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Working Paper

INANCING PUBLIC ENTERPRISE INVESTMENTS IN INDIA:
THE CASE OF CENTRAL GOVERNMENT ENTERPRISES

By

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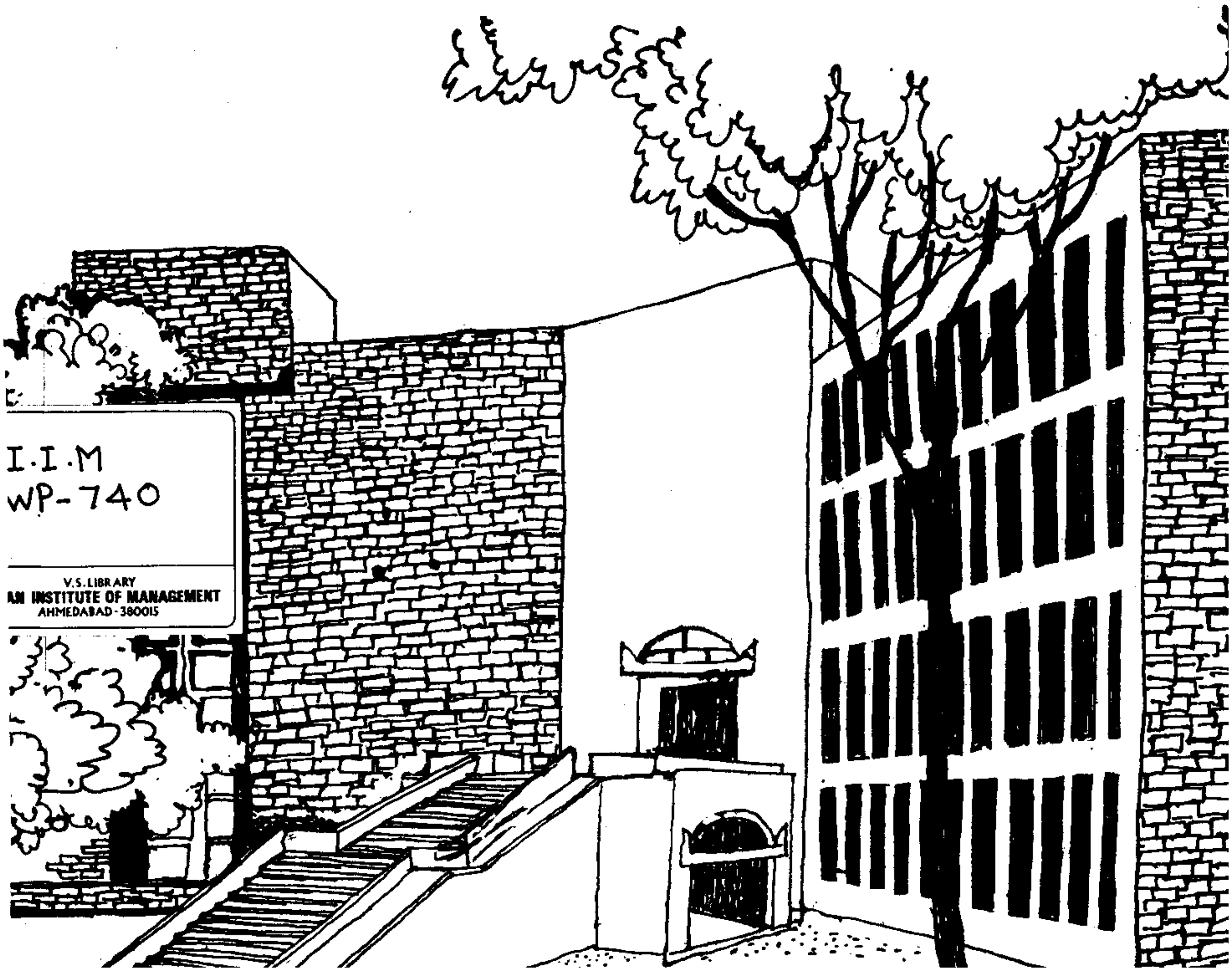

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FINANCING PUBLIC ENTERPRISE INVESTMENTS IN INDIA: THE CASE OF CENTRAL GOVERNMENT ENTERPRISES

SECTION 1: INTRODUCTION

In India, public enterprises have been categorized into departmental enterprises and non-departmental enterprises. Departmental enterprises are unincorporated enterprises owned, controlled and run directly by public authorities. The criteria followed to distinguish public enterprise activity from public administration activity are: use of commercial accounting methods to determine financial performance, and control of productive capital in the form of equipment such as machines, plants and stocks. Non-departmental public enterprises comprise (a) government companies (in which not less than 51% of the paid-up capital is held by the central government or state government or partly by the central government and partly by one or more state governments), and subsidiaries of government companies; and (b) statutory corporations set up under special enactments of Parliament or State Legislatures (such as Oil and Natural Gas Commission, Damodar Valley Corporation, State Electricity Boards, etc.). Non-departmental public enterprises include both financial and non-financial enterprises.1/

There are nearly 1,000 public enterprises in India, with enterprises belonging to the Central Government, or Central Public Enterprises (CPEs), constituting the most important component. CPEs, currently numbering nearly 250, include departmental enterprises such

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1/ Government of India: Transactions of the Public Sector 1960/61 - 1979/80 (New Delhi, 1983), pp. xiv - xvi.

as Railways and Telecommunications, and non-departmental financial and non-financial enterprises such as Industrial Development Bank of India, Industrial Finance Corporation of India, National Thermal Power Corporation and Steel Authority of India. The remaining public enterprises belong to the state, union territory and local governments. These include departmental enterprises such as Uttar Pradesh Irrigation, and hundreds of non-departmental financial and non-financial enterprises such as Gujarat Industrial Investment Corporation and Kerala State Cashew Development Corporation.

