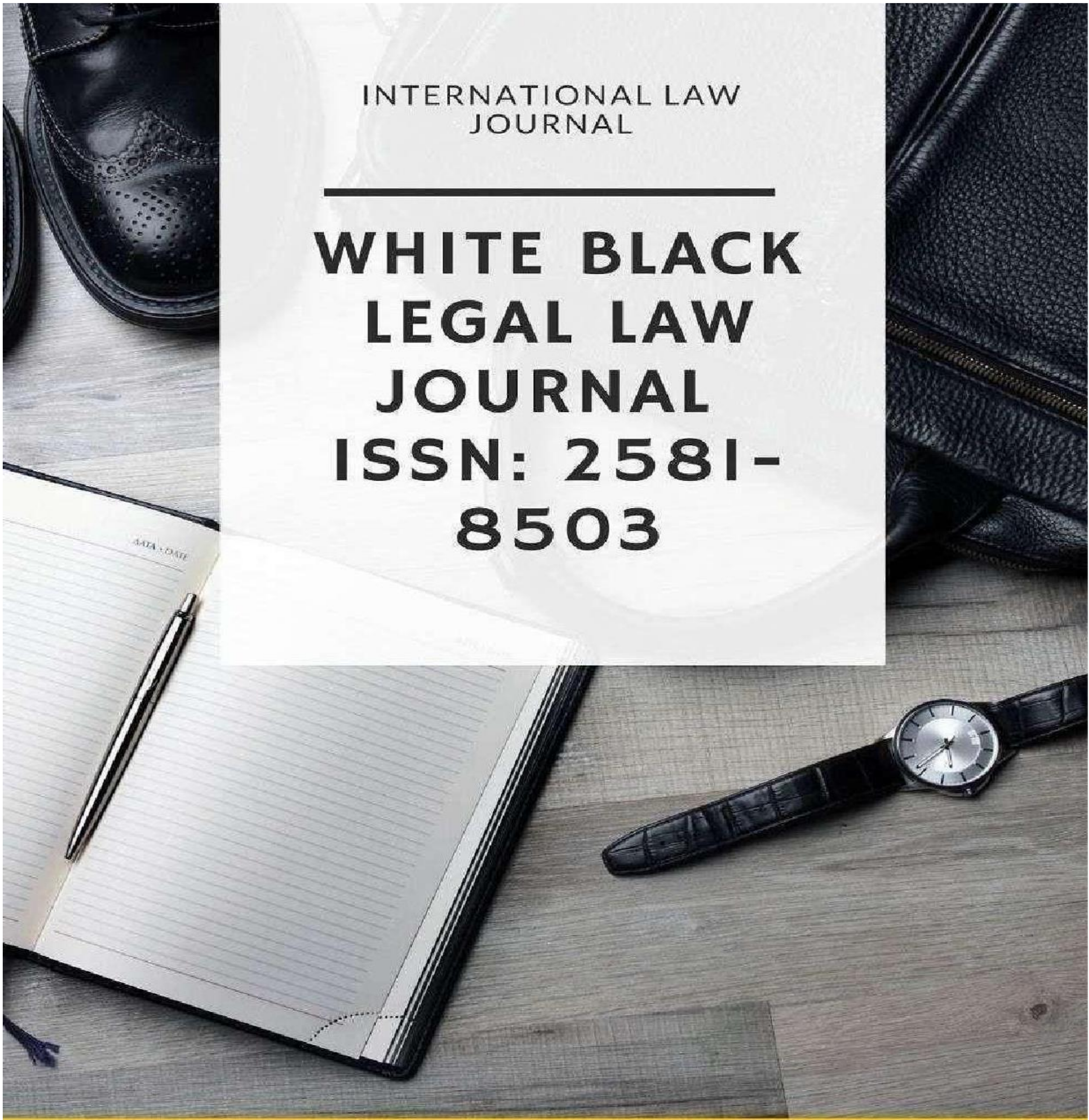

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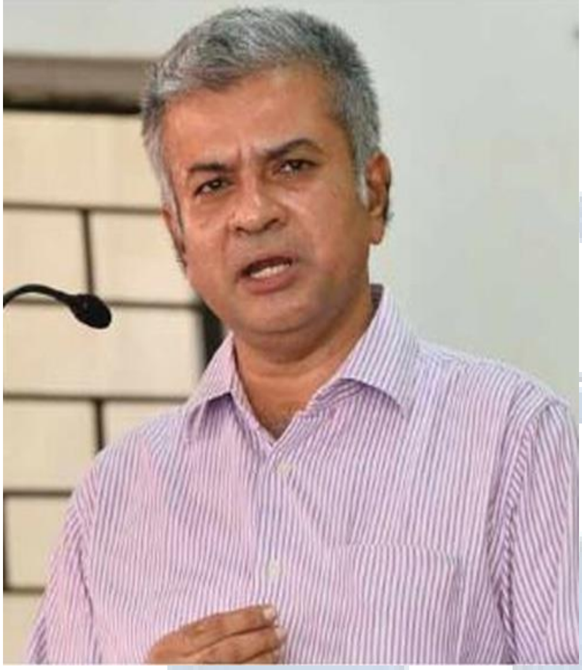

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ABOUT US

WHITE BLACK LEGAL is an open access, peer-reviewed and refereed journal providededicated to express views on topical legal issues, thereby generating a cross current of ideas on emerging matters. This platform shall also ignite the initiative and desire of young law students to contribute in the field of law. The erudite response of legal luminaries shall be solicited to enable readers to explore challenges that lie before law makers, lawyers and the society at large, in the event of the ever changing social, economic and technological scenario.

With this thought, we hereby present to you

DISINVESTMENTS IN INDIA: AN ANALYSIS OF THE “DESTINED” DISINVESTMENT OF AIR INDIA

Authored by - Arjun Singh

Introduction

India embraced the mixed economic system after gaining its independence, at which point economic planning was instituted. The coexistence of the public and private sectors is the primary characteristic of a mixed economic system. The boundaries between the public and private sectors were established by the Industrial Policy Resolutions of 1948 and 1956, respectively. Building infrastructure for economic growth and producing investable resources for development by earning adequate returns were only two of the many goals for expanding the public sector. The principle of "commanding heights" and the provision of consumer products at reduced prices are both justifications for growing the public sector.[11]

Public sector companies have contributed to the development of several key sectors of the Indian economy, including machine tools, steel, aluminum, copper, information technology, the telephone industry, heavy industries, automobiles, ship manufacturing, and shipping transportation. They also provide defense armaments and are in charge of nuclear energy research and development. The State's ability to generate financial resources has accelerated thanks to the public sector. Formerly, it was believed that the nation would be able to advance towards the socialistic structure of society that was desired to be accomplished as a goal by gradually expanding the public sector. India's industrial and economic growth has benefited greatly from the public sector, particularly in regions where the private sector is hesitant due to high capital requirements and associated risks. [2]

