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Case

A Journey towards Excellence: Steel Authority of India Limited from Navratna to Maharatna

Niranjan Kumar Singh[1] and Nita Choudhary[2]

Abstract

The Central public sector enterprises (CPSEs) have played a key and vital role in developing the nation on the global map. In 1996-1997, it was decided by Government of India that public sector companies having comparative advantages should be supported in terms of grant of autonomy in their drive to become global giants. SAIL was one of the companies identified by the Government to start the drive for grant of autonomy. This paper will focus on the journey of SAIL towards Maharatna status from Navratna and how the strategic decisions of SAIL has affected its performance due to economic reforms and fluctuating market conditions in the way to become a global giant.

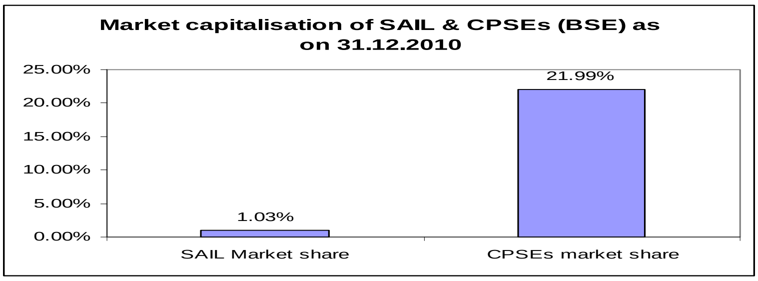
[1] Dept. of Management Studies, Jain University, Bangalore – 560004
E-mail: niju98@gmail.com,

[2]Dept. of Management Studies, Jain University, Bangalore – 560004.
E-Mail: nitu_bit2005@yahoo.com

Introduction

Central public sector enterprises (CPSEs) play a vital role in the development of the country in global arena having a 21.99 % of market capitalization as on 31.12.2010.

Figure 1: Market Capitalisation of SAIL as on December,2010



Source: http://divest.gov.in/Market_Capitalisation.asp?ord=comp_name

Steel Authority of India is one of the CPSE. Steel Authority of India Limited is India's largest steel producing company with a turnover of Rs. 43,935 crore, the company is among the four Maharatnas of the country's Central Public Sector Enterprises. SAIL has five integrated steel plants, three special plants, one subsidiary and nine joint venture companies in different parts of the country. The government of India has accorded the status of 'Navratna' and 'Maharatna' to Steel Authority of India (SAIL) through a memorandum DPE O.M. No. DPE/11(2)/97-Fin. dated 22nd July, 1997 and No. 22 (1) / 2009-GM-GL-101 dated 19th May

2010 respectively. The objective is to give more autonomy to the company so that they can take on global competition.

At the end of year 2009, the government announced a new policy under which select top performing central public sector units would be delegated substantially more financial and managerial powers than what they already have. The policy approved by the Cabinet seeks to provide further incentives to public sector enterprises that are in the category of Navratnas and already enjoy a substantial measure of operational freedom.

Literature Review

SAIL fulfilled all the eligibility criteria set by the Department of Public Enterprises (DPE), Government of India for achievement of Maharatna status as given below:-

Table 1: Status of SAIL's Fulfilment of SAIL's Criteria

Sl.No	Criteria suggested by DPE	SAIL's status on fulfillment
a.	An existing Navratna status	Since 1997
b.	Listed on the stock exchanges with minimum public shareholding as prescribed by the SEBI.	Since 1992
c.	An average annual	Average annual turnover in

	turnover during the last 3 years of more than Rs.25,000 crore	last 3 years is Rs. 44,475 crore: 2008-2009 – Rs. 48,681 crore 2007–2008 – Rs. 45,555 crore 2006-2007 – Rs. 39,189 crore
d.	An average annual net worth during the last 3 years of more than Rs.15,000 crore	Average net worth in last 3 years is Rs. 22,724 crore: As on 31.3.09 – Rs.27,984 crore As on 31.3.08 – Rs.23,004 crore As on 31.3.07 – Rs.17,184 crore
e.	An average annual net profit after tax during the last 3 years of more than Rs.5,000 crore	Average net profit after tax in last 3 years is Rs. 6,638 crore: 2008-2009 – Rs. 6,170 crore 2007-2008 – Rs. 7,537 crore 2006-2007 – Rs. 6,202 crore

