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Privatisation and Public Regulation: The Indian Experience by Simrit Kaur, Macmillan India Ltd., New Delhi, 2003, Page 276, Price Rs. 385

The first four decades since independence witnessed an impressive growth of Public Sector Enterprises (PSEs) as they were envisaged as a matter of policy to assume the 'commanding heights' of the economy. The generally poor performance of PSEs in relation to expected goals radically altered the perceptions about the role of PSEs in the last decade and a half, and a persistently weak fiscal position brought to the fore the need for reforming the PSEs. Privatisation aimed at enhancing competition and efficiency figured prominently in the initiatives launched to reform PSEs - a trend that is commonly observed now in many developing countries. But is the private sector a complete paragon of virtue? If yes, what should be the modality for privatisation? And what role should Government play in such a scenario? These are the issues, which have been extensively debated both at the national and international levels. Though the efficacy of privatisation is still being debated at the theoretical levels, there is a growing consensus in favour of privatisation among policy makers. The present book essentially reviews this debate, further reaffirms the broad consensus and analyses the various divesture and non-divesture options for privatisation.

Listing out the usual cases of market and non-market/ Government failures, the author contends that the issue is not to choose between Government and the market, but to explore the effective combination of the two, that would be economically and socially desirable. In this context, the author has emphasised the need for the State to reduce its role as a producer of goods and services and to expand its role as a regulator, facilitator and provider of welfare services and merit goods. The author further underscores the need to reform the PSEs either *via* privatisation or effective public regulation. Privatisation can take the form of: (a) Ownership transfer, where by the assets are privatised, fully or partially *via* disinvestment, (b) Management transfer, where by the assets are either subcontracted, leased or franchised or (c) Marketisation (Greenfield Privatisation), where by private sector participation is encouraged in areas, hitherto reserved for public sector. Public regulation, on the other hand, tries to privatise the 'public style of management' by enforcing performance contracts. Besides analysing the operation of each of these modes in the Indian context, the author has also empirically examined the relationship between (a) ownership and efficiency, (b) competition and efficiency and (c) Memorandum of Understanding (MoU) signed between the Government and the management of the PSEs and its associated impact on the performance of PSEs.

Assessing the performance of public sector in India (using the input output analysis), the author has opined that, PSEs, despite their poor financial performance *vis-a-vis* the private sector, have played an important role in laying down the India's industrial base and diversifying the industrial structure *via* its linkages with the rest of the economy. However, in the present day context, taking an ideological stand on the issues involved in PSE reforms could be grossly out of sync and there is a need to improve their efficiency so as to enable them to compete effectively with the private sector, which is well equipped today to undertake the production of all commodities, including infrastructural services. Against this backdrop, the author has analysed the *modus operandi* adopted for PSE disinvestments in India during the period 1991-2001 and has then, listed out the various divestiture options according to the hierarchy of political desirability and capital market sophistication of a country. On top of the author's list is public offering, which is the most preferred choice in view of the desire to spread ownership widely. Next in the list is employee buy outs, followed by private and overseas trade/strategic sales. The author, however, has not discussed what is today an appropriate method for India - is it strategic sale or public offering – the question that attracts the attention of the policy makers. While many support 'strategic sale' on the ground that it is revenue enhancing, others oppose it as a means to practice crony capitalism. The Disinvestment Commission is of the opinion that if the Government has a role to play in the sector in which the PSE is functioning, then in Initial Public Offering (IPO) route is to be adopted. This would enable the Government to retain ownership, while allowing the presence of outsiders to act as a check. If the Government's presence is not mandatory, then the ideal route would be the strategic sale. While adopting this route, the Government may sell enough to improve the quality of management, thus ensuring better market valuation, before selling the entire stake. The option of management employee buy outs that falls second in the hierarchy list of the author is attractive as it tackles both employment and divestment issues. However, it may be noted that we are still not up to the mark with regard to this approach. Employees have normally been put at par with strategic partner. Hence, there is a need to devise new systems, where by employee not only benefits but is also treated differently from the strategic partner.

The author has also tried finding an answer to - how far the PSE's shares subsequent to disinvestment are traded on the stock market, so that prices of these shares can be looked upon as an indicator of the management performance. The author observes that PSE stocks, which have been divested through public route/participation tend to be more liquid and more actively traded as compared with the dull stocks, divested directly through institutions and hence, he has favoured greater private/retail participation. It needs mention here that there has been a marked change in the mindset of the Government since the late 1990s. Earlier it was selling to institutional investors, while now it is trying to attract retail investors *via* various incentives-larger reservation for retail investors/employees, offering greater discounts, no lock-in period for employees, *etc*. The response of retail investors to Maruti issue in June 2003 was quite successful though it was not up to the mark in the March 2004 public issues, mainly because of bunching of too many issues and financial year ending compulsions.