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[1] Sri Santosh Koner, Professor Jaydeb Sarkhel. “Disinvestment of Public Sector in India: Concept and Different Issues”, *IOSR Journal of Economics and Finance (IOSR-JEF),* Volume 3, Issue 6. May-Jun. 2014, PP 48-52

[2] Dr. Mugdha A. Deshpande, “Disinvestment in India: An Analytical Study”, Volume 6 ,Issue 1, Jan. – March 2019

1.1. Definition of Disinvestment

Disinvestment is the exact opposite of investment. Investing is the financial purchase of an item that generates income. An investment might be, for instance, the purchase of bonds or stock in a company with money spent. While investing, money is turned into an income-producing asset to generate revenue.

In contrary, when an asset is disinvested, it is turned into cash that may be used immediately. The selling of government stock in public sector companies is known as disinvestment. The government's holdings in government-owned corporations are revenue-generating resources at its disposal. Selling these shares will result in the conversion of earning assets into cash. Disinvestment is the term used to describe it.

1.2. Difference between disinvestment and privatization:

- Privatization and disinvestment are two distinct processes. Privatization denotes a shift in ownership that affects management. Disinvestment, however, does not automatically signify a management shift.
- Disinvestment signifies the government's share in a public company being reduced. Government management is still retained even when disinvestment occurs if the dilution is less than 50%. It hasn't been privatised. However, there is a transfer of ownership and management if the dilution is more than 50%. Privatization will be the term used.
- Disinvestment is thus a broader concept than privatisation. Disinvestment may not always mean privatisation, but privatisation does imply disinvestment. Disinvestment only indicates privatisation when it exceeds 51%. As part of the disinvestment strategy, the degree of the government's share dilution is established.

