

When sacred cows block the intersection

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While much of the media and policy debate focuses on private infrastructure providers, most of India's roads, ports, airports, telephone connections, electricity and other infrastructure is provided by public-sector companies or departments.

Their performance obviously has an enormous impact on the quality of infrastructure. Every rupee spent on obsolete equipment, or not spent on maintenance, means one more reason for complaint for customers. But it is not just customers that are affected: public sector performance affects private providers' services as well as the overall business climate for private entry. Public entities are customers, competitors, suppliers, and carriers of private infrastructure services.

In telecom, private investors compete with public companies in all segments of the market. Service quality depends on interconnection with public networks BSNL and MTNL, which provide most of the fixed-line service and a significant share of wireless services. Many - though not all - of the most congested interconnections are between BSNL and private companies.

Similarly, private operators compete with public companies in transport, and rely on them as interconnected transport network and service providers. The public sector Indian Airlines still accounts for just over 21 per cent of domestic air travel, the second-largest market share among domestic airlines. Airlines land and take off at publicly owned and operated airports, where runway traffic forces planes to burn costly time and fuel in circling.

Regulatory favoritism for public-sector companies, real or perceived, has a deterrent effect on potential competitors in both sectors. Regulators' choices, whether in allocating lucrative air routes or scarce telecom spectrum, have the ability to dramatically shift companies' fortunes.

These public companies are the sacred cows in the middle of a busy intersection. They cannot be hurried or bothered, but at the same time they are risky customers, unreliable carriers, and threatening competitors that clog up the flow.

What are steps to clear the crossroads of these cows and improve public infrastructure provision?

First, India must continue and accelerate the move toward more commercial practices. Competitively selected professional management, even through international recruitment, should become more common. International competitive bidding is as important for talent as for projects. Benchmarking between public enterprises and private competitors, as is proposed for public sector banks, is also important.

Listed public-sector undertakings should also increase the proportion of independent directors (and thereby the potential expertise and oversight) to the SEBI standard of half. This will likely require some reduction in the number of government appointees.

Second, the norms for public companies should be altered to remove procedural restrictions that both hamper performance and provide excuses for poor returns. The most commonly cited constraints or excuses are that public companies have to obey civil service procurement procedures and provide uneconomical social services.

The present norms for procurement pose a trade-off between red tape and corruption: red tape, while frustrating, is meant to reduce corruption. There are other ways to reach the same goal of limiting corruption, without the costs of red tape, however, including stronger performance incentives for managers. Managers whose job and salary depend on commercial success are less likely to accept substandard goods for a bribe.

The cost of social obligations should be made more transparent, and accounted for explicitly in public companies' statement of performance. This will enable shareholders and the public in general to better evaluate public companies' contributions on both fronts. The subsidies to public enterprises for social services should be thought of as "viability gap funding," to be extended to public or private infrastructure providers (or used for other pressing needs.)

A more transparent and credible subsidy regime could also encourage private companies to bid to meet social obligations.

Third, India needs to create a firewall between the infrastructure incumbents and regulators. Ministers and secretaries should not serve as intermediaries between public-sector companies and regulators. India's need for regulatory independence has been noted before; reducing the deterrent effect of public incumbents is one more reason to move forward.

Taming the tuskers may also require more disinvestment. Increasing the proportion of non-government shareholders creates an arms-length relationship between public companies and government backing, assuring other competitors of a fairer playing field in addition to increasing incentives for performance.

Disinvestment through a program designed to encourage small shareholders, as has been done in countries ranging from Great Britain to Peru, will return public-sector companies to the actual public.

Sacred cows move slowly. But every small step in the right direction means that the momentum forward can be that much greater. Any reform matrix must not overlook the obvious.

Regular columnist N.K. Singh and Dr. Jessica S. Wallack, a professor of economics at University of California, are collaborating on a book on infrastructure reforms on India. Essays based on their research will appear on a bi-weekly basis.