

Under-Pricing and Undervaluation of PSUs' Shares in Disinvestment Programme: A Study

** Shrikrishna Mahajan*

1. INTRODUCTION

The Public Sector Undertakings (PSUs) have played a vital role in development of Indian economy. Public enterprises are concerned as 'an instrument for self-reliant economic growth of India in order to develop agriculture and industry, diversify public economy and overcome economic backwardness and prevent the growth of unaccountable monopoly power' (Reddy & Balaji, 2004). But since 1991, the Government of India changed its former policy and opened up the areas to private sector, which were formerly reserved for public sector. As the Government of India adopted liberalization & globalization policy, the privatization became compulsory to developing countries like India. Especially, the World Bank and IMF forced to carry out privatization as a condition for assistance under the economic stabilization and structural adjustment programme (S & SAP). Since 1991, the Government of India as a route of privatization has adopted the disinvestment. Disinvestment involves the sale of public-sector-equity to the private sector and to the public at large. When we talk of disinvestment or privatization in India, it is relevant that the objectives of setting public enterprises should not be forgotten. When the disinvestment or privatization is concerned, we have to take into consideration that whether the objectives of public enterprises are achieved, which were laid down for social objectives and national interest.

2. OBJECTIVES

The main objective of this research paper is to study the under-pricing and undervaluation of PSUs' shares in disinvestment programme. And the specific objectives are:

1. To take the review of the disinvestment policy and proceeds.
2. To estimate the extent of loss to the government due to under-pricing of PSUs' shares.
3. To suggest the remedial measures on it.

3. HYPOTHESES

To achieve the objectives mentioned above, the following hypotheses have been tested:

1. At initial phase of disinvestment, PSUs' shares were under priced.
2. The disinvestment programme of public sector undertakings was suffering from loss due to undervaluation and post-closing-adjustment.

4. METHODOLOGY

There are number of issues which are criticized in respect of disinvestment in India. But the specific study has not been undertaken. Instead, the vague statements have been made on these issues. This paper confines to study the extent of loss to government due to under-pricing and undervaluation of PSUs' shares. For estimating it, the present researcher adopted the methodology of the comparison between the price at which shares were sold and the potential proceeds by adjusting the closing price on the first day of trading by percentage movement of the ET index. The estimation of loss tests hypotheses.

5. LIMITATIONS

The present study has the following limitations:

1. It is limited to the disinvestment programme of central public sector undertakings.
2. It is dependent only on secondary data.

* *Lecturer (Senior)*, Department of Commerce and Management, Shivaji University, Kolhapur-416004, (Maharashtra).
E-mail : ssmahajan_suk@rediffmail.com

6. DISINVESTMENT POLICY IN INDIA

6.1 Beginning of the Disinvestment

Dr. Manmohan Singh, the then Finance Minister in the Congress led Government, implemented an idea of disinvestment in 1991. He fixed the first target of Rs.2500 crore in 1991-92 and actual receipts were Rs.3030 crore but after that the proceeds from disinvestment became low as compared to fixed target.

6.2 Disinvestment Committees

The Government of India appointed the Krishna Murthy Committee in 1991 and the Rangrajan Committee in 1992 for suggesting the procedures to be followed for disinvestment of public enterprises. However, the Government did not take any decision on the recommendations of this committee.

6.3 Disinvestment Commission

In August 1996, the Government of India set up Disinvestment Commission to advise on the extent, strategy, methodology and timing for disinvestment in each Public Sector Undertakings. First Disinvestment Commission under the Chairmanship of Mr. G. V. Ramkrishna submitted 12 reports to the Government making specific and general recommendations about the public sector units. The reconstituted commission under the Chairmanship of Dr. R. H. Patil submitted 13 reports to the Department of Disinvestment. The Disinvestment Commission played a role of advisory body only. It recommended the process of disinvestment. But these recommendations are not mandatory for the government.

