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# Disinvestment in India is a good Strategy?

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**Disinvestment has turned out to be one of the primary tools of government in the last few decades.** The establishment of public enterprises as an instrument of the fulfilment of the economic needs of the people is not new in the modern world. Expenditure of govt in India has increased in comparison to that of its receipt. It gives us a signal of the increasing need of the govt to borrow from different sources. Many economists argued that government must not enter those areas where the private sector can undertake jobs efficiently.

## Introduction

In India, we expected that the public sector would serve as the engine of growth. The shortcomings of PSU had started manifesting in many areas. There was a growing fiscal deficit in 1985-86 onwards due to a steady increase in govt expenditure. The fiscal deficit for 2012-13 was 5.3% of GDP. India's fiscal deficit has averaged 7.7 percent of GDP in the last 35 years. In one the single year, 2007-08 did it drop below 5%.

That is quite an extraordinary record of fiscal profligacy, matched by no other nation on earth. In 2015 the deficit was 7.5% of GDP. The measures to curb the Fiscal deficit may include reducing subsidies, disinvestment, or curtail borrowing. The Current Account Deficit is lessened by increasing export and encouraging foreign investment. Disinvestment is also preferred because it is not creating the capital receipt. Disinvestment will also seek excess liquidity from the economy and will check inflation. Foreign direct investment can also help to improve current account balance and aid the PSU in enhancing efficiency.

The objective of this study is to assess whether disinvestment is a notable instrument for economic growth.

## Indian Scenario

Privatization and disinvestment mean the shrinking of the welfare state. In the budget speech of 1991-1992, the government pronounced a 20% disinvestment. The Investors' universe consists of the public sector and workers in their firms. To raise resources for extensive participants and promote greater accountability, 20% of government equity is offered to mutual funds and investment institutions in the public sector. Disinvestment is an area of economic policy with multiple objects. In the case of disinvestment, an earning asset gets converted into liquid cash.

## Why Disinvestment?

The crucial reasons offered by the government are as follows:

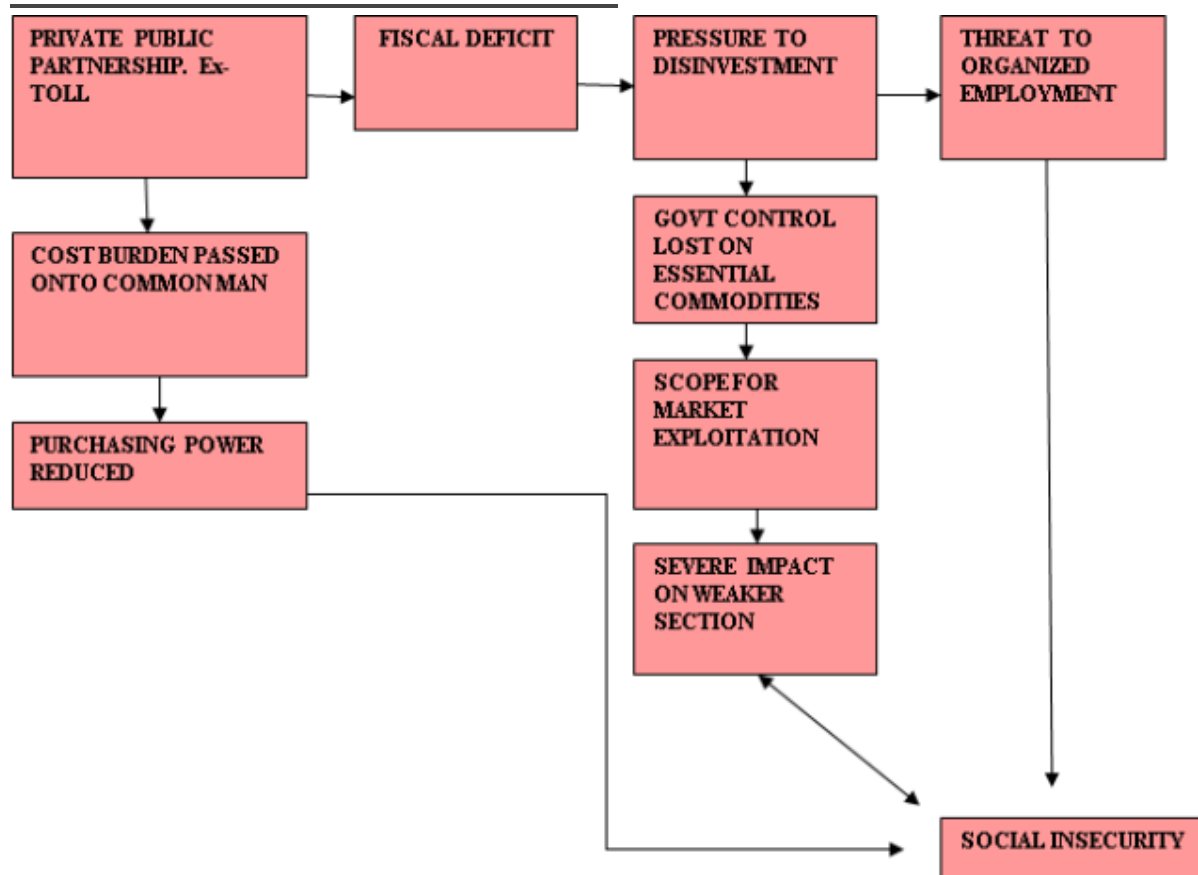
- One is to provide financial support and, the other is to improve the efficiency of the enterprise. The fiscal support argument runs as follows: Government's resources are limited. These resources should be devoted to social priorities such as health, family welfare, primary education, and social and economic infrastructure.
- More resources can be devoted, to priority areas by releasing them from nonstrategic enterprises. The demands on the governments both at the centre and in the states are increasing.
- There is a need to expand the activities of the state in priority areas. A part of the additional resources for such activity comes from the sales of shares earlier built up by the government.
- Disinvestment will improve the efficiency of working of the enterprise. Privatization of enterprise takes place. It becomes free from the control of the government and functions more efficiently. The efficiency is higher for a private sector than for a public sector unit. The extent of disinvestment is less than 50 percent so that the government can retain its control. But the induction of private ownership can have a salutary effect on the functioning of an enterprise. It increases the accountability of management.

## Approach to disinvestment

On 5 November 2009 Government took the following measures to resort to different ways:

- **INITIAL PUBLIC OFFERING AND STRATEGIC SALE:** privatization refers to a change in the ownership of public sector or government-run enterprises to private industries. Such transfer of ownership may be partial or complete. Government transfers ownership by offering the shares of public sector undertaking to retail investors and institutions. It is known as an initial public offering. Another method is called a strategic sale, in which public sector undertaking is passed to private partners.
- **GOLDEN SHARES:** In this process, the government retains a 26% share in PSU. The government's past disinvestment retains a minority stake in the company in its sales to the shareholder.
- **WAREHOUSING:** under this model, the government-owned financial institution take over the
  - Govt shares in selected PSU and holding them until a third party emerges
  - **STRATEGIC SALE:** Under this, the government may sell a majority of the stake to the shareholder and pass ownership under private management.
  - **CROSS HOLDING:** Here, the government will pass out the share of one PSU.

## Effect of fiscal deficit



All means of borrowing and revenue generation prove inadequate to wipe out the fiscal deficit. Disinvestment is the best option – sell valuable assets such as public sector units. Vast industrial assets created out of the hard-earned money of three generations of taxpayers are sold to the private sector. As a result, government control got lost on the pricing of several essential commodities such as oil, medicines. It has a direct impact on the purchasing power of weaker sections of society.

Downsizing of Manpower is another aspect of disinvestment. It is a threat to organized employment. Finally, the combination of a fiscal deficit and pressing need for investment in infrastructure has led to the birth of public-private partnerships. In simple words, it is nothing but the government using its power to allow private companies to build infrastructure with profits from the general public.

## Effects of disinvestment

### *A statistical framework*

If one examines the achievement of the PSEs by the yardsticks they expected to achieve, one would observe that many of these objectives have at best met with limited success. The returns earned by the public sector were significantly lower than the rate of returns for a time deposit. Hence, we shall make a comparative study and a statistical analysis.

