
Suvendu Bose

Poor performance has become a regular feature of the state-owned manufacturing enterprises in spite of their having experienced workforce, old brand reputation, etc. Most of them have fallen into a vicious cycle due to their prolonged poor performance.

The problem starts with the poor working capital position, leading to high raw material cost and uncompetitive final product pricing. This leads to the generation of a very low investible surplus. Not having investible surplus has forced the state-owned manufacturing companies to a financial situation where they are facing severe dearth of capital. The age-old plant and machineries coupled with outdated technology used for production face severe problem under the dearth of capital condition and the manufacturing units become incapable of generating sufficient investible surplus. Lack of modernization of machinery and upgradation of people skills lead to constraints in producing value-added product which have both market demand as well as the potential for greater contribution than the regular product. Therefore, the manufacturing companies continue to perform poorly, without any product-mix diversification. The poor operational performance also gets reflected in their financial performance. Despite having positive contribution at operating margin before direct labour, most of the state-owned manufacturing companies are incurring losses at Earning Before Interest, Tax, Depreciation and Amortisation (EBITDA) level, even under the best-case scenario, mainly because of huge amount of employee cost.

This paper suggests two solutions for these manufacturing companies – restructuring and disinvestments. The financial restructuring of the state-owned enterprises has become a unique programme in the country having the following key features:

- Broad political consensus has been arrived at on the financial restructuring programme.
- Unique and extensive stakeholder consultation process has been adopted to facilitate buy-in of staff associations and unions on restructuring proposals
- Innovative framework and principles have been established for:
  - categorization of enterprises
  - early retirement scheme for employees
  - Social Safety Net programme
  - financial restructuring
  - transparent and competitive bidding process with in-built safeguard
- A Public Enterprises Cell has been created for guiding the restructuring efforts.
- Impact of government’s budgetary resources is seen in reduction of the State loan exposure to the tune of around Rs. 344 crore, primarily through conversion of loans to equity.
- Impact on performance of enterprises identified for restructuring is reflected in the reduction in aggregate net loss to the tune of around Rs. 67.5 crore.

Further improvement of the state-owned enterprises has been recommended based on the lessons learnt during the process of financial restructuring. It is believed that opportunities do exist for widening the scope of the programme.
he world over, there has been a growing debate on the roles of the State in economic development. In an environment of increased globalization and liberalization, reforms in the public sector have been inevitable primarily for three reasons: (a) Greater economic efficiency through increased private initiatives in economic activities; (b) Achieving higher levels of economic growth and employment; and (c) Reducing budgetary deficit.

Although the first few national plans emphasized on the role of public sector units in the initial development of India, there has been a change in perception by the last decade of the previous century.

Preparations for unbundling of services and disinvestments at the national level started in 1984 when the first National Committee was set up to advise on public sector enterprise management. In this background, the Government of India undertook a reform agenda in 1991 for improving its financial position and the working of the state enterprises.

In 1991, the Central Government proposed to review public sector investments in order to limit their coverage to strategic, high technology, and essential infrastructure. The objectives of unloading government held equity were outlined as (1) furthering market discipline, (2) raising resources, and (3) encouraging wider public participation in the management of PSEs.

The process of public sector undertakings (PSUs) reform in India has been slow-paced and more orthodox as compared to other countries in the region. As disinvestments of Central PSUs began soon after the policy announcement in 1991, the states were required to develop their own disinvestment policy and identify PSUs for disinvestments to free the budgetary resource commitments. Many states, including Orissa, Andhra Pradesh, Madhya Pradesh, Uttar Pradesh, and Kerala started their process of restructuring public sector units through closure, reduction of equity, and complete divestiture of State PSUs. In contrast, one State Government that participated in the restructuring of its enterprises — the one which the author studied — initiated the process of reforms which was substantially different from that followed by the central government and other states in terms of both policy as well as implementation (hereinafter the state will be identified as ‘GoST’). The restructuring targeted only loss-making undertakings with a focus on turning around the PSUs aiming at long-term viability and unblocking of assets of structurally unviable PSUs to attain the objectives of justifiable economic growth and social development.

GoST embarked on public sector undertakings reforms for freeing the resources for infrastructural development to further economic growth in the state. Accordingly, the Public Enterprises Department (PED) was assigned the task by GoST, to evolve a transparent and consensual framework for the restructuring of loss-making PSUs. Based on PED recommendations, GoST decided that its loss-making PSUs that were becoming increasingly dependent on budgetary support, would be restructured in order to: (a) unblock the assets of PSUs that are structurally unviable for deployment in economic activity; (b) achieve viability under the continuing ownership of the government in respect of PSUs that have potential for viability without much investment, through a process of restructuring of their business, financial liabilities, and administration including manpower; and (c) achieve viability through a transparent joint venture transformation process in respect of PSUs requiring investment to achieve viability.

BACKGROUND OF RESTRUCTURING PSUs IN THE STATE

Unlike the central and many other state governments, GoST did not initially invest in many economic enterprises. The strength of its public sector undertakings is primarily due to the welfare approach of the government, which prompted the takeover of terminally sick private sector companies in order to protect the interests of the workers and creditors.