6.4 NDA Government Period

The National Democratic Alliance (NDA) Government after coming into power established Ministry of Disinvestment and appointed a separate Minister for Disinvestment. It started proceeding of disinvestment rapidly. In its first budgetary announcement, the NDA Government decided to bring down government share holding in the Public Sector Undertakings to 26 per cent in the generality of cases; it however stated that Government would retain majority holdings in Public Sector Undertakings involving strategic consideration and that the interest of workers would be protected in all cases. The then Minister of Disinvestment viewed on NDA Government Policy on disinvestment saying that the main objective of the disinvestment is to put national resources and assets to optimal use and in particular to unleash the productive potential inherent in our public sector enterprises (Government of India, 2005). The policy of disinvestment specifically aims at-

1. Modernization and upgradation of PSEs,
2. Creation of new assets,
3. Generating of employment,
4. Retiring of public debts

6.5 UPA Government's NCMP

The United Progressive Alliance (UPA) Government came into power under the leadership of Dr. Manmohan Singh. Then the Government took a decision to close down the Ministry of Disinvestment with effect from 27th May 2004 and the work relating to disinvestment had been allocated to the Department of Disinvestment in the Ministry of Finance. The UPA had already mentioned its strategy towards public sector in National Common Minimum Programme (NCMP) that 'the UPA Government is committed to a strong and effective public sector whose social objectives are met by its commercial functioning, but for this, there is need for selectivity and strategic focus. The UPA is pledged to devolve full managerial and commercial autonomy to successful profit making companies operating in a competitive environment. Generally profit making companies will not be privatized.' The UPA Government policy on disinvestment includes the following measures-

1. All privatization will be considered on a transparent and consultative case by case.
2. The existing 'Navratna' companies will be retained in the public sector.
3. Every effort will be made to modernize and restructure sick public sector companies and revive sick industry.
4. Chronically loss-making companies will be either sold off, or closed.
5. The government believes that privatization should increase competition, not decrease it.
6. It will not support the emergence of any monopoly that only restricts competition.

7. It also believes that there must be a direct link between privatization and social needs.
8. Public sector companies and nationalized banks will be encouraged to enter the capital market to raise resources and offer new investment avenues to retail investors.” (Government of India, 2005).

6.6 Recent Developments in Policy

As per its commitment in NCMP, the government has established a Board for Reconstruction of Public Sector Enterprises to advise the government on ways and means for strengthening public enterprises in general and making them more autonomous and professional. Recently, the government has decided to establish National Investment Fund (NIF). All proceeds from disinvestment will be comprised to the NIF and will be spent on revival of public sector undertakings and on social sector. It has also set up Infrastructure Finance Company Ltd. (IIFCL), a special purpose vehicle (SPV) for funding infrastructure. (The Economic Times, 2005)

7. ACTUAL DISINVESTMENT

There is a wide gap between actual disinvestment and target pre-determined. Total target was Rs. 96800 crores and actual disinvestment since 1991-92 is Rs. 47646.43 crores. During 1995-96 to 2002-03, the government could

Table 1 : Actual Disinvestment from April 1991 onwards

(Rs. In Crore)

Year	No. of Co.s in which equity sold	Target for the year	Actual receipts	Methodology
1991-92	47 (31 in one tranche and 16 in other)	2500	3037.74	Minority shares sold in Dec 1991 and Feb 1992 by auction method in bundles of “very good”, “good” and “average” companies
1992-93	35 (in 3 tranche)	2500	1912.42	Shares sold separately for each company by auction method.
1993-94	-	3500	Nil	Equity of 6 companies sold by open auction but proceeds received in 94-95.
1994-95	17	4000	4843.10	Sale through auction method, in which NRIs and other persons legally permitted to buy, hold or sell equity, allowed to participate.
1995-96	5	7000	168.48	Equities of 4 companies auctioned
1996-97	1	5000	379.67	GDR (VSNL) in international market.
1997-98	1	4800	910.00	GDR (MTNL) in international market.
1998-99	5	5000	5371.11	GDR (VSNL) / Domestic offerings with the participation of FIIs (CONCOR, GAIL). Cross purchase by 3 Oil sector companies i.e. GAIL, ONGC & IOC
1999-00	5	10000	1860.14	GDR—GAIL, VSNL-domestic issue, BALCO restructuring, MFIL’s strategic sale and others
2000-01	5	10000	1871.26	Strategic sale of BALCO, LJMC; Takeover - KRL (CRL), CPCL (MRL), BRPL
2001-02 #	8	12000	5632.25	Strategic sale of CMC – 51%, HTL – 74%, VSNL – 25%, IBP – 33.58%, PPL – 74%, and sale of hotel properties of ITDC & HCI; receipt from surplus cash reserves from STC and MMTC
2002-03 #	8	12000	3347.98	Strategic sale: HZL (26%), IPCL (25%), HCI, ITDC, Maruti: control premium from renunciation of rights issue, Put Option - MFIL (26%), Shares to employees in HZL, CMC and VSNL.
2003-04	2	14500	15547.41	Jessop & Co. Ltd.(72% Strategic Sale), HZL (18.92% Call Option), through Public Offer-Maruti (27.5%), ICI Ltd. (9.2%), IBP (26%), IPCL (28.945%), CMC (26.25%), DCI (20%), GAIL (10.%) and ONGC (9.96%)
2004-05	3	4000	2764.87	NTPC (5.25% Offer for Sale), IPCL (5% to Employees) and ONGC (0.01%)
2005-06	1	0	1567.60	Offer for sale of MUL to institutions and employees of MUL
Total		96800	49214.03	

