Disinvestment and Firm Performance- A Comparative Analysis of Strategic Sale vs. Public Offerings by Indian Pubic Sector Enterprises

Dr. Himanshu Joshi
Associate Professor
FORE School of Management
New Delhi
Email: himanshu@fsm.ac.in

Abstract

The state owned enterprises tend to suffer from operational and financial inefficiency due to severe agency problem and lack of market discipline. It has been assumed that private ownership is associated with a more effective incentive structure than public ownership; and there exist several mechanisms such as shareholder's activism in the stock market, takeover bids and bankruptcy threat in the private sector which constraint agents to pursue their own objectives at the cost of the principals. Disinvesting the state's stake in the state owned firms to either a strategic partner or offloading it to the general public or financial institutions, is considered as one of the effective solution to the agency problem of these firms. Sale of stake to the strategic partner is suppose to inculcate profit maximization objective in state owned firms and offloading minority stake to the general public and/or financial institutions is suppose to bring the firm under stock market monitoring mechanism, and better analyst coverage.

In the present paper, two modes of disinvestment are compared and contrasted for pre and post disinvestment performance of firms on certain parameters such as valuation, financial leverage, and operating efficiency. Paper found no statistically significant difference between pre and post disinvestment valuation ratios, financial leverage, and operating efficiencies for either of the data sets, i.e., minority sales as well as strategic sales. However, results indicate that strategic sale as a mode of disinvestment improves the valuation, operating efficiency and financial leverage for the firm.

Key Words: Disinvestment, Strategic Sale, Minority Sale, Agency Problem.

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