

# Comparing Public Sector/ State Owned and Private Enterprises in India on the Proposed ESCHEAT Model

## A Novel Approach

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### Abstract

State Owned Enterprises (SOEs) have been important instruments of State policy over many decades. Lately, however, there has been increased criticism of SOEs and large-scale privatisations have been carried out. Comparisons of SOEs with private companies have focussed on the financial and techno-economic/ productivity related measures of performance. These measures do not align with the *raison d'être* of SOEs. The authors have proposed a new model for evaluating the performance of SOEs which they implement to compare some pairs of public and private enterprise in India. The study finds that there is a stark difference in the comparative performance between the traditional financial measure and the proposed model.

**Keywords:** state owned enterprises, public versus private, performance, public sector enterprises

### Introduction

Public Sector Enterprises (PSEs, also known as State Owned Enterprises - SOEs) have been an important tool of public policy over the past century. By the mid 20th century, specially after the second World War and the independence of a number of nation States, SOEs had taken the centre stage in economic development of most economies (Toninelli, 2008). Even in India, the Industrial Policy Revolution of 1956 ushered in an era with the State and its enterprises at the commanding heights of the economy; by the turn of the century, PSEs contributed to over 25 per cent of the country's GDP (Goyal, 2000).

In the late 20th century, however, there was a feeling among most policy makers and practitioners, and even the society in general, that SOEs are inefficient and waste precious resources of the nation (Majumdar, 1998; Alchian, 1965; Shleifer and Vishny, 1994). A belief had set in that these enterprises face a lot of political intervention, are bureaucratic and cause a drain on the Government. There has, consequently, been a trend of privatisation (Makhijal, 2006) of state enterprises and a denationalisation thereof. Reasons cited by most nations are either ideological, financial or fiscal (Megginson et al., 1994).

In order to substantiate the theory of inefficiency or poor performance of SOEs, the extant research on the subject was considered (Afonso et al., 2005; Bhatt, 2016 Boardman and Vining, 1989; Caves and Christensen, 1980; Dewenter and Matatesta, 2001; Estache and

Rossi, 2002; Goldeng et al., 2008; Nagale, 2017; Savas, 1977). It was seen that while a number of such studies have been undertaken across industries and across nations, there is no conclusive evidence to assert that private enterprises are more efficient or perform better. Some studies did allude to the private sector being more efficient. However, all studies compared either financial or techno-economic performance/ efficiency. While such measures may be appropriate for private enterprises, which have the primary objective of shareholder wealth creation, they are not in consonance with the nature of objectives, largely non-financial, for which SOEs were established.

Literature is unanimous in the public sector having a distinct set of objectives and being very different from private enterprises (Bozeman and Bretschneider, 1994; Perry and Rainey, 1988; Rainey et al., 1976; Rainey and Bozeman, 2000). A number of differences and perceived objectives were found in literature. The authors have studied the mental models of policymakers and practitioners in India to propose a model for evaluating the performance of SOEs keeping in view their real objectives. The model, christened the ESCHEAT Model, shows that SOE performance should be evaluated taking into account objectives in the nature of Emergency Service/ Strategic, Socio-Economic, Climate Change/ Environmental, Handling of Public/ Unviable Goods, Employment, Accountability and Technological.

The focus of the present study is to perform a comparison of some SOEs and private enterprises in India on the basis of the aforesaid model and to ascertain as to which perform better. Given the complexity of the objectives, a questionnaire based survey was carried out to evaluate the performance rating on each dimension of the ESCHEAT Model. Four of the largest private sector entries, in terms of market capitalisation, in different sectors were selected and a comparison was made with the leading SOE in the same sector.

It was found that while all the private companies were perceived to fare better on the financial dimension, all the SOEs are perceived to perform better on the ESCHEAT model.

The present study establishes that SOEs having been setup for objectives very different from the private sector and ought to be evaluated differently. These should be compared on a level playing field with their private sector counterparts.

### **The ESCHEAT Model**

The authors of this study in a previous work (under submission for publication), have proposed a model for the performance evaluation of PSEs/ SOEs. This model has been developed on the basis of cognitive mapping carried out using the 3CM Method (Kearney and Kaplan, 1997) on policy makers and practitioners in India. The following table describes the proposed model.

