Adventures in capitalism

Indian businesses are rewriting the rules of capitalism in a distinctive and unexpected way, says Patrick Foulis

ON AUGUST iST India's finance minister, Pranab Mukherjee, gathered the country's sênior businesspeople for a pep-talk in New Delhi. The event (pictured) was notable for two reasons. First, the subject of discussion was the wobble in confidence that has taken place over the past year. Although a mini-industry has arisen of índia optimists who predict that the country's entrepreneurial spirit will make it an economic superpower over the next two decades, many business folk on the ground feel disillusioned. They worry that India's notorious red tape, graft and lack of infrastructure are finally catching up with it. Largely unnoticed abroad and eclipsed by the rich world's sovereign-debt crisis, the Indian economy has hit a sticky patch, with investment slowing, inflation high and growth expected to dip to perhaps 7%, from a peak of 10%. After two and a half hours, needless to say, the bosses emerged and expressed boundless optimism with the gruff air of men in the grip of a half-Nelson.

The second surprise, given India's reputation as a land of red-hot start-ups and new entrepreneurs, was the dynastic nature of those captains of industry. They included Ratan Tata, the fifth-generation head of Tata Sons, a conglomerate; Anand Mahindra, the chief executive of the Mahindra group, which was co-founded by his grandfather; and Anil Ambani, who inherited a chunk of the Reliance empire built by his father. The main representatives of first-generation entrepreneurs were Shashi Ruia, who built the Essar group with his brother and who has handed day-to-day management to his son; and Sunil Bharti Mittal, who controls India's biggest mobile-phone operator, and whose son recently joined the firm after a stint as an investment banker in London. True, not ali Indian firms are dynastic: Y.C. Deveshwar, a veteran business leader, attended in his capacity as chairman of **ITC,** a firm controlled by institutional investors, rather than a family. But **ITC** has become the kind of conglomerate that Western textbooks advise against, spanning everything from stationery, cigarettes and spice-grinding to noodles and hotéis.

Amid the barons and conglomerate bosses, the only man who represented a recognisably contemporary Western vision of the Corporation was N.R. Narayana Murthy, the lead founder of Infosys. It is focused on one business line, computer services, which are mainly sold to rich countries. And it is owned by diffuse institutional shareholders, has gold-stan-

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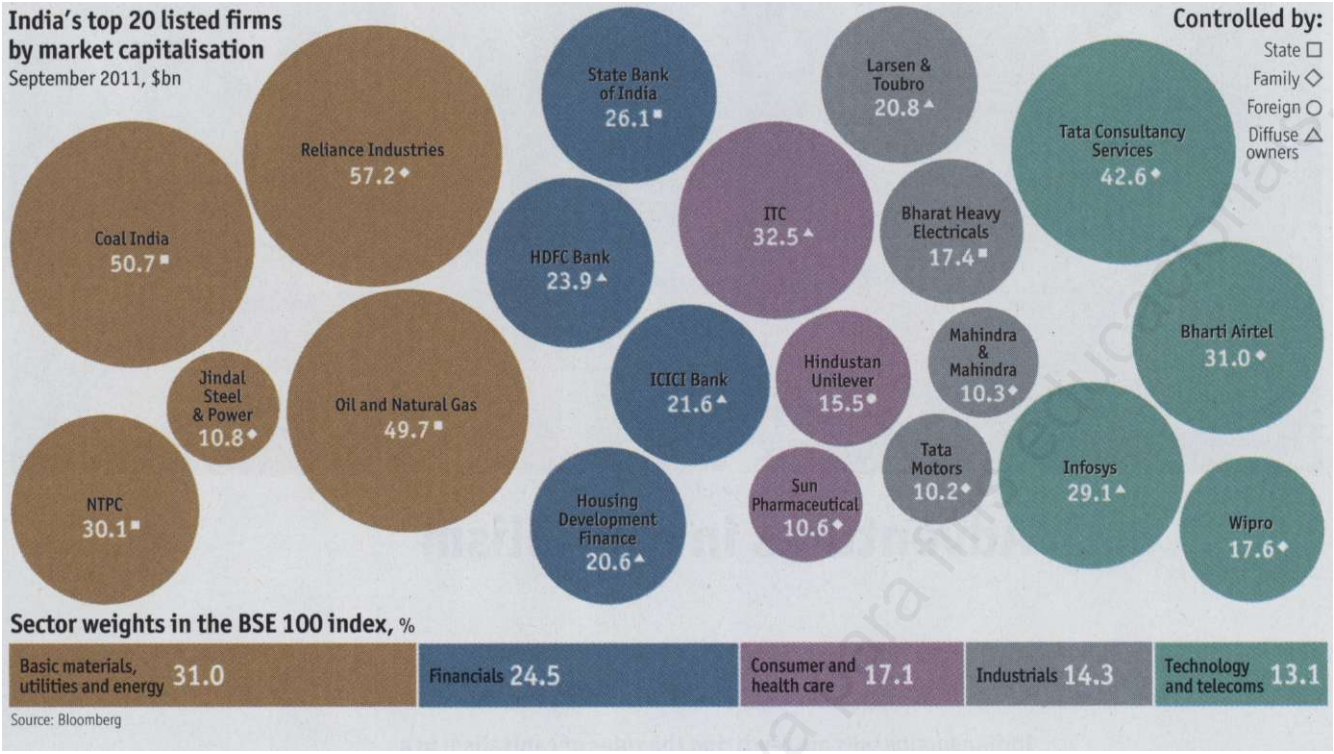