Figures (inclusive of control premium, dividend/dividend tax, restructuring and transfer of surplus cash reserves prior to disinvestment)
Source: Department of Disinvestment, Government of India, Disinvestment Till Now, from www.divest.nic.in

not achieve the target for each year. The target, actual disinvestment and methodology used each year have been given in Table 1.

8. UNDER-PRICING AND UNDERVALUATION OF SHARES

8.1 Valuations and Pricing of Shares

At initial phase of disinvestment, there was heavy criticism on under-pricing of shares. The government adopted a strategic sale as a modality of disinvestment and it has also come under hasty criticism due to under-valuation of PSUs. So the researcher felt it necessary to analyze critically the pricing and valuation. It is expected that the government has to value an enterprise prior to disinvestment to insure that national assets (family silver or national Patrimony) should not be handed over to private sector at throwaway prices. The valuation of shares or enterprise is an important component of disinvestment process.

Till March 1993, the Government raised Rs.4, 950 crores by disinvestment of PSUs shares, therefore, the Public Accounts Committee (PAC) held responsible the then Union Finance Minister Dr. Manmohan Singh and the then Industry Secretary Mr. Suresh Kumar, for under-realization of the value of the shares divested in 1991-92 and quantified the loss to be of the order of Rs.3, 000 crore in 1991-92 (Datt and Sundaram, 2006).

8.2 Under-Pricing of Shares and Loss to Government:

For the disinvestment in India at initial phase, a variant of tender offer method was used. The shares of PSUs were sold in bundles, which buyers could unbundle after three to six months. After that, in subsequent years, individual PSU shares were auctioned by tender process. But underwriters were not appointed so that there was no provision of getting the targeted revenue, if the issue resulted in the under-subscription. In the year 1991-92, the disinvestment was criticized for under-pricing of shares. The Comptroller and Auditor General of India in its report (No. 14 of 1993) relating to 'Disinvestment of Government Shareholding in selected Public Sector Enterprises during 1991-92' brought out the shortcomings in the process of disinvestment. Briefly the shortcomings were in formulating guidelines for valuation of shares, incorrect method of 'bundling', haste in accepting uncompetitive bids, re-fixation of reserve prices to accommodate those bids, and failure to incorporate 'claw-back provision'.

To estimate the extent of under-pricing in the U. K., Vickers and Yarrow (1988) have used the following methodology- They used the closing price on the first day of trading on the stock exchange for a PSU share to calculate the extent of appreciation or depreciation of the share relative to its offer price. This method implies acceptance of efficient market hypothesis. According to this hypothesis, the complete body of publicly available information about a company's prospect is interpreted correctly in the share price and the impact of the arrival of new data is incorporated instantaneously into the price. Vaidya (1995) has used a variant of Vickers and Yarrow method to estimate under-pricing of PSUs shares in Indian Disinvestment scenario.

Sudhir Naib (2004) has made similar exercise with 7 shares, but for the disinvestment in 1991-92 & 1992-93 he has taken 'current position' as on 28th March 2002. The time span is about 10 years, which does not permit the proper comparison because during the course, the capital structure has been changed in some cases. So it is thought that the current prices (taken by Naib) are not comparable with the average prices at which shares were disinvested. Hence, in the present study the researcher has adopted current prices as on 31st October 1992 as CAG has adopted the same. The present researcher adopted the similar methodology for estimating the extent of loss to the government due to under-pricing of shares. The researcher has restricted this exercise to 10 shares only. For assessing the extent of under-pricing of PSU shares at disinvestment in India, it would be useful to look into the comparison of the price at which shares were sold and the potential proceeds by adjusting the closing price on first day of trading by percentage movement of the Economic Times Index (ETI) for the relevant period.