1.3. Change in Government Policy towards Public Sector

The 1991 adoption of the new industrial strategy resulted in a significant shift in the government's attitude towards the public sector. The public sector's contribution to the new industrial policy of 1991 has been diminished. Under the industrial strategy of 1956, twelve more sectors were to be gradually taken over by the state, while seventeen industries were allocated exclusively for the public sector. However just eight industries were set aside for the public sector in the industrial strategy of 1991. Production, atomic energy, coal and lignite, mineral oils, iron ore, manganese, gold and diamond, atomic minerals, and railways are among these eight sectors.

It has also been mentioned that private sector entities could be allowed to enter certain industries if the necessity arises. As a result, there is no such thing as the public sector's exclusive domain in the new industrial strategy. According to the new policy, the government would manage the public sector using ethical business practises. Units in the public sector that are very unwell will be submitted to the Board for Industrial and Financial Reconstruction (BIFR) for a viability assessment. The inefficient public sector businesses will be shut down. For the rehabilitation of the employees who work in the impacted units, a social safety net will be established.Another important feature of the new policy on public sector is disinvestment of some selected public sector units. It has been decided that 20% of the shares of selected profit making public sector units will be sold to financial institutions, mutual funds etc. These institutions will hold the shares for a specified period of time after which they will be permitted to sell the shares in the share market.

The new policy also states that the government would give public sector organisations more autonomy. The government will not impede the public sector organisations' regular operations. As an alternative, these units will be under the government's authority thanks to an Agreement they signed with the government.[3]

Causes of Disinvestments

1. **Making the Public Sector Efficient-** Decision-making autonomy is lacking in public sector management. Ministers make decisions for public sector organisations. Politics influences how they make decisions. The result is a decrease in productivity as output is not utilised to its maximum potential.
2. **Burden on the government-** The management of public sector businesses is not responsible for losses caused by those businesses. Revenue from the government is used to cover losses. Management don't care if they make money or lose money. The enterprise's productivity and efficiency were not given any thought. The government is put under needless financial strain as a result. Privatization is therefore encouraged.
3. **Solve Financial Crisis of Government-** Our government experienced a financial crisis in 1990–1991 and ran out of money to invest in infrastructure. The government could raise money by selling a portion of its equity in public companies at profit-making prices, which would end the financial crisis.

[3] Sri Santosh Koner, Professor Jaydeb Sarkhel. "Disinvestment of Public Sector in India: Concept and Different Issues", *IOSR Journal of Economics and Finance (IOSR-JEF),* Volume 3, Issue 6. May-Jun. 2014, PP 48-52

4. **Promoting Industrial Growth-** Due to a lack of funding, the government believed that the public sector would be unable to develop the heavy and basic sectors on its own. In order to boost industrial expansion, privatisation was advocated.
5. **Promoting Globalisation-** As the preference of international businesspeople is to work with the private sector, privatisation is the only way to further globalisation. Benefits from foreign technology and investment can be reaped thanks to globalisation.[4]

Methods of Disinvestment

a) **Public Offer:** Offering shares of public sector companies through a general prospectus at a set price. The offer is provided to the general public via reputable market intermediaries as a conduit. At first, ordinary investors were provided shares through domestic public offerings. The Global Depository Receipts (GDRs) were then issued in order to access the international market.

b) **Sale of Equity:** The auctioning out of equity shares to a big, pre-selected group of clients. With merchant bankers' aid, it is possible to estimate the reserve price for the PSE's equity.

c) **Offer for Sale:** A public enterprise is offered for sale once a set price has been established, open bids are invited, and the highest bidder's offer is accepted.

d) **Cross Holding:** The government would merely sell a portion of its ownership in one PSU to another PSU or to many PSUs in the case of cross holdings.

e) **Golden Share:** The PSU is still owned by the government under this scenario to the tune of 26%. The Government will still be the biggest stakeholder thanks to its remaining 26 percent stake.

f) **Warehousing:** According to this approach, selected PSUs would be purchased by government-owned financial institutions, who would then hold onto them until a third buyer could be found.

g) **Strategic Sale:** Recently, the government has been using the strategic selling approach. In this technique, the government gives up managerial control while selling a significant percentage of its stake—51% or more—to a strategic bidder. PSU shares will fall under the Disinvestment Department, and disinvestment prices will be determined by the market rather than being predetermined.5

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[4] Kakkar, Bhawna, "A Study of Disinvestment of Central Public Sector Enterprises in India (1991-2016)" (December 27, 2017). Available at SSRN: https://ssrn.com/abstract=3093570 or http://dx.doi.org/10.2139/ssrn.3093570

