

2. Should the Government Exit Public Sector Units

Prelims level: Economy – Investments.

Mains Level: GS-III Investment Models.

Context:

- Government has recently approved the sale of its complete stake in Bharat Petroleum Corporation Limited which is a Maharatna company.

Categorization of PSUs:

- There is a sub categorization within PSU fold to award greater financial autonomy to certain PSUs to provide them with competitive advantage and enable them to become global giants.
- The categorization is of three kinds: **Miniratna, Maharatna and Navratna** in the order of increasing autonomy.
- Here are the Parameters on which government grants the status of Maharatna to Central Public Sector Enterprises (CPSEs).

Criteria for grant of Maharatna Status:

- The company should already have Navratna Status.
- It should be listed on Indian stock exchange with minimum prescribed public shareholding under SEBI regulations.
- Average Annual Turnover of more than Rs. 25,000 crore, during the last 3 years.
- Average Annual Net Worth of more than Rs. 15,000 crore, during the last 3 years.
- Average Annual Net Profit after tax of more than Rs. 5,000 crore, during the last 3 years.
- The Entity should have significant global presence/international operations.

How does Maharatna status helps in enhanced powers:

- As compared to other CPSEs, the Boards of Maharatna CPSEs have been delegated enhanced powers in the areas of: -
 1. Maharatna company can invest 15% of its net worth in a single project for establishing a new venture or undertaking an acquisition activity with a cap of Rs 5,000 crore without any permission from GOI.
 2. Make Equity Investment to establish financial joint ventures and wholly owned subsidiaries in India or abroad.

Criticism on Government Disinvestment in PSUs:

1. This step of the government is not the reflection of the long term agenda of privatization but rather it is driven by the revenue short falls.
 - The original idea for partial disinvestment of profit making PSU was Two Fold:
 - a. This would free up government resources to be invested in other loss making PSUs with potential for future profits.
 - b. Having minor private shareholders brings accountability and monitoring of the functioning.
2. One of the arguments put in favour of privatization is that it reduces political interference and rent seeking.
 - But let's look at some sectors which have been fully privatized and see what Privatization Has Done.
 1. **Telecom:** All the companies are debt ridden and barely surviving.
 2. **Aviation:** Airlines are burning deep pockets to stay afloat.
3. The argument that private sector is profit making is also flawed to some extent.
 - As we get to see only those who survived. The loss making firms close down and disappear. Eg: Recent shutdown of Jet Airways.
 - But Loss making PSUs continue to survive due to government backing and remain visible.
4. BPCL is already a market leader and highly profitable company (implying it is efficient as well) then why privatise it?

But why government is privatizing BPCL when it is Profitable?

- Government argues that this is the time for realization of maximum values on shares. As more and more private firms will enter the oil distribution market, their profitability will decline and hence the share value will fall as well.
- But again, even after entry of private players, we can see Public sector companies competing in the market (E.g. ONGC) and hence this argument doesn't hold either.
- Asset sales typically happen under distress conditions, where governments are under severe fiscal stress and they want to raise revenue quickly.

What are the Issues Regarding Valuation:

- Valuation is the trickiest part in privatisation. In general, if you go for strategic sales, where you sell a 100% or majority stake in one go, then the chances of getting the valuation right is lower as there is no price discovery process.

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- Later on, you realise the price was perhaps not right. Whereas with disinvestment, where you unload in tranches, there's a better chance of price discovery over time — the first tranche may be undervalued, but once it is listed and performance improves, the government can realise better valuations in subsequent tranches.

How have other countries done this?

- This is why contrary to popular perception in the country, a vast majority of privatisation sales the world over have happened through share issue privatisations (disinvesting partial stakes) as opposed to asset sales (what we call strategic sales).