The model consists of 7 dimensions on which the performance of an SOE should be ascertained. The weights for each of the dimensions (totalling to 100) are specified against each dimension for arriving at a cumulative assessment. It is amply evident the the dimensions are not at all related to any financial or productivity linked measure. In fact, the dimensions are more akin to the objectives of a welfare state and are more in agreement with public service values.

The above model is in stark contrast to the performance evaluation criteria followed so far for comparing state owned and private enterprises. It is based on the objectives that

have been set out for SOEs and is an attempt at looking through the correct lens on SOEs instead of through the private sector/ market oriented perspective. One caveat, however, is that this model, since based on inputs from India, would be more suitable for the Indian context and, in large measure, to countries that are in a similar socio-economic state of development.

Table 1: The Components of the ESCHEAT Model

<b>Objective Category</b>	<b>Description</b>	<b>Weight</b>
<b>Emergency Response/ Strategic</b>	To be a strategic tool for the government and be available in the times of need	20
<b>Socio-economic</b>	To provide social justice and development of backward areas	15
<b>Climate Change/ Environmental</b>	To set, promote and practice the best environmental standards and to aid the protection of the environment	10
<b>Handling Public/ Unviable Goods</b>	To Provide Public/ Non-Market Goods or Services	15
<b>Employment</b>	To do human resource development and employment generation	15
<b>Accountability</b>	To be accountable to the people	15
<b>Technological</b>	To promote new technologies in the country	10

Another aspect of the proposed model meriting mention is that it is an indicative one. Each dimension may need operationalization for each enterprise or sector thereof. For instance, the Emergency/ Strategic Services dimension would vary across industrial sectors and a measure of accomplishment thereof would also be a complex one. Same would be the case for each of the other dimensions. Some dimensions would be a composite measure of a number of sub-components; for instance, the socio-economic dimension may include diverse aspects such as development of backward areas and affirmative action. It is thus important to formulate an operative definition to implement the model in each attempt to do so.

### **Hypothesis and Methodology**

The hypothesis of this study is that the comparison of performance of state owned and private entries would yield very different results if a comparison was made on the ESCHEAT model as against one made on financial or productivity measures. The premise behind this, as explained earlier, is that the objectives of SOEs are not financial making it incongruous to measure their performance on financial measures, as has been done so far.

The first step of the study involved identifying some pairs of state owned and private enterprises in India for carrying out the comparison. For this purpose, the top listed companies on the basis of market capitalisation were identified. Four of the private

companies in the list which had a presence largely in a single sector of industry, in which sectors there was a significant presence of the public sector, were selected. Subsequently, this list was presented to about 50 policy makers/ practitioners on a convenience sampling basis. They were asked to simply identify a ‘comparable’ SOE to each of these private companies. The responses were near unanimous and the following pairs were established (presented in Table 2).

Table 2: Comparable Private and State Owned Enterprises

Sector	Private Enterprise	State Owned Enterprise
<b>Banking</b>	ICICI Bank (ICICI)	State Bank of India (SBI)
<b>Electricity Generation</b>	Reliance Power (Reliance)	NTPC (erstwhile National Thermal Power Corporation)
<b>Steel</b>	JSW Steel (JSW)	SAIL (erstwhile Steel Authority of India Limited)
<b>Telecom</b>	Bharti Airtel (Airtel)	Bharat Sanchar Nigam Limited (BSNL)

The pairs of companies in Table 2 were to be compared for their performance on financials as well as on the ESCHEAT Model.

The next step was to operationalize the ESCHEAT Model. For this, it was felt that since the dimensions of the model were complex and composite, a subjective assessment on each dimension elicited from experienced practitioners could be elicited. Developing objective measures for each dimension appears to be quite a tedious task. Since the assessment on the model was decided to be done on a subjective basis, so was the comparison on the financial measures to maintain a uniformity in the method of data collection. It was thus decided that a performance rating, on a scale of 1 to 10 (one being the least and 10 being the highest level of performance), would be elicited on each of the dimensions of the model and the financial dimension.