The majority of these enterprises have come from the private sector to the government through different modes of acquisition. At the time of their acquisition, they were all in the near-terminal stages of industrial ‘sickness’. The objective of the government was to protect the interests of the workforce; these acquisitions were not effected in consideration of their intrinsic potential for viability. Having taken over these industrial assets that inherently suffered from technological obsolescence and shrinking markets, the Government has discharged its responsibility towards the workforce by providing budgetary support as working capital loans year after year, to bridge the operating revenue deficits of these enterprises. The Govern-
ment’s constraints of resources have not, however, permitted adequate capital investments necessary for the modernization, diversification, and technology up-gradation that could bring viability to their operations in an increasingly competitive market environment. In view of this lack of viability, these enterprises have not been able to generate adequate resources to repay the loans provided by the Government, thereby accruing accumulating losses and a negative balance sheet that has denied them access to institutional resources for capital investment and working capital.

**Broad Objective of the Study**

The main objective of the current study is to ascertain the outcome of the different restructuring measures undertaken in the state-owned poorly-performing businesses depending on their nature of business and conditions of individual businesses. Pumping of fresh capital and abrupt reduction of resources may not always be the only solution for all the cases under study. The solution may even be found in outright selling of business, or the assets of the business if not the entire business. Financial restructuring may bring in solution for some businesses.

**Broad Steps Followed to Undertake the Study**

The following steps have been taken for the study:

**Step 1**: Study of the State as well as the Indian Policy Guidelines for Restructuring of PSUs

**Step 2**: Identification of the state-owned enterprises (SoEs) in consultation with the concerned authority

**Step 3**: Conducting initial round one-to-one interaction with the key managerial personnel of the 14 SoEs

**Step 4**: Collection, collation, and analysis of data/information from 14 SoEs

**Step 5**: Detailed study of the following aspects of individual companies:
- Infrastructural facilities available for production and other associated activities, which include condition and age of machinery, equipment, fund required for re-hauling, and replacement
- Maintenance facilities available
- Sources, availability, and procurement procedures of raw materials
- The product lines and/or services offered vis-à-vis market requirement and market demand
- Estimation of excess manpower, age profiling, and cost estimation for implementation of voluntary retirement scheme; identifying alternative source of human resources, if required (contractual)
- Ascertaining the soundness of industrial relations of individual companies
- Long-term and short-term financial resource management – budgeting, availability of resources, allocation of budget, and cost
- Detailed analysis of annual reports of all the companies under study
- Identification of Key Success Factors (KSFs) of individual units vis-à-vis major reasons for bottleneck in better performance.
- Undertaking peer group analysis with respect to consumption of raw materials and utilities (mainly power and water), human resources requirement, product quality and pricing, etc.

**Step 6**: Identification of general problems faced by the state-owned enterprises based on the studies and analysis undertaken in Steps 4 and 5

**Step 7**: Detailed interaction with the potential investors to know their perception regarding these companies and to ascertain their willingness to invest in these companies (SoEs)

**Step 8**: Categorization of companies based on the Policy Guideline and Strategy for Restructuring of the GoST PSUs (Step 1) as well as studies and analysis undertaken in Steps 3, 4, and 5

**Step 9**: Drawing of conclusions and recommendations on the possible methods of restructuring and key success areas of the financial restructuring based on Steps 4, 5, 6, 7, and 8.

**POLICY GUIDELINES AND STRATEGY FOR RESTRUCTURING PSUs**

The loss-making manufacturing enterprises of GoST have been categorized as ‘A,’ ‘B,’ and ‘C’ based on their extent of financial distress and operational capability to turn around. Like other state governments, the major bottleneck is the infusion of fresh capital, which these loss-
making enterprises required. These enterprises are all loss-making; however, the extent of financial bad health and operational capability differ from one enterprise to another. Some of these enterprises have extremely poor financial health and very old and outdated production facilities thus making it impossible for GoST to turn them around. Although these enterprises do not have any ‘business value’ by selling their assets, some fund may be realized. These enterprises are classified as ‘Category A’.

Then, there are enterprises which have substantial business potential; however, their operational infrastructure is so old that they require substantial amount of investment for turnaround. As mentioned earlier, GoST has fund constraint; it is unable to pump in the required fund to these enterprises. Therefore, these enterprises have been classified as ‘Category B,’ the stakes of which are targeted to be sold as business sale. To resist any special resolution to be passed against the interest of GoST, it retains 26 per cent stake.

‘Category C’ comprises of those loss-making enterprises, whose ownership GoST wants to retain. The amount of capital infusion required for turnaround of these companies was not substantial; hence GoST could afford to pump-in the same. These enterprises also provided ‘Quick-Return’ to GoST.

Therefore, the guidelines and strategies that have been thus evolved for restructuring of GoST-owned loss-making manufacturing enterprises are as follows:

**Category A:** A few of these enterprises have become non-functional due to their basic structural unviability. The government has, notwithstanding their status, continued with budgetary support towards meeting the employment cost of these enterprises over the years. As a consequence, the assets of these enterprises have remained blocked. The government now seeks to release the assets of these structurally unviable enterprises to allow their deployment in economic activity for contributing to the State’s economic growth.

Therefore, structurally unviable enterprises that have no scope for revival, are to be formally closed to permit the release of their assets for deployment in economic activity.

