Role of Privatisation in the Economic Development of India: Opportunities and Challenges

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Abstract:

Privatisation refers to transfer of ownership and/or management of an enterprise from the public sector to the private sector.Privatisation is associated with better results in terms of cost and quality of services. It achieves these results by replacing government monopolies with the competitive pressures of the marketplace to encourage efficiency, quality & innovation in the delivery of goods & services.The study aims to discuss opportunities as well as challenges that may occur as a result ofprivatisation. It further intends to analyse the impact of privatisation on the economic developmentof India.The study concludes that privatization is required for rapid growth in economy. It has been noticed that government is focusing on maintaining law and order in the country and also taking care of national security seriously. Doing business profitably has been left for the private sector, therefore, it can be said that future belongs to privatization.

Keywords: Privatisation, Economic Development, Opportunities, Challenges and Efficiency

I. INTRODUCTION:

Privatisation refers to transfer of ownership and/or management of an enterprise from the public sector to the private sector.It also means the withdrawal of the State from an industry or sector, partially or fully.Another dimension of privatisation is opening up of an industry that has been reserved for the public sector, to the private sector.

But in general terms, ***Privatisation is understood to be a process whereby activities or enterprises that were once performed or operated by the Government and its employees are now transferred, managed, or owned by private business and individuals.***

Prof. D.R. Pendse states that"Privatisation is a process that reduces the involvement of the state or the public sector in the nation's economic activities. Government role is reduced, as it does not disappear"

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History:

The process was started by Margaret Thatcher when she became the Prime Minister of Great Britain around 1980.It was actually a reaction to the indiscriminate expansion of the public sector and the associated problems. Further, it become an integral part of economic reforms an many countries all over the world.

Over the years, various developed and developing countries, alongwith communist countries, have been carrying out privatisation in varying forms, degrees and measures of success.

Privatisation in India:

In India, although there were some isolated cases of privatisation, no definite policy decision was taken, until the new economic policy was introduced in 1991.

In our country, the public sector has expanded greatly over the years. Due to populist political appeal and vested interests of politicians and bureaucrats, public corporations were set up in large numbers.

The accumulated losses of many Public Sector Undertakings (PSUs) were more than the capital invested in them. So, the government had to increase taxation and curtail development expenditure for overcoming public sector deficits.

Thus, privatisation of certain sectors & enterprises became necessary to reduce the budgetary burden on the public; to make available more resources for the development activities; to enable the government to concentrate more on the essential governmental functions and priority areas and to relieve the consumers from the indifferent and arrogant attitude of the public sector.

In India, the process of privatisation began in 1991-92 with sale of minority stakes in some PSUs. The disinvestment Commission was set up by Government of India in August, 1996 for giving suggestions and for undertaking disinvestment of equities for select PSUs. From 1999-2000, the forcus shifted towards strategic sales.

The Disinvestment Commission recommended disinvestment at varying levels for a no. of PSUs like NALCO, MTNL, GAIL, ET & T etc.Strategic sales in various proportions werealso recommended for many enterprises like BALCO, ITDC, IBP, NEPA, PPCL, IPCL, SAIL etc.For several enterprises like ONGC, OIL, RITES, NTPC, NHPC etc, the Commission advocated no further disinvestment under the present circumstances. Out of these, various PSUs like BALCO, VSNL, IPCL, Maruti Udyog Ltd, Hindustan Zine Ltd, ITDC etc. have already been privatized.

Privatisation was at the peak during NDA Govt., but it came to a halt with the coming of UPA Govt. in power at the centre. This government is supported by 'left'parties which are against privatisation of profit-making PSUs. Now the new government has closed the Ministry of Disinvestment and converted it into a department. Under Ministry of Finance, Common Minimum Programme has made it clear that:

1. Profit making PSU will not be privatized;
2. The government identified 11 PSUs 'Navratnas', but out of these, 2 namely IPCL & VSNL are already privatized; so now the remaining 9 'Navratnas' PSUs will be kept in public sector.
3. Proposal of privatisation of loss-making PSUs will go through consultation with the workers.

4. Privatisation will not be done if it creates monopoly or restricts competition.

II. PURPOSE OF THE STUDY:

The purpose of the research is to analyse the concept of privatization critically.It further aims to discuss opportunities as well as challenges that may occur as a result ofprivatisation.The study intends to analyse the impact of privatisation on the economic developmentofIndia.