Public enterprises account for substantial investment -- Rs. 300 billion, 9.1% of GDP, in 1987/88, for example. Yet little work has been done on how this investment is financed. This paper reviews the way plan investments of CPEs1/ have been financed in recent years, with a view to identify some of the main issues of public enterprise investment financing in India.

SECTION 2: FINANCING OF CPEs' PLAN INVESTMENTS

CPEs' plan investments account for nearly three-fifths of total gross domestic capital formation (gdcf) by Indian public enterprises

1/ CPEs' plan investments comprise all of their investments included in the development plan outlay approved by the Planning Commission. CPEs also undertake investments which do not form a part of the plan outlay. Such investments, called non-plan investments, account for a very small proportion of the CPEs' total investments.

(Table 1).1/ Of the CPEs' plan investments, non-financial non-departmental CPEs account for the largest share (nearly three-fourths), followed by departmental CPEs (nearly one-fifth) and financial non-departmental CPEs (nearly one-twentieth). CPEs have depended on three broad sources for financing their plan investments: internal resources, budgetary support, and extra-budgetary resources. This section describes each of these sources and reviews their role in financing CPEs' plan investments in recent years.

2.1 INTERNAL RESOURCES

Internal resources of a public enterprise comprise those internally-available resources which can be used to finance its plan investment. They are arrived at by first adding up its retained profits, depreciation, deferred revenue expenditures written-off, and carry-forward surplus available from previous year(s),2/ and then substracting the following from the gross internal resources (aggregate of these four items): (a) loan repayments; (b) net increase in working capital requirements for financing inventories, works-in-progress, etc.; and (c) non-plan capital requirements. Thus, internal resources available for financing a year's plan investment, do not necessarily mean internal resources generated in that year. Indeed, a public enterprise (PE) may have internal resources available for financing its plan investments in a year even though it may have suffered a loss, even a cash loss, in that year.

1/ The remainder of gdcf is accounted for by investments (both plan and non-plan) of enterprises other than CPEs and non-plan investments of CPEs.

2/ A public enterprise will have a carry-forward surplus when its plan investment in a year turns out to be less than its internal resources.

Internal resources are expected to finance nearly two-thirds of CPEs' investment outlays during the Seventh Plan. However, the actual performance so far has lagged far behind: internal resources financed only 37.6% of the CPEs' investment outlay in the first year of the plan (1985/86), 32.3% in the second year (1986/87), 31.9% in the third year (1987/88), and are budgeted to finance 41.3% of the outlay in the fourth year (1988/89) (Table 2). It needs to be noted that the CPEs' internal resources budgeted for 1988/89 (Rs. 83.11 billion) represent a rise of 45.8% over the revised estimates of these resources for 1987/88. This is substantially higher than the rise (6.2%) recorded by CPEs in 1987/88 over 1986/87. Indeed, the budgeted increase in CPEs' internal resources over 1987/88 (Rs. 26.11 billion) is substantially higher than even the budgeted increase in CPEs' plan investment (Rs. 22.69 billion)! Almost three-fourths of the additional internal resources are projected to come from seven CPEs - Steel Authority of India, Telecommunications, Oil and Natural Gas Commission, Railways, Mahanagar Telephone Nigam, Indian Oil, and Coal India. Two of these CPEs generated little or no internal resources in 1987/88: Steel Authority of India and Coal India are budgeted to generate internal resources of Rs. 4.88 billion and Rs. 0.70 billion in 1988/89 against Rs. 0.02 billion and nothing in 1987/88, respectively. The CPEs expect to be able to achieve these ambitious targets largely, if not wholly, as a result of the recent increases in the administered prices of the goods and services they produce.

Depreciation provisions account for nearly seven-tenths of CPEs' gross internal resources. If account is taken of inflation in the cost of capital goods and depreciation provisions are appropriately adjusted, the contribution of depreciation funds to CPEs' gross internal resources would be still higher. This reflects the state of affairs on the front of CPEs' financial performance: the rate of net profit on net worth in 1986/87,1/ 4.5%, remains low, although it improved marginally from the 3.7% rate achieved in 1985/86. Moreover, this overall rate of return is largely because of the petroleum enterprises, which accounted for nearly three-fourths of the net profits of profit-making CPEs. But as the net profits of non-petroleum CPEs were inadequate to offset the losses of loss-making CPEs, the net return in the non-petroleum sector was in the negative -- -1.2%.