**Category B:** A second category of loss-making manufacturing enterprises are those that require investments for modernization of their obsolete manufacturing processes and for product diversification, to attain viability. Instead of continuing with such enterprises accumulating losses due to lack of investment from the government, it has been decided to open these enterprises to private investment as joint ventures to facilitate their attainment of viability and contribute to the growth of the State Domestic Product (SDP). This will result in a further decrease in claims upon the States’ budgetary resources to subsidize their operating losses.

**Category C:** A third category of loss-making manufacturing enterprises are those that are presently earning a fair share of their total expenditure with the government providing budgetary support to balance the deficit. These enterprises have a market share and possess brand equity and are in a position to achieve viability with necessary restructuring measures. The government will retain ownership of these manufacturing enterprises with the enforcement of well-considered restructuring measures that will facilitate their access to institutional resources and end their dependence on budgetary support.

The state government’s emphasis is thus on facilitating the evolution of a vibrant and self-reliant public sector that will catalyze economic growth in the State.

**PROBLEMS FACED BY LOSS-MAKING STATE-OWNED ENTERPRISES**

Poor performance has become a regular feature of the state-owned manufacturing enterprises in spite of their having experienced workforce, old brand reputation, etc. Most of them have fallen into a vicious cycle due to their prolonged poor performance. It is true that all the manufacturing companies do not face the same problem as the market and industry characteristics of individual com-
panies are different from each other. However, the basic problems remain the same across all industries. That is why though the issues and challenges faced by the state-owned manufacturing enterprises today are quite diverse, the basic principles to be followed for their solution are somewhat similar.

The issues and challenges faced by the state-owned manufacturing enterprises can be expressed as a vicious cycle. All the factors mentioned in Figure 1 create a chain system, the terminal of one being joined with the other, finally closing the loop and creating a circular problem. In such cyclical problems, one reason for non-performance leads to the other reasons for non-performance. In the following paragraphs, we will see how, starting from a particular point on the cycle, we will come back to the same point.

**Working Capital**

The problems of state-owned manufacturing enterprises start from the dearth of working capital. The working capital requirement ranges from 2 months sales value to as high as 10 to 11 months sales value depending on the industry characteristics. Due to the declining performance of these manufacturing companies, it is becoming very difficult for them to accrue the required fund for working capital. At the same time they have lost their credit worthiness for obtaining working capital loans. As a result there is a severe shortage of working capital resulting in no raw material stock, no finished goods stock, and a minimum level of spare parts inventory.

**Cost of Raw Material**

The next bottleneck is high raw material cost. It constitutes a major percentage of sales value and is therefore an important factor in determining the product price. Even if the state manufacturing companies know that the raw material from alternate sources will cost them lesser than the existing sources (e.g., imported raw material *vis-à-vis* the indigenous one), they cannot switch over mainly due to their inadequate working capital position. Even from the point of view of quality, sometimes raw material from the imported source is better than the indigenous one and therefore, requires lesser quantity than the indigenous raw material to produce the same quantity of final product, in the process reducing the raw materials component in the final product pricing. However, the state-owned manufacturing enterprises cannot shift their raw material resources due to huge requirement of working capital. This finally leads to higher raw material cost, thereby also enhancing the product prices.

**Product Pricing**

As explained above, product pricing for the state-owned manufacturing enterprises becomes non-competitive (due to high raw material cost) with respect to their private sector competitors. Moreover, even quality-wise (due to use of better raw materials), the private sector products are more attractive to the customers than the state manufacturing companies’ products.
Low Contribution and Loss of Revenue

High prices and lack of appeal of the products are leading to loss of market at the marginal contribution levels. On the one hand, the sales volume is going down in competition to the private sector and on the other hand, the profit margin is going down due to high cost of raw materials. There is therefore loss of revenue and low contribution from the products manufactured by the state-manufacturing units.

Low Investible Surplus

Low contribution from the products and loss of revenue lead to the generation of a very low investible surplus. Since there is loss of revenue generation, whatever revenue is generated through sale of products gets consumed for meeting the costs of production under different heads. In most of the state-owned enterprises, the Profit and Loss account shows a negative figure after accounting for depreciation, amortization, and tax (if any). Therefore, there is no money left for company reserves and surplus account. Such kind of business operation for a prolonged period results in no investible surplus for these companies.

No Capital for Modernization

Not having investible surplus has forced the state-owned manufacturing companies to a financial situation where they are facing severe dearth of capital. Most of the state-owned manufacturing facilities – not only plant and machineries, but also technology – are outdated. They do not have resources for undertaking R&D activities. Moreover, the condition of maintenance is extremely poor. For re-hauling of these facilities and modernization of manufacturing system, a huge amount of capital is required, which these companies do not have. Moreover, these state-owned manufacturing companies cannot afford to hire specialists with appropriate skills and expertise due to poor financial condition. They are not in a position to pay the experts at the market rate. Thus poor, outdated manufacturing facilities coupled with lack of expert supervision lead to quality deterioration in the final product, loss of market, and lack of commercial orientation in the overall business.

