Business environment (MBA 107)
Assignment Answers.
Week 1

Ques. Discuss the problems and performance of public sector in India.

Ans. **Here we detail about the eleven major problems of the public sector enterprises in India.**

(i) Endowment Constraints:

Some of the public sector enterprises, particularly some of the loss-incurring enterprises are suffering from endowment constraints as the selection of sites of these enterprises were done on political considerations rather than on rational considerations.

(ii) Under-Utilisation of Capacity:

Under-utilisation of the production capacities are one of the common constraints from which almost all public sector enterprises are suffering. In 1986-87, out of the 175 public sector units 90 units had been able to utilize over 75 per cent of its capacities, 56 units achieved utilisation of capacities between 50 and 75 per cent and the rest 29 units could somehow managed to utilize under 50 per cent of its capacities.

This had been mainly due to the reasons such as long gestation periods, huge in-built capacities, ambitious scales of planning based on inadequate economic (particularly market) data, inadequate motivation, lack of initiatives and obsolescence of the product mix.

(iii) Absence of Rational Pricing:

Public sector enterprises in India are suffering from absent of rational pricing as the prices of their products are determined by such a price policy which has three considerations like:

(a) Profit as the basis of price fixation.

(b) No-profit basis of public utility approach,

(c) Import-parity price.

Thus, formal, and informal regulations of prices by the Government in the interest of the economy and consumers, in general, and of price stabilization are also responsible for huge losses incurred by some of these enterprises of our country. Moreover, subsidization of the prices of some of the produce by these public enterprises had added a new dimension to the problems.

(iv) Technological Gap:

Some of the public sector enterprises in India are suffering from technological gap as these enterprises could not adopt up-to-date technologies in their production system leading to high unit cost and lower yield. Enterprises like I.I.S.C.O., E.C.L. etc. are suffering from this constraint.

(v) Government Interference:

Much government interference in the day to day activities of the public sector enterprises has reduced the degree of autonomy of the managements in respect of employment, pricing, purchase etc.

(vi) Heavy Social Costs:

Public sector enterprises are suffering from heavy social costs such as the outlays on townships and allied provision of amenities to its employees.

(vii) Operational and Managerial Inadequacies:

The public sector enterprises in India are also suffering from operational and managerial inadequacies and inefficiencies leading to huge wastages and leakages of funds in their day-to-day activities.

(viii) Evil Competition and Sabotage:

Between the public sector and private sector units within the same industry sometimes there exists evil competition which leads to sabotaging of public sector units at a large scale.

(ix) Marketing Constraint:

Some public sector units are even faced with marketing constraints where due to repetitive type of production mix they could not collect a good market for some of their products where the market is already captured by some big private industrial houses leading to a constant increase in inventories.

(x) Surplus Manpower:

In some of the public sector units there is the problem of surplus manpower which is creating drainage of resources unnecessarily leading to increase in the unit cost of production. Political considerations have also contributed towards overstaffing of unskilled workers in these units.

(xi) External Factors:

Workers engaged in the public sector enterprises are lacking sincerity and devotion to their job leading to wastage of working hours which finally affects productive capacities of these enterprises. Moreover, external factors like too much trade unionism, union rivalries and labour troubles are also disrupting the smooth functioning of the production system of these public sector enterprises in the country.

Considering the problems of sickness faced by the Public enterprises, the Standing Conference on Public Enterprises (SCOPE) had recently constituted a committee to study various aspects of sickness of public enterprises. In its recently submitted report (in December, 1995) on its analysis of PSU problems, the committee felt that too much interference by the Government in areas like autonomy and accountability, constitution of board of directors, continuity to top management and little discretionary powers to management for investment, employment, pricing and wages affected the PSU performance.

Performance of Public Sector Enterprises in India

Following are some of the performances of public sector enterprises in India:

1. Employment Generation:

In the various Five Year Plans although we have invested around 60 per cent of our total planned resources on the development of public sector but this sector generated employment to the extent of only 181.97 lakh till 2004. But the total employee strength of Central Public Sector Enterprises (CPSEs) has been coming down from 20 lakh in 2001-02 to 16.14 lakh in 2006-07 and then to 15.7 lakh in 2007-08.

About 5.94 lakh employees had opted for Voluntary Retirement Scheme (VRS) till March, 2008. Thus, total number of, persons employed in the public sector enterprises is about 6.6 per cent of the total number of workforce in the country. In India, 90 per cent of the total numbers of workforce are employed in un-organised sector and the rest 10 per cent are employed in organised sector. Out of this total employment generated in the organised sector, 7.13 per cent of these workers are employed in the public sector in 1991. Thus in respect of employment generation the share of public sector enterprises remained very poor as these enterprises were mostly capital-intensive in nature.

