously for the last five years. The over-employment and out-moded technology have led to increase in costs thereby reducing the profits. To overcome this pathetic work environment in public enterprises, the government has recently adopted a new approach, the key elements of which are as follows:

(i) The existing portfolio of public investments will be reviewed with a greater sense of realism to avoid areas where the private sector will be more efficient.
(ii) Greater degree of managerial autonomy will be provided to those public enterprises whose continued existence is justified.
(iii) Budgetary transfers to public enterprises will be progressively reduced.
(iv) Competition from the private sector will be encouraged.
(v) Part of the equity in selected enterprises will be disinvested.
(vi) Chronically sick public enterprises will not be allowed to continue to incur heavy losses.

Currently decision makers, media and public in general are keen to know the future role of the public sector. Mostly the debate centres around

(a) its viability in terms of profitability;
(b) its competitiveness to face onslaught from national and international competitors; and
(c) its technological upgradation efforts to match international standards and to produce and market high quality products at minimum cost.

II

The New Industrial Policy and Public Enterprises

The new industrial policy clearly indicate that the government policy is tilted towards MOU. We consider this to be a healthy sign. However, the success of MOU would depend on the sincerity of both the parties, namely the government and the public enterprise. Moreover, MOU, being a two-way agreement, should be between equal parties. Whether bureaucracy representing the government would keep this in mind while entering into agreement with those public enterprises which do not enjoy the status of ONGC, BHEL, IOL etc., is a moot question.

The industrial policy has resolved to create a social security to protect the interest of the workers likely to be affected by rehabilitation schemes to be formulated by BIFR for chronically sick enterprises. This is an excellent approach. However, the creation of this fund would not reduce the pressure from workers associations in implementation of such a rehabilitation programme. Does the government have the required political will to overcome such pressure?

The industrial policy states: "In order to raise resources and encourage wider public participation, a part of government shareholding in the public sector would be offered to mutual funds, financial institutions, general public and workers". The policy has not indicated the percentage of disinvestment but from various press reports it appears that the government is considering 20 per cent disinvestment of shares to selected public enterprises. It is difficult to visualise what benefits would occur from this 20 per cent disinvestment except immediate generation of some resources. If government decides for privatisation or a complete remodelling of the board of directors, it has to disinvest a much higher percentage of its investment in public enterprises.

III

Public Sector Disinvestment

On 4th March 1991, the then Finance Minister announced 20 per cent disinvestment of public sector equity in his interim budget for 1991-92. This was endorsed by the new Finance Minister in July in his budget speech. A time-frame for the off-loading of PSU investment was announced by Mr. Singh at the Fund Bank Annual Meet in Bangkok on October 12, 1991. Though initially 50 companies were mooted for disinvestment, only 31 companies were eventually taken up (decision taken in late November). Even after that, Air India and Indian Airlines were dropped from the list on the excuse that they have yet to get corporate status, while Indian Petro-chemicals and SAIL were last minute entrants. Deepak Raja of Strategic Private Ltd., officials of the Government and the executives of the company have discussed the issue of 'reserved price'. Incidentally, each public enterprise will offer up to 5 per cent of its shares to employees at the same terms that the financial institutions receive. On 10th

December, the government has issued letters to all the concerned mutual funds and financial institutions (excluding ICICI, IDBI and IFCI) inviting their bids. The face value of each share was Rs. 10.

The companies selected for disinvestment were then clubbed into seven or eight companies per package. Each package consisting of shares of 8 to 9 PSUs (majority of which are highly profitable and a pair of marginally profitable companies) was valued at an average price of Rs. 4 to Rs. 5 crore. A total of 825 packages were created. The Government allowed the institutions to bid for any or all of the total of 825 packages offered. Each institution apart from UTI earmarked about 20 per cent of its funds for equity investment towards this programme.

Small and newer mutual fund companies found it difficult to bid for many packages. BOI Mutual Fund (nil), Inbank Mutual Fund (3 packages of Rs. 8.5 crores) and PNB Mutual Fund (one package of Rs. 3.5 crore) have faced the problems of funds. Canbank Mutual lived upto its aggressive image, consistently bidding the highest for its chosen packages. Its average bid of Rs. 4.5 crore per package exceeded rivals by about a crore on average. For Bharat Petroleum, Canbank's bid of Rs. 446 per share is very high in comparison with its reserve price of Rs. 330. The Government collected Rs. 1300 crores in which UTI has a share of Rs. 700 crore (bid Rs. 1200 crores). LIC, SBI, Canbank and OIC were the other bidders. The listing process will now begin as the Government has promised to list all the 31 scrips on all the major stock exchanges in the country. This environment should be welcomed as the Government and Mutual Funds have behaved competitively.