III. REVIEW OF LITERATURE:

Estrin, Hanousek, Kocenda, and Svejnar (2009) in their research entitled "The Effects of Privatisation and Ownership in Transition Economies" had examined the impact of privatisation on efficiency, profitability, revenues and other indicators. The evidence assembled in this studysuggests that privatisation and performance are related but that the relationship is morecomplicated than has been assumed.It was analysed thatprivatisationalonedoes not guarantee improved performance, at least not in the short- to medium-run. Type of private ownership, corporate governance, access to know-how and markets, and the legal and institutional system matter for firm restructuring and performance. Foreign ownership tends to have a positive effect on performance. The positive effect of privatisation to domestic owners, to the extent that it exists, takes a number of years to materialize.

Adams (2007) in his thesis entitled "The Impact of Privatisation on Economic Growth and Income Inequality in Developing Countries" examined the impact of privatisation on economic growth and income inequality in various regions of the developing world between 1991 and 2002. The study finds that privatisation did not play a significant role in promoting economic growth and reducing income inequalities in developing countries. The results of the study, however, indicate that country conditions including good governance infrastructure is more likely to promote growth and contribute to a reduction in income inequality, which suggests that country-specific characteristics may be more important in promoting growth and reducing income inequality than any economic policy per se.

Filipovic (2006) in his research entitled "Impact of Privatisation on Economic Growth", had suggested that incentives play a significant role in the potential success of privatisation as a factor of economic growth. In fact, privatisation, accompanied by appropriate structural reforms, creates incentives to improve economic efficiency, increase investment, and adopt new technologies. Furthermore, the methods of implementing privatisation play an important role in creating the right incentives and leading the way for the appropriate economic restructuring. It is essential to note that the success of privatisation largely depends on the government commitment to legal and regulatory reforms.

Cook and Uchida (2001)in their study entitled "Privatisationand Economic Growth in Developing Countries", have analysed that there is a robust partial correlation between privatisation and economic growth, suggesting that privatisation has contributed negatively to economic growth. If the change in ownership alone 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.

Megginson and Netter (2000) in their study entitled "From State to Market: A Survey of Empirical Studies on Privatisation" had supported that the proposition that privately owned firms are more efficient and more profitable than otherwise-comparable state-owned firms. The benefits which can be gathered out of privatisation involve that the private firms can become more efficient, more profitable, can increase their capital investment spending, and become financially healthier.

IV. OBJECTIVES OF PRIVATISATION:

The objectives of Privatisationare as follows:

1. To improve the performance of Public Sector Undertakings (PSUs), so as toreduce the financial burden on taxpayers.
2. To make more financial resources available to the government for its development activities, and to bridge its fiscal deficit.
3. To reduce the size of administrative machinery.
4. To enable the government to concentrate more on the essential state functions.

5. To reduce government interference in the economy and promote greater private initiative and entrepreneurship.
6. To promote wider share ownership among a number of workers & common man.
7. To accelerate the pace of economic development, as it attracts more resources from the private sector for development.
8. To promote competition and reward efficiency.
9. To reduce the burden of public debts.
10. To increase efficiency of Industries
11. To provide benefits to consumers.

V. METHODS OF PRIVATISATION:

The Privatisation can be done in many ways by adopting any one or more of the following methods:

1. Auction:

When government organizes sale to invite government owned bids for small commercial and service businesses or nationalized property, it is called auction.

2. Direct Sale:

When a public undertaking is transferred to private ownership through direct sale to a private investor, it is called direct sale.

3. Stock Offers:

This is a public sale of shares of PSUs through stock exchange or private offers to investment groups. This method has been adopted in our country several times. Here, some shareholdingsremain with the government.

4. Liquidation:

This refers to legal abolition of a PSU so that the plant, equipment and other assets can be sold. It is a method of disposing off the assets of unprofitable or uncompetitive state enterprises that cannot be restructured or sold through ant other means.

5. Takeoverby Employees or Management:

When whole or part of an enterprise is sold to its workers, managers or a combination of both, it may be called privatisation through workers participation in management. In India, this method was much talked about but due to lack of resources with workers, it could not be followed meaningfully.

6. Public Distribution of Shares:

Public distribution of shares is done to widely spread the ownership in private hands so that one group or a few individuals and many not control the privatized company. Holding of the government becomes less than half.

7. Denationalisation:

Denationalisation is the process of transferring an asset from public ownership, specifically ownership by a national government, to private ownership and operation. Where the ownership of a public enterprise is transferred to private sector, it is known as denationalisation.

8.Franchising:

Under a franchise agreement, the government gives a special monopoly privilege to a private firm to produce and supply some part of a particular service. The government either makes a contract with a single private firm or several firms to produce and supply the goods and services.

