State-Owned Enterprises (SOEs) in India

EU Asia Corporate Governance Dialogue

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February 24, 2015

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- Evolution of SOEs in India
- Their Size and Performance
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- Issues and Concerns

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Evolution

- Post-independence economic policy
- Great emphasis on the role of state in industrial development
- “Mixed” economy
- Most SOEs were established under this policy
- Subsequently, in the 1960s & 1970S, there was nationalization (e.g. banks)

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Evolution

More Recent Trends

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Size & Performance

- 248 Central Public Sector Enterprises (CPSEs)
  - Both listed and unlisted
  - Apart from state-level enterprises
- Out of 220 operational CPSEs
  - 158 are profitable
  - 62 are loss-making
- 91 are listed on the stock exchanges
  - including banks and state-level PSEs
- Under 20% market capitalization on BSE
  - gradual decline though

Sources: Department of Public Enterprises, Annual Report 2012-13
BSE PSU

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Size & Performance

Empirical Evidence

CPSEs have generally done well on performance	Substantial contribution to the country's GDP	Several of them have outperformed private sector companies

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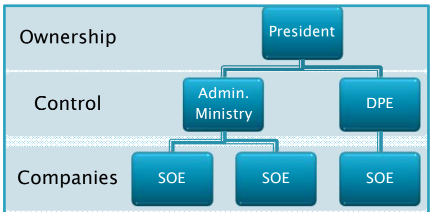
Corporate Governance Framework

Structural law – e.g. corporate law

- Listed SOEs – Clause 49 of the listing agreement
- Non-listed SOEs – guidelines from Department of Public Enterprises (DPE)
- Right to Information Act, 2005 (transparency)
- "State" under the Constitution (subject to writ jurisdiction of courts)

Corporate Governance Framework



Exercise of Control

Flexibility

- Maharatnas
- Navaratnas
- Miniratnas I
- Miniratnas II

Issues and Concerns

Private Sector

- Identifiable ownership
- Private benefits of control
- E.g. related-party transactions
- More tangible to put in place measures

SOEs

- No single ownership
- Interests rather diffused
- Political motivations
- E.g. focus on public interest
- More difficult to regulate

Identity of Controlling Shareholder

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Issues and Concerns

- Robust governance norms, but lack of proper implementation
- High levels of non-compliance by SOEs compared with private sector
- Boards not free from governmental interference
- Stakeholder interests preferred over minority shareholders

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Case Study 1

- Following board independence requirements, a study showed 13% firms were yet to comply
- Principal offenders were SOEs
- SEBI (securities regulator) initiated regulatory actions for non-compliance
- But, actions were dropped

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Case Study 1

- Approval of President not forthcoming
- Hence, non-compliance was not “deliberate or intentional”
- This result gives rise to a signaling problem
  - Negative consequences in the marketplace

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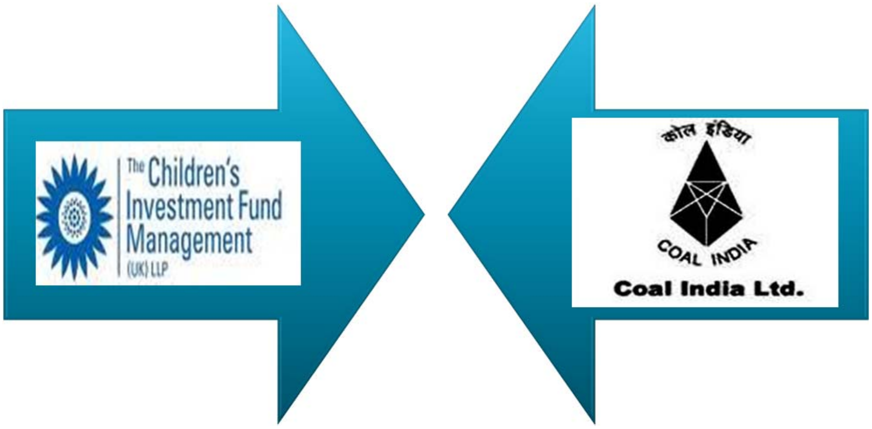
Case Study 2



Case Study 2

- The Government held 90% shares in CIL
- TCI acquired 1% shares in CIL's IPO
- TCI unhappy with CIL's management
- CIL was selling coal to other SOEs at 70% below international market price
  - Effectively a breach of fiduciary duties of directors

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Case Study 2

- CIL's board received instructions from the Government to sell at that price
  - Power to Government in CIL's articles of association
  - Disclosed in the IPO prospectus
- TCI initiated a derivative action (Mar. 2012)
  - First instance of aggressive shareholder activism in India
- But, later TCI exited the investment (Oct. 2014)
  - Cases withdrawn

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Conclusions: Way Forward

- Independent boards
- Minimal governmental interference
- Possible consolidation in holding structure (a Temasek / SASAC-type entity?)
- Greater recognition and protection of minority rights
- Better balance between shareholder and stakeholder interests

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THANK YOU