2. Contribution to NDP:

In-spite of huge investment the public sector enterprises contributed a little portion of the Net Domestic Product of the country. Although average rate of growth of investment in the public enterprises remained very high (i.e., 16 per cent to 21 per cent) but the share of public sector enterprises in N.D.P. has been increasing at a very slow rate i.e., from 3 per cent in 1950-51 to 7.5 per cent in 1970-71 and then rose to 11.12 per cent in 2005-06.

3. Contribution to Gross Domestic Capital Formation:

The share of public sector enterprises in gross domestic capital formation has also increased at a very slow rate, i.e., from 3.5 per cent during the First Plan to only 10.7 per cent during Seventh Plan period.

4. Foreign Exchange Earnings:

The foreign exchange earning of the public sector enterprises has gradually increased from Rs. 35 crore in 1965-66 to Rs. 170 crore in 1969-70 and then to Rs. 10,345 crore in 1992-93. But in physical terms the rate of growth of these earnings would be much less.

5. Contribution to Government Exchequer

The contribution of the public sector enterprises towards Government exchequer through dividend, corporate tax, excise duties, custom duties and other has increased from Rs. 7,985 crore during the Fourth Plan to Rs. 85,445 crore during the Tenth Plan. But a good portion of this contribution has been done at the cost of increased tax burden on the people of the country.

6. Profitability:

In respect of profitability, the public sector enterprises are showing a dismal picture. Although some public enterprises are earning a good amount of profit but a good number of other public enterprises are incurring a huge loss leading to a fall in the amount of overall net profit earned by the public sector enterprises in general.

In 1992-93, the top ten profit leaders of the public sector enterprises with their amount of profit were as follows: IOC (1085), NTPC (1007), ONGC (530), MTNL (421), SAIL (367), BPCL (225), NSML (237), HPCL (206), MMTC (199), and BHEL (187). On the other hand, the top ten loss leaders in our public sector enterprises with their amount of losses (shown in brackets in crores of Rupees) were as follows: RINL (987), HFC (330), FCI (225), DTC (204), IA (199), HEC (193), IDPL (112), HSL (104), HPC (71) and HSCL (69.4).

If we look back at the profitability of these public enterprises then in the initial period the picture was really gloomy. During the period 1966-67 to 1970-71, these public enterprises have earned a net loss to the tune of Rs. 800 crore.

Ques 2. Discuss the need for foreign investment.

Ans. Foreign direct investment (FDI) has become an integral part of national development strategies for almost all the nations globally. It's global popularity and positive output in augmenting of domestic capital, productivity and employment; has made it an indispensable tool for initiating economic growth for countries.FDI in India has contributed effectively to the overall growth of the economy in the recent times. FDI inflow has an impact on India's transfer of new technology and innovative ideas; improving infrastructure, thus makes a competitive business environment.

FDI so indispensible for a country that we can't imagine development without it? Perhaps not, if we imagine entire world as a one country, then the word is developing and growing without investment from any other planet. However, if there were some investments from Moon or Venus, the level of development or growth must be different and better. Thus, India can grow without FDI and in fact developed without or with very little FDI till 1980s but pattern and rate of growth is entirely different from the post 1990 years. Since, the GDP growth rate is falling now, export growth and Index of Industrial Production (IIP) abysmally low, need for big push is felt for the economy and if domestic investment is unable to provide that impetus, foreign investment can bridge that gap.FDI provides a win – win situation to the host and the home countries. Both countries are directly interested in inviting FDI, because they benefit a lot from such type of investment. The 'home' countries want to take the advantage of the vast markets opened by industrial growth. On the other hand, the 'host' countries want to acquire technological and managerial skills and supplement domestic savings and foreign exchange.

Moreover, the paucity of all types of resources viz. financial, capital, entrepreneurship, technological know- how, skills and practices, access to markets- abroad- in their economic development, developing nations accepted FDI as a sole visible panacea for all their scarcities. Further, the integration of global financial markets paves ways to this explosive growth of FDI around the globe.

Developing countries like India need substantial foreign inflows to achieve the required investment to accelerate economic growth and development. It can act as a catalyst for domestic industrial development. Further, it helps in speeding up economic activity and brings with it other scarce productive factors such as technical knowhow and managerial experience, which are equally essential or economic development.