CPEs have done poorly because of several factors such as: relatively high capital intensity, coupled with low capacity utilization; excessive inventories; large, and often unruly, labor forces receiving salaries and wages generally not commensurate with the levels of productivity achieved; substantial social/welfare obligations-related costs; and prices set too low for socio-economic reasons. Although the relative importance of these factors may differ from sector to sector and even from CPE to CPE, it appears that many CPEs suffer from one common problem - high costs. A recent study, for example, has shown that a major CPE in the fertilizer sector has performed poorly largely because of its relatively high capital and operating costs: to produce one ton of urea, this CPE uses larger quantities of feedstock and utlities, incurs higher

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1/ 1986/87 is the latest year for which the relevant data on CPEs' financial performance are presently (March 1988) available.

conversion and marketing costs, and carries a heavier burden of interest and depreciation.1/ This suggests that CPE managers have no strong incentives to reduce costs.

2.2 BUDGETARY SUPPORT

With internal resources financing only one-third to two-fifths of their plan investments, the CPEs have a substantial deficit which is financed through support from the Central budget and resort to several extra- budgetary sources. Although budgetary support continues to be a major source for financing the CPEs' deficit, its contribution has registered a substantial decline in recent years -- it is expected to be 59.2% in 1987/88, against 87.3% in 1984/85. As per cent of GDP, budgetary support for CPEs' plan investments is expected to decline from 2.8% in 1984/85 to 2.2% in 1987/88.

The Government of India (GOI) has set up procedures to determine the level and form of budgetary support to CPEs. Most CPEs with plan schemes are required to submit, well before the start of a new fiscal year, a detailed statement2/ indicating, among other things, the plan investment proposed to be undertaken during the coming fiscal year, the

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1/ Anand P. Gupta, "Financial Performance of Public Enterprises in India: A Case Study of XYZ Limited", The World Bank, New Delhi, October 15, 1987.

2/ This statement is not required from (a) certain departmental CPEs such as Atomic Power Station of Department of Atomic Energy, Badarpur Power Station of Department of Power, Delhi Milk Scheme of Department of Agriculture, and Mints and Press of Department of Economic Affairs, and (b) non-departmental financial enterprises operating under the administrative control of the Department of Economic Affairs' Banking and Insurance Divisions.

internal and external resources1/ expected to be available for financing it, and the budgetary support sought from the Central Government. These statements are scrutinized by the concerned administrative ministeries/departments, the Planning Commission, and the Ministry of Finance. The purpose of the exercise is to ensure that once a CPE's plan investment is approved,2/ it fends for itself to the extent feasible, with budgetary support provided only to finance the dificit, if any. However, this has not always been achieved: there have been instances where certain CPEs had drawn budgetary support from the GOI although they had adequate internal resources to finance the entire plan schemes.

The budgetary support for CPEs' plan schemes comprises of half equity and half loan, with equity released first and loan released after the entire equity has been released.3/ There are however two exceptions

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1/ External resources here include only those directly coming to CPEs. As discussed later in this paper (see sub-section 2.3.2, para 2), external assistance for CPE projects from sources such as the World Bank, International Development Association, and Overseas Economic Cooperation Fund of Japan, is transmitted to the concerned CPEs as part of budgetary support from the GOI.

2/ As a result of the scrutiny, the approved plan investment outlay of a CPE for a year may differ from that proposed by it. The Railways, for example, had proposed a plan investment outlay of Rs. 43 billion for 1988/89, but the approved outlay is Rs. 38.5 billion.

3/ The equity and loan received by a CPE in a year may not be in the prescribed ratio of 1:1, as the budgetary support may be on account of more than one plan schemes, with different commencement dates. Thus, a CPE with two Plan schemes under implementation in a year, may receive in that year budgetary support of, say, Rs. 100 million in the form of equity for one scheme and the loan component of the budgetary support, say Rs. 50 million, for the other scheme, with the equity-loan proportions in the budgetary support received by the CPE thereby working out to 2:1, not 1:1.

to this general guideline. First, certain CPEs such as Food Corporation of India and Indian Dairy Corporation receive the entire budgetary support in the form of equity. Second, departmental enterprises are also treated differently - they being part of the GOI, budgetary support to them is treated on par with that to other administrative departments, with no distinction made between debt and equity.

Loans carry an interest obligation,1/ whereas equity capital is free from any obligation. If a PE is unable to pay interest, it can approach the GOI for (a) an interest subsidy, (b) grant of a non-plan loan to cover cash lossses (including the interest due), or (c) conversion of the whole or part of the loan in question into equity. The CPEs have resorted to all of these devices, with the GOI generally responding favourably. For example, in 1986/87 the GOI provided substantial interest sunsidies to several CPEs, including National Textile Corporation (Rs. 817 million), Coal India Limited (Rs. 581 million), Steel Authority of India (Rs. 238 million), and Fertilizer Corporation of India (Rs. 229 million).

