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FROM WELFARE TO WEALTH: ANALYZING THE PROFIT-DRIVEN TRANSFORMATION OF INDIAN GOVERNMENT COMPANIES

AUTHORED BY - SHRUTI SHENOY

ABSTRACT:

PSUs have played a critical role in shaping the country's socio-economic development since the independence of India in 1947. Initially, as tools for industrial and social welfare, PSUs later became instruments of industrial development and social welfare. However, because of liberalization and globalization policies introduced in the early 1990s, they drastically changed into profit-driving businesses. Examining the PSU development history, which spans from Jawaharlal Nehru's time when the government-owned large industries in a mixed economy to self-sufficiency to mitigate poverty, the Indian socialist period emphasized state ownership in critical sectors such as steel and energy.

However, with the License Raj and bureaucratic supervision, it had created inefficiencies which, by the 1980s, had caught up as a negative impact on PSU performance. Nationalization led by Indira Gandhi increased state power; however, in 1991, economic reforms arrived when it was realized that PSUs were inefficient. The objective of reforms in 1991 aimed at increasing PSU operational freedom along with competition by introducing deregulation and liberalization.

Even with these positive effects, the trend towards a profit-oriented approach has outweighed traditional objectives for social welfare. Profit maximization leads to more significant regional imbalance, erosion in employment opportunities, and increased costs of staple necessities. National control over strategic sectors is no longer an issue, but monopolistic practices are also dangerous.

Therefore, although PSUs remain highly important for the Indian economy, sustainable development based on equilibration between social responsibility and profit is required.

Policymakers must face the challenges of the essential mandate of PSUs continuing to serve national purposes without infringing on their fundamental social mandates. How PSUs will be integrated into India's quest for inclusive growth and increased competitiveness in the global arena will depend entirely on their future development.

Keywords: Public Sector Undertakings (PSUs), Economic Reforms, Social Responsibility, Profitability, Sustainable Development

ESTABLISHMENT OF PSUs IN INDIA:

When India became independent in 1947, the nation was primarily an agricultural economy with a poor industrial base, low savings, poor investment ratios, and weak infrastructure[1]. The newly independent country faced several socio-economic issues, such as geographical disparities in economic development, a dearth of skilled workforce, and an infrastructurally underdeveloped country. To encourage self-sustaining economic growth and equitable allocation of resources, the government of India prepared the ground for creating Public Sector Undertakings (PSUs). The Industrial Policy Resolution 1956 was a milestone in this respect, which catered to capital shortages and the absence of private sector initiative for undertaking large-scale industrial ventures. Thus, the state assumed direct control over industrial growth through Public Sector Enterprises (PSEs)[2].

Essentially, the main goals of PSEs, as outlined in the 3rd Pay Revision Committee (PRC) Report, out of many others, were:
To speed up economic growth and industrialization and construct basic infrastructure;
To raise revenue and provide a return on investment to fund additional development;
To promote equitable income and wealth distribution;
To increase employment opportunities;
To foster balanced regional development;
To support small-scale and ancillary industries and

[1] Aggrawal, N. (2022, Aug). Digital Roadmap for Corporate Governance. Chartered Secretary: The Journal for Governance Professionals, Vol. 52(08). pp. 36-42
[2] 3rd PRC. (2016, Jun 06). Report of 3rd Pay Revision Committee for Central Public Sector Enterprises effective from 01.01.2017. Retrieved on 04.12.2022 from https://dpe.gov.in/report-3rd-pay-revision-committeecpses

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To decrease dependence on imports and increase foreign exchange reserves[3].

The development of public sector units, specifically in India, can be roughly categorized into three phases, each mirroring the current political ideology and economic concerns.

EARLY YEARS: NEHRUVIAN SOCIALISM AND THE COMMANDING HEIGHTS:

Nehru's socialist ideology, which strongly emphasized government control over vital sectors, has left its imprint on his economic development policies. This was crucial in building the industrial base to have an independently self-sustaining economy. The state, therefore, became the owner and controller of those industries deemed fundamental for the country's development and thus became the commanding height of the economy. PSUs dominated production in energy, heavy machinery, coal mines, and steel. Nehru believed these sectors would eventually contribute to the long-term development of India's economic growth, poverty elimination, and employment generation[4].