Ques 3. What are the reasons of growth of MNC. Explain their harmful and favourable effects on Indian economy.

Ans. The main factors which have contributed towards the growth of multinational corporations are given below:

1. Market Expansion: The growth of GDP and per capita income in various countries led to increasing demand for goods and services. Companies in developed economies, explained their operations overseas to exploit the expanding markets abroad.

2. Marketing Superiorities : Multinationals enjoy the following marketing superiorities over the following over the domestic companies :

a) Availability of more reliable and up-to-date information about market conditions.

b) Reputation in the market due to popular brands and image.

c) More effective advertising and sales promotion techniques.

d) Wide distribution network.

e) Quick transportation and warehousing facilities.

3. Financial Superiorities : Multinationals are financially superior to domestic companies in the following respects :

a) Huge financial resources.

b) More effective and economical utilisation of funds through transfer of excess funds from one country to another.

c) Easy access to foreign capital markets.

d) Easy mobilisation of high quality resources of different types.

e) Access to international banks and financial institutions.

4.Technological Superiorities : Multinationals have strong R & D departments. They can invent and innovate new products and processes more easily and frequently. This provides them an edge over national companies. Developing countries invite multinationals for advanced technology due to the following reasons :

a) Developing countries do not have the resources to develop advanced technology and the level of industrialisation is low.

b) They are unable to exploit their rich mineral and other natural resources due to shortage of funds and low level technology.

c) They do not have adequate foreign exchange reserves to import raw materials, capital equipment and technology on their own.

d) They face difficulty in marketing their products in highly competitive world markets.

Role of Multinational Corporations in the Indian Economy!

Prior to 1991 Multinational companies did not play much role in the Indian economy. In the pre-reform period the Indian economy was dominated by public enterprises.To prevent concentration of economic power industrial policy 1956 did not allow the private firms to grow in size beyond a point. By definition multinational companies were quite big and operate in several countries.

While multinational companies played a significant role in the promotion of growth and trade in South-East Asian countries they did not play much role in the Indian economy where import-substitution development strategy was followed. Since 1991 with the adoption of industrial policy of liberalisation and privatisation rote of private foreign capital has been recognized as important for rapid growth of the Indian economy. Since source of bulk of foreign capital and investment are multinational corporation, they have been allowed to operate in the Indian economy subject to some regulations. The following are the important reasons for this change in policy towards multinational companies in the post-reform period.

Some of world's largest multinational corporations are given below:

1. Promotion Foreign Investment:

In the recent years, external assistance to developing countries has been declining. This is because the donor developed countries have not been willing to part with a larger proportion of their GDP as assistance to developing countries. MNCs can bridge the gap between the requirements of foreign capital for increasing foreign investment in India The liberalized foreign investment pursued since 1991, allows MNCs to make investment in India subject to different ceilings fixed for different industries or projects. However, in some industries 100 per cent export-oriented units (EOUs) can be set up. It may be noted, like domestic investment, foreign investment has also a multiplier effect on income and employment in a country.

For example, the effect of Suzuki firm's investment in Maruti Udyog manufacturing cars is not confined to income and employment for the workers and employees of Maruti Udyog but goes beyond that. Many workers are employed in dealer firms who sell Maruti cars.

Moreover, many intermediate goods are supplied by Indian suppliers to Maruti Udyog and for this many workers are employed by them to manufacture various parts and components used in Maruti cars. Thus their incomes also go up by investment by a Japanese multinational in Maruti Udyog Limited in India.

2. Non-Debt Creating Capital inflows:

In pre-reform period in India when foreign direct investment by MNCs was discouraged, we relied heavily on external commercial borrowing (ECB) which was of debt-creating capital inflows. This raised the burden of external debt and debt service payments reached the alarming figure of 35 per cent of our current account receipts. This created doubts about our ability to fulfill our debt obligations and there was a flight of capital from India and this resulted in balance of payments crisis in 1991. As direct foreign investment by multinational corporations represents non-debt creating capital inflows we can avoid the liability of debt-servicing payments. Moreover, the advantage of investment by MNCs lies in the fact that servicing of non-debt capital begins only when the MNC firm reaches the stage of making profits to repatriate Thus, MNCs can play an important role in reducing stress strains and on India's balance of payments (BOP).

3. Technology Transfer:

Another important role of multinational corporations is that they transfer high sophisticated technology to developing countries which are essential for raising productivity of working class and enable us to start new productive ventures requiring high technology. Whenever, multinational firms set up their subsidiary production units or joint-venture units, they not only import new equipment and machinery embodying new technology but also skills and technical know-how to use the new equipment and machinery.