Limitation on Value Added Products

Lack of modernization of machinery and upgradation of people skills lead to constraints in producing value-added product which not only has market demand but also provide higher contribution than the regular product. Product mix diversification not only gives higher contribution but also protects the companies from getting eroded due to product life cycle and helps in occupying a greater market share. Therefore, the manufacturing companies continue to perform poorly, without any product-mix diversification.

Deteriorating Performance

The ultimate result of all the points mentioned above leads to poor and continuously declining performance of state-owned manufacturing enterprises. The declining performance is incapable of generating working capital for future production.

Therefore, the poor performance for lack of required level of working capital continues.

Financial Performance of State-owned Manufacturing Enterprises

As far as financials of these companies are concerned, at a gross margin level (sales value less the cost of raw material), most of the companies show a positive contribution. Even at the level of operating margin before direct labour cost (gross margin less stores and spares cost, power and fuel cost, repair and maintenance cost and other direct expenses), barring a few companies, most of the companies show a positive value. Out of the above-mentioned cost components for determining operating margin before indirect cost (including employee costs), power and fuel costs are the major ones. For all the manufacturing companies, power and fuel cost components are considerably higher than the industry norm, mainly because of extremely low level of capacity utilization by the state-owned manufacturing companies. Moreover, outdated machineries and their poor maintenance lead to higher consumption of power and fuel.

In almost all the cases, production planning and capacity utilization are dependent on the position of sales order. However, there is no marketing effort to enhance the order position as well as the capacity utilization of the plant. There is hardly any incentive for marketing. A low level of production leads to a low level of distribution of fixed cost; hence there is an increase in production cost.

Despite having a positive contribution at operating mar-
gin, most of the state-owned manufacturing companies are incurring losses at Earning Before Interest, Tax, Depreciation, and Amortization (EBITDA) level, even under the best-case scenario, mainly because of the huge employee cost. In some cases, employee cost is 2 to 3 times of the annual sales value and in most of the cases, the employee cost is substantially higher than the industry norm. High employee costs are mainly due to more employment than required and narrow difference between the salary level of the highest and the lowest paid employees.

**THE PILOT STUDY**

A pilot study for restructuring of fourteen State-Owned Enterprises (SoEs) was conducted. The author was the leader of the study team and visited and studied the operations of all these 14 companies.

The key financials as well as categorization of enterprises, recommendations, and conclusions drawn based on the outcome of this pilot study have been provided in the Annexure.

The study adopted two different methodologies and principles depending upon the category of enterprises:

Methodology & Principle I: For 10 enterprises (Categories ‘A’ and ‘B’)

Methodology & Principle II: For 4 enterprises (Category ‘C’)

**Restructuring of 10 Enterprises (Categories ‘A’ and ‘B’)**

As mentioned earlier, a company’s categorization as ‘A’ or ‘B’ was dependent upon its future earning potential, and thus on the future business proposition and the amount of further capital infusion required for business revival. Otherwise, the business would have only asset value, but no business value.

Ten enterprises were identified as belonging to Categories ‘A’ and ‘B.’

**Stages of the Study**

The methodology and principles were divided into four stages:

**Stage I:** ‘Restructuring phase’ comprising studies of the businesses of 10 enterprises.

**Tasks undertaken:** Determination of their earning potential and offering recommendations with the objective of securing private investments in equity up to 74 per cent; suggesting short-term measures for quick improvements in their earning potential; expansion of their equity base through debt conversion, etc.; and suggesting potential investors for their enterprises.

These 10 enterprises were designated as Company 1 to Company 10.

**Stage II:** ‘Qualification phase’ for the 10 enterprises.

**Tasks undertaken:** Drafting of Qualification Criteria (QCs) of potential investors; Preliminary Information Memoranda (PIMs) in respect of the enterprises; and draft invitations for Expression of Interest (EOIs) by potential investors, for approval of the PE Department.

**Stage III:** ‘Bidding phase’ for the 10 enterprises with which the government had decided to proceed further taking the results of Stage II into consideration.

**Tasks undertaken:** Preparation of a “Bid Pack” for approval of the PE Department that included a detailed Information Memorandum (IM), Confidentiality Agreements (CAs), Shareholders and Share Purchase Agreements and Notices inviting separate Technical and Price Bids for purchase of up to 74 per cent equity in the enterprises.

**Stage IV:** ‘Contracting phase’ for the offers with which the PE Department had decided to proceed further.

**Tasks undertaken:** Divising the completion of all legal and accounting measures till the conclusion of the Shareholders and Share Purchase Agreements.

**Restructuring of Four Enterprises (Category ‘C’)**

‘Category C’ comprises of those loss-making enterprises whose ownership GoST wants to retain. The amount of capital infusion required for turnaround of these companies was not substantial; hence GoST could put in effort to pump in capital. These enterprises also provided ‘Quick-Return’ to GoST.

**Tasks undertaken:** The four enterprises under Category ‘C,’ undertook determination of business optimization plans for achieving viability which are mainly different measures for business and financial restructuring includ-
ing improvement in management and governance. These four enterprises were designated as Company 11 to Company 14.

