BPCL sale s key n d vestment race

Besides the funds the Indian government stands to raise, the sale of BPCL is crucial to steer PSU disinvestment in the direction of true privatization

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After four extensions, the government finally closed the first step in the privatization of oil marketer Bharat Petroleum Corp. Ltd (BPCL) last week. The response was unflattering. There was nothing from Reliance, Total, Aramco or BP. The government said it received "multiple" expressions of interest (EOIs) without naming them. However, mining major Vedanta confirmed it was one of the firms to express interest.

The sale of BPCL is pivotal for the government. One, the ₹40,000 crore or so it is expected to fetch will help its disinvestment target of ₹2.1 trillion, or about 7% of its total projected revenue for 2020-21. Given the pandemic blow to tax revenue, disinvestment proceeds become even more vital. Two, the government was looking at BPCL as a rare instance of a public sector undertaking (PSU) being sold to a private player, paving the way for more privatization. Speaking to industry leaders on Monday, finance minister Niramala Sitharaman promised to accelerate privatization of state-owned firms in the coming days.

The government needs the private sector to revive the disinvestment momentum. In terms of collections, 2017-18 was the big year, with proceeds crossing ₹1 trillion for the first time. Collections tapered in the following two years and have evaporated this year (*see chart 1*).

If the disinvestment strategy of the Congress-led United Progressive Alliance (UPA) was to sell minority stakes in PSUs, the BJP-led National Democratic Alliance (NDA) government also started selling majority stakes in PSUs that were not of strategic importance. But these were not sold to private entities. Instead, these were sold to—or foisted on—other PSUs. So, for example, Oil and Natural Gas Corp. Ltd (ONGC) bought the government's stake in Hindustan Petroleum Corp. Ltd (HPCL), for ₹36,915 crore. Such inter-PSU transfers played a big part in the three big disinvestment years (*see chart 2*).

BPCL's proposed sale will be a test case at a time when the govt needs to ramp up revenues to fight the crisis

With such inter-PSU transfers, the Centre meets its short-term objective of raising more funds for itself. But whether such transfers contribute towards the long-term objective of unlocking value in PSUs is questionable. Given the imperative to raise funds, the easy option is to sell PSUs to other cash-rich PSUs, whether there are synergies or not.

The proposed BPCL sale is different. From the outset, the government said it would sell its 53% in BPCL to a private player. Thus, neither of the other two PSU refiners, Indian Oil Corp. Ltd (IOC) and ONGC, submitted EOIs. On 18 November, responding to a news article, the government official handling the disinvestment again clarified that PSUs cannot bid for BPCL.

Other than BPCL, there are 19 more PSUs, or parts of them, that have received the government's in-principle approval for disinvestment. None, though, match up to BPCL, India's second-largest PSU by revenue in 2018-19 (*see chart 3*).

This is not the first time a government is trying to sell BPCL. The Atal Vajpayee-led NDA government (1999-2004), too, had expressed intent. That government is the only one so far that has sold majority stakes in PSUs to private players. It did so in a range of sectors, including mining (Balco and Hindustan Zinc), oil refining (IBP), petrochemicals (IPCL), telecom (VSNL) and IT (CMC).

Most of these PSUs have since been merged into the company that bought them, and have ceased to exist as listed entities. Hindustan Zinc—which was bought by Sterlite, a Vedanta Group company—is one that is still listed. Its performance is illustrative of the potential of disinvestment.

A sum of ₹100 invested in Hindustan Zinc in August 2002, when it was sold, is today worth ₹50,745—a compounded annual return of 41%, against 16% delivered by the bellwether BSE Sensex. Around that time, BPCL and HPCL too were in the longlist to be sold. Their sale never got underway. And though they have both beaten the bellwether BSE Sensex in returns since, the gap with Hindustan Zinc is enormous (*see chart 4*).

While both partial and full privatization are useful, performance improvements are "significantly and positively related" to the fraction of equity sold, wrote Nandini Gupta, associate professor of finance at Indiana University's Kelley School of Business in a 2011 research paper.

"Compared to partially privatised firms, sales and returns to sales increase by 23% and 21%, respectively, on average when firms sell majority equity stakes and transfer management control to private owners," wrote Gupta, who has extensively researched this issue in the Indian context.

Two decades ago, as India battled industrial stagnation and economic slowdown in the wake of the Asian financial crisis of 1997, the Vajpayee government used the privatization drive to raise government revenue and lend more dynamism to the Indian economy. It remains to be seen if the Modi government can do the same in the wake of another crisis. BPCL will be a test case.

