The Strange form of "Disinvestment"*

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As the term of the current NDA government nears its end, with signs of popular dissatisfaction over its performance on the economic front, the urge to ramp up expenditure to woo the electorate intensifies. But a number of factors have combined to render that task difficult, with the failure of the government's misplaced disinvestment programme being among the most important.

Disinvestment receipts are crucial to the government this year for two reasons. First, while direct tax collections in 2018-9 are according to official figures on track to reaching targets, indirect tax collections have fallen short after implementation and periodic revision of the GST regime. According to the Controller General of Accounts, total tax revenue collection till November 2019 was just short of 50 per cent of the budgeted figure, whereas the achievement in the corresponding period of the previous year was 57 per cent. Second, the government is hell bent on realizing its fiscal deficit target of 3.3 per cent of GDP or thereabouts, as part of its effort to convince international capital that it is both working to improve "the ease of doing business" in India, as well as successfully pursuing the neoliberal requirement of fiscal consolidation.

This increased dependence on disinvestment receipts is not a new phenomenon. The cumulative total of receipts from disinvestment, including sale of exchange traded funds linked to public sector equity, is estimated at Rs. 390,787 crore. More than 60 per cent of this sum has been garnered in just close to five of those fifteen years (since 2014-15), when the Modi-led NDA government has been in power. This is despite the fact that actual disinvestment receipts have fallen short of ambitious targets in all these years except one. In financial year 2017-18, receipts from disinvestment touched a record Rs. 100,000 crore, as compared with a budgeted target of Rs. 72,500 crore.

There were three elements to the strategy that ensured this unusual "success" on the disinvestment front. One was to bundle good equity from multiple PSEs into exchange traded funds, that are listed and can be traded like stocks, that were offered as a good investment opportunity to financial institutions, mutual funds and retail investors. The second was the strategic sales privatisation route, in which a private buyer of a minority shareholding of at least 26 per cent of the equity held by the government in a public sector unit is handed over full managerial control through a shareholders' agreement. This gave the private buyer full control with an investment smaller than if required to buy a controlling block of shares of up to 51 per cent. The power that the shareholders' agreement accompanying such sales gave the buyer became clear when the Tatas, who were still minority shareholders post-strategic sale, chose to invest cash surpluses available with privatized VSNL in Tata Teleservices, then still a start-up firm controlled by the group. The NDA's commitment to big ticket disinvestment leading to privatization at whatever cost was revealed when it decided to adopt this strategic sale route to divesting itself of PSE assets. And the third was the siphoning off of current and potential surpluses from cash rich PSEs, by opting for a PSE to PSE transfer, or the sale of government equity in one public sector unit to another such unit. Thus, the government's entire shareholding of 51.1 per cent in

HPCL was sold to ONGC for Rs. 36,915 crore, contributing more than a third to total disinvestment receipts in 2017-18. Interestingly, ONGC borrowed Rs. 25,000 core in the year it acquired HPCL, suggesting that in this case the government was merely substituting its borrowing with that by a public sector unit it owned.

In keeping with the trends generated by this strategy, Finance Minister Jaitley had set his disinvestment target in Budget 2018-19 at Rs. 80,000 crore. He was possibly expecting even larger realizations through measures such as cross-holding by PSEs, giving him much fiscal maneuverability in a pre-election year while achieving his fiscal deficit targets. Surprisingly, thus far there does not seem to be evidence of success. Excluding the most recent sale of equity in the National Hydo-Power Corporation, disinvestment receipts are currently placed at Rs.33,763 crore in 2018-19, which is not even half-way to target. The government plans to mobilise in excess of Rs. 10,000 crore by selling its 52.63 per cent stake in the Rural Electrification Corporation to the Power Finance Corporation, which too it owns. But even if the process is accelerated through dubious means such as these over the next two months, it is unlikely that the government would be able to establish a record this financial year of the kind that it managed in 2017-18.