1/ Interest rates currently applicable to GOI loans to CPEs are as follows:

1. Industrial and commercial enterprises and cooperatives having equity capital exceeding Rs. 10 million:	
(a) Investment loans	15%
(b) Working capital loans and loans to meet cash losses	17%
2. Financial institutions, port trusts, Khadi and Village Industries Commission, etc:	
(a) Rural Electrification Corporation:	
For Minimum Needs Program	9.25%
For other purposes	10%
(b) National Bank for Agriculture and Rural Development	10%
(c) Others	10.5%

There is reason to believe that many CPEs receiving budgetary support, do not make any contribution to the GOI's receipts by way of loan repayments, interest, dividends and business income taxes. GOI's budgetary supports to such CPEs, it must be noted, are tantamount to unbudgeted government grants.

2.3 EXTRA-BUDGETARY RESOURCES

Extra-budgetary resources (EBRs) are resources other than budgetary support, which CPEs raise to finance the deficit in resources required to finance their plan investments. EBRs have grown in importance recently: they financed 30.8% of the CPEs' plan resources deficit in 1986/87 and a substantially higher proportion (40.8%) of the deficit expected in 1987/88, against 7.8% during the Sixth Plan period (1980/81-1984/85). This is certainly a development in the right direction: the more CPEs have to fend for themselves, via directly raising more resources through, say, internal and/or external borrowing, so much the better.

Currently, EBRs include resources raised through: public enterprise bonds, external commercial borrowings, inter-CPE deposits, loans from the Oil Industry Development Board and the Oil Coordination Committee, loans from the Steel Development Fund, deposits from the public, loans from financial institutions, and equity participation by cooperatives and foreign collaborators.

2.3.1 PUBLIC ENTERPRISE BONDS

Of the several instruments in use to raise EBRs, public enterprise bonds account for the largest share--42.5% in 1987/88, for example. But bonds are not a popular means for raising resources, in the sense that only about fifteen CPEs, out of a total of about 250 CPEs, have raised resources through bonds. They include: National Thermal Power Corporation, National Hydro Electric Power Corporation, Telecommunications, Mahanagar Telephone Nigam, Neyveli Lignite Corporation, Indian Petro-Chemicals Corporation, and Railways.

CPEs currently offer 13%, 7 and 10-year bonds, and 9%, 10-year bonds, both with generous tax benefits; some enterprises (e.g., Hindustan Photo Films) offer only 13% bonds. The tax benefits are: interest on a 13% bond qualifies for deduction upto Rs. 7,000 per year; interest on a 9% bond is completely exempt from income tax without any limit; wealth tax exemption for both 13% and 9% bonds without any limit. Because of these tax benefits, public enterprise bonds are much more attractive than bonds issued by even well-known private sector firms.1/ This has begun to divert capital resources from private sector to public enterprises, while at the same time creating an implicit loss of tax revenue. Indeed, the implicit returns are so good that public enterprise bonds may have begun diverting some private sector firms' internal resources (retained profits and depreciation funds) from reinvestment.

1/ To illustrate, the marginal post-tax return to an individual belonging to the highest income and wealth tax brackets works out to 13% if he invests in a 13% public enterprise bond, against only 4.175% if invested in a 13% bond issued by a private firm. To put it differently, the regime of public enterprise bonds has created conditions such that the net return on an investment carrying at least some risk works out to be substantially lower than that on a safe investment!

Despite all this, however, CPEs, by and large, are not happy with raising resources through bonds--they prefer the easier and cheaper alternative of budgetary support for financing their plan investments.

2.3.2 <u>EXTERNAL COMMERCIAL BORROWINGS</u>

External commercial borrowings by CPEs form a part of the country's overall external borrowing program. The 1987/88 revised estimates for external commercial borrowings (including suppliers' credit) by CPEs stands at Rs 5.8 billion, substantially lower than the 1986/87 figure of Rs. 11.4 billion. The CPEs allowed/asked to borrow abroad on commercial terms are generally the ones which have done better (e.g. Oil and Natural Gas Commission, National Thermal Power Corporation). The reason for this is obvious: CPEs with good track records are able to borrow on relatively soft terms - Oil and Natural Gas Commission, for example, has recently concluded a deal for a 10 year $300 million Eurodollar loan at LIBOR plus 3/16% interest for first two years and LIBOR plus 1/4% interest thereafter, with a 7 1/2-year grace period.

It needs to be clarified that the above external borrowings by CPEs are in addition to the external assistance provided by various sources such as the World Bank, International Development Association, and Overseas Economic Cooperation Fund of Japan. External assistance for CPE projects, currently totalling roughly Rs. 20 billion, some 10-12% of CPEs' total plan investment, is transmitted to the concerned CPEs as part of budgetary support from the GOI. This support follows the same terms and conditions as applicable to other GOI budgetary support to CPEs. To elaborate, all budgetary support to CPEs is provided on the same terms and conoitions (e.g., half equity, half loan), regardless of, for example, whether the GOI obtained the external assistance in the form of loan, grant, or a combination of both. The responsibility for repayment of loans obtained from external assistance sources, payment of interest thereon, and other charges, if any, is assumed by the GOI. Foreign exchange risk, if any, is also borne by the GOI.