IV

Exit Policy

Public Enterprises which are chronically sick and unlikely to be turned around, will be referred to Board for Industrial and Financial Reconstruction (BIFR) for rationalisation. The decks have been cleared with the Parliament recently approving the Bill to amend the Sick Industrial Companies (Special Provisions) Act, 1985. The selection of 50 public enterprises for reference to BIFR has been made by considering the figures of 1989-90. Out of 98 loosing public enterprises, the DPE has picked up 59. Of the chosen 'chronically sick' 58 enterprises, eight units including DTC are deemed to be enterprises rendering services. These 50 public enterprises have a total of 3.40 lakh employees. The annual loss per employee works out to Rs. 38,714 during 1989-90. The accumulated losses per employee is of the order of Rs. 2.09 lakh. While NTC's subsidiaries dominate the list, practically all sectors find representation, be it engineering, chemicals, fertilisers, mines, steel and so on. The prominent public enterprises like IISCO, FCI, HFC, IDPL, HSL, SAIL and the National Jute Manufacturers Corporation are in the list.

V

Emerging Dimensions

In such an environment, it is proper and feasible for the Government to allow the public enterprises to approach the capital market for their long term financial requirements. In this connection, it is also important to note that the Committee on Public Undertakings (COPU) as in 1955 had recommended that atleast 25 per cent of the share capital of public enterprises should be made available for subscription by the public and the Government could fix a ceiling for individual holding as well as on the dividends to be declared by these companies. Similarly, Krishna Menon Committee, had also recommended 25 per cent equity participation by the public at large. Incidentally, a company can combine both Government share-holding and private share-holding and this can be done within the provisions of both the Industrial Policy Resolutions of 1956 and 1991 and the Companies Act, 1956.

Public Enterprises, by approaching the stock exchange with their securities can greatly boost the capital market by substantially increasing the availability of floating stocks. Nothing is a better index of a company's good health than its market quotations which, in essence, signify the degree of confidence of the public in the company's future. Thus in the present day context, there is very strong case for permitting the public enterprises to approach the capital market. Earlier experience had also favoured the public enterprises to utilise the services of stock exchanges. It may be noted that about 15 PEs had already issued their bonds to the investing public and financial institutions.

The union Budget envisaged that Rs. 2,500 crores would be raised through disinvestment of public enterprises shares to mutual funds of Life Insurance Corporation of India (LIC), General Insurance Corporation of India (GIC), and the Unit Trust of India (UTI). It was subsequently decided that public enterprise shares would be offered in two lots – one lot before December 1991 to raise Rs. 1,250 crores and the other in 1992 to mop up the remaining 1,250 crores. However, it is important to note that disinvestment of public enterprise shares and the shares to be offloaded would be determined by two factors, viz., the government's need for additional resources, and the availability of resources with the mutual funds for making investment in public enterprise shares.

VI

Mutual Funds (MFs) Boom

In a short span of just of about 4 years the mutual funds, sponsored mainly by major commercial banks, the Unit Trust of India and the two insurance giants, have overshadowed all other modes of investment on the capital market. These funds have collected huge sums of money from investors, who are interested in high yields or assured appreciation with security and safety of investment.

In the first three years the MFs collected around Rs. 2,000 crore in their ever

increasing number of schemes. But the year 1990-91 was decidedly the most fruitful when around Rs. 4,000 crore flowed into various MFs schemes. The year 1991-92 started on a real promising note and the indications are that a bigger tranche of funds would percolate into MF schemes.

Although Unit Trust is the pioneer in the field of mutual funds, the Canara Bank has taken the lead in mobilising funds from the open capital market. In fact the UTI is the oldest mutual fund in the country established well over 25 years ago but its original concept differed substantially from the shape and content of the present day mutual fund schemes.

For well over two decades the Unit Trust had been prospering mainly on the strength of tax concessions and other sops provided by the Government to the people acquiring UTI Units. But the mutual fund schemes sponsored by banks and other organisations do not enjoy any preferential treatment in resepect of investment made in the instrument. The only shelter available to the belssed sponsors is that as yet the private sector has not been allowed to enter this major fund raising activity.

The unprecedented boom on the stock market last year has been squarely attributed to the availability of huge sums of money with mutual fund managements and their eagerness to maximise the returns by deploying bulk of those funds in blue chip and growth oriented shares. This year the mutual funds have stock-loads of investible resources but the only inhibiting fector is the uncertainty in respect of attitude of the Government at the Centre. Now things may stabilize for the better.

