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ABSTRACT

For nearly a decade since the onset of economic liberalization in India, a key component—privatization—remained dormant. The usual explanation has been that weak governments could not overcome the many vested interests, from rent seeking bureaucrats and ministers to public sector trade unions. In addition, ideational resistance in India's elites has also been attributed to the virtual absence of privatization in India's economic reforms. How then does one explain the recent acceleration of privatization in India and what does it reveal both about state capabilities and the strength of societal actors? This paper argues that it was not just "vested interests" alone, but institutional structures, in particular those embedded in the judiciary, parliament and India's financial institutions, that played an important role in the long lag between the onset of economic liberalization and privatization.

The time variable however, has been important in two additional ways. For one, just as the external debt crisis forced the initial round of economic reforms, the growing internal debt problem and the fiscal crisis of the Indian state has increased the opportunity cost of state owned enterprises. Second, the passage of time has also resulted in significant ideational changes in India, both with regard to the relative effectiveness of the state and markets in commercial activities, as well as assumptions of the Indian state being a "guardian of the public interest". The privatization of state owned enterprises severely underestimates the degree to which privatization de jure and especially de facto—has been occurring in India, ranging from the privatization of public space to education, to privatization-like processes in the bureaucracy itself. We examine this issue briefly and some of its implications then offer some thoughts on the road ahead.

Keywords: privatization, economic liberalization, assumption, bureaucracy

1. INTRODUCTION

Privatization of public enterprises has generated much debate; developing economies, which had previously opted for planning as a strategy and system for national socio-economic development. Under the Five Year Plans, the Indian state took upon herself the responsibility to undertake investments in basic and strategic economic activities and to control and direct private sector through a network of regulatory institutions. After pursuance of planned development for nearly half a century, a stage was reached when questions were raised about the relevance and the need to continue the planned development strategy. There is an ideological position that asserts to 'end all direct and indirect state interventions in the economy'.

The state should, according to this viewpoint, roll back and occupy the minimum possible space. The market forces instead of the arbitrary decisions undertaken by bureaucrats and politicians should decide all economic decisions. The contrary viewpoint is that since the Indian economy is ridden with extreme disparities in incomes, wealth and consumption, macroeconomic decisions cannot be left to the operation of the free market system. Third World economies suffer from so many socio-economic limitations that it is obligatory on part of the state to operate from the 'commanding heights' and aim at the highest level of socio-economic good for the largest numbers.

2. THE CONCEPT

Privatization, in its broader sense, stands for policies to reduce the role of the state, assign larger role for the private sector pursuing the logic of the market in all economic decisions. Viewed in this perspective departure from the policy of reservations of certain economic activities for exclusive development by the public sector (dereservation) implies a reduction in the relative position of the state sector and larger role for the private sector.

The entry of new private sector enterprises could introduce competition where public sector enjoyed monopoly. The existing public enterprises (PSEs) would be forced to go commercial and respond to the market discipline. The dereservation process has sometimes been described as 'Parallelization' in the privatization framework. Privatization is also witnessed when governments take a decision to reduce their obligations to regulate and direct the behavior of private actors in the economy. Pursuance of deregulation policies is aimed to make the restrictive regulatory system less important. In India, deregulation would imply loosening such statutes like the Industries (Development & Regulation) Act, 1951 (IDRA), Monopolies & Restrictive Trade Practices Act, 1969, (MRTPA), Foreign Exchange regulation Act, 1973 (FERA), Capital Issues Control and technical scrutiny by the Directorate General of Technical Development (DGTD).

Privatization, however, is most often associated with transfer of public sector enterprises and services to private ownership, management and control. The privatization process for public enterprises can involve steps ranging from dilution of state-held equity, to adoption of practices like franchising, award of lease and management contracts, sub-contracting of select activities and tasks, down-sizing of workforce, and changes in the process of decision making even without change in ownership, so that business decisions are guided by market and commercial principles of profit maximization than vague societal concerns. Privatization in India has been carried out in several stages; such as, deregulation, dereservation, privatization and disinvestment. These are discussed in the subsequent sections.

3. CONTEXT OF PRIVATIZATION

Soon after the initiation of development planning in India it became evident that the public sector was an economic necessity for the economy and the private sector. Public sector was envisaged as a major instrument for pursuance of plan targets. It was universally accepted that the Indian private sector was neither capable of making the necessary large investments nor was it expected to take up projects with long gestation periods and carrying low rates of return. Industrial Policy Resolution, 1956 reserved a large sector both for exclusive (Schedule A) and priority (Schedule B) development by the public sector.