As a result, the Indian workers and engineers come to know of new superior technology and the way to use it. In India, the corporate sector spends only few resources on Research and Development (R&D). It is the giant multinational corporate firms (MNCs) which spend a lot on the development of new technologies can greatly benefit the developing countries by transferring the new technology developed by them. Therefore, MNCs can play an important role in the technological up-gradation of the Indian economy.

4. Promotion of Exports:

With extensive links all over the world and producing products efficiently and therefore with lower costs multinationals can play a significant role in promoting exports of a country in which they invest. For example, the rapid expansion in China's exports in recent years is due to the large investment made by multinationals in various fields of Chinese industry.

Historically in India, multinationals made large investment in plantations whose products they exported. In recent years, Japanese automobile company Suzuki made a large investment in Maruti Udyog with a joint collaboration with Government of India. Maruti cars are not only being sold in the Indian domestic market but are exported in a large number to the foreign countries.

As a matter of fact until recently, when giving permission to a multinational firm for investment in India, Government granted the permission subject to the condition that the concerned multinational company would export the product so as to earn foreign exchange for India.

However, in case of Pepsi, a famous cold -drink multinational company, while for getting a product license in 1961 to produce Pepsi Cola in India it agreed to export a certain proportion of its product, but later it expressed its inability to do so. Instead, it ultimately agreed to export things other than what it produced such as tea.

5. Investment in Infrastructure:

With a large command over financial resources and their superior ability to raise resources both globally and inside India it is said that multinational corporations could invest in infrastructure such as power projects, modernisation of airports and posts, telecommunication.The investment in infrastructure will give a boost to industrial growth and help in creating income and employment in the India economy. The external economies generated by investment in infrastructure by MNCs will therefore crowd in investment by the indigenous private sector and will therefore stimulate economic growth.

In view of above, even Common Minimum Programme of the present UPA government provides that foreign direct investment (FDI) will be encouraged and actively sought, especially in areas of (a) infrastructure, (b) high technology and (c) exports, and (d) where domestic assets and employment are created on a significant scale.

Ques 4. Differentiate between disinvestment and privatisation.

Ans. disinvestment indicates only a partial dilution of control by the Govt and still retaining overall ownership of a particular enterprise, whereas privatisation for all purposes signify relinquishing the entire ownership in favour of private parties.

Definitions of Privatization and Disinvestment:
• Privatization involves transforming the ownership of a public sector business to the private sector known as strategic buyer.

• Disinvestment is also a transformation process that happens while retaining 26% or, in some contexts, 51% percent of share right (i.e. the voting power) with the public sector organization. The rest is transferred to the desired partner.

• Ownership:
• In privatization, full ownership is transferred to the strategic partner.

• In disinvestment, usually, 26% or 51% of share is retained with the government company, and the rest is transferred to the strategic partner.

Ques 5. Discuss problems and constraints of disinvestment in India.

Ans. To address operational inefficiencies in PSEs without comprising their social objectives, disinvestment policy is often used. However, there are concerns regarding the extent of impact on firm performance since disinvestment may involve transfer of ownership but not control. Analysing data from 1991-2010 on all manufacturing PSEs owned by the central government, this column shows that the average annual efficiency score of disinvested enterprises rose by almost 20%.

Public sector enterprises (PSEs) have an indistinct mandate of meeting objectives beyond the narrow paradigm of profit maximisation. Generating employment, investing in projects that have long gestation periods, setting up operations in certain locations, and regulating prices of some of their products, are some of the objectives that may fall under the social ambit of PSEs. When this multidimensional mandate is combined with an environment free of competitive pressure, PSEs may suffer from operational inefficiencies. To address this inefficiency without compromising on the social objectives that PSEs are expected to achieve, minor disinvestment may be a useful remedial policy.

Theoretically, disinvestment is defined as the transfer of ownership/control of PSEs from the government to the private sector. Privatisation, on the other hand, is a stronger form of disinvestment in which the control is always transferred to the private sector[1]. Hence, by selecting a PSE for disinvestment the government reduces the haziness of the multidimensional objective function (pure social welfare) by making it a combination of social welfare and profits (due to the transfer of ownership to the private sector). However, unlike privatisation, disinvestment does not imply a complete compromise on the social mandate of the government by reducing it to just profit maximisation. Thus, partial privatisation or disinvestment should be preferred over privatisation. However, there exists a counterargument questioning the limited impact of disinvestment on firm performance since the realm of control continues to lie in the hands of the government.