2.3.3 INTER-CPE DEPOSITS

This is a recent addition to the list of EBRs. It is supposed to work as follows: Managers of non-financial CPEs with surplus funds in a year, operating at arm's length, would put these funds on deposit with other non-financial CPEs. Before the introduction of this scheme, the CPEs were generally asked to deposit their surplus funds with the GOI which, in turn, used them to finance its various obligations, including budgetary support to CPEs. The amount of inter-CPE deposits budgeted for 1987/88 is Rs. 5.9 billion against the 1986/87 revised estimates of a mere Rs. 0.4 billion. Information on revised estimates for 1987/88 and budget estimates for 1988/89 is not available.

As the interest rates on inter-CPE deposits are expected to be much higher (about 14%) than on CPEs' deposits with the GOI, the scheme will have a positive effect on the finances of CPEs with surplus funds. What is more, the scheme may also have the effect of making the borrowing CPEs more efficient in the use of their resources.

There are, however, indications suggesting that the scheme may run into rough weather unless timely, corrective steps are taken. Take, for example, the issue of Oil and Natural Gas Commission and Rashtriya Chemicals and Fertilizers Corporation's deposits with heavily-losing, almost insolvent, Coal India Limited (CIL), Fertilizer Corporation of India (FCI) and Hindustan Fertilizer Corporation (HFC).1/ These deposits do not appear to have been arranged at arm's length; indeed, the concerned administrative ministries of the GOI seem to have played a major role in arranging them. If such things continue to happen, the scheme may backfire - for example, the employees of CPEs with surplus funds may ask their managements to use the funds to, say, raise their wages and salaries instead of lending them to CPEs such as CIL, FCI and HFC.

2.3.4 LOANS FROM OIL INDUSTRY DEVELOPMENT BOARD (OIBD) AND OIL COORDINATION COMMITTEE (OCC)

The OIBD, administering the resources raised through a cess on indigenous crude, currently levied at the rate of Rs. 600 per tonne, provides assistance to organisations engaged in the development program of oil industry - from the exploration and production of crude oil to its refining, further downstream processing, distribution, marketing, and research and development. Although the GOI which collects the cess is supposed to transmit the entire proceeds to the OIBD, it has generally not done so in recent years. The reason for this is that in the GOI's estimate OIBD's present resources (which include repayments of earlier loans and interest receipts) are adequate to meet the eligible CPEs' likely demands.

1/ For details, see Table 3.

As regards the OCC, although its main functions are to (a) prepare long-term demand estimates for petroleum products, assess the import requirements of crude oil and to prepare the annual Oil Economy Budget, (b) allocate imported and domestic crude oil among various refineries in the country, (c) determine refinerywise monthly production pattern of petroleum products, (d) administer the elaborate Petroleum Retention Pricing Scheme, and (e) manage the oil industry pool accounts,1/ it also provides support to finance plan investments of CPEs in the oil and gas sector. This support is provided out of the surplus funds in the oil industry pool accounts.

The two institutions provide their support in the form of loans carrying an interest rate (12%) which is substantially lower than the current market rates. The total amount of OIBD-OCC support targeted for 1987/88 is Rs. 3.6 billion, with Gas Authority of India alone accounting for 87% of it. The other CPEs targeted to benefit from this support are: Cochin Refineries (Rs. 0.28 billion), Bongaigaon Refinery (Rs. 0.16 billion), and Lubrizole India (Rs. 0.01 billion).

2.3.5 LOANS FROM STEEL DEVELOPMENT FUND (SDF)

The SDF, comprising the resources raised through a development surcharge on steel products, currently at rates ranging between Rs. 400-500 per ton, is used to provide concessional (2-8%) loans to steel

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1/ These accounts are formally known as Crude Oil Price Equalization Account, Cost and Freight Surcharge Account, Freight Surcharge Pool Account, and Product Price Adjustment Account.

producers. SDF loans represent a major source of funds, accounting for 11.8% of the EBRs budgeted for 1987/88 and for 32.6% of the steel sector CPEs' plan investments budgeted for that year.

2.3.6 DEPOSITS FROM PUBLIC

CPEs are allowed to accept 1-3 year deposits from the public at the Reserve Bank of India-administered interest rates (10.5-13.5%), provided the deposits do not exceed 15% of a CPE's paid-up capital and reserves. However, as the interest on these deposits does not qualify for any concessional tax treatment, they are not much of an attraction for taxpayers. Those who generally go in for these deposits are people who are outside the tax net and who do not want to take the risk associated with private sector company deposits offering slightly higher interest rates.1/ The amount of deposits targeted for 1987/88 is a mere Rs. 0.23 billion, to be raised by just one CPE - Indian Petro-Chemicals Corporation.

2.3.7. LOANS FROM DOMESTIC LONG TERM FINANCIAL INSTITUTIONS

CPEs' dependence on domestic long term financial institutions (other than OIBD, OCC and SDF) for resources to finance their plan investments does not add up to much - Rs. 0.27 billion in 1987/88, for example. This is not surprising, given (a) the relatively high normal

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1/ Many private sector companies have defaulted on the payments due on deposits from the public.

rate of interest (about 14%) charged by these institutions, and (b) the eligible CPEs' inability to pay even the concessional interest rates charged by these institutions on certain loans (e.g., 11.5% loans under Industrial Development Bank of India's Textile Modernization Fund Scheme).