9.Divestiture:

Divestiture means selling a stake in a company, subsidiary or other investments. Governments often sell stakes in public sector companies to raise revenues. Privatisation has come through divestiture in many countries, including India.

10.Leasing:

Another method of privatisation is called "leasing", which is similar to the franchising and contracting-out method in the sense that both the management and operation are transferred to the private sector.

11. Joint Venture:

Joint venture refers to the joint/ combined ownership of Government and private players. It involves sharing of risks and benefits among the two. There are many projects which are run in Public Private Partnership Mode. It is also called PPP Model, in which fixed assets are owned by the Government, but management is private.

12.Reconstruction:

Reconstruction is a process of the company's reorganization, concerning legal, operational, ownership and other structures, by revaluing assets and reassessing the liabilities. Privatisation through reconstruction refers to transfer of public company to private ownership.

VI. OPPORTUNITIESARISING OUT OF PRIVATISATION:

Privatisation brings many opportunities, which can never be overlooked. Private sector is known for its better quality of goods and services at competitive price.The following are some of the potential opportunities that may arise out of privatisation:

1. Incentive for greater efficiency and hard work:

Privatisation inspires both the entrepreneurs and workers to become more efficient and to do more work. The entrepreneurs try to get maximum work to earn maximum profit and workers try to achieve maximum efficiency in order to get more remuneration.

2. Increase in Productivity and Production:

The entrepreneurs try to get maximum work to get maximum profit and workers try to achieve maximum efficiency for more remuneration.

As both the entrepreneurs and workers try to work with greatest efficiency, the result is that the productivity of all the resources of production increases considerably. As a result, the production of these enterprises increases. It accelerates the pace of economic development.

3. Efficient Utilization of Resources:

All the resources of production are used most economically. No part of these resources is allowed to waste. All the best efforts are made to utilize these resources to their maximum extent. It results in minimum cost of production. Producers under private sector are always concerned for minimization of wastage, which leads to minimization of cost.

4. Incentives to take Risk and bear Uncertainty:

Privatisation provides due incentives to undertake enterprises and to bear risk. Entrepreneurs introduce new innovations and this leads to progress in the long run.It is said that profit is a reward for bearing risk and uncertainty. It seems to be true as regard to privatization.

5. Higher Rate of Capital Formation:

Private entrepreneurs try to save a major part of their income to reinvest in their business to earn more income in future and employees who earn more now are also able to save more, all this leads to higher rate of capital formation. They keep using the concept of ploughing back of profits.

6. Economic Growth and Affluence:

This is the greatest success of privatisation that it promotes rapid economic growth. Those countries that have adopted privatization have experienced better economic growth, which also proves to be true in case of India.

7. Minimum Cost of Production:

As there is maximum and most efficient utilization of resources, it results in minimum cost of production. As a result consumers, customers get good quality goods at reasonable prices.

8. Free and Fair Competition:

Privatisation results in free and fair competition among producers and sellers, which is very important for economic progress of a country. For e.g. BSNL, IDEA, HUTCH, AIRTEL.

9. Reduction in the burden of Government in budget:

It reduces the burden of Government. As a result of privatisation, burden of loss-making PSUs, on the government is reduced, so the government can invest its resources in high priority areas.

As a result of healthy competition, public sector enterprises strive to perform well, modernize themselves and eventually make profits. It makes the remaining unprivatisedpublic sector units more competitive.

10. Increase in turnover:

Privatisation can result in increased turnover due to efficient performance of private stakeholders. It helps improve quality and efficiency in the organisation.

11. It enables the government to concentrate more on essential state functions:

As privatisation involves transfer of ownership to private players by the Government, the government is relieved to focus on more essential state functions, which cannot be performed by the others. The Governments are in a state to perform their duties and responsibilities in a more efficient manner.

12. Encourages entrepreneurship:

Privatisation enables the encouragement of entrepreneurship among the private players, as they get an opportunity to prove themselves in the field of business as well. They are able to show their talent, creativity and management ability as they get control to run the whole business organisation.

13. Better management:

Privatisation, no doubt, brings improvement in managing the organisation, as it gives control and opportunity to the private players to use their capability to run the business enterprises. Giving the control to the capable ones would definitely improve quality and efficiency in the management of the enterprise.