[5] Smriti Chand, "7 Methods implemented to Achieve Objectives of Disinvestment in India" October- December 2018

Issues Related to Disinvestment

1. Reasons offered by the government for disinvestment

a) The administration cites two main justifications for disinvestment. The first is to offer financial help, and the second is to boost business productivity. According to the fiscal support argument, The resources of the government are few. Priority social sectors that should receive these funds are basic health, family assistance, elementary education, and social and economic infrastructure.

b) Additional funds can be allocated to these priority areas by freeing funds held in non-strategic public sector firms. The pressures placed on the federal and state governments are growing. The state's initiatives in key sectors need to be expanded. So, it is acceptable that some of the extra funds required to fund these operations come from the sale of shares that the government had earlier amassed using its resources.

c) The second justification for disinvestment is that it will increase the business's operational effectiveness. The firm will be liberated from governmental supervision and be able to operate more effectively if the amount of disinvestment is such that the enterprise is privatised and management is assumed by the private sector. The assumption made here is that a private sector organisation will operate more efficiently than a public sector one. The introduction of private ownership can be beneficial for an enterprise's operation, even if the level of disinvestment is less than 50% and the government retains control of the unit. It promotes management responsibility.

The expectations of the shareholders regarding the returns on their investments are to be met. This will force the company to operate more profitably and effectively. Ownership structure flexibility may actually increase efficiency. In reality, the inclusion of the general public in the ownership structure may also foster circumstances that would allow for greater autonomy in how the public sector firms operate. Disinvestment may be used as a tactic to increase economic productivity.

2. Extent of disinvestment to be made in an enterprise?

a) The degree of disinvestment in any given year should be calculated based on the medium-term objective level of government ownership in that firm. The desired levels of ownership may be as low as 26% to ensure limited control over special resolutions introduced at general body meetings of the company, as high as 51% to have real control, and as high as 100% to secure full ownership.

b) It is best to calculate the desired amount of public ownership in a unit before determining the goal level of disinvestment. A significant amount of disinvestment was called for by The Rangarajan Committee in 1993. It was suggested that disinvestment in sectors expressly earmarked for the public sector may be as high as 49%. The goal public ownership level might be maintained at 26% in exceptional circumstances, such as businesses with a disproportionately large market share or those where maintaining a distinct identity was necessary for strategic reasons.

c) In all other circumstances, it advised complete divestiture of all government holdings. For the goal of disinvestment, the government divided public sector businesses into strategic and non-strategic groups in 1999. Those public sector companies that produce defence goods, produce nuclear energy, or operate railroads would be considered strategic. The remaining public sector businesses were to be regarded as non-strategic. It was agreed that the government's interest in non-strategic public sector companies would not automatically decrease to 26%, and that the method and speed of doing so would be determined on a case-by-case basis.

3. What process adopted for disinvestment?

a) The third issue is: What procedure should be used for disinvestment? Finding the share valuation and the selling modality are the first two things that must be done in order to execute this. If the government owns 100% of the stock in a public company, such shares are not traded on the stock market.

b) There are no market pricing for these shares. But how do you calculate the worth of these shares? There are three ways to calculate share values:

A. The net asset value approach.
B. the discounted cash flow approach, and
C. the profit earning capacity value method.

c) The outcomes of various valuation methodologies differ. Also, it should be highlighted that while the various valuation techniques might serve as a benchmark for price, the price at which a share can be sold depends more on investor perception than on any objective indicator of underlying value. An enterprise's share value may increase or decrease shortly after disinvestment, but this does not prove that the shares were overvalued or underpriced at the time of disinvestment.

d) The selling of shares can be done in one of two ways. Shares are being offered through a public prospectus at a set price. The alternative method involves holding an auction for shares among a selected group of buyers and setting a reserve price. Both approaches have benefits and drawbacks. The first method's drawback is that "Fixed prices" cannot be set by market forces under this approach.

e) But nonetheless, this approach has the benefit of allowing for the distribution of shares among a large number of people. The second technique has the benefit of generating more income for the government since the shares are sold through an auction. The shares are owned by a small number of people under this technique, which strengthens the concentration of economic power.

f) The tender mechanism would be helpful for those public businesses that have yet to conduct their maiden equity sale. The fixed price technique would be suitable if a decent market price has been set over a reasonable amount of time in a typical trading environment. The government sold minority holdings without transferring managerial control in the early years.