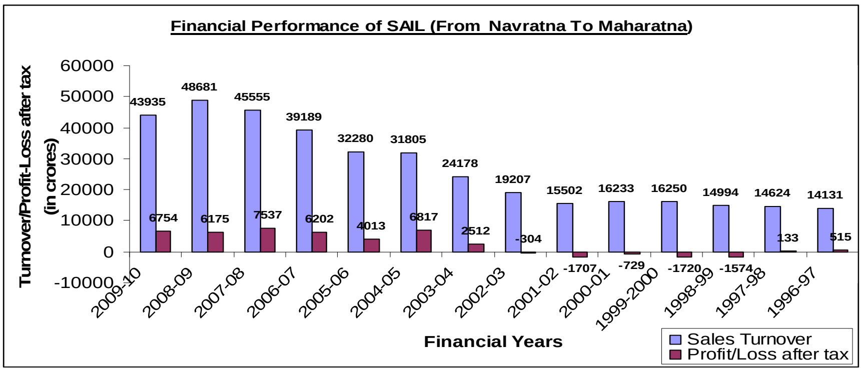
f.	Significant global presence or international operations	a) SAIL's International Trade division exports to around 20 countries, including the EU, Middle East, SE Asian countries etc. SAIL also has its offices in China & Nepal. b) SAIL is a JV partner in International Coal Venture Limited formed with other Navratna companies – NTPC, NMDC, CIL & RINL –for the purpose of acquiring coal mines/equity in coal mines abroad. c) SAIL has a Consultancy Division which has been providing consultancy to many of the steel companies in the world, especially in the Middle East. d) SAIL is implementing its expansion plan with emphasis on state – of – the – art technologies which will enhance SAIL's hot metal capacity to over 26 million tones per annum from the current level of 14 millions tones for which major equipment and technologies are being sourced from abroad.

Source: http://www.sail.co.in/pdf/maharatna.pdf

Enhanced Autonomy of SAIL with Maharatna Status

The boards of SAIL will have powers for equity investment to establish joint ventures and wholly owned subsidiaries in India and abroad. SAIL can undertake mergers and acquisitions in India or abroad. However, company will have a ceiling of 15 per cent of its net worth for investment in a project. There will also be an absolute ceiling of Rs.5, 000 crore for each project. The board of directors can also fill up most managerial positions without government clearance up to E9 level.

Figure 2: Financial Performance after becoming Navratna



Source: Annual Reports of SAIL

The steel-making giant once considered a jewel in the public sector crown in July'1997, faced massive hemorrhaging.

SAIL, which has the largest workforce among corporate entities in the country, had been a profitable enterprise until 1996-1997. However, it suffered a sudden downturn in 1998-1999 and posted losses of Rs. 1,574 crores. In terms of provisions of Sick Industrial Companies (Special Provisions) Act 1985, the case of SAIL was report to BIFR.

Objectives of the study

1. To examine the reasons for SAIL's decline and almost imminent fall.
2. To study what key strategic decision taken
3. To study the result of strategic decisions of SAIL

Data and Research Methodology

The entire data used for the present study have been obtained from the secondary sources; the data required for the analysis of different periods are collected from