The government took upon herself the task of providing essential infrastructure and utilities as also heavy industries. This process was aided by nationalization of certain sectors and selected undertakings. By mid-seventies public sector accounted for a little less than one fifth of the GDP and nearly half of the Gross Capital Formation (GCF). In the organized industrial sector, it accounted for about two-thirds of the fixed capital invested. In certain industries public sector acquired a dominating position, often accounting for ownership and production to the extent of near 100 per cent.

Public sector in India has two main forms. One, the departmentally owned and managed establishments like railways, posts, telecommunication, irrigation, and power projects; and two, enterprises established under the Companies Act, 1956 and under special statutes. At the end of 1992, there were 1,180 undertakings in which government owned majority equity capital and which were categorized as government companies. Of these, the Central government undertakings numbered 239.

While in numbers the Central PSEs accounted for only a fifth of the total, these accounted for nearly 85 per cent of the overall risk capital and assets of the PSEs organized as joint stock companies. The State-owned PSEs were 941. The central government manufacturing companies accounted for 41.12 per cent, and those engaged in mining and quarrying for 28.62 per cent of the total PUC, Combined with electricity and water the three sectors accounted for nearly 90 per cent of the risk capital of Central public sector companies. The State sector had a different pattern of activities. In their case, manufacturing accounted for nearly one-third, agriculture and forestry a little more than one quarter, and finance and business nearly 20 per cent. In the present study we are not attempting to review the State enterprises for reason of time available with us as also due to the lesser significance of State PSEs in the national set up.

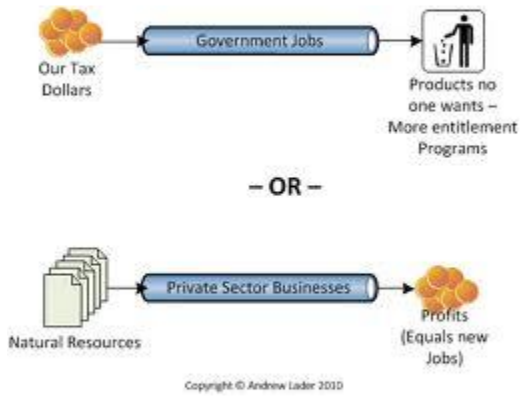
Public sector has been an important employer, especially in the organized labour market. The sector accounted for 56.84 per cent of the total number of 14.3 million employees in the organized sector1 in 1980-81. From about 8.1 million in 1980-81, those employed in public sector manufacturing increased to 9.8 million by 1990-91. In spite of the efforts at downsizing workforce by public sector during the nineties, the number of employees remained at 9.8 million at the end of 1996-97. During the nineties, its share in total hovered around 60 per cent.

4. DISINVESTMENT AS A FORM OF PRIVATIZATION

The process of privatization in terms of removal of administrative controls and regulations was discussed in the preceding paras. The process is, however, more frequently associated with transfer of public enterprises to the private sector. Privatization of public enterprises could take any one of the following forms:

a) Divestment of government-held equity to:
- ✓ strategic/joint venture partners through open bidding or negotiated settlement;
- ✓ financial institutions (foreign, public sector and mutual funds); or

- ✓ general public;
- b) Promotion of joint ventures for further expansion or through transfer of certain existing units/operations;
- c) Entering into management contracts with private professional groups or entrepreneurs;
- d) Nomination of private individuals on Board of Directors of PSEs even when their equity is insignificant; and/or
- e) Contractualisation of operations.



Private Sector jobs

IPS 1991 proposed to review public sector investments in order to limit their coverage to strategic, high tech and essential infrastructure. The objectives of unloading government held equity were outlined as: (a) to further market discipline, (b) raise resources, and (c) encourage wider public participation in management of PSEs.1 Chronically sick public enterprises were proposed to be referred to the Board for Industrial and Financial Reconstruction (BIFR) for revival or reconstruction. The IPS 1991 also proposed to provide for more professionals on Management Boards of PSEs. Social safety measures were proposed to protect the interests of workers who may be affected by other steps proposed under IPS 1991.