dard corporate governance and accounting, and in the next four years is expected to wave goodbye to the last of its founders still playing an executive role. It is a corporate fairy tale: in a single generation Infosys has leapt from a start-up, founded by a handful of engineers with $250, to global blue-chip company. The Infosys vision of Indian capitalism was popularised by Thomas Friedman, an American journalist who had an epiphany after playing golf in Bangalore and meeting Infosys's chief executive. Mr Friedman went on to write the 2005 bestseller "The World Is Fiat". It described an índia of buzzing entrepreneurs and start-ups, turbocharged by the internet, outsourcing and global communications-a kind of giant Silicon Valley with worse roads and spicier food. In the years since, perhaps reflecting the woes of the West and the rise of China's state-backed approach, some observers have been less restrained, celebrating a reassuring índia of a billion innovators who, through a bottom-up revolution, would propel their country to prosperity.

Just as Lenin hoped Rússia could skip a Marxist phase or two and jump from agriculture to communism, so these cheerleaders hoped índia could leap from sclerotic socialism, which prevailed between independence in 1947 and liberalisation in 1991, towards a Western form of institutionally run capitalism. But that is not how things have turned out. Infosys has just been overtaken as India's most valuable computer-services firm by **TCS,** part of the 143-year-old Tata group. Look at India's leading 100 firms by market value and you will not see any others like Infosys-blue-chip, focused, diffusely owned, created in the past three decades and run on non-hereditary principles-bar a few financial firms. And whereas Mr Friedman cited "software, brainpower, complex algorithms, knowledge workers, call centres, transmission protocols [and] breakthroughs in optical engineering" as the new sources of wealth, many of the latest generation of Indian oligarchs made their cash from old-fashioned things like roads, mines, energy and property. In short, índia has not conformed to anyone's template. It has gone its own way.

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What does this new kind of capitalism look like? An immense, often unrecorded informal sector employs the majority of Indians. But in terms of value added—a crude way of measuring activity that is used by economists-Indian capitalism is concentrated. In 2007 a government survey of almost 200,000 services firms, formal and informal, concluded that the top 0.2% of them accounted for almost 40% of output, and that companies in two states, Maharashtra and Karnataka, which host the commercial hubs of Mumbai and Bangalore, collectively accounted for about half of output.

Next, look at the stockmarket. It is not an ideal proxy for índia Inc, but it is the only reliable one. About 70% of its value sits in the **BSE** 100 index of the largest firms, the smallest of which is worth just under a billion dollars, below which a firm is considered a tiddler by global standards. As a group, these businesses have a return on equity that has declined in recent years but remains solidly in the mid-teens, making Indian firms more profitable than many of their Asian peers, reckons Anirudha Dutta of CLSA, a brokerage. Debt leveis are low and growth has been strong, with profits rising sixfold since 2001 in dollar terms to $64 billion.