The book also lists out certain cases of strategic sale of PSEs by Government such as BALCO, MFIL, Laganjute, CMC and Air India. The case of BALCO has been analysed very critically bringing out all the relevant issues/controversies and certain lessons to be learnt which are important from the policy angle. These include: (a) standardisation of the method of valuation and division of stake of power between the State and the Centre prior to disinvestment decision, (b) legal aspects concerning transfer of land and other assets to private management to be sorted out at the earliest and, (c) employees, concerns to be taken care of *via* an assured Voluntary Retirement Scheme. The author has raised very valid concerns here. Modality for transfer of land and other assets to private hands obtained on lease/low rent from State/Centre are the issues to which policy makers are still in search of solutions.

Continuing his analysis of different modalities of privatisation in India, the author has devoted one full chapter to the 'Greenfield privatisation' approach used extensively in the field of infrastructure. The author points out that unlike many other developing countries, where an aggressive policy of privatisation involving transfer of ownership from the public to private hands has been adopted as a part of liberalisation of infrastructure sector, India's 'Greenfield privatisation' approach has prompted private industrialists to venture into areas earlier reserved for public sector, such as power, aviation, telecommunications, roads and railways. The author has then elaborated upon the progress so far on the privatisation of infrastructure - sector wise (transportation, telecommunication and power), drawing heavily from Rakesh Mohan's India Infrastructure Report, 1996. The author observes out that as a result of enhanced private participation, the share of private sector investments in infrastructure will soon touch the 45 per cent mark, as envisaged in the Report and will help to enhance efficiency in the sector.

Having discussed some of the privatisation modalities adopted in India, the book makes an attempt to address the fundamental issue as to whether ownership or competition is more important for efficiency. Although empirical literature so far provides mixed results, the author has provided overwhelming evidence to support that efficiency is ownership neutral and it is competition, which alone matters. To prove his point, he has examined a diverse group of public and private enterprises in terms of growth in productivity (using the translog index) over the period 1988-89 to 1994-95. Results showed that both the groups, *i.e.* public and private companies performed equally well, as the average annual growth rate of their productivity was almost the same, thus, proving his point that efficiency is ownership neutral. In order to estimate the effect of competition (rather than ownership) on the efficiency of the firm, an attempt has been made to compare the average growth rate in total factor productivity of PSEs operating under monopoly market environmentwith the PSEs operating under competitive market conditions. The author has shown that PSEs operating under monopoly environment have experienced a negative average annual growth rate over the period 1988-89 to 1994-95; while competitive PSEs, on an average, experienced a positive growth rate of 1.5 per cent during the same period. Thus, the author has established the primacy of competition over ownership and hence, has emphasised the need for a policy shift away from an overriding concern from transfer of ownership to private sector towards ensuring a more competitive environment. There is no denying the fact that whether it is public or private sector, they function well in a competitive environment. However, it needs mention that the author's analysis is debatable, on both technical and theoretical grounds. First, the author has used the combined translog index, though the individual industry - wise break up portrays a different picture, enunciating the need for a case by case evaluation. Secondly, does the author's analysis mean that PSEs be allowed to function if competition is promoted? The answer could be 'yes' only if a lot of other complementary factors associated with ownership change also work at the same time. More than efficiency, ownership matters for companies for ensuring a level playing field with their private sector counterparts in terms of access to capital markets while avoiding the political interference and imposition of non-economic objectives on PSEs. The pressures under which a private firm operates such as - shareholders monitoring, threat of liquidation and take over - get diluted for PSEs. Infact, there is a whole host of literature now, that says that competition without privatisation might be difficult to sustain in the long run. Hence, the choice between privatisation and competition could be more about sequencing rather than exclusive use of one over the other.

Irrespective of the results obtained from ownership *vs* competition analysis, some PSEs will continue to remain in the public sector.

According to the author, for such PSEs, Government has to attempt an improvement in efficiency, within the existing ownership pattern by effectively regulating the PSEs *via* use of performance contracts. In this context, the author has attempted a very logical and unique way of analysing the role of MoUs as a regulatory device, with first questions and concerns clearly specified and then empirical exercises carried to find out the answers. The author has indicated that MoUs in India suffer from the problem of soft targeting, and hence, there is a need to make it more effective either by providing monetary incentives linked to MoU system and factor productivity improvement as in countries like, Pakistan and South Korea or *via* other innovative methods.

To conclude, the choice between 'privatisation' and 'public regulation' or between the different modalities of privatisation is far from being simple and straightforward. While some of the author's conclusions are debatable, yet she has been successful in portraying a clear picture on many aspects / issues related to privatisation. The book indeed marks an important contribution to the ongoing debate on the economics of privatisation. The author's analysis of role of competition and that of MoUs are quite unique and interesting. The analysis of the disinvestment policy for the Government, however, remains incomplete. Readers could have been well served by a discussion on a range of conceptual and micro issues related to privatisation/disinvestment, which are being publicly debated more recently. Which route to adopt while privatising/divesting PSEs? Whether profit - making PSEs/Navaratnas should be treated differently from loss-making ones? Whether restructuring, both organisational and employment, should be taken up prior or post to disinvestment? What should be the strategic timing of an IPO sale? Whether to follow bidding route or market valuation route? How to ensure effective retail participation? How best to tackle legal issues? These are some of the dilemmas- the answers to which would go a long way in providing direction to the current Government policy. Nevertheless, the theme of the book is highly topical and relevant in the present context.

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