The extent of loss to the government in respect of the disinvestment in ten leading PSUs in first two trenches has been presented in Table 2. In case of BPCL, shares had been sold for Rs.243.89 against the market price of Rs.750. The loss to the government was 208 per cent. The shares of BHEL were sold at Rs.38.05 against the market price of Rs.140. The loss to government in this case was identified at 268 per cent. In the disinvestment of HCL, shares had been sold at Rs.25.17 against the market price of Rs.65. It resulted in loss to government at 148 per cent. In case of HOCL, shares had been sold for Rs.56.93 against the market price of Rs.143.75. The loss to the government was 153 per cent. The shares of HPCL were sold at Rs.242.70 against the market price of Rs.550. The loss to government in this case was identified to be 127 per cent. In the disinvestment of HZL, shares had been sold at Rs. 21.65 against

Table 2 : The extent of loss to the government on account of PSU share disinvestment

Sl. No.	Name of PSU ²	Average price at which share value of Rs.10 was sold	Market price as per the Economic Times, 31.10.92				Loss to the government
				52nd week			
			Closing price 30.10.92	High	Low	Average	
		(Rs.)	(Rs.)	(Rs.)	(Rs.)	(Rs.)	(Rs.)
1.	BPCL	243.89	750	1275	650.00	962.50	506.11 (208)
2.	BHEL	38.05	140	200	130.00	165.00	101.95 (268)
3.	HCL	25.17	65	65	60.00	62.50	37.33 (148)
4.	HOCL	56.92	143.75	220	135.00	177.50	86.83 (153)
5.	HPCL	242.70	550	1200	550.00	875	307.30 (127)
6.	HZL	21.65	58.75	65	47.50	56.25	34.60 (160)
7.	HMT	18.11	80	85	67.50	76.25	58.14 (321)
8.	SAIL	13.24	42	80	41.25	60.62	28.76 (217)
9.	RCPL	9.87	43.75	55	41.00	48.00	33.88 (343)
10.	NLC	11.46	82	NA	NA	NA	70.54 (616)

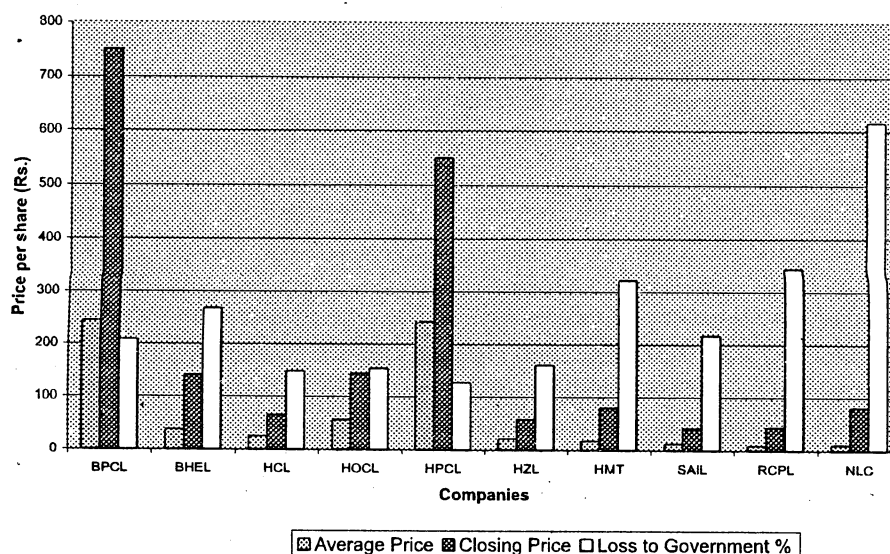
Source: Government of India (1992, Annexure III), Report No.14 of 1993, the Comptroller and Auditor General, New Delhi.

Note: 1. The loss has been worked by deducting the lowest of closing price on 30.10.92 or average of 52nd week from the average price at which shares have been actually sold.