## *Disinvestment and stock market*

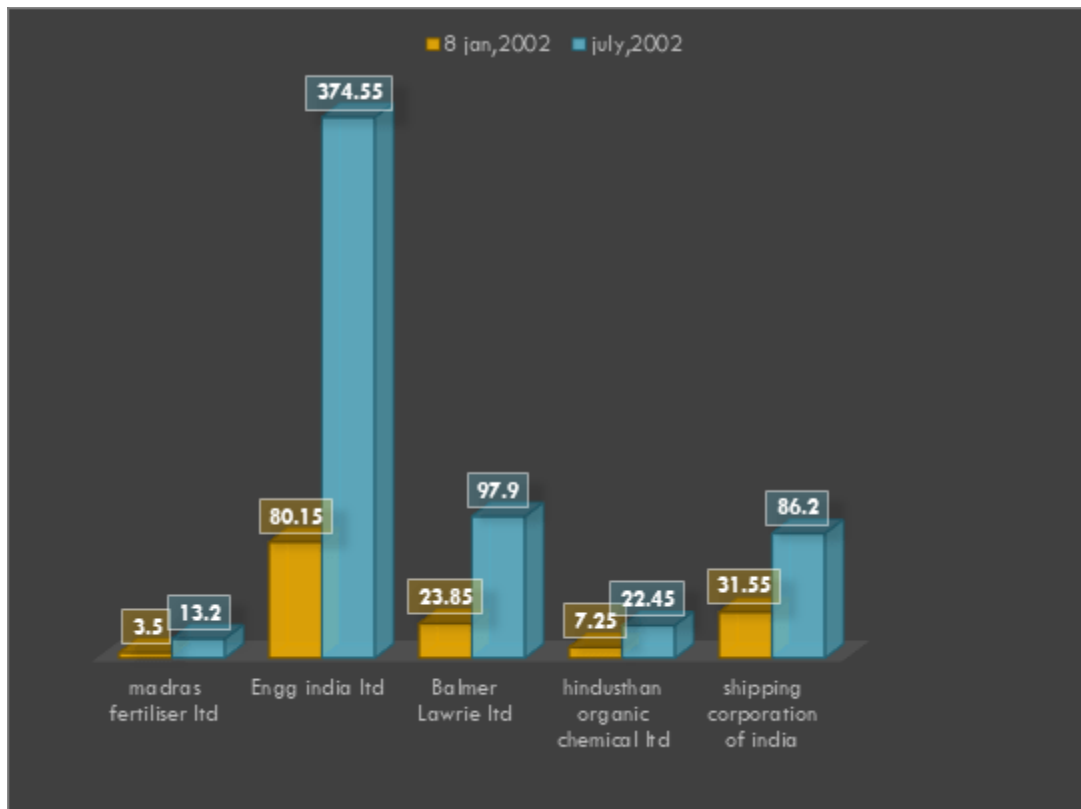
Bombay stock exchange has established a PSU index comprising 34 listed public sector undertakings. The PSU under disinvestment has also shown a particular increase in their share prices during this period. In contrast, the companies in which disinvestment decision was deferred show specifically high percent of the decline in their prices.

<b>Company name</b>	<b>Share price on 8 jan,2002</b>	<b>Share price on July 15,02</b>	<b>% increase during this period</b>
Madras fertiliser ltd	3.5	13.20	277
Engg India ltd	80.15	374.55	364
Balmer Lawrie ltd	23.85	97.90	310
Hindustan Organics Chemicals Ltd	7.25	22.45	209
Shipping Corp. Of India	31.55	86.20	173
Hindustan Machine Tools	4.50	28.40	531
Total	150.80	622.70	313

### **Change in price of shares**

**Source: BSE 2003**

Now we shall graphically represent such a study.

