POLICY WATCH

Disinvestment via cross-holding a bad concept

Tapping cash-rich PSUs to meet fiscal targets would take away all advantages of selloff

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CASH-RICH public sector undertakings (PSUs) could help the government push through its current fiscal's disinvestment plan, which has been disrupted by weak market conditions amidst worries of another recession in Europe and slowdown in the US.

The finance ministry has asked several PSUs with details such as their cash levels and capital expenditure plans to ascertain whether disinvestment could be done through cross-holdings by these cash-rich PSUs. State-owned companies like Coal India, NTPC and NHPC, have significant cash on their balance sheets (see chart).

The Centre could raise only ₹1,145 crore so far this fiscal through disinvestment in Power Finance Corporation, far below its target of ₹40,000 crore. It has already deferred the proposed ₹12,000-crore follow-on public offer of Oil and Natural Gas Corporation.

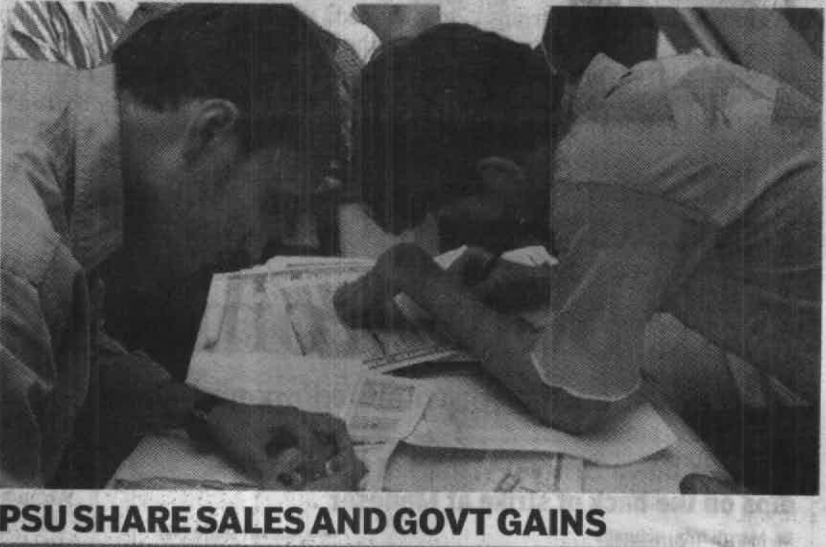
Besides ONGC, the government has planned share-sale in Steel Authority of India (SAIL), Hindustan Copper, Bharat Heavy Electricals and National Buildings Construction Corporation (NBCC).

The government is keen to utilise the cash available with PSUs to aid its disinvestment target through cross-ownership. But the plan may not find favour with the PSUs. Also, this would require the government to seek a fresh Cabinet approval.

The cross-holding proposal has also been criticised on the grounds that it would not lead to the many benefits disinvestment or a stock listing is expected to yield. These include improvement in the corporate governance standards and public disclosures at PSUs, promotion of competition & managerial efficiency and development of the capital markets. Besides, retail investors are given the chance to own a part of the state-owned companies' stakes.

Raising money through disinvestment is crucial for keeping the fiscal deficit target below 4.6% by March-end 2012. Slackening economic growth, low expansion in tax collections and higher subsidy to oil companies have already hit the government's fiscal deficit calculations.

The ministry has already announced plans to borrow ₹53,000 crore more from the market to finance the deficit. This has pushed the yields up on 10-year government bonds to as high as 8.9%, resulting in steep losses for the banks and other buyers of government papers.



PSU SHARE SALES AND GOVT GAINS

Company	IPO month and year	Post-IPO Govt holdings %	Value of Govt holdings on issue date	Value of Govt holdings as on 03.11.11	% Gain / loss	PSU's cash & bank balance as at June end, 2011
NTPC	Oct-2004	89.5	45754	131357	187	17859.83
PGCIL	Sep-2007	86.36	18901	37803	100	4805.87
REC	Feb-2008	81.82	7377	13629	84	
NHPC	Aug-2009	86.36	38244	26558	-30	4265.31
OIL	Sep-2009	78.43	19803	24442	23	11771.4
CIL	Oct-2010	89.99	139276	185322	33	45862.28

Source: Bsepsu.com, FE research

Value in Rs crore

Last month, in its macroeconomic and monetary developments second quarter review 2011-12, the Reserve Bank of India said the government may miss its disinvestment target, which would make it difficult to achieve the fiscal deficit target.

According to a research report by Citigroup Global Markets Inc, "There could be fiscal slippage due to both lower revenues and higher expenditures. Depending on the timing of the pay-out to oil companies, the fiscal deficit number for 2011-12 could come in the 5.1% to 5.8% range, as compared to the budget estimates of 4.6% of GDP."

The government has so far raised a cumulative ₹97,218 crore through disinvestment in state-owned companies over the years. As on October 31, 2011, PSUs accounted for 27% of the total market capitalisation of the Bombay Stock Exchange.