Massive industrial projects were considered more than India's private sector capability and capital resources. Therefore, PSUs were established to bridge this gap and ensure the state could spearhead the economic development agenda. It was during this period that many popular PSUs were established. The nation came to witness the Steel Authority of India (SAIL) and Bharat Heavy Electricals Limited (BHEL) and their massive impacts on the country's industrial development[5].

THE LICENSE RAJ AND BUREAUCRATIC CONTROL:

This was around the time when PSUs were established, and the system of the Licence Raj, which began industrial licensing to oversee and regulate the private sector's entry, began. Under such a system, the government would have final discretion over what to produce, how much to make, and who would deliver it. This led to an unworkable system of rules that often encouraged inefficiency

[3] *Id.*

[4] N. Kundra, *Politics of Political Representation: Gandhian Nationalism vs. Nehruvian Socialism in Raja Rao's Kanthapura*, (2021).

[5] Jayant Sinha, Ashutosh Varshney, India must harness the profit motive in the spirit of Nehru , Financial Times, (August 6, 2012), https://www.ft.com.

and suppressed private enterprise. However, the State's stand at the given time was that this represented an essential mechanism to prevent monopolistic practices and ensure growth was balanced.

PSUs were engaged in a wide range of industries, including telecommunication and energy, transportation, and infrastructural activities, and constituted a significant component of the Indian economy till the 1970s[6]. Yet, when India was looking for independence, bureaucratic interference and absence of competition coupled with a lack of profit motive led to most PSUs getting bloated and inefficient. The welfare-centric approach of PSUs in social goals was often combined with suboptimal financial performance.

NATIONALIZATION AND EXPANSION IN THE 1970S AND 1980S

Another wave of nationalization occurred in the 1970s under Prime Minister Indira Gandhi. The state assumed several private enterprises, such as banks and insurance companies, under its fold and amalgamated them into one government-controlled entity. Today, the role of PSUs in India is of great repute and must be considered an integral part and pillar of the nation's overall social and economic objectives.

However, by the 1980s, it became evident that PSUs were doing dismally in almost every industry. The inherent inefficiencies of the system- inadequate state control, a lack of transparency, and opposite modernization were strangling economic growth. Though PSUs were ineffective at galvanizing growth and development, they perpetuated their stranglehold over the Indian economy.

The most crucial stage was the third stage, wherein the change of PSUs from welfare organizations to profit-orientated businesses began in the early 1990s when India faced an economic crisis and was compelled to introduce high-level economic reforms. An evident change took place in the Indian economy, along with the PSUs, in 1991 with the implementation of liberalization,

[6] K. P. Kalirajan & R. T. Shand, *Public Sector Enterprises in India: Is Privatisation the Only Answer?*, 31 **Econ. & Pol. Wkly.** 2683, 2683-86 (1996), http://www.jstor.org/stable/4404630

privatization, and globalization policies.

LIBERALIZATION AND DEREGULATION:

The Indian government passed a new industrial policy in 1991 with Finance Minister Dr. Manmohan Singh and Prime Minister P. V. Narasimha Rao at the helm. The motives of this policy were not only for deregulation in many key sectors and curtailing governmental intervention but also for foreign investment. This marked the beginning of the Licence Raj's end, with a drastic reduction in the number of industries hitherto reserved for the public sector and opening many previously monopolized sectors to private competition. PSUs ushered in a new environment of competition with liberalization. PSUs were no longer immune to competition; they had to become more productive and achieve greater returns to flourish. Along with this shift, PSUs were allowed to compete in the home and international markets and granted increased operational independence as part of reorganization moves.

POLICIES GOVERNING THE TRANSITION:

Before delving into the impact of privatization of PSUs, it becomes crucial to understand why the shift took place in the first place. What were the reasons behind the inefficiencies of the PSUs? Why did the enterprises that were supposed to boost the nation’s economic growth become the leading reasons for its downfall? The country's economic, social, and political situations in various periods must be analyzed.

In the late 20th century, several political and economic factors led to the privatization of Indian Public Sector Enterprises (PSEs). By the early 1990s, the Indian economy was experiencing a severe fiscal and balance of payments crisis, which was made worse by the public sector's inefficiency. Due to PSEs' over-reliance on government support and a bureaucratic structure that hindered their ability to compete and develop, timely reform was required. Domestic business associations and foreign financial institutions, such as the World Bank and the International Monetary Fund (IMF), had an opportunity to advocate for economic restructuring and liberalization during this crisis.