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Chart 1
This year has been a disinvestment washout so far
Total receipts from disinvestment (₹ crore)

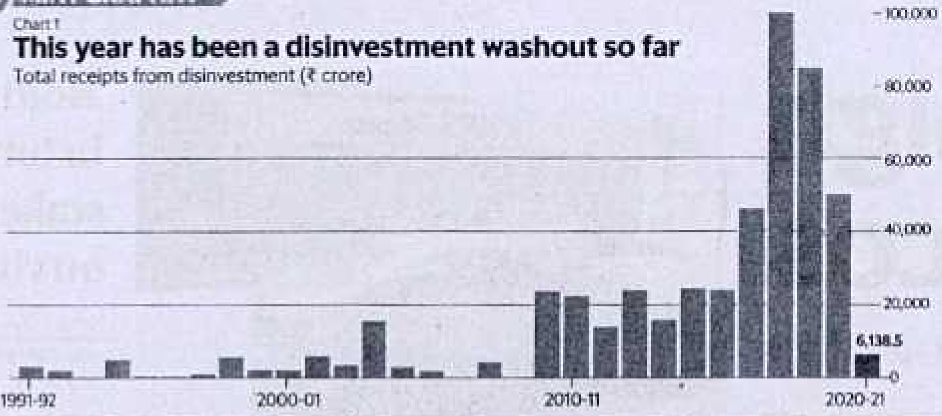


Chart 2
Beyond minority stake sales, this government has relied on PSU buyers for divestment
Amount (₹ crore)

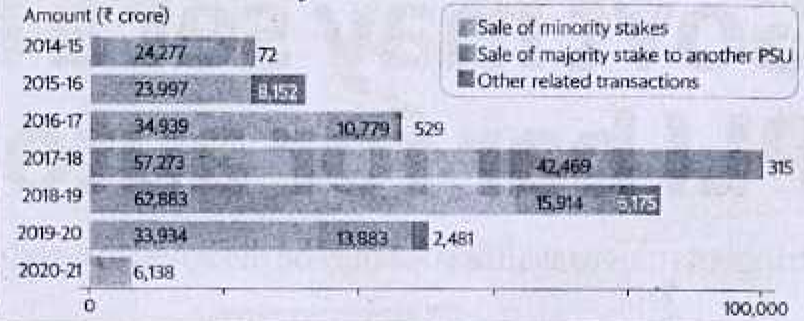
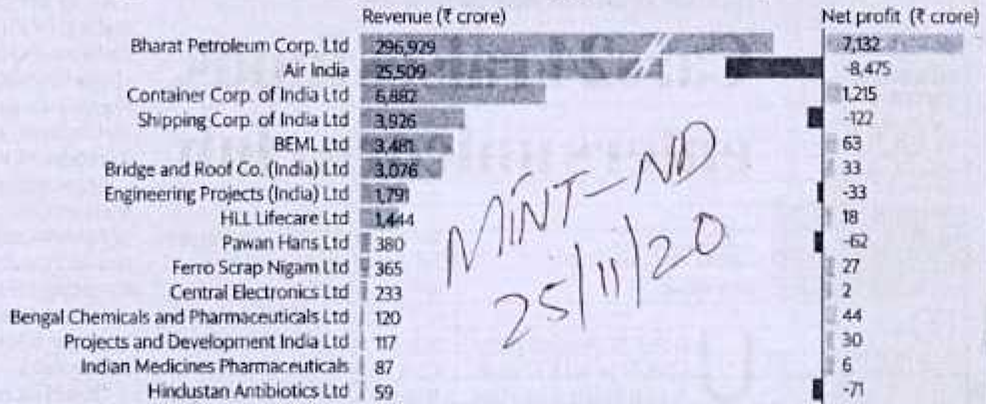


Chart 3
Among the PSUs lined up, BPCL is the biggest and most profitable



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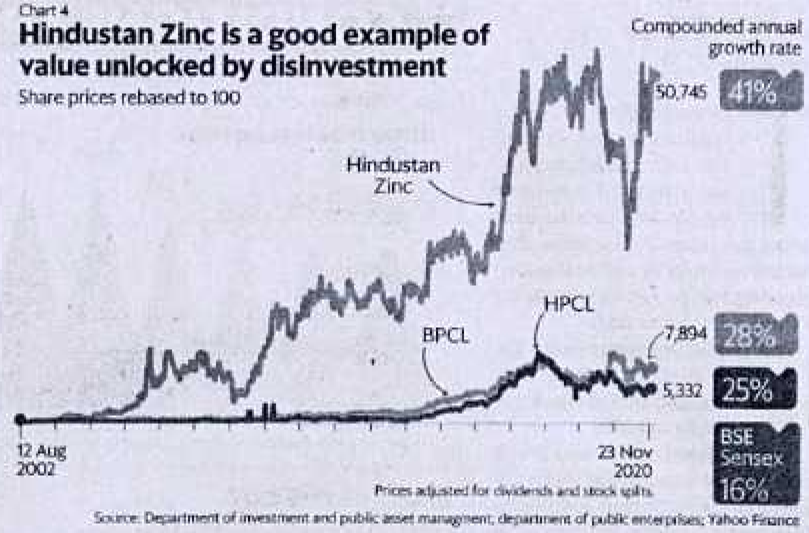
Data for 2018-19. The remaining five transactions lined up for divestment are Neelachal Ispat Nigam Ltd. and units of Cement Corp. of India Ltd, National Mineral Development Corp. Ltd, Steel Authority of India Ltd and India Tourism Development Corp. Ltd. Data for them was not available.

Chart 4
Hindustan Zinc is a good example of value unlocked by disinvestment
Share prices rebased to 100



Prices adjusted for dividends and stock splits

Source: Department of investment and public asset management; department of public enterprises; Yahoo Finance

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