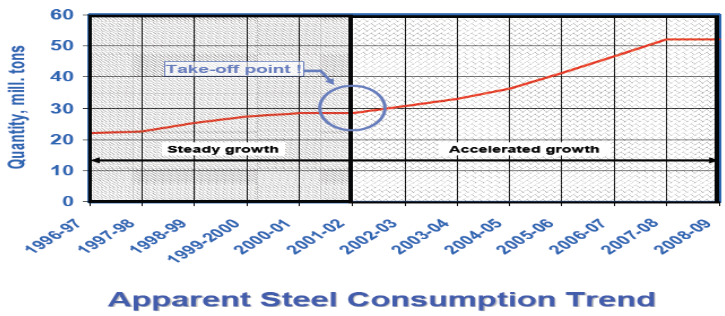
1) SAIL Annual Reports
2) Reports of department of public enterprise, government of India
3) Financial and business-restructuring plan proposed by McKinsey & Co in Feb'2000
4) Data published by the Steel Exporters Forum (SEF)

Reasons for SAIL's Decline and Almost Imminent Fall

1) <u>Sluggish demand in the steel consuming sectors</u>

The demand for steel slowed down mainly due to the poor take-off of infrastructure or construction, auto, oil sector, power sector, fertilizer sector projects where the intensity of steel consumption is high and low levels of foreign direct investment and private investment (Sridhar, 1997). Fig.3 shows the steady growth of the steel consumption from 1996 to 2002 (Roy, 2009).

Figure 2: Apparent Steel Consumption Trend



Source: CII Steel Summit 2009

2) <u>Overall economic slow down in the country</u>

All major core sectors of the economy was facing an economic slow down. These include power, coal, cement industry, mining and steel. The slow down phenomenon was not restricted to the steel sector alone. Only when the overall economy of the country picks up, the steel sector would also show signs of revival.

3) Lack of investment by Government/private sector in major infrastructure projects

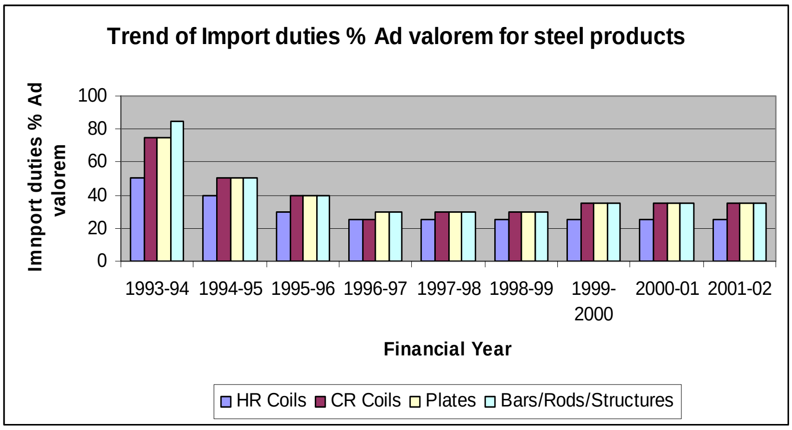
Due to budgetary constraints, no major construction activity in mega projects including fertilizer, power, coal, railways etc. was planned by the Government. Despite liberalization of the economy and relaxation in the investment norms, private sector investment was yet to materialize in the core sectors of the economy. This also contributed to slowing down demand for steel.

4) Continuous reduction in import duty on iron and steel

After liberalization, import duty rates on iron and steel items gradually reduced over the years. This opened up the domestic iron and steel sector to international competition. Due to rationalization in the import duty structure in 1999-2000, the rates of basic custom duty generally went up. The fall in customs duties attracted desperate steel producers from abroad to India. SAIL had to contend with steel imports from

Ukraine, Russia and other countries, which sold steel here at prices below their cost of production.

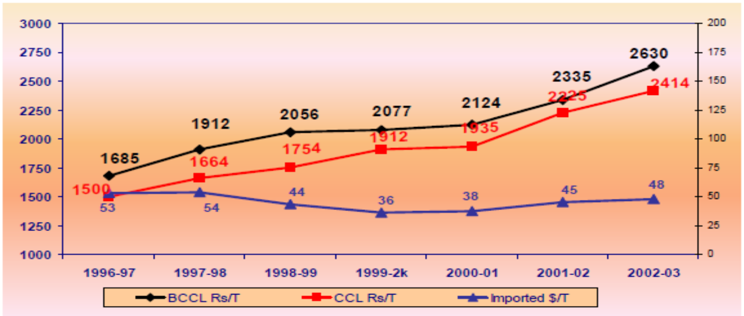
Figure 4: Trend of Import Duties as % Advalorem of Steel Products