Interestingly, even the current tally in 2018-19 has been achieved in substantial measure either by the sale of exchange traded funds linked to PSE equity or through a new mechanism: the (enforced) buybacks of small chunks of equity by PSEs from the government, using the cash surpluses of the former. Buybacks have been undertaken by Kudremukh Iron Ore Company Ltd, National Aluminium Company Ltd, Neyveli Lignite Corporation, Cochin Shipyard and BHEL. Not all of these are cash rich companies and are likely to have to borrow to finance their modernization or expansion plans. In addition, it seems likely that, besides persuading the RBI to "disinvest" and transfer a large part of its reserves to the exchequer, the government would also call on PSEs to make large dividend payments to enhance its non-tax revenues. In sum, 'disinvestment' is turning out to be a process in which surpluses are wrung out of PSEs or government linked institutions to support the budget, adversely affecting their own stability or modernization and expansion plans. This compares with the understanding that disinvestment involves sale to private buyers.

This change in the nature of so-called disinvestment is surprising, given the evidence quoted earlier to show that the NDA was more than willing to sell off public assets, despite opposition to the process. Given this experience it is indeed surprising that in pre-election year the NDA and its Finance Minister have been unsuccessful in capitalizing on the disinvestment drive to even meet their budgetary targets, let alone mobilise additional resources. One reason is that mega-scale privatization plans, such as that of Air India, could not go through. What the Air India case illustrated was that the government's confidence that even loss-making and debt-burdened PSEs could be sold, however significant they were, was completely misplaced. Past success with disinvestment, strategic scale and privatization was because the deals on offer were immensely attractive.

Consider Air India. Its net loss in financial year 2016-17 stood at Rs. 3,643 crore. An obvious factor generating high net losses was the servicing cost of Rs. 6,000 crore on debt, then estimated at around Rs. 52,000 crore. Unless the government was willing to infuse funds to write off the debt and clear the books of the company, private interest was unlikely. But that would have defeated the whole process of trying to mobilise money through sale of the corporation. The government did not relent. Nor did private buyers, who ignored the offer.

A second reason why disinvestment is flagging is that the bull run in equity markets has ended and they are in decline. According to an analysis by Capitaline, reported in October 2018, the value of 41 state-owned stocks had halved when compared to their 52-week highs and another 32 were trading at prices 12-44 per cent below their 52-week highs. Any sale would have been at prices much lower than appeared reasonable. And if chunks of equity from multiple PSEs were to be flogged, the price received would have been even lower. That would have laid the ruling party open to criticism that it could not have easily countered, muddying the water in a politically sensitive period. Mobilising money to finance spending aimed at gaining legitimacy in ways that undermine legitimacy in the first instance would be foolish.

Finally, for those investors still looking for opportunities for investment, new avenues had been opened up, such as the purchase of assets being released for sale by the debt resolution process under the Insolvency and Bankruptcy code. These were in many cases real assets with potential that were available cheap, as opposed to long-neglected public sector assets with uncertain prospects of returns.

In sum, the government's hype with respect to the health of India's economy and its rapid growth is out of sync with the state of business confidence on the ground. Going by the latter, unless the government was willing to offer substantially more by way of concessions that rendered public equity unusually attractive, buyer interest was likely to be subdued. Add to that the rather chaotic state of implementation of policy, whether good or bad, and the welcome failure on the disinvestment and privatization front is understandable.

In the event, the government has become even more dependent on the public sector's own resources, central bank dividend and reserve transfers, and off-budget expenditures, to window-dress its budget. The controversy over transfer of the RBI's reserves has to be seen in this light. Further, as per a recently released CAG report, off-budget financing was resorted to by deferring fertilizer arrears/bills through special banking arrangements; covering food subsidy bills/arrears of FCI through borrowings; financing implementation of the AIBP irrigation scheme with borrowings by NABARD under the Long Term Irrigation Fund (LTIF); and much else.

Unfortunately for the NDA, while this may help dress up its fiscal indicators, it does not raise spending to levels and give it enough visibility to make the difference that 'free' resources from the sale of assets would have.

*** This article was originally published in the Frontline Print edition: February 15, 2019.**