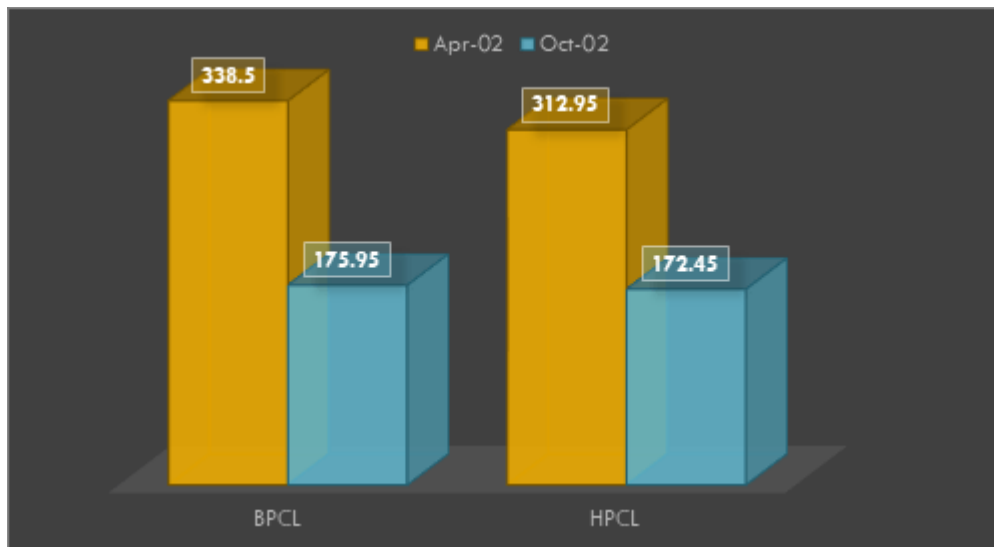


Bar diagram showing changes in the price of shares before and after disinvestment

Now we shall show the prices of shares in companies in which disinvestment decision was deferred and observed that they experience a high percentage decline in the price of shares.

Company name	Price on 01/04/02 ( Rs per share)	Prices on 1/10/02
BPCL	338.5	175.95
HPCL	312.95	172.45

**PRICES OF SHARES IN CASE OF DEFERRED DISINVESTMENT**  
Source: BSE (2003)



BAR DIAGRAM SHOWING PRICES OF SHARES IN CASE OF DEFERRED DISINVESTMENT

## Analysis

Disinvestment brought an extremely positive change for the Indian share market. The share prices of different PSUs increased at a high rate. Madras fertilizer ltd share price increased at the rate of 277%. Hindustan machine tools share prices surged at a rate of 531. As a whole, the share prices of all the disinvested industries increased at the rate of 313%. This increase in share prices will further induce investment. But if we see the companies in which disinvestment kept deferred, the share prices have fallen. In the case of BPCL, the share prices before disinvestment were 338.5 it fell to 175.95. HPCL share prices fell from 312.95 to 172.45.

## Actual vs total receipt from disinvestment

Other than Modern Food Industries (India) limited, only minority stakes in different PSEs were sold before the year ending March 2000. The government has since modified its policy to emphasize strategic sales. The disadvantages of the sale of minority stakes by the government are as follows:

- Control is not transferred because of lower realization.
- The government gets left with limited stakes after minority sales. It depresses the possibility of higher realizations from the strategic partner, especially since the latter has to offer the same price to other shareholders also through an open offer.
- The minority sales also give a wrong impression that the main objective is to obtain funds for reducing the fiscal deficit of modern food industries as if it is not concerned about other industries.

The given table focuses upon the actual and total receipt received from 1991 till now:

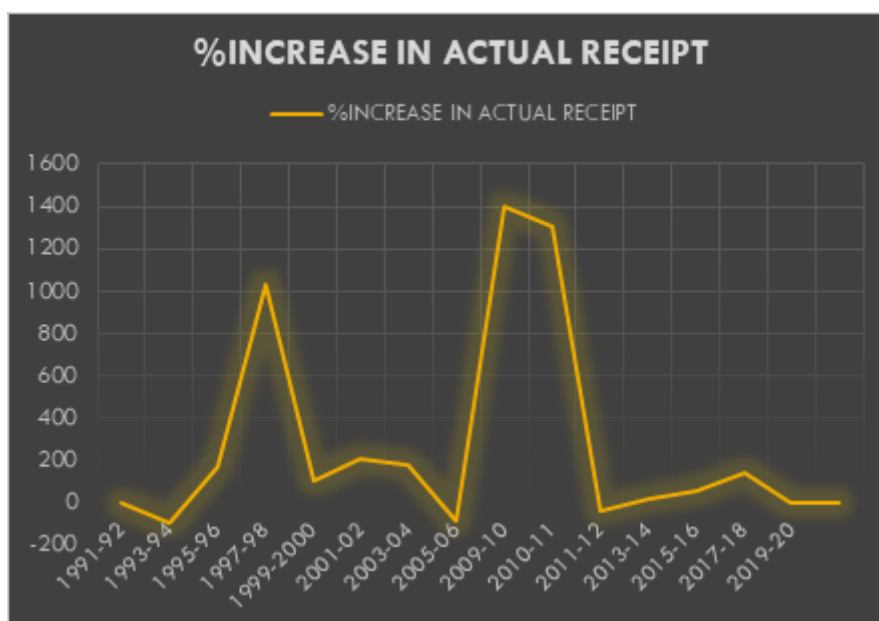
YEAR	TARGET RECEIPT (in crore)	ACTUAL RECEIPT (in crore)	% increase in actual receipt	Actual- target receipt
1991-92	2500	3037.34	—	537.34
1993-94	3500	0	-100	-3500
1995-96	7000	168.48	168.5	-6831.5
1997-98	4800	910	1033	-3890
1999-2000	10000	1860.14	104	-8139.86
2001-02	10000	5657.69	204	-4342.31
2003-04	14500	15547.41	174.8	1047.41
2005-06	No target fixed	1569.68	-89	—
2009-10	25000	23553	1400	—
2010-11	40000	22144.21	1310	-17855.79
2011-12	40000	13894.05	-37	-26105.95
2013-14	40000	15819.46	14	-24180.54
2015-16	69500	23996.80	51.7	-45503.2



2017-18	72500	57273.05	139	-15226.95
2019-20	105000	16213.38	-71.7	-88786.62

**TARGET VS ACTUAL RECEIPT YEAR**

Source: dipam.gov.in



**LINE DIAGRAM SHOWING % INCREASE IN ACTUAL RECEIPT**

There is a wide gap between actual disinvestment and target disinvestment. During 1995-96 to 2002-03, the govt could not achieve the desired target. Due to the hasty undertaking of disinvestment policy and lack of coordination, there was considerably lacking behind the target. It is seen in the above data presentation that except for the years 1991-92 and 2003-04 there has been no positive outcome. In 2009-10 against a target of Rs, 25000crores government could achieve Rs 23553 crores. However, the % increase in the actual receipt is almost positive except 1993-94, 2005-06. In 2011-12 actual receipt fluctuated at the rate of -100%, -89%, and -37% respectively.

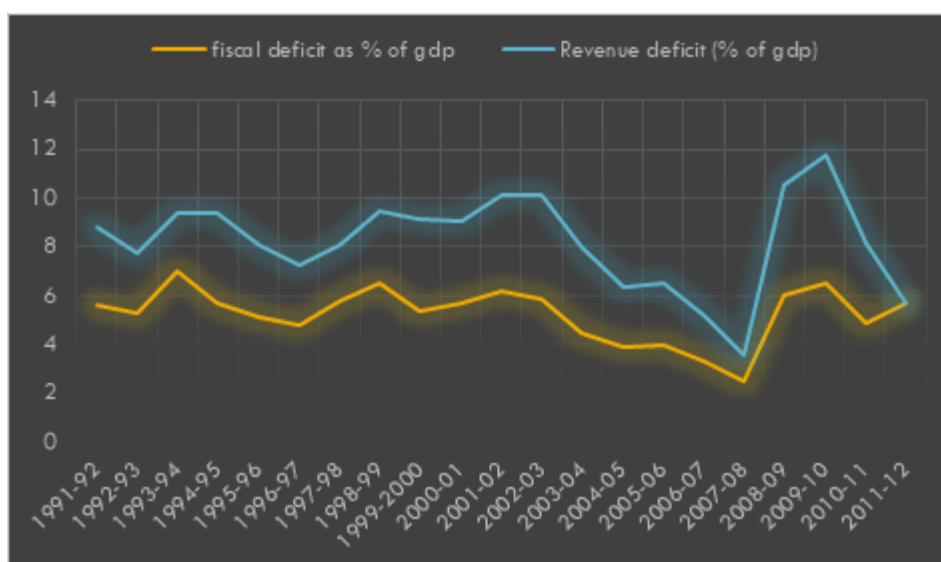
YEAR	GDP AT MARKET PRICE (base year- 1998)	FISCAL DEFICIT AS % OF GDP	REVENUE DEFICIT (% OF GDP)
1991-92	6738.75	5.6	3.17
1992-93	7745.45	5.3	2.41