In order to collect the data, an online questionnaire was devised. Performance ratings on each of the dimensions of the ESCHEAT model and the financial performance rating for each of the companies was elicited thereby. The questionnaire was administered to 75 respondents who comprised largely of senior policy makers in the Government of India/ Practitioners. Convenience purposive sampling was resorted to for this survey in view of the specialized target group requiring personal acquaintance to elicit a response.

### **Research Findings**

The responses received were then analyzed. A mean of the responses received for each of the performance parameters for each of the companies was calculated, rounding off to the first decimal. The overall performance rating on the ESCHEAT Model was calculated using the ratings on each of the 7 dimensions and calculating the weighted average in accordance with weights assigned to each dimension in the model. The resulting analysis is shown in Table 3 below.

A look at the table 3 shows that all the private companies, except Reliance Power, are perceived to have a better financial performance than the PSEs. On the Emergency Service/ Strategic dimension, PSEs have a high rating across the board, though Airtel is almost at the same level as BSNL in this respect. The Socio-Economic dimension reveals an interesting result. These ratings are significantly higher for the SOEs than their private sector.

Table 3: Analysis of Responses Received

Parameter	ICICI	SBI	Reliance	NTPC	JSW	SAIL	Airtel	BSNL
<b>Emergency</b>	5.2	7.1	4.4	7.1	5.2	6.5	6.3	6.2
<b>Socio-economic</b>	4.5	7.2	3.7	7.0	4.9	6.4	5.5	6.5
<b>Climate change</b>	4.5	5.1	3.9	5.6	4.5	5.3	4.9	4.9
<b>Handling Public Goods</b>	4.4	6.8	3.9	6.3	4.4	5.9	5.0	6.3
<b>Employment</b>	6.0	7.1	4.7	6.9	5.4	6.5	6.3	6.0
<b>Accountability</b>	4.8	6.4	3.7	6.6	4.6	6.3	5.3	5.7
<b>Technological</b>	6.9	6.1	5.4	6.5	6.3	5.8	7.2	5.1
<b>ESCHEAT</b>	5.1	6.7	4.2	6.7	5.0	6.2	5.8	5.9
<b>Financial</b>	6.9	6.4	4.7	6.3	6.0	5.5	6.3	4.0

counterparts; even BSNL has a high rating in this regard. The Climate Change/ Environmental dimension is more or less similarly rated for both sectors, with the PSEs showing slightly better ratings. Handling Public/ Unviable Goods is an important dimension for SOEs, which is clearly perceived to have a much better performance ratings for the SOEs considered; the private sector is perceived to fare badly on this dimension. While on the Employment dimension, the SOEs perform somewhat better than the private enterprises, on the Accountability dimension, SOEs have a significant lead. Private enterprise paper to have a better rating on the Technological dimension.

The overall ESCHEAT ratings were separately calculated using the individual dimension rating for each company and the weights earlier determined for each dimension to arrive at the overall performance ratings as per the proposed model. The above table shows that the Overall Performance Ratings on the ESCHEAT Model are better for all the SOEs, including BSNL which had a very poor financial rating by the respondents.

It is thus amply evident that while the private companies may perform better on a financial performance parameter, the overall performance comparison carried out taking into account all the objectives of SOEs, is very different. The considered SOEs perform better on

the ESCHEAT Model of performance evaluation in comparison to their private sector counterparts even when the same SOEs report a poorer comparative financial rating.

### **Conclusion**

A model for the performance evaluation of SOEs was implemented on four pairs of public and private enterprises demonstrating the entirely opposite results of a pure financial comparison and a comparison on the proposed model. While on the financial rating parameter, private companies are perceived to fare better, on the ESCHEAT Model, the SOEs have a much better overall performance.

The study thus makes a strong case of re-considering the present approach to evaluating SOEs and comparing them with private enterprises, specially in the Indian context, which would be possibly true for other developing countries. Further, the study indicates that the practice of privatisation of SOEs in many countries may be out of ill conceived notions of performance of SOEs. It is hoped that the present study causes a reappraisal of the way SOEs are considered and looked upon by policy makers, practitioners, academia and the society.

It, however, must also be noted that the ESCHEAT Model is only a proposition at present and requires stringent testing and further development to gain greater acceptance. Further, in the present study only perceptual/ subjective performance ratings have been used which may have an inherent bias; objective measures/ proxies to assess the performance level on each of the Model parameters may also be developed.

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