2.3.8 EQUITY PARTICIPATION BY COOPERATIVES AND FOREIGN COLLABORATORS

More than 99% of the CPEs' equity totalling Rs. 283 billion is held by the GOI. Cooperatives' equity participations in two CPEs (Indian Farmers Fertilizer Cooperative and Krishak Bharati Cooperative) total some Rs. 0.67 billion. Foreign equity participations in 15 CPEs (e.g., Paradip Phosphates, Maruti Udyog) add up to a slightly higher figure, Rs. 0.73 billion. Cooperatives' equity participation in CPEs is low because cooperatives run as businesses have not been much of a success in India - it is only in the State of Gujarat that cooperatives have achieved some success. Foreign equity participation, on the other hand, is low largely because of the GOI's generally restrictive policy, with non-financial considerations playing a major role in GOI's decision-making on such participation. To illustrate, the GOI may not allow foreign equity participation in a CPE if it is found that the technology sought by it (the CPE) may be available on an outright-purchase or royalty-payment basis. It is only when it is felt that the technology in question would not be available unless the foreign firm is offered a share in the CPE's equity, that the GOI generally allows foreign equity participation.

SECTION 3: MAJOR ISSUES

Two major issues emerge from the foregoing discussion. They relate to (a) CPEs' Seventh Plan internal resource targets, and (b) incentives to CPE managers.

3.1 CPEs' SEVENTH PLAN INTERNAL RESOURCE TARGETS

The Seventh Plan envisages internal resource generation of Rs. 448.88 billion (at 1984/85 prices) by CPEs. Of this, Rs. 306.48 billion are expected to be raised at the prices, tariffs, etc. obtaining in 1984/85, and the balance through additional resource mobilization efforts.

Table 4 presents data on the top ten CPEs' internal resources at the prices, tariffs, etc. obtaining in 1984/85, as estimated by the Planning Commission while formulating the Seventh Plan. It also presents the available data on these CPEs' (a) targets of internal resources mobilization through additional measures, and (b) internal resources utilized/expected to be available for financing their plan investments in 1985/86, 1986/87, 1987/88 and 1988/89.

Two things emerge from these data. First, of the nearly 200 CPEs with plans to invest during the Seventh Plan period, the top ten accounted for as much as 85.8% of all CPEs' internal resources at the prices, tariffs, etc. obtaining in 1984/85. These CPEs are: Air India, Indian Airlines, Indian Oil Corporation, National Fertilizers, National Thermal Power Corporation, Oil India, Oil and Natural Gas Commission, Railways, Rashtriya Fertilizers and Chemicals, and Telecommunications.

Second, given that the 1985/86, 1986/87, 1987/88 and 1988/89 data are in current prices, not in 1984/85 prices,1/ and also reflect the resources attributable to the CPEs' additional resource mobilization measures, no one can be sure that CPEs will be able to hit the Seventh Plan's overall internal resource mobilization target. Indeed, there is reason to believe that despite the recent increases in the prices of several goods and services (e.g., gasoline, rail transport, telecommunications), majority of the above 10 CPEs may fail to hit their internal resource generation targets.

This is a serious matter and needs to be investigated, in order to determine what went wrong, why and what needs to be done, so that this experience is not repeated during the Eighth Plan.

3.2 INCENTIVES TO CPE MANAGERS

There are two major aspects of the environment CPE managers operate in. First, all CPEs have access to instruments which enable them to raise resources at rates which are generally substantially lower than market rates. Examples of such instruments are: budgetary allocations and 9% completely tax-free bonds.

Second, the overall return on net worth employed in CPEs continues to be substantially less than even the artificially low nominal interest rates which the GOI pays on the resources it borrows. Moreover,

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1/ Prices have risen in each year of the Seventh Plan. Wholesale prices, for example, rose by 5.7% in 1985/86 and 5.4% in 1986/87, and are expected to be up by about 10% in 1987/88.

a large number of CPEs make cash losses, with the GOI bailing such CPEs out through what are called non-plan loans.

CPE managers operating in this environment would not have much incentive to be efficient. This urgently needs to be changed: the environment should be such that it makes CPE managers raise resources at market rates and respond to the resulting higher cost of capital by improving efficiency.

SECTION 4: CONCLUDING REMARKS

This paper provides a perspective on how CPEs' plan investments are financed. It reveals that although budgetary support continues to be a major source of financing CPEs' plan investments, its contribution has declined from 53% in 1984/85 to 46.9% in 1986/87 and is expected to decline further to 40.3% in 1987/88. As per cent of GDP, budgetary support for CPEs' plan investments has declined from 2.83% in 1984/85 to 2.66% in 1986/87 and is expected to decline further to 2.18% in 1987/88. There is reason to believe that this trend would continue.