2. Figures in brackets indicate the loss to the government in percentage terms.

the market price of Rs.58.75. It resulted in loss to government at 160 per cent. In case of HMT, shares had been sold for Rs.18.11 against the market price of Rs.80. The loss to the government was 321 per cent. The shares of SAIL were sold at Rs.13.24 against the market price of Rs.42. The loss to government in this case identified to be 217 per cent. In the disinvestment of RCPL, shares had been sold at Rs.9.87 against the market price of Rs.43.75. It resulted in loss to government at 343 per cent. In case of NLC, shares had been sold for Rs.11.46 against the market price of Rs.82. The loss to the government was 616 per cent. If we apply this percentage to the divestiture proceeds of 1991-92 and 1992-93, the potential proceeds would have been Rs.12554 crore as against the actual realization of only Rs.4, 904 crore. So the estimated loss accounts to Rs.7650 crore. There was no provision of getting the targeted revenue because underwriters were not appointed in these cases of disinvestment. The extent of loss to the government due to the under-pricing of PSUs shares has thus varied from 127 per cent to 616 per cent, and on an average the loss

**FIGURE 1
THE EXTENT OF LOSS TO GOVERNMENT DUE TO
UNDERPRICING IN DISINVESTMENT**



has been about 256 percent. If we apply this percentage to divestiture proceeds of 1991-92 (given in Table 6.3), then potential proceeds would have been Rs.77, 773 million, as against the Rs.30, 380 million that have actually been obtained. The extent of loss due to under-pricing has been graphically presented in Figure 1.

8.3 Valuation of PSUs:

From the year 1999-2000, Government of India has adopted modality of strategic sale in most of the cases of disinvestment in PSUs. The determination of reserve price is difficult task where most of the PSUs are either not listed on the stock exchanges or their shares are highly undervalued. In this situation, the valuation of the PSU becomes a challenging task.

Share valuation is a process whereby the value of the stock of a company is measured in Rupee terms. Disinvestments in the corporate world necessitates share valuation. Share valuation is a very new phenomenon to PSUs as the ownership, management and control of these enterprises till very recently rested with the government. In the present phase of economic liberalization, the government is disinvesting its shareholdings in many PSUs.

Based on recommendations of the Disinvestment Commission¹⁰ and in keeping with the best market practices, the following four methodologies are being used for valuation of PSUs: 1. Discounted Cash Flow (DCF) Method, 2. Balance sheet Method, 3. Transaction Multiple Method, 4. Asset Valuation Method

Although the aforesaid valuation methodologies being followed are broadly based on the Discussion Paper of the Disinvestment Commission and the best market practices, it is necessary to standardize the valuation methodology for all PSU disinvestments so that there are no variations from case to case. Therefore, all the four methodologies for valuation should be followed for all PSU disinvestments, with further improvements in respect of DCF Method and Asset valuation Method, for arriving at a range of valuation figures, to arrive at the indicative Benchmark or Reserve Price. It is very difficult to consider the particular method for share valuation for PSUs. The special features of the various techniques point out that no one method could meet the requirement of the situation. A basket of techniques needs to be used to arrive at fairly reliable estimate. For instance, for PSUs listed on the stock exchanges, the market value method would be the right choice. For companies with staggering investments but low profit-making, the net worth method would be appropriate although it would need to be modified to provide for inflation factor. For medium/ high profit making companies/ dividend paying companies, profit earning capacity value method would be an ideal choice. For companies with stable operations and moderate growth, the face value plus interest method could provide genuine estimate. There is no single method, which could be unanimously recommended for the share valuation in PSUs. The selection of methods would be guided by the significance of factors such as the quantum of investments, listings on stock exchanges, profit status, nature of operations and sensitivity of fixed assets base to the inflationary spiral etc (Misra, 1998).

According to Chief T. O. Fatolcum, a fellow of Nigerian Institute of Surveyors and Valuers, under-pricing would be tantamount to deliberate plundering of the national wealth and it would erode all public confidence in the administration. Overpricing would not only bring about mis-allocation of scarce resources, but it would also worsen the gulf between the rich and poor, since only the rich will be able to buy the overpriced enterprises (Faruqui and Sud, 2001). The government has obtained higher value than the 'reserve price' in almost all the strategic sales so far. But this issue came under criticism that valuation was carried out lower than justified and the valuation made by advisors was conservative. Although efforts have been made to streamline procedures for valuation of PSUs, yet the vested interests within the Government have been manipulating valuation process to the benefit of private companies by privatizing a number of profit-making PSUs at prices that are well below the intrinsic worth of assets which used to belong to the people of India (Datt and Sundaram, 2006).