_**Source: Annual Report (2001-02), Ministry of Steel, Government of India, Chapter 11, page no.8**

5) <u>Cost escalation in the input materials for iron and steel</u>
Power tariff, freight rates, coal prices etc. have been under the administered price regime. These rates have been frequently enhanced, thereby contributing to the rise in input costs for steel making. Coking coal constitutes nearly 30% of cost of steel production in India (Prakash, 2003).

Figure 5: Price Trend of Coal from Various Sources



Source: Prakash, C (2003),
BCCL: Bharat Coking Coal Ltd, CCL: Central Coalfield ltd.

6) Modernization Effect

Huge investments in update, plants were in a position to achieve significantly higher production and thereby economies of scale but the market situation did not permit them to derive optimum benefits of modernization. The modernization programme was being entirely funded by internal resources and commercial borrowings. SAIL's problems compounded by the high interest charges it incurred in mobilizing commercial borrowings for the programme. SAIL's modernization drive to make hot rolled coils was delayed for seven years since 1990) because of the delays in getting Government approvals. By then the competition had already moved in with upgraded technology.

7) <u>Merger of VISL</u>

Visvesvaraya Iron & Steel Limited (VISL) merged with SAIL in 1998-99. At the time of merging, it was a loss making company.

8) <u>Retirement age from 58 to 60 years</u>

By increasing the age of retirement from 58 to 60 years in May 1998, the Company overlooked the recommendation of Disinvestment Commission of March 1998 for downsizing the manpower.

In order to assist the Company to improve its poor financial health and make it profitable on sustainable basis, the Government of India approved a big restructuring package for Steel Authority of India Ltd. (SAIL) in February 2000 to be completed over a 2-year period. But this decision was delayed.

While approving it, the Government of India (GOI) noted that since financial re-structuring alone was not a long term solution, Ministry of Steel (MOS) signed a Memorandum of Understanding (MOU) with SAIL for implementation of a business restructuring with detailed milestones. The financial re-structuring measures aimed at mitigating the financial risk by improving the Company's debt service capability while the business re-structuring measures aimed at providing long-term competitiveness to the Company in its core business of carbon steel.

SAIL management appointed Mckinsey, a World Bank sponsored MNC consultancy firm, to suggest restructuring of the organization. In March, 1999, Mckinsey gave the following recommendations: -

1) Sale of Alloy Steel Plant Durgapur, Salem Steel Plant and VISL.

2) Privatization of IISCO.

3) Advised SAIL to reduce its workforce from 1, 70.000 to 1, 00,000 by 2003 and increase the workload on the workers.

4) Advised to divide the four integrated steel plants into two strategic business units (SBUs), one for flat products, comprising the Bokaro and Rourkela plants and the other for long products, comprising the Durgapur and Bhilai plants.

5) Advised SAIL to revamp its Central Marketing Organisation (CMO) in order to save on operating costs, to improve quality

6) Inventory- reduction

7) Advised to be on the Core areas

SAIL did not accept all the recommendations given by McKinsey.

Strategic Decisions taken by SAIL & its effect

1) SAIL planned a cost-reduction target of Rs. 1,000 crores in 1997-98. The plan was to use less coal, increase yields and improve operational performance at each stage of processing to cut costs. A detailed micro-planning was made to reducing costs. In the first six months of 1997-98 (ending September 1997), the company reduced costs by Rs. 277 crores. In five years from 1997-98, a cost saving of over Rs 3,000 crore was achieved - Rs 731 crore in 1997-98, Rs 812 crore in 1998-99, Rs 533 crore in 1999-2000, Rs 525 crore in 2000-01 and Rs 450 crore in 2001-02 (Sinha,2002).