VII. CHALLENGESARISING DUE TO PRIVATISATION:

There are many challenges, which are associated with the implementation of privatization in India. Indian economy is a developing economy, where poverty can be seen in a large group of population. Their welfare is the responsibility of the government.Private sector can never provide welfare to poor people, as their main motive is profit earning. Our independence is not very old. We cannot forget the rule of English people, who have squeezed the economic potential of the country and spoiled our education system. Implementation of privatization is always challenging in India.The following are some of the potential challenges that may arise due to privatisation:

1. Social Welfare is Ignored:

Privatised Enterprises are working only for profit motive, so they produce and provide only those goods and services which provide higher profits to them. Needs and desires of people having lower paying capacity are ignored. Moreover, balanced regional development is ignored. This is against the social goals of business.

2. Wastage of Resources due to Competition:

As a result of privatisation, a large amount of financial resources are wasted on competitive advertising as firms spend huge amounts on advertising to face stiff competition. It is a sheer wastage of resources which could be used profitably in productive areas. Burden of advertisement is ultimately borne by the consumer.So, the consumers end up paying higher prices and productive resources are not utilized in efficient and judicious manner.

3. Economic Instability:

Private sector causes economic instability, as because of free market mechanism, there may be depression or inflation at any point of time, which leads to fluctuation in the market. There are ups and downs in the business. Business is affected by external business environment. There are always threats along with opportunities

4. Class Struggle:

Privatisation increases and promotes class struggle. The society is divided into two classes of people, i.e., the rich people and the poor people.Their interests always clash with each other and this gap goes on increasing. Products are promoted in such a way that they belong to rich class of people. It gives a discrimination in the mind of medium or poor class.

5. Concentration of Income and Wealth:

Privatisation encourages concentration of income and wealth in the hands of few persons. Rich become richer and the poor become poorer. Those who have a strong financial family background or ancestral wealth, they are multiplying their wealth with leaps and bounds. They have more opportunities of becoming richer than before.

6. Concept of Free Competition is a Myth:

Free competition which is meant to be an advantage of privatisation is not practical in real world. Oligopoly and Monopoly results & competition declines. So, the consumers end by paying higher. Prices and productive resources are not utilized in efficient and judicious manner.

7. Does not Ensure Economic Development:

Privatisation does not ensure economic development as private sector does not consider it as their responsibility. They do not take interest in development of basic infrastructural facilities, basic and key industries and social activities.

8. Threat of Monopoly:

Free competition which is meant to be an advantage of privatisation is not practical in real world. Privatisation sometimes gives birth to monopoly and unfair competition.

9. Economic Development is not the responsibility of the Private Sector:

Privatisation does not ensure economic development as private sector does not consider it as their responsibility. They do not take interest in development of basic infrastructural facilities. Private sector demands presence of infrastructure facilities from the government, so that they can run their industries smoothly. Development of infrastructure is a task which is left for the government. Such development enhances the gap of fiscal deficits.

10. Lack of social responsibility:

It is seen that private sector does not show interest in corporate social responsibility due to their profit motive. To overcome this problem, government of India in Companies Act, 2013 made spendings in CSR activities mandatory for specified companies.

VIII. CONCLUSION:

In India, government offices are an alternative expression to corrupt systems and officials. At the same time, we have seen the private sector growing leaps and bounds, all these years. This leads to a belief that privatization can reduce corruption to a large extent and it can enhance the efficiency and quality.Privatization can be the means to one thing but may trigger multiple other impacts. There is no guarantee that privatization in India will reduce corruption and operate successfully in favour of Indian citizens. Corruption is not correlated to being a private or public sector, it is about the individual’s attitude. Tax evasion is a big example of corruption found in the private sector. Privatization of the Indian economy will impact us in both ways, positively and negatively.We need to find a way to implement it in the best way.

Privatisation has both quantifiable and non-quantifiable long-term consequences. Privatization may be successful or can fail as well depending on many attributable factors. Talking about India there is so much political interference on the economy and its policy. Privatization steers the companies in the right direction by increasing good competition in the market. If driven right, privatization pushes efficiency and performance.

Public and private sectors are not opponents.The key to economic development of a developing country like India lies in the co-existence of both the sectors.Public sector should take up the responsibility of development of basic and heavy industries exclusively and private sector should manage consumer goods industries.

A blind process of privatisation should not be followed by the Government. Only sick or loss making PSUs should be privatized and that too only when they can’t be revived by the Government.Under the political pressure and threat of trade unions, now the government has slowed down the process of privatisation and hopefully, in future it will stick to its declarations of not privatizing profit making PSUs and its Navratnas and be cautious in the process of privatisation in India.

Considering the entire scenario, it can be concluded that privatization is required for rapid growth in economy. It has been noticed that government is focusing on maintaining law and order in the country and also taking care of national security seriously. Doing business profitably has been left for the private sector, therefore, it can be said that future belongs to privatization.

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