Objectives for Financial Restructuring

The objectives underlying the financial restructuring exercise have been detailed below:

- The financial restructuring exercise should enable this category of organizations to approach banks/financial Institutions for funding its future expansion/modernization. The proposed financial restructuring plan therefore addressed the following issues:
  - With the company barely managing to break-even at the operating level, there ideally should not be any debt serviceability obligations as this would strain cash flows.
  - The restructured balance sheet should comprise minimum accumulated losses and other intangible assets like unrealizable debts, obsolete inventory, etc.
- The cash outflow on financial restructuring on account of incremental income-tax liabilities and/or fees payable to the Registrar of Companies (RoC) on increase of authorized capital should be minimized to the extent possible.

Assumptions for Restructuring

- The financial restructuring plan had been developed based on outstanding unsecured GoST loans and unpaid interest thereon as on March 31, 2004. Any subsequent GoST loan and/or incremental interest accruals on or after April 1, 2004 would have been considered at the time of implementation of the financial restructuring plan.
- The income tax liability on financial restructuring has been computed based on the tax audit reports and tax returns for the assessment year 2003-04 or earlier. Consequently, profit figures available for calculation of income tax, on account of incremental loss during the assessment year 2004-05, have not been considered.

Options Considered for Restructuring

Based on the objectives identified above, the following alternative financial restructuring options have been considered:

Option I

- Conversion of a part of the unpaid interest on unsecured GoST loans to equity shares.
- Repayment of the entire outstanding principal of unsecured GoST loans and balance sheet interest through a one-time non-refundable grant-in-aid of the nature of promoter’s contribution from GoST. The repayment and grant-in-aid would be mere book entries and would not be backed by any cash inflow/outflow.

Option II

- Conversion of the entire outstanding principal of unsecured GoST loans and unpaid interest to equity shares by issuing at face value.
- Subsequent rationalization of the issued share capital through a scheme of capital reduction to be effected after 1-2 years of implementing financial restructuring. The share capital not represented by tangible assets will be cancelled as part of the capital reduction exercise. The accumulated losses in the balance sheet can be written off against the cancelled share capital at the time of capital reduction.

Option III

- Conversion of the entire outstanding principal of unsecured GoST loans and unpaid interest to equity shares by issuing at a premium.
- Subsequent rationalization of the issued share capital through a scheme of capital reduction to be effected after 1-2 years of implementing financial restructuring. The share capital not represented by tangible assets will be cancelled as part of the capital reduction exercise. The balance in the share premium account can also be used to write off part of the accumulated losses being carried in the balance sheet.

Options Preferred

Based on the above assessment, option II, i.e., conversion of the entire outstanding principal of unsecured GoST loans and unpaid interest to equity shares at face value is preferred due to the following reasons:

a) The objectives underlying financial restructuring, viz. (i) Minimizing future debt servicing obligations; (ii)
Cleaning up the balance sheet in terms of accumulated losses; and (iii) Minimizing the cash outflow on financial restructuring are met by this option.

b) It complies with the existing income-tax regulations unlike option III where it may be difficult to justify issue of shares at a premium to the income-tax authorities.

Given that one of the primary objectives underlying financial restructuring is cleaning up of the Balance Sheet of the company, it is recommended that these organizations examine their current assets and liabilities from the viewpoint of recoverability/need to pay and effect a one-time write-back/write-off as part of the financial restructuring exercise.

**KEY SUCCESS AREAS OF THE FINANCIAL RESTRUCTURING PROGRAMME**

Financial restructuring of the state-owned enterprises has become a unique programme in the country resulting in the following key benefits:

- Broad political consensus has been arrived at on the financial restructuring programme.
- Unique and extensive stakeholder consultations process had been adopted to facilitate buy-in of staff associations and unions on restructuring proposals
- Innovative framework and principles have been established for:
  - categorization of enterprises
  - early retirement scheme for employees
  - social safety net programme
  - financial restructuring
  - transparent and competitive bidding process with in-built safeguard
- A Public Enterprises Cell has been created for guiding the restructuring efforts

**Impact of Government Budgetary Resources due to Financial Restructuring**

There was a reduction of GoST loan exposure to the tune of around Rs. 3,440 million, primarily through conversion of loans to equity. The reduction of government loan due to the financial restructuring process and changes in net profit/loss of the Category ‘C’ enterprises have been provided in Tables 1 and 2 respectively.

<table>
<thead>
<tr>
<th>Table 1: Outstanding Government Loans for Category ‘C’ Enterprises (in Rs. million)</th>
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<tbody>
<tr>
<td>Enterprise</td>
</tr>
<tr>
<td>Company 11</td>
</tr>
<tr>
<td>Company 12</td>
</tr>
<tr>
<td>Company 13</td>
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<tr>
<td>Company 14</td>
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<tr>
<td>Total</td>
</tr>
</tbody>
</table>

Source: Report of C&AG

<table>
<thead>
<tr>
<th>Table 2: Impact on Performance of Category ‘C’ Enterprises Identified for Restructuring (in Rs. million)</th>
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</thead>
<tbody>
<tr>
<td>Enterprise</td>
</tr>
<tr>
<td>---</td>
</tr>
<tr>
<td>Before Restructuring (FY 03)</td>
</tr>
<tr>
<td>Company 11</td>
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<tr>
<td>Company 12</td>
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<tr>
<td>Company 13</td>
</tr>
<tr>
<td>Company 14</td>
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<tr>
<td>Total</td>
</tr>
</tbody>
</table>