1993-94	8913.55	7	2.4
1994-95	10455.90	5.7	3.67
1995-96	12267.25	5.1	2.97
1996-97	14192.77	4.8	2.42
1997-98	15723.94	5.8	2.3
1998-99	18033.76	6.5	2.95
1999-2000	20231.30	5.4	3.71
2000-01	21774.13	5.7	3.34
2001-02	23558.45	6.2	3.91
2002-03	25363.27	5.9	4.25
2003-04	28415.03	4.5	3.46
2004-05	32422.09	3.9	2.42
2005-06	36933.69	4	2.5
2006-07	42947.06	3.3	1.87
2007-08	49870.90	2.5	1.05

2008-09	56300.63	6	4.5
2009-10	64778.27	6.5	5.23
2010-11	77841.15	4.9	3.24
2011-12	90097.22	5.7	4.46

### TREND IN FISCAL DEFICIT

SOURCE: dipam.gov.in



### LINE DIAGRAM SHOWING % CHANGE IN FISCAL DEFICIT

The disinvestment policy had a comparatively significant impact on the fiscal deficit of our country. This had a twin effect, firstly it leads to a decline in capital expenditure and an increase in capital receipt. As a percentage of GDP, the revenue deficit fell from 2.41% in 1991-92 to 2.3% in 1996-97. Falling capital requirements and rising capital flow caused the gap between fiscal and revenue deficits to narrow down.

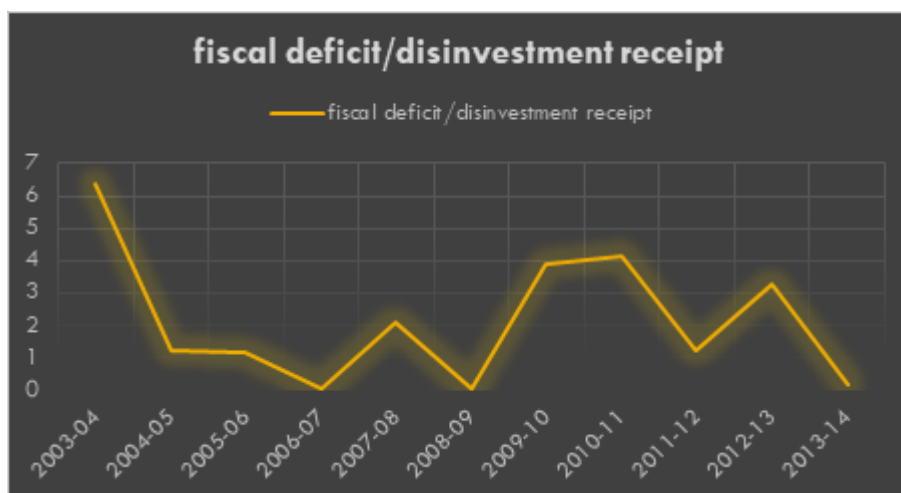
A high 5.6% in 1990-91 to 5.3% in 1991-92 and the downward trend continued till 1996-97 when the fiscal deficit stood at 4.8%. From 1997-98 the fiscal deficit started to rise again and, it stood up to 2001-02. In this period, there was an immense rise in public debt involving large interest payments. The government took a renewed effort to decrease the fiscal deficit by .5% GDP, a result Fiscal deficit and revenue deficit again started to decline.