2) Divestments and long-term lease of houses in steel plant townships. The upfront realization was Rs. 172 crore.

3) For SAIL, manpower costs alone accounted for 16.69% of the company's gross sales in 1999-2000. This was the largest percentage, as compared with other steel producers such as Essar Steel (1.47%) and Ispat Industries (1.34%). During 2000-01, 2001-02 & 2002-03 (upto 30th September2002), the Company separated 10368 employees through VRS against

the proportionate target of 25,000. In the process, the Company was unable to use fully the subsidised loan of Rs.1500 crore guaranteed by the Government to reduce its manpower.

4) The Company was losing heavily in IISCO, SSP, ASP, & VISL, but it failed to sell them off on priority basis. Due to socio-political resistance from employees and political parties, non/ inadequate-response etc," targets were not achieved. Instead the Company opted to divest profit generating power plants. Due to divestment of power plants to joint ventures formed on 50:50 basis with other public sector undertakings, the Government of India continued to remain, in essence, a major stakeholder in all the power plants. Further, the Joint Ventures have refused to accept the excessive manpower and the Company continued to be saddled with the loss making units and incur heavy losses.

Table 2: Comparative Financial Performance Pre and Post Restructuring

(Rs. in crore)

	Pre-Restructuring period	Post Re-structuring period

	1997-98	1998-99	1999-00	2000-01	2001-02
Sales	14665	14994	16250	16233	15502
Other income	678	671	1009	781*	1284**
Total income	16403	14983	15296	17118	16364
Expenditure	13905	13480	14094	14951	15353
Interest	1554	2017	1789	1752	1562
Depreciation	795	1104	1133	1144	1156
Net profit/ (-)loss	149	(-)1618	(-)1720	(-)729	(-)1707

Source: CAG Report 2002 – 2003

5) Steel Authority of India Ltd, Tata Steel and Kalayani Steels Ltd signed a joint venture agreement for the formal creation of metaljunction.com Pvt. Ltd, to manage their e-marketplace, metaljunction.com in 2000.

The year 2003-04 was a remarkable one for the international steel industry. After a prolonged period of depression, the industry was able to bounce back into the reckoning during 2003-2004, following strong revival of steel demand, triggered mainly by China. As the months passed, there were symptoms of all round recovery and soon the demand upsurge in South East Asia, Europe and USA strengthened the positive trend.

Quite in tune with the global recovery, steel demand in the domestic market also headed northward, backed by 8.2% growth in GDP during 2003-04. Manufacturing was up by 7.3% while the consumer durables sector grew by 11.5%. Demand for steel increased by 5% in 2003-04. Steel consumption projected to grow by about 6% to 7% in 2004-05 with continued growth in construction and automobiles, besides improved outlook for the general engineering sector.

The year 2003-04 was remarkable for SAIL. SAIL was bestowed with the prestigious national award for ‘Excellence in Cost Reduction (Manufacturing Sector)’ for the year 2003 and the Golden Peacock Innovation Award presented by the Institute of Directors further acknowledged its efforts in the area of research and development. Besides these, the company received several reviews in the media for authoring one of the most spectacular turnarounds in the history of the Indian corporate world.

The ongoing modernization process, cost reduction in production, optimum utilization of resources, non-selling off of IISCO, SSP, ASP, & VISL clubbed with the strong demand of steel in 2003-2004 led SAIL to bounce back on the profit of Rs.2512 crore from a loss of Rs.304 crore in 2002-2003.

Conclusion

The growth plan envisaged full utilization of all existing assets along with technological up gradation in identified areas to raise hot metal production to about 20 million tons per annum by 2012 from the current level of 13 million tons and the proportion of finished steel to be enhanced to a level of above 95%, from the existing level of about 80% (in 2003-2004).The Corporate Plan was visualized in 2004 at an investment of about Rs. 25,000 crore up to 2011-12. From financial 2003 – 2004 onwards, SAIL never ending journey towards excellence started and received “Maharatna” status in May, 2010.

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