Significantly, while budgetary support for CPEs' plan investments is declining, GOI's budget deficit continues to be high - it is expected to be about 8.5% of GDP in 1987/88 against 7.8% in 1984/85. Indeed, the 1987/88 deficit would have been 9% of GDP, not 8.5%, had the GOI not changed the accounting treatment of oil surplus funds. (These funds amounted to a least Rs. 35 billion during 1982/83-1985/86 and were shown in the GOI's books as interest-bearing capital receipts from the

OCC. The GOI has now decided to treat most of these surplus funds as a current contribution from the OCC. The contribution amounted to Rs. 13 billion in 1986/87 and is expected to be Rs. 17 billion in 1987/88.)

What all this boils down to is that it is the rapid growth in GOI's disbursements other than budgetary support to finance its enterprises' plan investments, which is responsible for the rising budget deficit. This is an important point, given the general tendency of many commentators to attribute the recent rises in GOI's budget deficits to its budgetary support to CPEs to enable them to finance their plan investments. Clearly, a strategy to control the GOI's rapidly rising expenditures urgently needs to be developed.

There is also a strong case for determined efforts to improve the financial performance of CPEs.' The paper shows that net return on net worth employed in CPEs is pitifully low - 4.5% in 1986/87, the latest year for which the relevant data are available. This is substantially less than even the artificially low interest rates which the GOI pays on the resources it borrows.

What is more, even the above overall net return is largely because of the petroleum enterprises, which accounted for nearly three-fourths of the net profits of profit-making CPEs. Indeed, as the net profits of non-petroleum CPEs were inadequate to offset the losses of loss-making CPEs, the net return in the non-petroleum sector was in the negative - -1.2%. Clearly, this is not a happy situation.

TABLE 1

CONTRIBUTION OF CENTRAL PUBLIC ENTERPRISES (CPEs) IN TERMS OF PLAN INVESTMENT AND RESOURCE MOBILIZATION

(Amount in Rs. billion, at current prices)

Year	Total Public Sector Plan Outlay \a	Central Plan Outlay	CPEs' Plan Investment	CPEs' Internal Resources	Total Gross Domestic Capital Formation in Public Enterprises	CPEs' Plan Investment as % of Central Plan Outlay	CPEs' Internal Resources as % of Central Plan Outlay	CPEs' Plan Investment as % of Total Gross Domestic Capital Formation in Public Enterprises
1	2	3	4	5	6	7	8	9
1980/81	150.23	70.49	51.68\b	13.62	108.99	73.3	19.3	47.4
1981/82	183.73	91.97	70.50\b	22.28	141.41	76.7	24.2	49.9
1982/83	217.25	112.85	88.51\b	33.55	162.49	78.4	29.7	54.5
1983/84	253.14	136.44	101.85 (RE)	42.06	173.29	74.6	30.8	58.8
1984/85	300.33	166.50	122.64 (RE)	48.18	209.07	73.7	28.9	58.7
1985/86	330.60	191.15	147.49 (RE)	55.46 (RE)	240.76	77.2	29.0	61.3
1986/87	402.61(RE)	236.25 (RE)	166.25 (RE)	53.68 (RE)	268.89\b	70.4	22.7	61.8
1987/88	446.98(BE)	257.01(RE)	178.47 (RE)	57.00 (RE)	300.31\b	69.4	22.2	59.4

\a Total public sector plan outlay consists of investment outlay and current outlay. Investment outlay is targeted at 85.7% of the total Seventh Plan public sector outlay. Break-up of annual plan outlays into investment outlays and current outlays is not available.

\b World Bank Estimate/Projection.

RE = Revised Estimates BE = Budget Estimates

Sources: Based on data from several sources, including: Government of India: Indian Economic Statistics - Public Finance (1986); Annual Plan 1986/87 and 1987/88; Budget at a Glance, various issues; Explanatory Memorandum to the Budget of the Central Government, various issues; Expenditure Budget 1987/88 and 1988/89, Vol I; and New Series on National Accounts Statistics with 1980/81 as Base Year (1988).

TABLE 2

FINANCING OF CENTRAL PUBLIC ENTERPRISES' (CPEs') PLAN INVESTMENTS

	Sixth Plan (Rs billion, at current prices)	Seventh Plan Targets (Rs billion, at 1984/85 prices)	1984/85 (Rs billion, at current prices)	1985/86 (RE) (Rs billion, at current prices)	1986/87 (RE) (Rs billion, at current prices)	1987/88 (RE) (Rs billion, at current prices)	1988/89 (BE) (Rs. billion at current prices)
1	2	3	4	5	6		
1. CPEs' Plan Investment	435.18 \a	669.69 \a	122.64(RE)	147.49	166.25	178.47	201.16
2. Internal Resources	159.69 (36.7)	448.88 (67.0)	48.18 (39.3)	55.46 (37.6)	53.68 (32.3)	57.00 (31.9)	83.11 (41.3)
3. Deficit (1 minus 2)	275.49 (63.3)	220.81 (33.0)	74.46 (60.7)	92.03 (62.4)	112.57 (67.7)	121.47 (68.1)	118.05 (58.7)
4. Financing of Deficit:							
Budgetary Support	254.00 (58.4)	162.81 (24.3)	65.00 (53.0)	72.86 (49.4)	77.92 (46.9)	71.90 (40.3)	74.02 (36.8)
Extra Budgetary Resources, of which:	21.49 (4.9)	58.00 (8.7)	9.46 (7.7)	19.17 (13.0)	34.65 (20.8)	49.57 (27.8)	44.03 (21.9)
Bonds	-	-	-	3.15 (2.1)	13.64 (8.2)	21.08 (11.8)	20.39 (10.1)
External Commercial Borrowing/ Suppliers' Credit	21.49 (4.9)	35.00 (5.2)	9.46 (7.7)	7.71 (5.2)	11.44 (6.9)	5.77 (3.2)	6.17 (3.1)
Other Extra-budgetary Resources	-	23.00 (3.4)	-	8.31 (5.6)	9.21 (5.5)	22.72 (12.7)	17.47 (8.7)