* Data available only for FY 05

Source: Report of C&AG

**CONCLUSION**

The question is how to overcome the problems to make the state-owned enterprises viable. As mentioned earlier, the issues and challenges faced by the state manufacturing enterprises are trapped in a vicious cycle. Therefore, the only solution lies in breaking this cycle. As envisaged above, the easiest way of achieving this will be to put in more money in the business as working capital so that other associated problems can be addressed one after another. However, pumping in money as working capital will be a short-term solution. For bringing a sustainable development and prospect for these companies, two long-term solutions are left for these manufacturing companies — restructuring and disinvestment. However, restructuring of these companies sometimes becomes difficult, since it involves reduction of manpower, which not only creates socio-political problem (which can be addressed through planning of proper social safety net), but also makes it difficult to achieve the targeted enhanced production level. This can only be sorted out through contractual employees at a lower cost.
On the other hand, these companies have lost their lustre for attracting investors who can put in money into their operation in case of disinvestments. Most of these manufacturing companies have a negative earning potential and thus do not offer any business value. In case of companies having no business value, the only option remaining is asset sale. However, even in the case of asset sale, the asset value will reduce drastically mainly due to (1) long outstanding liabilities, provision for which have not been given in the annual accounts, (2) a substantial portion of plant and machinery (P&M) not being used for long time, (3) poor condition of infrastructure and P&M, (4) last but not least, low demand of land for industrial usage.

Therefore, the implementation methodology for the above-mentioned suggestions should follow a step-wise approach. The first step should be to take some ‘quick measures’ like restructuring of companies through reduction of manpower, optimization of raw material costs, enhancing marketing efforts, etc. This step will focus on reduction of net losses as well as making the company more attractive to the future investors which would ultimately result in better value for the company.

After successful implementation of the first step, the next step will be to undertake the disinvestment process starting from invitation to ‘Expression of Interest (EOI)’ to selection of potential investors by issuing ‘Request for Proposal,’ evaluation of proposal and undertaking negotiation process.

Though from the above discussions, it appears that addressing the issues faced by the state-owned manufacturing enterprises becomes really difficult for the government, these problems are not unsolvable. Merely pouring in money may not solve the problem; it should be coupled with a well-thought-out strategy for implementing change management for survival of these companies. These state-owned manufacturing enterprises are thus going to pose a real challenge for the Governments in the coming years.