9. CASES OF UNDER-PRICING AND UNDER-VALUATION:

Now we summarize some of PSUs and their disinvestment to see the cases of under-pricing of shares and under-valuation of PSUs.

9.1 Paradeep Phosphate Limited:

Zuari Maroc Phosphates, a 51:49 joint venture of K. K. BIRLA GROUP and Maroc Phosphate of Morocco, acquired PPL, a fertilizer company; it was a virtual stretcher case. As on March 2002, PPLs accumulated losses,

which were estimated to be a staggering Rs.625 crore plus besides outstanding liabilities of a whopping Rs.500crore (Bakshi and Singh, 2003). The valuation was made by the agency appointed by the Disinvestment Ministry, and it was at around Rs.250 crore. But the ministry rejected the same. The Ministry supported another team then brought down the valuation of PPL to almost less than half. The PPL was handed over to Zuari Maroc combine at Rs.151.7crore on the basis of practically single-bidding. 'The post closing adjustment clause, inserted in the sell-off agreement, was utilized by Zuari Maroc to claim Rs.192 crore from the government' Net result, the PPL has become a free gift to the Zuari plus Rs.41crore cash bonus! (Sen, 2003).

9.2 Bharat Aluminium Company Limited:

According to the CAG estimates, BALCO, which was sold to Sterlite Industries, was undervalued to the extent of Rs.300 crore (The Economic Times, 2003). Meanwhile, Sterlite Industries purchased 74% of BALCO shares for Rs.551.5 crores now claims that the government owes it more than Rs.16.7 crores because the company's new auditors contend that former PSUs assets and liabilities were wrongly valued (Thakurta, 2002).

9.3 Centaur Hotel Airport Mumbai:

Some instances have highlighted serious deficiencies in the valuation process. In 2001, Batra Hospitality, which bought the Centaur hotel near Mumbai airport for Rs. 83 crore, sold the same to the Sahara Group after 4 months for Rs.115crore, an appreciation of about 39% (The Economic Times, 2004). Land value itself is much more than the sale price, not to speak of the buildings and other properties. The questions arise are: why was the hotel under-valued and was there no lock-in-period? This also raises suspicion about the role of bureaucracy, which quietly but cleverly puts Government money into the private pocket of the so-called strategic partner or investor (Thakurta, 2002).

9.4 Indian Tourism Development Corporation:

The demerger route does yield benefits initially. Therefore, what the GOI did with ITDC's nine hotel properties and Hotel Corporation of India's (HCI) three spinning them off as separate entities with separate balance sheets and dividing the overall equity bases of the individual companies- did seem successful. The success is visible from the sale price of some of the prime properties like Qutab Hotel (Rs.35.67 crore), Lodhi Hotel (Rs.76.22 crore) and Centaur, Juhu (Rs.153 crore).

For these three properties, the buyers paid a hefty premium of between 17 times to 73 times the face value of the shares (face value Rs.100) and the figure was Rs.3900 per share in the case of Qutab Hotel. The GOI's realization should also be seen in the perspective that these hotels were loss-making.

ITDC's Lodhi Hotel was the worst case with net loss in the past three years. In 2000-01, it posed a loss of Rs.2 crore on sales of Rs.5.6 crore, which had come down from a peak of Rs.8.4 crore in 1996-97. HCI's Centaur, Juhu, posted a net loss of Rs.2.30 crore in 2000-01(Sales: Rs.30.90 crore). This was shocking as it had shown profits in the previous five years with the highest profit of Rs.19.13 crore in 1996-97(Sales: Rs.41.84 crore)(Singh, 2003).

In smaller cities like Agra, Madurai, and Rajgir, the properties attracted much lower valuation multiples. Especially, if one considers the fact that buyers were basically paying for the real estate. ITDC's property in Agra was sold for Rs.3.98 crore, or less than four times the face value.