The Indian government introduced a New Industrial Policy (NIP) as part of economic reforms in

1991 (as described previously in the third phase), significantly limiting PSE operations[7]. The program liberalized the economy to foreign investment, allowed the private sector to enter industries previously dominated by the public sector, and encouraged mergers and acquisitions by removing regulatory barriers. To further integrate the Indian economy with global financial markets, foreign institutional investors (FIIs) were permitted to invest in Indian stock markets.

By restricting PSEs to specific strategic domains like defense, atomic energy, and railways, these reforms weakened the PSEs' historical significance during India's industrialization.

The poor financial standing of most PSEs was one of the primary drivers of privatization. Due to heavy subsidies and price controls, profitability was challenging for government-owned businesses in the 1970s and 1980s. PSEs were forced to offer goods at below-cost pricing in sectors like power and petroleum, which led to underinvestment and losses. Despite being essential forces behind economic growth, they were viewed as ineffective due to their reliance on government assistance and ability to generate income independently.

The government implemented disinvestment programs that sold minority shares in PSEs while keeping majority control as part of the liberalization goal. It was believed that partial privatization would improve efficiency through market discipline. Later, financial constraints forced several industries to privatize fully. Some loss-making PSEs were closed down or sold to private companies in the late 1990s and early 2000s; some sales were controversial because of undervaluation claims.

As part of the PSEs' restructuring, the staff was reduced through voluntary retirement plans, a tactic intended to lower costs and boost the companies' competitiveness. However, insufficient alternative employment possibilities for the thousands of people who lost their jobs caused a significant social problem[8].

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[7] Joshi, V and I M D Little (1996): India's Economic Reforms, 1991-2001 (New Delhi: OUP).
[8] Khanna, Sushil (2012): "State Owned Enterprises in India: Restructuring and Growth", Copenhagen Journal of Asian Studies, 30(2), December.

Despite these obstacles, the drive for privatization continued since it was believed that competition and the effectiveness of the private sector would drive economic expansion. State control of industries was quickly becoming viewed as outdated, and the policy reform was in step with the global trend toward market-based economies. Some PSEs struggled in the absence of strategic direction and government support. In contrast, others could adapt to the new climate and emerge as competitive actors on the global stage.Therefore, privatization in India was a response to changing political ideas that favored free markets as well as an economic need[9]. There are still disagreements on whether the privatization process has improved efficiency or benefited chiefly huge private companies at the expense of the general welfare.

ANALYSIS OF AIR INDIA:

The Air India privatization was a milestone moment in India's corporate and economic history, revealing the difficulty of state-owned businesses and defining the changing role of private capital in the airline industry. J.R.D founded it. Tata in 1932 as Tata Airlines. It was nationalized in 1953 under the Air Corporation Act, marking the state's decision to command central sectors that were considered vital to the country's infrastructure[10]. Through the years, Air India defaulted on financial efficiencies, ineffective management decisions, and a lack of competitiveness against private carriers, piling up losses of more than ₹700 billion by 2020. Despite repeated attempts at restructuring its finances and bailout by the government, the poor performance of the airline and increasing debt made privatization an inevitable policy choice. In 2021, the Indian government finally sold the ownership back to the Tata Group for ₹180 billion, ending Air India's days as a state-run airline and bringing it back under private control[11]. The privatization of Air India was motivated by various reasons, including the government's inability to carry on financial losses, inefficiencies in bureaucratic decision-making, and the desire for a competitive air transport sector capable of attracting investments and enhancing the quality of service. The operational

[9] SUSHIL KHANNA, The Transformation of India's Public Sector: Political Economy of Growth and, Economic and Political Weekly, Vol. 50, No. 5 (JANUARY 31, 2015), pp. 47-60

[10] CAPA. (2013, February 19). Air India: The time has come to stop procrastinating and act. The final scene is near.https://centreforaviation.com/analysis/reports/air-india-the-timehas-come-to-stop-procrastinating-and-act-the-final-scene-isnear-97853