### Annexure: Summary of 14 Companies of GoST

<table>
<thead>
<tr>
<th>No.</th>
<th>Name of the Company and Major Products/Activities</th>
<th>Year of Establishment</th>
<th>Category</th>
<th>Accumulated Loss in Rs. Million</th>
<th>Networth in Rs. Million</th>
<th>Outstanding Loan &amp; Interest in Rs. Million</th>
<th>Earning Potential and Key Recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td><strong>Company 1</strong>&lt;br&gt;Manufacture of metal zippers, bottom stops and cotton tapes; jeans and baggage (procured and traded)</td>
<td>1954</td>
<td>A</td>
<td>364.70 as on 31.03.2002</td>
<td>(-)363.94 as on 31.03.2002</td>
<td>359.93 as on 31.03.2002</td>
<td>• It is felt that Company 1 does not offer a viable business proposition in the core areas and has a negative earning potential. There has not been any positive feedback from potential investors in this industry.&lt;br&gt;• Against the above negative earning potential, the asset value would be around Rs.29.67 million (as per the valuer’s report in 2002).&lt;br&gt;• Since the company does not have any ‘business value’, GoST should try to sell the assets of the company.</td>
</tr>
<tr>
<td>2</td>
<td><strong>Company 2</strong>&lt;br&gt;Biscuits</td>
<td>1887</td>
<td>A</td>
<td>385.10 as on 31.03.2002</td>
<td>(-)376.40 as on 31.03.2002</td>
<td>561.15 as on 31.03.2002</td>
<td>• The company does not have business value, thus GoST should try for selling the assets of the company.&lt;br&gt;• However, as far as asset value realization is concerned, it will have very less value since plant &amp; machineries are very old with outdated technology and one of its unit has been designated as “Heritage Property” (hence cannot be sold)</td>
</tr>
<tr>
<td>No.</td>
<td>Name of the Company and Major Products/Activities</td>
<td>Year of Establishment</td>
<td>Category</td>
<td>Accumulated Loss in Rs. Million</td>
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<td>Earning Potential and Key Recommendations</td>
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<tr>
<td>3</td>
<td>Company 3 Glass bottles, glass tumblers and glazed wall tiles</td>
<td>1948</td>
<td>A</td>
<td>438.52 as on 31.03.2001</td>
<td>(-) 408.52 as on 31.03.2001</td>
<td>614.47 as on 31.03.2001</td>
<td>• It is felt that Company 3 does not offer a viable business proposition and has no business value excepting for the new tiles plant; the tiles it produces are obsolete in the market. Market responses also indicate that there are no potential investors interested in the glass plant. The glass plant along with the other disposable asset should be sold as “asset sale” (around Rs. 105.0 million for unutilized/surplus land as per Asset Valuation Report prepared in Dec’02 plus scrap value of glass plant and machinery).</td>
</tr>
<tr>
<td>4</td>
<td>Company 4 Plywood, block board &amp; flush door</td>
<td>1950s</td>
<td>A</td>
<td>207.40 as on 31.03.2002</td>
<td>(-) 210.30 as on 31.03.2002</td>
<td>210.20 as on 31.03.2002</td>
<td>• It is felt that Company 4 does not offer a viable business proposition and has negative earning potential both under “As-is” case and “Best Case Scenario” with short-term restructuring and improved workforce. Market responses from large branded players corroborate to the same. • Against the above negative earning potential, the asset value as revalued in 2002 stands at Rs. 562 million. However, as highlighted in the report this seems to be on the higher side. The valuation of plant &amp; machinery provided in the asset valuation report, as Rs. 197 million may still be lower as Rs. 4.0 millions P&amp;M are not being used and the rest may fetch lower realization because of its obsolescence.</td>
</tr>
<tr>
<td>5</td>
<td>Company 5 Forklifts, bus body fabrication and renovations, disaster management equipment</td>
<td>1940</td>
<td>B</td>
<td>275.19 as on 31.03.2002</td>
<td>(-) 265.69 as on 31.03.2002</td>
<td>292.74 as on 31.03.2002</td>
<td>• It is felt that there exists an opportunity for joint venture in this company (business value) only if a potential investor is willing to use the limited facilities in the company for fabrication of quality bus bodies. Initial response has been positive from a couple of players. In this case the business value ranges from Rs. 5.0 – 7.0 million. • Against the above business value, the asset value as revalued in 2002, stands at Rs. 27.516 million. However, as has been highlighted in the report, this seems to be on the higher side. Also, land is leased to the company and hence building/sheds (estimated at Rs. 13.602 million) has little value in case of an “asset sale”.</td>
</tr>
<tr>
<td>No.</td>
<td>Name of the Company and Major Products/Activities</td>
<td>Year of Establishment</td>
<td>Category</td>
<td>Accumulated Loss in Rs. Million</td>
<td>Networth in Rs. Million</td>
<td>Outstanding Loan &amp; Interest in Rs. Million</td>
<td>Earning Potential and Key Recommendations</td>
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| 6   | Company 6 Injection moulding machines and polymers | 1940                  | A/B      | (-) 470.67 as on 31.03.2002     | 513.90 as on 31.03.2002 |                             | • In the best possible scenario, i.e., at production and sales of 48 machines with 20% having high technology (technology from a collaborator), the company can generate an EBITDA of Rs. 16.30 million only. The net free cash flow is only Rs. 10.60 million after deducting the cost of adequate working capital amounting to Rs. 5.70 million. But to produce 48 machines, capital expenditure to the tune of Rs. 82.50 million is to be incurred over a period of 3-4 years with a present value of Rs. 56.0 million. In this case the business value would be negative.  
• The polymer division is currently making negative contributions to the company. If the division operates at full capacity and earns sales consideration at current market price, the EBITDA would be negative making the business value negative.  
• Against the above business value, the asset value as revalued in 2002 stands at Rs. 57.883 million. However, this seems to be on the higher side. Also, land is leased to the company and hence building (estimated at Rs. 41.519 million) has little value in case of an “asset sale”. |
| 7   | Company 7 Copper and copper alloy extrusion products – Rods, squares & hexagonal, flat, sections, wires. | 1942                  | B        | 498.06 as on 31.12.2002          | 482.59 as on 31.12.2002 |                             | • It is felt that Company 7 does not offer a viable business proposition and has negative earning potential both on ‘as is’ basis and under the best case scenario. Market responses also indicate that there are no potential buyers or joint venture partners from amongst the consumers and competitors. However, a few (around three) national and international traders and end-users of copper and copper alloys extrusion products already showed/submitted their expression of interest to GoST either for becoming a joint venture partner or for investing money for Company 7. These cases required to be explored further before taking any final decision.  
• Against no business value, the asset value as revalued in June, 2002 stands at Rs.65.554 million. However, the valuation of P&M provided in the asset valuation report as Rs. 13.60 million may still be lower because of its obsolescence and no residual value. |
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| 8   | Company 8 Cold Twisted Deformed (CTD) steel bars and round bars that are being manufactured in the Rolling Mills since late 2001; prior to this, the enterprise was trading in rolled steel products. | 1934 | B | 1040.70 as on 31.12.2002 | (-) 795.50 as on 31.12.2002 | 1111.70 as on 31.12.2002 | ▪ It is felt that Company 8 has some business value to the competing rollers, who are interested about their rolling mills. Valuer’s assessment for the rolling mill and associated land is around Rs. 84 million.  
▪ For mid-sized diversified business groups, the primary motivator would be large land holding of Company 8. Some of the companies in this category may also be interested in the rolling mill as a potential diversification opportunity. Valuer’s assessment of the documented unutilized un-encroached land is around Rs. 380 million. |
| 9   | Company 9 Construction of vessels for coastal and riverine shipping (shrinking market segment because of global competition), repair, general engineering works and engineering project jobs. | About a Century Back | B | 665.50 as on 31.03.2010 | (-)646.20 as on 31.03.2010 | 788.80 as on 31.03.2010 | ▪ It is felt that Company 9 has some business value to the competing ship builders and repairers based on its building and machinery, which is estimated at Rs. 37.60 million as per asset valuation report.  
▪ For the mid-sized diversified business groups, the value would be driven primarily by the value of building and structures, which is estimated at Rs. 14.80 million as per asset valuation report. |
| 10  | Company 10 Pharmaceutical grade fine chemicals, bakery chemicals, industrial chemicals and ISI certified packaged drinking water | 1961 | A | 139.10 as on 31.03.2010 | (-) 137.70 as on 31.03.2010 | 179.50 as on 31.03.2010 | ▪ For chemical manufacturers, the value proposition is only asset valuation, which is estimated at Rs. 656 lakh.  
▪ For the competing PWD, value would depend primarily on the packaged drinking water plant and the value of the fixed assets is estimated at Rs. 23.30 million, including land.  
▪ For diversified businesses, value would be driven primarily by the value of land. The valuation exercise has indicated a value of Rs. 71.90 million, without considering the value of plant and machinery. |
<p>| 11  | Company 11 Caustic soda, Chlorine, Bleaching powder, Hydrogen gas, Dichlorobenzene and other chloro-products | 1960 | C | 2,565.80 as on 31/03/2001 | (-) 2,514.90 as on 31/03/2001 | 2,617.30 as on 31/03/2001 | ▪ Company 11 appeared to have substantial business value inspite of its bad past financial performance. At the same time it was envisaged that to revive the company, GoST does not require huge fund; only certain revival steps were required to be taken. Hence it was recommended to GoST to retain Company 11 and take the necessary revival steps to bring out the company from its financial disaster. |</p>
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<tr>
<td>12</td>
<td><strong>Company 12</strong>&lt;br&gt;Pethidine hydrochloride; medical formulations as tablets, ORS powder, capsules, injectable lotions and ointments</td>
<td>1987</td>
<td>C</td>
<td>(-) 509.70 as on 31/03/2001</td>
<td>626.70 as on 31/03/2001</td>
<td>GoST has been advised to retain the company with actions to be taken for revival of the company.</td>
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<tr>
<td>13</td>
<td><strong>Company 13</strong>&lt;br&gt;Railway brakes systems for diesel &amp; EMU Coaches; Railway signaling systems; Route relay inter-locking projects for Railways; Civil construction projects</td>
<td>1923</td>
<td>C</td>
<td>(-) 2,771.29 as on 31/03/2001</td>
<td>2,965.00 as on 31/03/2001</td>
<td>Company has the future business potential to revive without much of fresh capital infusion. Therefore, GoST has been advised to revive the company, instead of going for disinvestment.</td>
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<tr>
<td>14</td>
<td><strong>Company 14</strong>&lt;br&gt;Tea machinery, jute machinery, road rollers and spares; fabrication &amp; machining of engineering spares, jobbing work</td>
<td>Early 1950s</td>
<td>C</td>
<td>(-) 573.30 as on 31/03/2001</td>
<td>636.80 as on 31/03/2001</td>
<td>Company has future business potential to revive without much of fresh capital infusion. Therefore, GoST has been advised to revive the company instead of going for disinvestment.</td>
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**Notes:**
1. It is to be noted that the entire study is the outcome of a consulting assignment. It is based on the study of operations of the respective companies – production, maintenance, marketing and HR function; analysis of annual reports & MIS reports; collecting market feedback; interacting with potential investors through structured questionnaires; financial projections and analysis through development of financial models. Therefore, for the sake of academic ethics, I am hereby certifying that the study is completely based on primary data. No published data/information/paper has been referred to for undertaking this study.
2. The opinion and interpretation presented in this paper are entirely that of the author, and not of the organization he belongs to.