Even Sushil Gupta, one of the promoters of the Delhi-based Hyatt who paid Rs.35.67 crore or 39 times the face value of the shares for Qutab Hotel, may have got the property cheap. That's because, apart from the 65 rooms, Qutab owns 30 apartments that have been leased out to various tenants. Now, if the new owner decides to get rid of these apartments through long leases, he could recover over 80% of the money, which he has paid for the entire property on very conservative pricing of Rs.1crore per apartment. Obviously, it is seen that the GOI did not take this into account while doing its calculations. The above discussion gives that there is a feeling that the GOI could have delinked the apartments from Qutab Hotel and sold them separately. The same logic can be applied to the number of dwelling units owned by PSUs in the townships situated next to their plants. Many of them can be separated from the manufacturing entity and sold off prior to the disinvestment (Alam, 2003).

The government had also to remit similar cash prizes to the buyer of ITDC Hotels. They got the hotels at throw-away prices and thereafter got back substantial portions of the money (Rs.27.5crore) they had paid, as post-closing adjustment (Sen, 2003). The ITDC after completing the sale of 18 privatized hotels has now sought a budgetary provision of Rs.42crores as 'post-closure' adjustment (Thakurta, 2002).

9.5 Indian Petrochemical Corporation Limited:

In this company also there were sharp discrepancies in valuation. The valuation had almost jeopardized the disinvestment process at a point of time. The Vadodra unit of Indian Petrochemicals Corporation Limited was valued at Rs.1234 crore by KPMG while Delott's Harkins valued it at Rs.3456 crore (The Economic Times, 2004). It was 3 times less than the later.

9.6 Computer Maintenance Company:

As per the ministry of disinvestment, CMC was valued at Rs.293.49 crore based on a discounted cash flow method, Rs.37.58 crore based on the assets valuation method, Rs.72.74 crore using the balance sheet method, and Rs.102.53 crore based on the comparable companies method. The Evaluation Committee computed the reserve price of Rs.108.88 crore for 51 per cent equity of CMC based on the discounted cash flow method. TCS acquired 51% of the CMC for Rs.152 crore from the government (effectively valuing the entity at Rs.330 crore.) Since this was the highest bid above the reserve price, it was accepted. Meanwhile, CMC shares were trading at a prior six-month average price of approximately Rs.284, indicating an entity value Rs.430 crore (or Rs.219 crore for 51 % equity). One naturally wonders to read the figures of valuation. To add more fuel to the fire, hardly anyone surrendered his/ her shares in the mandatory public offer made by TCS at Rs.281 per share- a clear indication that the market anticipated synergies in the acquisition beyond what was reflected in the Rs.281 offer price. And during the year 2002-03, CMC shares had touched a high (low) of Rs.736 (Rs.336), with the average daily price being Rs.518 (implying a valuation ranging from Rs.513 crore to Rs.1150 crore and an average value Rs.785 crore).

More interestingly, TCS actually paid a lower price (Rs.197 per share) to the majority shareholder (GOI) as compared to minority shareholder (Rs.284 per share). If at all, the majority stake should be associated with a control premium and trade at a higher valuation than a minority stake! After all, strategic sales are undertaken precisely to account for a control premium (Singh, 2003).

10. POST-CLOSING ADJUSTMENT

Then Ministry of Disinvestment had devised a provision of 'post-closing adjustment' in the sell-off agreement for the PSUs. It bid down that the government would make good to the private buyer the difference between the assets value presumed as on the date of the disinvestment and that at the end of the financial year as reflected in the balance sheet. The government (or then Minister) knew fully well that, post-disinvestment, the private owner will draw the balance sheet. Yet, this dubious clause was inserted to favour the chosen buyers (Sen, 2003).

The government had claimed that the prospective interest earning, at the market rate, on the sale proceeds of a particular PSU would come to much more than the dividend earned from that PSU. The disinvestment ministry has indulged in a statistical jugglery here. While calculating the interest on the sale proceeds, they did not take into account the money that flows out to the private buyer under the provision of 'post-closing adjustment'. On the other hand, the interest calculated on sale proceeds was only notional, as the government was nowhere going to park the sale proceeds in interest-bearing assets. Even this notional calculation could not justify the sacrifice of the sources of recurring income to the exchequer, in lieu of one-time money as sale proceeds. After all, 'selling the family silver for paying the butler' cannot be called economic prudence (Sen, 2003).

