



An Evaluation of Profitability of Public Sector Undertakings (with Special Reference to Iron & Steel Units)

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Abstract

Earning profit is equally important for all undertakings whether manufacturing or providing services, and whether in public or in private sector. The nationalization of the basic industries and setting up public sector undertaking have been entrusted with the responsibility to look after the requirements of the relevant services as the basis of economic development and also to develop the socio-economic status of the society, by making them available comfortable, economical and effective services/raw materials. It clearly indicates that various units under steel sector being a public sector undertaking should run with adequate profits. Iron and steel is the backbone of almost all the large-scale industries including construction services, as without plant and machinery no industry can produce or manufacture anything. Even the small-scale industries get their primary infrastructure from iron and steel. In more clear terms, a basic industry like iron and steel has to consider itself as one of the infra-structural institutions and has to work as per the requirements of the country's industrial and economic development as a whole. Since poverty and unemployment are the two major problems of the country, the iron and steel industry assumes a wide responsibility to play its role in solving the problem of unemployment and thus, also to reduce the clutches of poverty to a more or less extent as the iron and steel is one of the employment generating industries. In fact, the iron and steel Industry being a basic industry creates a basis for the economic and industrial development, and by making this development possible, it reduces poverty, raises the standard of living of the people and improves the socio-economic status of the masses. All these responsibilities have added a new dimension to the public sector industries in steel sector. If the objective to earn profits is kept in mind in the normal working of steel Industries, public sector undertakings under steel sector cannot fulfill such obligation to the people as well as the country by ensuring adequate supply of iron and steel, which is an infrastructural necessity of almost all the large scale industries. In this research paper the authors have taken all the causes of poor profitability in public sector manufacturing undertakings and also suggested some suggestions for improving the profitability of public sector.

Key words: PSU, MOU.

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1. INTRODUCTION

Profit is the ultimate result of all the business concerns. The objective of all the business concerns is to secure a fair return on capital employed. Profit should always be seen as a measure of efficiency of the capital employed. If the investment does not earn satisfactory rate of return, it would be a concerning factor for the enterprise for itself and also for all the other related parties. Essentially, profit is the owner oriented concept and it signifies the share of income which goes to those who contribute in the equity of the enterprises. However, profitability is operation-oriented and it is related to creation of new wealth. We may, thus, stress that potential profitability of different alternatives provides the criterion for economizing the case of productive resources, while profit maximization is the mission for economic effectiveness. In the Public Sector Units (both Manufacturing and Service Rendering Units) there has been a problem of poor profitability if we could solve the problem of poor profitability; the public sector would prove its worth and social relevance. Profit is the main driving force which keeps the concern in to operation. In the absence of appropriate profits the production process would come to set at rest. Profitability is the benchmark for measuring the performance of any commercial organization. Without sufficient profits, the continuance of any unit would be difficult for the reason of inadequate profitability; the public sector units have invited several criticisms from all corners.

Some think that public sector units have their own social relevance, undoubtedly; the losses in these units cannot be taken up very freely in the name of the social excuse. The public sector units must earn at least some minimum percentage of profit on the capital employed. The impact of inadequate profitability in the public sector units may be pin pointed as under.

2. OBJECTIVES

- To focusing on the different causes and effects of poor profitability of public sector manufacturing enterprises.
- To provide the solutions for improving profit

3. RESEARCH METHODOLOGY

Both primary and secondary data is used for the purpose of analysis. We visited various public sector undertakings for research on several occasions. And secondary data is taken from Annual reports of company, journals, research papers and various books.

4. LIMITATIONS

In this research paper we have included only 5 units of public sector undertaking, so our research is limited to these five iron and steel units. These five units and their year of incorporation is as under:

Table 1: PSEs Manufacturing and Selling Steel

| Sl. No. | Name of Enterprise | Year of Incorporation |
|---------|--------------------------------------|-----------------------|
| 1. | Steel Authority of India Ltd. (SAIL) | 1973 |
| 2. | Maharashtra Elektros melt Ltd. (MEL) | 1974 |
| 3. | Sponge Iron Indian Ltd. (SIIL) | 1978 |
| 4. | Ferro Scrap Nigam Ltd. (FSNL) | 1979 |
| 5. | Rashtriya Ispat Nigam Ltd (RINL) | 1982 |