5. CONTRACTUALIZATION

Some of the public sector enterprises have closed down certain of their activities by subcontracting them to private parties. Contractualisation of specific tasks has been assisted by the general ban imposed by government on new recruitments. The activities privatized and brought under subcontracting include catering; message and courier service; and security, cleaning and maintenance of office buildings and office transport (staff cars). Railways appear to have taken to sub-contracting of services in a big manner. Sale of beverages and snacks on platforms by private vendors is an old practice but now the departmental catering on main routes has been privatized. Experiment has been undertaken in privatizing platform management and maintenance. Additionally, the railways are contemplating commercial exploitation of space over railway land and tracks in metropolitan towns with private sector participation.

Award of security contracts to private security agencies is gaining acceptance both in public and private sectors. There are no available estimates of the number of regular employees who have been affected by the introduction of the practice of contract labour or privatization of certain services. It is reported that the nine PSEs (termed as Navratnas) employ about 20,000 contract workers.2 Another estimate has placed the number of contract labour at 16,000 in SAIL and 12,000 in NTPC.3 The Chairman of Standing Conference of public Enterprises (SCOPE) is reported to have reacted to the Supreme Court's directive 4 to Air India for absorption of contract labour by saying that such a move will have major implications for most PSEs including NTPC, ONGC and SAIL. The Navratnas were reported to have requested the government to approach the Supreme Court to review its decision.5 PSEs defend the use of contract labour on the ground of seeking to remain competitive. The Director, Personnel, NTPC said:
Outsourcing is an international business norm. If we are to handle our security, catering and health services departmentally, the cost will be enormous and we will be in no position to compete with private companies who are outsourcing a large part of their requirements.

6. CONSEQUENCES OF PRIVATIZATION

Each form of privatization has differing implications for the labour, consumers and the economy. Dereservation, for instance, is likely to have little immediate adverse impact on employment. Dereservation, because of the removal of entry barriers, may motivate additional investments and offer enlarged employment opportunities. It is, however, possible that new private sector entrants may indulge in 'poaching' of senior and experienced employees of the public sector by offering attractive emoluments. The outgoing public sector employees would carry the advantage and access to business networks and knowledge of the market with them. This phenomenon has already been seen in the aviation sector and communications industry. Privatization could lead to a reduction in the workforce if the new managements were to opt for modernization and automation. This, in all probability, is unavoidable.

Downsizing of labour is often considered a pre-condition to privatization of PSEs. Privatization
in the form of sub-contracting could result in replacement of permanent and better-paid jobs with low wage unorganized casual labour. Dilution of government held equity by itself did not have any significant direct implications on labour. The general thrust at downsizing of labour in PSEs, however, had an across the board effect on PSEs whether profit-making or chronically sick. The existing PSEs are likely to lose a part of their market shares due to competition from new private sector entrants and from imports under the new liberalized system. It would in all probability become necessary for these enterprises to opt for technological upgradation and seek higher productivity. Adoption of new technologies may result in lowering of the overall labour requirements and making certain types of jobs wholly redundant. At the same time, however, adoption of new technologies could enlarge demand for certain type of skilled employees as also reduce avenues for employment in certain sectors. There is bound to be a change in the employment structure.

7. REGULATORY BODIES

Privatization of large public enterprises and entry of private sector in erstwhile reserved areas has the potential of giving rise to establishment of private monopolies. The interest of the consumers may therefore have to be protected from the normal instinct of private monopolies to exploit consumers in order to maximize their profits. One should not stretch the point too far as for the tendency of a public monopoly to be always better. Yet, there can be no denying of the fact that monopoly is a monopoly irrespective of it being in the private or public sector. Monopolies always need to be regulated to protect consumers and to control indulgence in wasteful and unproductive expenditure. It is only the regulations and obligations imposed on them that can ensure adequate attention being paid to R&D or participation in technological change.

It is true that the government has appointed the Telecom Regulatory Authority of India Act, 1997, Electricity Regulatory Commission, and it is envisaged to have Insurance Regulatory Authority. The regulatory authorities are expected to oversee the operation of the sectors concerned. Given the experience of the functioning of the regulatory mechanisms in India it is only too early to assert the contribution of the newly appointed regulatory bodies. The example of SEBI has not been a very happy one.

The jurisdiction of regulatory bodies and the government remains yet to be clearly defined in spite of many years having passed since enactment of SEBI legislation. For instance, when SEBI sought to penalise Hindustan Lever Ltd. and its officials for insider trading, the Ministry of Finance overruled SEBI. The Telecom Regulatory Authority of India (TRAI) is locked in a dispute with the government and has approached the Delhi High Court to define its role in a case of dispute between cellular operators and the government. There were also disputes regarding fixation of tariff and permitting entry of MTNL into cellular service.1 In the case of power and telecommunication sectors dereservation and approval for individual company entry preceded a number of important policy decisions leading to inordinate delays, controversies and scams.