g) The government has changed its approach recently and placed more focus on strategic sales. A strategic sale is when you sell the bulk of your stock to a partner while keeping managerial control. The following are the drawbacks of selling minority holdings, according to the government:

a) Lesser realisation due to the retention of managerial control.

b) If a strategic sale is ultimately decided upon, only tiny stakes can be provided to the strategic partner due to the government's minimal holding following minority sales. The prospect of more realisation from the strategic partner is dampened by this.

c) Minority sales also generate the impression that the government's primary goal is to raise money to reduce its budget deficit rather than to enhance the performance of the units disinvested.[6]

Disinvestment of PSUs – Case Study of Air India

The government's efforts to revive Air India appear to have fallen short given the national carrier's declining market share, ongoing losses, and mountain of debts. The 2007 merger of Indian Airlines, which solely handles domestic operations, and Air India, which handles international operations, did not result in any increase in performance and nearly no profits for a decade.

The government's debt of Rs. 52,000 crore, of which Rs. 22,000 crore was a loan for the purchase of aircraft, and the remainder, which was a sizable amount, were the main factors in the decision to disinvest. In his remarks, Finance Minister Arun Jaitley made it very apparent that instead of paying off Air India's debt, around Rs. 50,000 crore could be invested in social welfare fields.

Out of the budgeted expenditure of Rs. 30,231 crore for its turnaround budget, the current administration has already committed Rs. 23,993 crore. However, due to competition from private firms in the domestic market, its market share has been trending downward by about 6%.

The initial step was the NITI Aayog's advice to strategically divest from Central Public Sector Units, including Air India. The sale of Air India outright was advised by NITI Aayog. A core

[6] supra

committee of secretaries on disinvestment, led by the Cabinet Secretary, was then tasked with reviewing the plan.

The Cabinet Committee on Economic Affairs, led by Prime Minister Narendra Modi, received the proposals from the Cabinet Secretary-led panel and gave its "in-principle" approval for the sale of the national carrier.

On June 28, 2018, the Union Cabinet approved the strategic disinvestment of stakes in Air India, including those of its five subsidiaries: Air India Engineering Services (AIESL), Air India Transport Services, Air India Charters, which runs Air India Express, Airline Allied Services, which runs Alliance Air, and Hotel Corporation of India, which owns Centaur Hotels. R.N. Choubey, the secretary of civil aviation, later made this announcement in a news conference on June 29, 2018.

Past History on divestment

During the previous NDA administration, the privatisation of Air India, which was first planned in the year 2000, was abandoned due to resistance from the civil aviation minister at the time. Thereafter, it was decided to divest 60% of the share in Air India, which was operating internationally and had a 26% foreign entity stake, and to sell 51% of the equity of the former Indian Airlines, which had a 26% holding, to a strategic partner.

Causes for revival of disinvestment decision.

- **Huge debt:** Poor management, operational inefficiency, and inability to compete with businesses in the private sector. As a result, it has a significant debt of over Rs 50,000 crore and is completely dependent on government assistance.

- **Profits are always overstated:** There is a widespread misconception that the financial statements indicate operational gains whereas the reality shows constant losses. Their operating profit of Rs. 105 crore for 2015–16 was questioned by CAG.

- **Failure of 2012 bailout package:** When AI failed to produce the expected outcomes, the 2012 turnaround plan, which included a bailout package worth Rs 30,000 crore, was a complete disaster. By the monetization of assets from FY 2012–13 to FY 2015–16, it has raised a total of Rs 64.06 Cr as opposed to the desired amount of Rs 500 Cr.

- **Wastage of tax payers' money-** If the AI scenario persists and the government is forced to keep bailing out Air India, taxpayer money will be wasted, which would also have an impact on the government's ability to manage its finances. The government might as well use these cash in more beneficial and pressing sectors like health and education.

- **Give a push to pending reforms-** In addition to paving the way for the disinvestment of other loss-making businesses like Mahanagar Telephone Nigam Ltd (MTNL) and Bharat Sanchar Nigam Ltd (BSNL), which are unable to compete in India's fiercely competitive telecom market, this will send a clear message to investors that India is serious about reforms.

- **Principles of market Economy-** The government should refrain from offering products and services in some areas given the fundamental principles of the market economy that are practised internationally. where there is a robust and active private sector. With continual easy access to government funds, almost little fear of failing, and no incentive to take action against failures, price discovery in the market is impacted and can harm private sector company operators.