## Association between fiscal deficit and disinvestment

Year	Disinvestment receipt	Fiscal deficit	Col 2/3*100
2003-04	15547.41	243904	6.37
2004-05	2764.87	233568	1.18
2005-06	1569.68	236519	1.17
2006-07	0	220081	0
2007-08	4181.39	202367	2.07
2008-09	0	471581	0
2009-2010	23552.93	607301	3.88
2010-11	22144.21	535053	4.14
2011-12	13894.05	723865	1.91
2012-13	23956.06	736191	3.25
2013-14	831.27	542499	0.15

Data showing the ratio of disinvestment receipt and fiscal receipt

Source: a handbook on statistics( 2009) Mumbai & Disinvestment manual (2003)



line diagram showing a gradual decline of fiscal deficit

With the tax collection likely to be a shortfall from the target, disinvestment is the key to keep the fiscal deficit under control. As the rate of Fiscal deficit gradually increased government gradually increased the disinvestment rate to achieve the target fixed. Though there were many shortfalls from the target there was an insistent rise in the actual receipt observed from the previous table. The (disinvestment receipt/ fiscal deficit) ratio was very high initially, the rate being about 6.37 in 2003-04. As the Fiscal deficit increased further from 243904 to 607301 in 2009-10 the amount of disinvestment receipt also increased from 15547.41 in 2003-04 to 23552.93 in 2009-10 to cover up the gap. Thereby the rate of the gap is found to fall from a high rate from 6.37% to 0.15%. So, disinvestment is a key to reduce the rising fiscal gap in the future.

## Effect of disinvestment upon employment

A comparative study between private and public sector:

year	GOI	State government	Local bodies	Quasi government	Private sector	total
1981	3.1	5.8	2	4.6	7.4	22.9
1990	3.4	7	2.2	6.2	7.6	26.4
1991	3.4	7.1	2.3	6.2	7.7	26.6
1992	3.4	7.2	2.2	6.4	7.8	27

<b>1993</b>	<b>3.4</b>	<b>7.3</b>	<b>2.2</b>	<b>6.5</b>	<b>7.9</b>	<b>27.3</b>
<b>1994</b>	<b>3.4</b>	<b>7.3</b>	<b>2.1</b>	<b>6.5</b>	<b>7.9</b>	<b>27.2</b>
<b>1995</b>	<b>3.4</b>	<b>7.4</b>	<b>2.2</b>	<b>6.5</b>	<b>8.1</b>	<b>27.6</b>
<b>1996</b>	<b>3.3</b>	<b>7.4</b>	<b>2.2</b>	<b>6.5</b>	<b>8.5</b>	<b>27.9</b>
<b>1997</b>	<b>3.3</b>	<b>7.5</b>	<b>2.2</b>	<b>6.5</b>	<b>8.7</b>	<b>28.2</b>
<b>1998</b>	<b>3.2</b>	<b>7.5</b>	<b>2.2</b>	<b>6.5</b>	<b>8.7</b>	<b>28.1</b>
<b>1999</b>	<b>3.3</b>	<b>7.5</b>	<b>2.3</b>	<b>6.4</b>	<b>8.7</b>	<b>28.2</b>
<b>2000</b>	<b>3.3</b>	<b>7.5</b>	<b>2.3</b>	<b>6.3</b>	<b>8.6</b>	<b>28</b>
<b>2001</b>	<b>3.3</b>	<b>7.4</b>	<b>2.3</b>	<b>6.2</b>	<b>8.7</b>	<b>28</b>

## EMPLOYMENT IN ORGANISED SECTOR (in millions)

Source Economic survey (2002-03)