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RESTRICTURING OF STATE-OWNED ENTERPRISES OF A STATE GOVERNMENT OF INDIA: ...
INTRODUCTION

Neharika Vohra and Deepti Bhatnagar

About six to seven years ago, probably like many of our professional colleagues, we started noticing a systematic change in the pattern of demand for training. Almost every single request we received from training heads or learning and development heads of companies for training was for leadership development. Our management development programme on leadership and change management was receiving close to 100 applications from all sectors of the industry. These requests came from a variety of organizations, irrespective of the size, ownership pattern of the organization, or industry. Like everybody else, we got busy in designing and delivering programmes on developing leadership.

A few months ago, we stepped back, observed a pattern and wanted to decipher it. We noticed that while leadership development as a topic acquired prominence for executive development, either through customized or open-enrolment programmes, dialogue among academia and practitioners on leadership development was scant. It appeared that while everyone including companies, consultants, academic institutes, and trainers were busy working on their leadership agenda, there had not been an adequate organized effort to collate experiences, share processes, look at best practices, reflect on trends, and learn from each other. This Colloquium is an attempt to put together in one place such practices and, hopefully, begin a healthy dialogue among academicians, consultants, practi-

Multinationals, including those with an established presence in India as well as the new ones which have started their India operations recently, are endeavouring hard to find the right people and induct them in their culture.

* The contribution of these authors will appear in Part II of the Colloquium in the October-December, 2011 issue of Vikalpa. The names of all the authors appear in alphabetical order.