In the fast expanding circle of MF operations, Canara Bank has earned the distinction of being the most innovative. Its series of schemes, all bearing 'Can' as prefix, have been a roaring success. 'Canstar', the ambitious scheme floated by the bank last year created history when it attracted cash resources amounting to Rs. 1,000 crore. Another historical event in the annals of the 4-year old 'CANFIN' services was the issuance of bonus shares to the holders of Can shares at the completion of the very first 11 months issue. In a surprise move the Canara Bank subsidiary recently came out with two absolutely unorthodox schemes – Canbonus and Canpremium. Canbonus is meant for existing holders of various schemes in the CAN family circle, and promises a minimum allotment of at least 100 shares to each eligible applicant. The investors will not be paid any regular dividend but the investment will stand augmented by the issue of bonus shares at the discretion of the management. CANFIN record so far promises a rich harvest for the potential applicants.

The Rs. 500 crore Canpremium scheme, launched recently is a class apart. It is directed towards corporate entities and extra affluent individual investors. The minimum investment in the scheme is rupees 10 lakh and its multiples thereof, comprising 10 units, of Rs. 1 lakh each. The scheme ensures a minimum appreciation of 51 per cent in 3 years, over 70 per cent in 4 and 100 per cent in 5 years. The level of response to the scheme is evident from the fact that the management stopped accepting contributions to the high profile instrument within a few days of its formal opening for subscription.

Amongst other major operators in the field, the State Bank of India has in-

troduced a whole lot of Magnums to suit the fancy and needs of a variety of investors. Similarly, the Life Insurance Corporation of India has been flooding the capital market with an unending series of schemes bearing 'Dhan' as the common prefix. Other names which made their presence felt in the mutual funds networks are Bonanza from Bank of India and Ind Jyoti sponsored by the Indian Bank.

The names of the public enterprises whose shares have been offered to mutual funds and the number of shares offered are as follows: (1) Hindustan Petroleum Ltd. (1,27,68,000); (2) Indian Railway Construction Corporation (IRCON) (9,89,900); (3) Minerals and Metals Trading Corporation (MMTC) (1,98,000); (4) Bharat Earth Movers Ltd. (BEML) (60,00,000); (5) Bharat Petroleum Corporation Ltd. (BPCL) (1,00,00,000); (6) Videsh Sanchar Nigam Ltd. (VSML) (1,20,00,000); (7) Dredging Corporation of India (56,00,000); (8) Bongaingaon Refineries Ltd. (3,99,64,000); (9) National Fertilisers Corporation (2,45,29,000); (10) Fertilizers and Chemicals Travancore Ltd. (1,69,65,604); (11) Hindustan Photo Films (2,19,00,000); and (12) Computer Maintenance Corporation (30,00,000).

VII

Convertible Debentures

Convertible debentures are very popular nowadays. People prefer to purchase convertible debentures in comparison to equity and preference shares. The main advantage of convertible debenture is that the holder not only gets fixed rate of interest on investment, but can also convert these into equity shares, Table 1 shows how the percentage of convertible debentures has increased from 2.8 per cent in 1985 to 51.5 per cent in 1989 in the composition of total capital shares.

TABLE 1: Composition of Capital Market — Total Capital Issue

(In Million Rupees)

Types of	1981	1985	1986	1987	1988	1989
Equity and Preference shares	2048	7298	11810	12218	8464	12631
% of Total	(49.5)	(34.6)	(25.8)	(33.4)	(19.3)	(12.3)
Debentures/Bonds Non-Convertible	769	13239	25590	16530	24304	37576
% of Total	(18.6)	(62.6)	(55.9)	(45.0)	(55.4)	(36.2)
Convertible Debentures	1319	570	8360	7956	10979	53374
% of Total	(31.9)	(2.8)	(18.3)	(28.6)	(25.3)	(51.5)

Source: Stata Bank of India, *Monthly Review*, Feb. 1990.
(Figures in brackets show the percentage of the total).

It also reveals that equity and preference shares' percentage has gone down from 49.5 per cent in 1981 to 12.3 in 1989 in the total issue. Similarly the per-

centage of Non-convertible debentures has also declined from 62.6 per cent in 1985 to 36.2 in 1989 of the total issue.

VIII

Capital Issues by Public Enterprises

Owing to risk in accepting public deposits, the Government of India has allowed public sector enterprises to enter into capital market by floating debentures and bonds. The public sector needs funds for its modernisation and diversification programmes. Public enterprises have competed with the private sector in capital market particularly during the last 4-5 years. It has entered well in the capital market by capturing 42 per cent of the total issue in the capital market in the year 1988. Table 2 reveals this fact.