5. CHALLENGES BEFORE PUBLIC SECTOR

It would be unreasonable to argue that all is well in the public undertakings. There is much scope for improving the efficiency and working of public sector enterprises. The main points which are worth thoughtfulness given below:

- It has been noted that in many situations, political factors influence decisions about location of projects. Powerful ministers in the ruling party promises about the future location of projects in a state irrespective of the result of the feasible study about costs.
- Public sector projects are charged with over-capitalization. In other words, the input-output ratio obtaining in many projects was unfavorable. The Study found several undertaking over-capitalized. The cause leading to over capitalization can be traced to inadequate planning delays and avoidable expenditure during construction, surplus machine capacity, tied aid resulting in the compulsion to purchase imported equipment on a non-competitive basis, expensive turn-key contracts, bad location of projects and the provision of housing and other amenities on liberal scale.
- The pricing policies of the public sector undertakings are not guided solely by the profit maximization principle, but are under the regulation and control of the Government. Most of the public enterprises produce products which serve as inputs for other sectors of the economy. It would be suicidal from the point of view of the overall growth of the economy if the prices of steel, oil, fertilizers or coal are fixed very high. The public sector has to keep in mind the social implications of its price policy. In this connection it is important to remember that in many cases, under public pressure, prices are kept low even when costs and prices have been rising. This naturally adversely affects commercial profitability.
- It has been brought out that in most public enterprises manpower is in excess of actual requirements. There is poor manpower planning and this is clearly reflected in the inadequate arrangements for training and education of workers. The unsatisfactory salary and wage rates and the absence of incentives to staff have resulted in the flight of personnel from the public sector to the private sector. It has been suggested that top position in a public sector undertaking should also be opened to its employees.
- Labour indiscipline was one of the causes for the poor show of the public sector enterprises in recent years. Labour relations plagued many of the large government enterprises. Supervision is also difficult in oversize undertakings. The situation is not very happy. Government should make a unwavering proposal to look up industrial relations.
- Managerial effectiveness and efficiency are crucial factors in improving the overall performance of the public enterprises. For efficiency in business and industrial enterprises it is necessary that operational decisions should be prompt. This necessitates a large measure of autonomy and flexibility of operations in the Government enterprises. Again, delegation of authority and elasticity in working are needed in a high degree. Within the enterprise itself the delegation of authority from the top management to lower levels is another essential condition for efficiency in operation. Every officer should know what he is required to do and what result he is expected to produce. Unfortunately, there has been general failure to define responsibilities and duties in public sector enterprises in India.

6. MAIN CAUSES RESPONSIBLE FOR POOR PROFITABILITY IN PUBLIC SECTOR UNITS

The causes responsible for poor profitability in public sector units have been:

1. **Commissioning the Projects:**-Heavy cost of commissioning the projects, taxes and the related concerns keeps the profitability of the units poor.
2. **Gestation Period:**-These units have long gestation period, these units take long time in producing results in terms of profits. The profit yielding state comes after a very long time. This all reduced profitability aspect of the concern.
3. **Welfare Expenses:**-Expenses made on welfare measures become an integral part of the cost of production. This all renders the profitability of these units poor.
4. **Cost in Expansion:**-In the expansion of the public sector units heavy cost is involved. The profits of the expansion of the units may be had at a later stage. This all renders the profitability poor at least for some time.
5. **Expense Ratio:** - In these units the expense ratio usually runs higher. This all reduces the profitability of the units.
6. **Production of Low Priced Items:** - The public sector units produce/supply of low priced items in case of certain products, the prices are fixed at a lower rate than the cost of production in some cases. This all hampers the profitability of the units.
7. **Lack of Efficiency:** - Lack of efficiency added and individual performance.
8. **Poor Management Practice:** - Inefficiency arising out of the poor management practice.
9. **Delay in Audit:** - Delay in auditing the financial performance and lack of an effective internal check system.
10. **Heavy Losses of Loans:** -Heavy losses of loans with a fixed and recurring burden of interest and increase in cost element of the units.