The Indian experience tends to suggest that it is possible to create regulatory agencies but these do not perform their designated functions in a free and objective manner. The successful functioning of regulatory bodies pre-supposes a political will to perform. The cost of learning to administer regulations is high. This is especially so when the policies do not originate from within the political party in power or the government, and the timing and nature of regulations has to accommodate pressures from within and outside the country. If political leaders and the bureaucrats were in the main responsible for the problems facing the public sector, the same nexus could scuttle the functioning of regulatory institutions.

The experience of Disinvestment Commission is a pointer to this possibility. The Monopolies and Restrictive Trade Practices Commission met with a similar fate earlier.2 but the system takes a long time to change. Initial preparation may delay swift implementation of certain policies; but this still appears to be better than administering 'shock therapy' as indeed it was sought to be done for SAP. The period of transition could probably be reduced substantially.

8. OVERSTAFFING

The last two decades have seen widespread criticism of the performance of the Indian public sector and this too on many counts. One cannot brush aside the criticism as if it was always a motivated one. The criticism of the public sector in Parliament, by expert committees and by independent observers has to be taken seriously. Of the many aspects criticized, a prominent one has been with regard to overstaffing in the public enterprises. Government's response has been to put a ban on new recruitments. The general ban has its own implications.

With a certain number of employees retiring each year, the overall number of employees with the enterprises is bound to witness a decline. The ban on new recruitments has also been accompanied by a sharp decline in new investments in public sector projects. There has also been a lowering of the demand for labour within the public sector due to upgradation of technologies and replacement of labour by switching over to capital intensive and modern production systems. This is besides the impact of contractualization of certain activities in public enterprises. Production processes have three main partners, namely, the owner/manager, the worker and the consumer. There is undoubtedly a certain degree of conflict of interest between management and labour. It is true for public as well as the private sector. For a healthy and stable growth there must be better appreciation of each other's viewpoint and problems. There is a growing awareness among trade union leaders that opposition to adoption of new technologies can no more be continued without hurting their own long term interests. While discussing with a trade union leader of the State Bank of India (SBI), it was surprising to find that the leader1 himself explained that if the SBI does not adopt new technologies (e.g. computerisation) it would soon be left behind.

SBI employees, according to him, recognize that foreign banks have already entered the Indian market in an aggressive manner. They are reaching out to clients. The SBI employees can no more behave indifferently nor oppose changes within. To help strengthen such tendencies it is essential that there is continuing dialogue, communication and frank exchange of views among the management, labour and users of the services provided by the enterprises. Discussions with trade union leaders have revealed that while government and PSUs have pursued privatisation policies there has been an absence of efforts to take the labour into confidence. It is fortunate that but for the token expression of disagreement with the package of liberalization and privatisation, there has not been any violent organized opposition. There could have been unrest in the form of long drawn demonstrations or strikes. So far this has been within limits. Whatever may be the reasons, it is necessary to understand that non-involvement of labour in the ongoing changes may delay the implementation of substantive changes in the public sector.

9. CONCLUSION:

Foreign Direct Investment can play a crucial role in supporting a country's industrialization and private sector development. Privatization of public sector enterprises can serve as an important mechanism to enhance this process, not only through direct involvement of foreign investors in the privatization program itself, but also by using the privatization program as an effective advertising program to show the international investor community that the country is developing into an attractive investment location. Experience has shown that FDI inflows tend to increase rapidly in conjunction with a successful privatization program.

There certainly is no such thing as a standard model or a blueprint for creating a successful privatization program. However certain fundamental rules and principles exist which have to be observed, if privatization should serve as an effective macroeconomic tool. Foreign investors will carefully watch the government's privatization efforts in order to evaluate its sincerity to improve the business climate in the country. Public announcements and declarations in support of a reform program will not suffice. The government has to prove its commitment to open the economy to private economic activity by reducing public sector involvement. A wide ranging privatization program has to be established that is legally and institutionally equipped to efficiency and effectively transfer ownership in SOEs to private entrepreneurs. Equally important, the process has to be managed in an objective and fair manner, assuring investors that they can compete on a level paying field, free of any undue interface by the government.

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