The government handed over the PPL to Zuari Marol at Rs.151.7 crore almost less than half of Rs.250 crore the value, which was estimated by earlier agency appointed by the Disinvestment Ministry. Zuari-Marol had made claim of Rs.192 crore as post-closing adjustment, while the PPL was acquired by it only for Rs.151.7 crore. It means they got the PPL as free gift with the cash bonus Rs.41 crore. BALCO was under-valued by Rs.300 crore. Sterlite Industries claimed Rs.16.7 crore as post-closing adjustment, in Balco case. Centaur Hotel Airport Mumbai was sold to Batra Hospitality for Rs.83 crore in 2001. After 4 months, they sold it for Rs.115 crore. This appreciation about 39% shows serious deficiencies in valuation process. So it is the case of under-valuation. Qutab Hotel of ITDC was sold to 'Hyatt' for Rs.35.67 crore, apart from 65 rooms, Qutab owns 30 apartments. The new owner could recover 80% of the money he paid for the entire property. The government did not take it into consideration the value of apartments attached to hotel properties and townships attached to other PSUs. ITDC's property in Agra was sold for Rs.3.98 crore or less than four times the face value. The buyer of ITDC hotels got the hotels at throw-away prices and thereafter got back substantial portion of the price (Rs.27.5 crore) they had paid, as post-closing adjustment. The valuation showed sharp discrepancies. The Vadodara Unit of IPCL was valued at Rs.1234 crore by KPMG while

Delottes Harkins valued it at Rs.3456 crore. TCS acquired 51% of the equity of CMC for Rs.152 crore from the government. This was highest bid above the reserve price of approximately Rs.219 crore for 51% equity. The claim of post closing adjustment resulted in ultimate reduction in the net proceeds. It was criticized that this dubious clause was inserted to favour the chosen buyers. To assess the extent of loss to government in under-pricing of shares, the researcher has adopted the method which uses the closing price on the first day of trading on the stock exchange for PSU shares to calculate the extent of depreciation or appreciation of the share relative to its offer price. This exercise has provided us the extent of loss in different cases in the first phase of disinvestment.

11. CONCLUSION

There was no provision of getting the targeted revenue because underwriters were not appointed in these cases of disinvestment. As given the fact that the pricing has not been done 'properly', the proceeds have been much less than the discounted value of future after-tax yields. The process of disinvestment should be made more transparent. The hypothesis to be tested was set- "In the process of privatization and disinvestment, the pricing at initial stage and the valuation of assets was made far lower than justified which resulted in the considerable loss to government." This hypothesis is accepted on the ground of obtained quantification of the extent of loss to government in selected cases. Before going for disinvestment, PSUs should be listed on stock exchanges. Government should not go for straight-way disinvestment in all PSUs. PSUs, which are facing certain problems, should be extended a well designed package and should be asked to perform turnaround in a given time or else face the eventuality. When disinvestment is made through public offering, underwriter should be appointed as precautionary measure. The guidelines issued by CAG, regarding the valuation and pricing of shares, should be strictly followed. Even before declaring reserve price, the opinion may be invited from the different strata of the society. After the analysis of these invited opinions, the reserve price may be declared. The mechanism of deciding the reserve price should be transparent. The highest value irrespective of methodology used should be taken for fixing 'reserve price'. The value of land and assets should be taken into account separately. Post-closing adjustment clause should be eliminated. The practice of considerable 'under pricing' of public sector shares and under realization of its assets resulting in considerable loss to government should be stopped immediately. The responsibility should be fixed up and the guilty should be punished.

NOTES:

1. The claw-back provision is to the effect that as and when these shares were subsequently sold by the institutions concerned to the general public, a reasonable fixed percentage of the gain would be transferred to the exchequer.
2. BPCL- Bharat Petroleum Corporation Limited, BHEL- Bharat Heavy Electricals Limited, HCL- Hindustan Cables Ltd., HOCL- Hindustan Organic Chemicals Ltd., HPCL- Hindustan Petroleum Corporation Limited, HZL- Hindustan Zinc Limited, SAIL- Steel Authority of India Limited, RCPL- Rashtriya Chemicals and Fertilizers Limited, NLC- Neyveli Lignite Corporation Ltd.

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