[11] Chowdhury, A. (2017, April 20). IndiGo flies high in the Gulf route. https://economictimes.indiatimes.com/industry/transportation/airlines-/-aviation/IndiGo-flies-high-in-the gulfroute/articleshow/58269139.cms?from=mdr

inefficiencies of the airline were compounded by its bloated staff, political meddling, and a record of poorly managed mergers, including the 2007 merger with Indian Airlines[12], which did not yield expected synergies but instead increased financial woes. Furthermore, competition from low-cost carriers such as IndiGo and SpiceJet severely undercut Air India's market share, resulting in falling passenger numbers and revenue shortfalls. The privatization of Air India has its pros and cons. On the one hand, the shift to the private sector will likely introduce operational efficiency, financial prudence, and strategic decision-making unencumbered by bureaucratic red tape. The Tata Group's experience in corporate governance and customer-driven management would likely revive Air India's image and quality of service. Moreover, privatization does away with the requirement of constant state-funded bailouts, releasing public resources for more essential sectors like healthcare and infrastructure. The opportunities for more excellent investment, fleet renewals, and extended route coverage under Tata's management hold enormous promise for future growth in the airline. At the same time, the choice is also surrounded by apprehension, especially concerns about employee welfare, national strategic interests, and the broader connotations of privatizing public assets of significant importance. The change has resulted in insecurity among Air India's employees, who are worried about job security and restructuring. Additionally, privatization of a national carrier, usually viewed as a matter of market force non-interference in such vital public services, has raised questions about whether key public utilities should be handed over to market forces. There is also the possibility that privatization could result in increased ticket fares or service monopolization if competition is not maintained in the aviation industry[13]. Although the privatization of Air India is part of the broader trend of narrowing the state's role in commercial ventures, its long-term success will rely on the Tata Group's capacity to deliver financial and operational reforms. If handled well, the process would be a model for subsequent privatization attempts in India, showing that private sector efficiency can rejuvenate loss-making state-owned businesses. However, if the process cannot tackle essential issues like cost control, competition, and labor transition, it might reinforce doubts about privatizing national resources. Finally, the Air India case highlights the intricate nexus between government policy, market forces, and company

[12] Correspondent, S. (2017, June 28). Union cabinet gives in-principle nod for Air India disinvestment. https://www.thehindu. com/news/national/union-cabinet-gives-in-principle-nod-forair-india disinvestment/article19164141.ece

[13] A. B. Mishra & Ruchi Karjodkar, *A Case Study of Air India - Maharajah Back to Home*, Int'l J. Emerging Res. Eng'g, Sci., & Mgmt., Vol. 1, Issue 3, at 19-21 (2022).

management in defining the destiny of public-sector business in India[14].

CRITICAL ANALYSIS OF THE TRANSITION

The transformation of PSUs from welfare-oriented entities to profit-oriented enterprises has had positive and negative implications. As far as the outcome is concerned, there is still scope for improvement in efficiency and profitability. Nevertheless, the social and financial consequences of such a transformation remain a cause of concern[15].

Overshadowing Social Welfare Objectives

PSUs have traditionally been set up to achieve national objectives, including offering low-cost services to low-income groups and regions. However, the philosophy of profitability has withered away the role of PSUs. PSUs have increasingly turned out to be cost recovery-oriented and profit margin-oriented rather than striving to offer low-cost services to the deprived sections and rural communities in sectors such as health, education, transport, and energy[16].

For instance, the thrust on profit has resulted in higher tariffs and service charges for utilities and public transport, making life more difficult for the weaker sections to access such elementary services. It hurts more intensely for the marginalized sections of society since PSUs remained a lifeline for service outreach to the regions where private industries were unwilling to invest mainly due to low business profitability. Aband abolishing subsidies and low-cost services negates the very purpose of PSUs, from what they were established to serve society's important objectives like social welfare and equity, which widens inequality.

Job Losses and Labour Unrest

Efficiency and profitability are often compromised to ensure job security, characteristic of India's PSU sector. PSUs undertook cost-cutting through RRs and privatization of specific activities during reorganization to better adapt to market forces. This has resulted in substantial employment

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[14] *Id.*

[15] Prajapati Trivedi, " Public Enterprises in India: If not for profit Then for What?", Vol. 21, no.48, Economic and Political Weekly, pp. MI37-48, (1986).

[16] LIC of India v. Consumer Education and Research Centre ,(1995) 5 SCC 482.

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losses in labor-intensive industries such as coal, steel, and telecommunication.

Widespread labor unrest has been another fallout of the shift to a profit-driven model[17]. Unions are protesting layoffs and the reduction of employee benefits, which were once the defining characteristic of working at PSU. Once considered safe havens with government-backed jobs, PSUs today axe posts to augment profits, leading to increased unemployment, mainly in the industrial sectors. Privatizing significant PSUs, such as Air India, also drives the growing job insecurity concerns among the workforce.