What were the challenges in its privatization?

The process may not be as easy as in other PSUs due to some factors:

- According to the NITI Aayog, any debt that is unconnected to aviation should be forgiven in order to attract investment. But nevertheless getting banks, financial organisations, energy companies, and the Airports Authority of India to agree to such a significant write-off would be difficult.
- The restructuring's human resources component will be politically challenging but financially crucial. All key personnel must be rehired into the aviation corporation "at market levels"; this is essential for any investment.
- The government has been threatened with a "major confrontation" by the Air Corporation Workers' Union if it decides to move through with this disinvestment. The whole selling procedure and terms need to be reviewed/revised in light of the fact that Air India's strategic disinvestment has failed to attract investors and guarantee that the firm is perceived as an alluring investment option.

Process of AI disinvestment - No taker for Air India stake sale as bids close without a single offer, until the 2021 bid

- The government had opened the market for offers for a 76% interest in Air India, which comprises a 100% investment in the low-fare foreign subsidiary Air India Express and a 50% ownership in the ground handling business AISATS.

- In a huge blow to the government's disinvestment programme, the proposal to sell a majority interest in national carrier Air India failed to attract any takers. The government had extended the deadline for bids from May 14 to May 31 and had targeted completion of the sale by December this year.

- Although Indigo, the largest low-cost carrier in India, officially showed interest in taking over Air India's overseas operations, it later abandoned that plan.

- The government's decision to retain a 24% stake in the company and the airline's total debt and liabilities of Rs 33,000 crore are said to be the factors that may have influenced interest in the company.

- An airline official who spoke on the condition of anonymity said there won't be any interest in bidding for the company unless the government decides to sell 100% of Air India.

- To determine the terms of the disinvestment and return with a comprehensive plan, the government had assembled a group of ministers, led by the late Mr. Jaitley. The group must make decisions regarding the amount of the stake sale, its unsustainable debt, whether to permit foreign investors to bid for the national carrier or not, whether Air India's operations will be divided into domestic and international before being sold off, and whether Air India's subsidiaries will be divested simultaneously or separately.

'Group of ministers would decide on the future course of action. Inputs will be taken from the transaction advisor on what went wrong.

BLESSING IN DISGUISE: HANDING OVER TO AIR INDIA TO TATA GROUP

The Government received Rs 2,700 crore from the Strategic Partner (M/s Talace Pvt Ltd, a wholly owned subsidiary of M/s Tata Sons Pvt Ltd), retained the debt of Rs 15,300 crore in Air India and AIXL, and transferred shares of Air India (100% of Air India and its subsidiary AIXL and 50% of AISATS) to the Strategic Partner, concluding the strategic disinvestment transaction for Air India.

What do the employees get?

- None of the over 10,000 employees will be retrenched for the next year
- Employees will be eligible for VRS from the second year onwards with all benefits
- They can stay in company colonies for six months after the takeover
- Employees will continue to get statutory benefits like PF, gratuity etc.

- Tata group will continue to provide benefits to employees
- 50,000 retired employees will continue to get medical benefits under CGHS and NHIS
- Tata group is expected to continue negotiations with various staff unions to resolve their pending demands and issues

What does the country get?

Since its 2007 merger with the state-owned Indian Airlines, Air India has been a losing venture. Reports state that the airline required annual public bailouts to keep operations afloat due to accumulated losses of Rs. 78.953 crore.The government suffers a "loss of Rs 20 crore per day despite Air India generating money," according to the then-Civil Aviation Minister Hardeep Singh Puri, in March 2021.

One less burden on the government's budget might be viewed as a result of the Tata group acquiring Air India.

[7] Suseela Sarma L and Rao PS, "Disinvestment of PSUs – An Indian Case Study of Air India", Published on**:** 2019-04-30

Conclusion

Since the middle of the 1980s, when it was discovered for the first time that the central government's current income were insufficient to cover its current expenditures, the public sector firms' poor financial performance has been a source of significant and persistent worry.

Although studies of PSEs at the firm and industry level frequently highlighted their glaring inefficiencies and low profitability, many of them also suggested their immeasurable (or challenging to quantify) non-economic benefits. The "crowding-in" impacts of public investment and the necessity for institutional mechanisms to protect PSEs from political and bureaucratic intervention, however, have received the majority of attention in India's macroeconomic debate. In-depth analysis have attempted to provide political and economic justifications for the persistence of such a situation.