\a World Bank Estimate

Note: Figures within brackets indicate percentages to central public enterprises' investments.

RE = Revised Estimates BE = Budget Estimates

Sources: Based on data from several sources, including: Government of India: Expenditure Budget 1987/88 and 1988/89, Vol. I; Annual Plan 1986/87 and 1987/88; Indian Economic Statistics - Public Finance (1986); Budget at a Glance, v issues; and Explanatory Memorandum to the Budget of the Central Government, various issues.

TABLE 3

INTER-CENTRAL PUBLIC ENTERPRISE DEPOSITS

1987/88 (Budget Estimates)

Central Public Enterprises Making Deposits	Amount (Rs. billion)	Central Public Enterprises Accepting Deposits	Amount (Rs. billion)
Krishak Bharati Cooperative	1.40	Fertilizers and Chemicals Travancore	0.30
Rashtriya Chemicals and Fertilizers	0.40	Pradip Phosphates	0.50
		Fertilizer Corporation of India	0.20
		Hindustan Fertilizer Corporation	0.30
		National Thermal Power Corporation	0.50
Oil & Natural Gas Commission	2.89	Coal India	1.00
		National Thermal Power Corporation	0.50
		Rashtriya Ispat Nigam	1.39
Bharat Heavy Electricals	0.20	Cement Corporation of India	0.20
Air India	0.20	Vayudoot	0.05
Indian Airlines	0.57	National Airports Authority	0.40
International Airports Authority of India	0.06	Indira Gandhi Rashtriya Udan Academy	0.10
		Helicopter Corporation of India	0.28
Bombay Port Trust	0.20	Nhava Sheva Port	0.20
Total	5.92	Total	5.92

Sources: Government of India, Ministry of Finance.

Table 4

CENTRAL PUBLIC ENTERPRISES' SEVENTH PLAN INTERNAL RESOURCES TARGETS, AND THEIR INTERNAL RESOURCES UTILIZED/ EXPECTED TO BE AVAILABLE FORFINANCING THEIR 1985/86,1986/87, 1987/88 AND 1988/89 PLAN INVESTMENTS

(Rs. billion)

Public Enterprise	Seventh Plan's Targets of Internal Resources Mobilization (at 1984/85 prices): At Prices, Tariffs, etc. Obtaining in 1984/85	Through Additional Measures	Total (2+3)	Internal Resources (at current prices) Utilized/Expected to be Available for Financing Plan investments in: 1985/86 (RE)	1986/87 (RE)	1987/88 (RE)	1988/89 (BE)
1	2	3	4	5	6	7	8
Oil & Natural Gas Commission	130.73	NA	NA	19.34	18.37	18.96	22.50
Railways	42.25	25.00	67.25	NA	11.82	13.20	15.78
Tele-Communications\a	24.82	2.50	27.32	NA	4.18	6.62	13.04
Oil India	19.29	NA	NA	NA	2.01	1.95	1.99
National Thermal Power	8.52	NA	NA	NA	1.85	3.42	2.82
Indian Oil	9.35	NA	NA	NA	1.29	1.51	2.50
Indian Airlines	7.00	NA	NA	NA	1.19	1.37	0.86
Air India	8.00	NA	NA	NA	0.99	1.06	1.29
National Fertilizers	6.05	NA	NA	NA	0.70	0.33	1.26
Rashtriya Chemicals & Fertilizers	7.09	NA	NA	NA	0.43	0.20	0.42
Other CPEs	43.38	NA	NA	NA	10.85	8.38	20.65
All CPEs	306.48	142.40	448.88	55.46	53.68	57.00	83.11

NA = Not Available

\a Including Mahanagar Telephone Nigam Limited (MTNL). MTNL, set up recently, is responsible for operations which earlier formed part of the activities of the GOI's Department of Telecommunications.

Sources: Based on data from several sources, including: Government of India: Expenditure Budget 1987/88 and 1988/89, Volume I; and K. S. Sastry: "Financial Performance of Public Enterprises in 1986/87 and Prospects for 1987/88 and the Remaining Part of the Plan Period with Emphasis on Resource Mobilization", Keynote Address Delivered at the Conference of Chief Executives of Public Enterprises, New Delhi, January 14, 1988.