Monopolistic Tendencies in Certain Sectors

In some circumstances, the policies of privatization and disinvestment of the past few decades have resulted in monopolistic practices by which very few powerful private companies carry on an entire industry. These are noticed quite clearly in various sectors, such as energy, aviation, and telecommunications, wherein the deployment of private oligopolies or monopolies has been made possible by reduced state control.

It is offered at increased prices since there are fewer choices for the consumers and few players in control of the market, reducing competition. While private companies have come to dominate much of the markets in industries such as telecommunications, which were previously dominated by PSUs like BSNL, it clearly disadvantages state-owned enterprises. This has led to greater market concentration, and some of these firms are now using their power to fix prices and limit consumer benefits.

Regional Inequities and Neglect of Backward Regions

PSUs were formed to promote balanced regional development by setting up infrastructure and industries in underdeveloped and disadvantaged regions. This boosted local economic activities and provided employment opportunities in such areas. The interest of PSUs, however, started to lie in other more remunerative markets and regions, primarily urban and economically developed areas, as the PSU organizations started gaining more profit orientation.

[17] Air India Statutory Cororation v. united Labor union, (1997) 9 SCC 377.

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PSUs ignored the development of backward areas where they operated early and gave employment, services, and economic activities. The regions have been kept with regional imbalances between regions. PSUs change their investments from less profitable but socially important areas to places of higher demand, profitability, and infrastructure. This relocation increases regional disequilibrium in rural and urban areas. It risks the initial aim of inclusive development by offering some poor areas worse public services and fewer prospects[18].

Dilution of Social Responsibility in Strategic Areas

PSUs have always played a vital role in protecting strategic national interests and satisfying public needs in national defense, energy, and healthcare. In recent years, PSUs' social and strategic responsibilities have been diluted with an emphasis on profit. For instance, it was raised as an issue when the now-privatized defense manufacturing industry, led to date by erstwhile PSUs like HAL, was opened for private groups, and the question was whether national security was taken into any priority system before profits.

Similarly, the retreat of PSUs from public service missions in areas like energy and healthcare raises concerns that those sectors cannot continue performing critical public functions. Energy and healthcare public-sector utilities (PSUs) formerly guaranteed the affordability of essential services for everyone; now, they often compete with private firms, prioritizing shareholder returns over the more significant good[19].

Risk of asset stripping and loss of national control.

Disinvestment raises questions regarding asset stripping. Asset stripping is the process whereby private investors buy the state assets, and value is extracted from them, and they leave without adequately investing in the business enough. Strategic disinvestment happens when a majority stake in PSUs is sold to private entities[20]. The whole process has the potential of decreasing both the public assets initially bought through taxpayers' money and the long-term sustainability of these businesses[21].

[18] B.K. Rao v. State of Orissa, (1996) 9 OCR 439
[19] A.K.Bindal and Anr. V. Union of India and Ors. (2003) 5 SCC 163
[20] K. R. Narayanan v. Union of India, (1993) 2 SCC 573
[21] Manmayi Sharma, Kriti Pradhan, How can Companies Blend Social Welfare and Profit Making?, Vidhi Centre for

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Further, when sold to foreign or private firms, national control loss in essential industries such as energy, defense, and telecommunications negatively affects PSUs. In this regard, national security questions arise because of the consideration of losing resources and industry control, which PSUs have traditionally operated in the national interest[22].

CONCLUSION:

A significant shift in Indian economic policy can be identified with changes in PSUs from welfare-oriented organizations to profit-oriented business concerns. Increased efficiency, global competitiveness, and fiscal discipline are some of the indicators of improvement as bases for the transformation. However, restructuring and privatization have escalated apprehensions concerning the social costs of restructuring and privatization and disrespect for social welfare objectives.

PSUs continue to play a vital role as India moves closer to becoming a major player in the world economy. For this reason, policymakers will pursue the policy of achieving profitability and social responsibility balance in the future. Issues such as profitability and social responsibility delicately weighed between themselves will determine whether India can keep using the potential of its PSUs for more inclusive and sustainable development.

Legal Policy, (May 12 2020), Https://vidhilegalpolicy.in

[22] Tata Consultancy Services v. State of Andhra Pradesh, (2005) 1 SCC 308