These units have been facing the acute shortage of resources and are heading towards economic reforms and financial discipline, in all these conditions the losses of public sector units would have to contain and quantum of profitability upgraded in a realistic manner. It is a hard fact that a long term and realistic solution to the problems would alone strengthen the base of the public sector units. The government would lay emphasis on improving the performance of public sector. It was made clear that government would strengthen the public sector units which fall in the reserved areas of operation or are in high priority areas. These units would be provided a much greater degree of management autonomy through the system of MoU. In the case of selected enterprises, the equity share capital will be disinvested in order to provide further market discipline. The government has highlighted in the industrial policy that technological up gradation through an integrated R&D efforts and import technology would be restored. In the matter, better R&D practices would be restored for improving the productivity of public sector units and this would help in attaining better rate of profitability. The government of India decided to enter into Memorandum of Understanding (MoU) with the largest Central Government owned Public Sector Enterprises in India. The MoU is a document in which the government and related units enter into agreement and decide mutual obligation and responsibility. The scheme of privatization and Memorandum of Understanding are the outcome of the poor performance of public sector units. Both the schemes are responsible to a question that the public sector has not developed the levels it was supposed to do so. Privatization is a long

drawn and continuous process even when the state decided to private its assets. The common minimum program (CMP) of United Front Government 1996, sought to carefully examine the public sector non-core strategic areas and to set up a Disinvestment Commission for advising on the disinvestment related matters; to take and implement decision to disinvest in a transport manner and to ensure job security, opportunities for retraining and redeployment. The commission has recommended disinvestment of varying levels for a number of PSUs, Strategic sales in various proportions have been recommended for many enterprises.

7. CONCLUSIONS & SUGGESTIONS

It may be said that removing corruption in the public sector units, improving technology, implementing better R&D measures, involving private skill and entrepreneurship ensuring sincere and honest involvement of worker through effective work ethics and culture, using stick against ailing units, improving managerial efficiency, making work and performance the main security of the employers and ensuring private participation in the public sector units in general and service units/groups in particulars. Unless we provide a long-terms practical solution to the problems of poor profitability the very notion of social contribution of the public sector units would be immaterial from the angle of profitability, Public sector units in India all together have been an utter failure. However, it is inspiring to note that lately the government has shown heartfelt wish and will in its parts to deal with the problem and has started taking strict action the below par units. So far, the government has used the carrot, and now the government has warned all the sick units that the stick shall now be used against them, if they do not perform well. The public sector units should have to strong on the profitability front or they would be handed over to private sector. Entire public sector is presently suffering from the severe ills, which list upon adversely on the very survival of the public sector. Unless we ensure better performance of the profitability level, the social concept of public sector would stand a myth. Following suggestions are referred to improve the profitability and over efficiency of the entire public sector:

- To establish long - term relationship with the major customers through a memorandum of Understanding (MOU) and better customer service;
- The units whose profitability measured as return on net worth has been less than ten percent continuously for the last five years be handed over to the private sector;
- To improve sales by introducing the systems like Order Booking System, After Sales Service, Customer Feedback System, etc;
- To increase the revenue from interest and dividend, it should invest its surplus funds in short term deposits;
- To arrange the sales of empties at frequent intervals to ensure their full value and prevent them from any deterioration lying in the workshops;
- To provide export services to its customers and, thus, to increase such head of earnings;
- To make all efforts to avoid strikes and lock-outs because it is the employer who has to suffer because of such strikes and lock outs. All possible efforts should be made to maintain the harmonious labor-management relations;
- To improve efficiency and productivity through incentives;

- The employees should made realize the value of such welfare measures in terms of motivation;
- All basic industries like steel should be exempted from the Corporate Tax;
- Stern warning should be given to sick public units and if they do not respond effectively, the related units should be wound up;
- The effective work ethic should be developed and the result oriented performance be made criterion for promotion;
- The politicians and bureaucrats should be kept unapproachable from the control and management of these units;
- Efforts to be made to ensure efficiency audit, cost audit and internal check measure;
- The public units losing continuously should be sold out to private entrepreneur;
- A separate high-power board be set up at the centre for monitoring, streamlining the performance of public sector units;
- On the profitability front only those units should be granted concession which could be reviewed and made viable;
- The schemes of economic reforms, revival measures, concessions, privatizations, disinvestment etc. be not taken up as an end in themselves but on the starting point;
- Privatization and disinvestment schemes be not taken up as an end in the matter of privatization and disinvestment the following points be considered;
- Procedural safeguards for the interests of the state should be ensured;

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