## BAR DIAGRAM SHOWING UPWARD TREND IN EMPLOYMENT

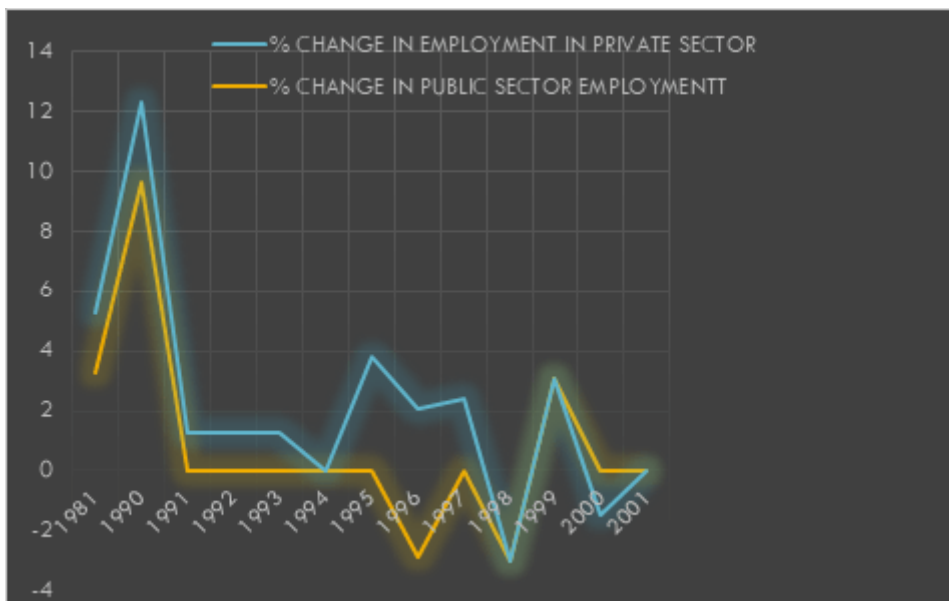
The table above illustrates that employment levels were stagnant in the 1990s. Of the 1.6 million jobs newly created two-third of employment increased in the private sector from 1991 to 2001. It indicates that the private sector has become the substantial source of increments in the organized sector of the economy.

It is observed from the above table that employment in the public sector is more or less stagnant at 3.4. In the years 1996, 1997, and 1998 the rate even fluctuated further to 3.2. but, on the other hand, the private sector kept pace in providing employment. Private-sector employment gradually increased from 7.4 in 1981 to 8.7 in 2001. There is consequently a shift of workers from the public to the private sector. According to some critics, it is a movement from safe to an unsafe status.

YEAR	% CHANGE IN PUBLIC SECTOR	% CHANGE IN PRIVATE SECTOR
1981	3.3	2
1990	9.6	2.7
1991	0	1.3
1992	0	1.3
1993	0	1.3
1994	0	0
1995	0	3.8
1996	-2.9	5
1997	0	2.4
1998	-3.03	0

1999	3.1	0
2000	0	-1.5
2001	0	1.16

### PERCENTAGE CHANGE IN EMPLOYMENT IN PRIVATE AND PUBLIC SECTOR



### LINE DIAGRAM SHOWING % CHANGE IN EMPLOYMENT IN PRIVATE AND PUBLIC SECTOR

Public sector being the engine of growth of our economy before disinvestment accounted for the maximum employment. After disinvestment in PSUs, the employment growth in this sector for the year 1991-1995 and 2000 and 2001 has been nil. Even the rate of growth has become negative in the year 1996 and 1998. But private-sector performance is relatively better employment change has been almost positive, stagnant in 1994, 1998 and 1999 but never negative except in 2000. There has been a decline in employment level(-1.5 %) but again increasing in the subsequent year. But according to some critics, the growth that has happened is jobless.

## Conclusion

Disinvestment is a process. The disinvestment process needs to be taken more seriously by the government. Government should try to come out with a time-bound program to conduct the process with transparency. Disinvestment is a necessary instrument for economic growth in our future and for bridging the gap in our economy. The above study made us conclude that disinvestment leads to economic growth.



The resources initially blocked in nonstrategic PSUs can be used in efficient ways. It is the key to mitigating the problem of fiscal deficit and, it also can lead to an increase in the employment level but it should be kept in mind that such growth must not be jobless growth and, the mechanism of the capital market must be also taken into account so that crowding out doesn't take place. Change in ownership at the microeconomic level is not sufficient to guarantee greater enterprise efficiency. Then other reforms, more directly related to enterprise development, may indeed play a crucial role. If the success of privatization is linked to competition and the regulation of competition then weaknesses in these fields may explain why privatization is negatively related to economic growth in developing countries.