TABLE 2: Capital Issues

(In Million Rupees)

Ownership Private	1981	1985	1986	1987	1988	1989
Corporate	N.A.	19215	27837	21585	21641	67582
% of Total	—	(90.2)	(60.8)	(58.7)	(49.3)	(65.0)
Term Lending Institution	N.A.	1892	2490	3340	3605	5399
% of Total	—	(9.8)	(5.3)	(9.1)	(8.3)	(5.2)
Public Sector	N.A.	N.A	15434	11839	18501	30600
% of Total	—	—	(32.7)	(32.2)	(42.4)	(29.8)

Source: State Bank of India, *Monthly Review*, Feb. 1990.
(Figures in brackets show the percentage of total).

It further reveals that private corporate sector's percentage in total capital issue has gone down from 90.2 in 1985 to 65.0 in 1989; the share of public sector enterprises was 32.7 in 1986 in total capital issues which has gone up to 42.4 in 1989. This shows the increased trend of publc sector in the capital market. This is a good sign. It has relieved the government to some extent from the financing of public sector enterprises. Prior to this, the public sector enterprises mostly depended on the government for funds. Now they can also raise it from the capital market.

It is observed that fresh capital issues' percentage is increasing in the total external sources of public enterprises. If we compare this percentage with that of the private sector, it is less in private sector in comparison with the public sector. This fact is clear from Table 3.

The important trend in public sector's capital issues is that the whole issue goes in the form of private placements with banks, financial institutions and mutual funds. In 1989 57.6 per cent of the total capital issue was in the form of rights and private placement issues. Funds raised by way of rights and private placements increased 3.8 times the amount raised similarly in 1988, from 16032 million rupees in 1988 to 59490 million rupees in 1989.

TABLE 3: Key Ratios (Percentage)

Private Sector	1985-86	1986-87	1987-88	1988-89
(a) Internal Sources/ Total uses	54.3	35.4	40.7	36.9
(b) External Sources/ Total uses	45.7	64.6	59.3	63.1
(c) Fresh Capital issue/ External sources	2.4	5.6	6.0	4.8
Public Sector	**1984-85**	**1985-86**	**1986-87**	**1987-88**
(a) Internal Sources/ Total uses	19.6	38.6	43.6	39.3
(b) External Sources/ Total uses	80.4	61.4	56.4	60.7
(c) Fresh Capital issue/ External sources	20.0	31.1	41.0	17.0

Source: Trends in Company Finance 1984-85, 1988-89, Centre for Monitoring Indian Economy, Bombay, Jan. 1990.

IX

Venture Capital

The scheme of venture capital is of recent origin. The Capital Venture Funds (CVF) is the first private sector company to go public. The other institutions which floated venture capital funds are:

(a) Technology Development and Investment Corporation of India (A subsidiary of ICICI),
(b) Technology Development Fund (A subsidiary of IDBI),
(c) SBI Capital Markets (Equity support scheme of State of Bank of India),
(d) Can Finance (Canara Bank subsidiary),
(e) India Investment Fund (Grindlays Bank), and
(f) Infrastructure Leasing and Finacial Services Ltd. (ILFS), set up by the Central Bank of India, UTI and Housing Development Finance Corporation.

X

Recent Trends

It is estimated that at present there are 10 million investors (including 5 million shareholders and 5 million investors) operating in the Indian capital market. It is further estimated that by the end of this century the number of investors including the shareholders will be around 20 million. There is awareness in the public not only in the metropolitan cities but also in other cities for investing in the share market.

At present 5000 companies are registered with the stock exchanges. It is estimated that around 15000 companies will be registered with the stock exchange by the end of this centure and the annual volume of transactions will be of the order of Rs. 75,000 crores. So, in order to handle all these affairs we need more stock exchanges and it is hoped that by the end of 2000 A.D., 25 stock exchanges will be established.

At present, 1400 share brokers are operating in the country. In order to handle this increasing number of investors we need 1500 brokers and a vast network of sub-brokers and agents. It is estimated that during the Eighth Plan Period (1992-1997), the Indian capital market would provide Rs. 75,000 crores.

XI

Conclusion

The Government of India has been formulating an open policy regarding public enterprises entry to capital market. However, it is a chellenge for the Government as well as public enterprises to create a conducive environment for the investors' confidence and protection. A proper open policy in this connection is highly desirable. Only those public enterprises should be selected for capital market entry which are efficient in their operations and viable on economic fronts. A selected approach is needed to strengthen the capital market.

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