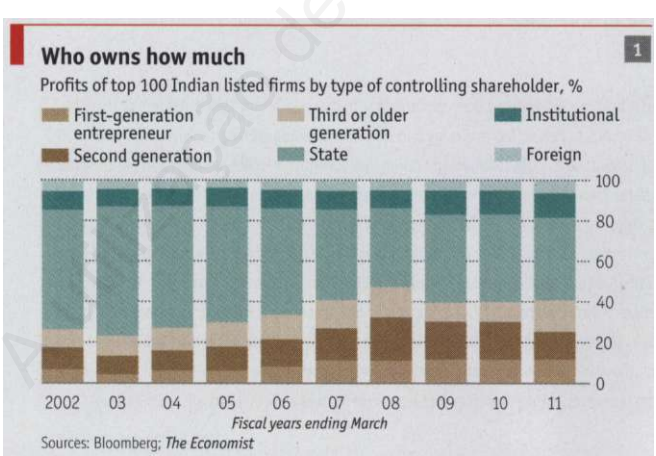
That makes índia big, but not that big. It accounts for about 3% of the world's stockmarket value. Cheered, feared and jeered at home, India's giants are mere middleweights on the global

stage. State Bank of índia, India's largest lender, is a tenth of the size of China's biggest, measured by profits. Reliance Industries, a family-run conglomerate with a skew towards chemicals and energy that is the subcontinenfs most valuable firm, is only a third as big as Total of France. If ali goes to plan and India's economy grows quickly it will still be a decade before its firms begin to challenge those of the rich world and China by size. After two decades in which sunrise industries such as mobile telecoms, media, health care and finance have thrived, India's distribution by sector now looks pretty conventional by global standards (see graphic on previous page).

What makes índia unusual, aside from its rapid growth, is its form of ownership. Its evolution can be crudely split into three periods. Until 1991, when liberalisation began, Indian businesses that had not been nationalised were family affairs that survived in a world of micromanagement and official targets-the "licence raj", a surreal mix of Soviet stupidity, British pedantry and Indian improvisation. Firms responded by branching out into any activity where they could find room to breathe, while facing little serious competition in their main businesses. Many enjoyed close links with the Congress Party that formed India's first post-independence government and dominates the ruling coalition today. By the time an economic crisis brought on liberalisation in 1991, though, most business folk were utterly fed up.

The pattern of ownership in the second period, between liberalisation in 1991 and 2003 (when the economy's growth rate moved up another gear) was far more turbulent, as lazy old family groups were exposed to fierce competition at home and from abroad and the prices of everything from machines to India's currency were freed up. Many firms didn't survive. Of the largest 20 listed on the stockmarket in 1990, only five remain in a recognisable form in the top 20 private firms today, ranked by market value. The big textiles houses that dominated the scene in 1990 were much diminished over the next decade (although Bombay Dyeing is, despite its name, still in business), and some of the grand families behind them such as the Mafatlals dropped from the upper ranks of capitalist clans. Indian business in its first decade of freedom, then, did destruction and creation. Indeed, as the economy took off in 2003 the possibility that the old, oligarchic form of capitalism might be obliterated altogether, perhaps even to be replaced by a freewheeling approach that had more than a whiff of America about it, seemed a sensible prediction.

Sensible, but wrong. For if an alien investor landed in Mumbai today and ignored every aspect of life there other than the structure of the stockmarket, the closest thing would not be New York's bourse, but a weird mix of São Paulo, Seoul and Shanghai. Some 41% of índia Inc, measured by the profits of the



biggest 100 firms, sits in the hands of state-controlled companies, from big oil firms to Coal índia, with its vast empire of opencast mines, its own corporate song and 377,932 loyal workers. Blue-chip firms controlled by institutional owners, such as **ITC,** and a handful of subsidiaries of foreign firms such as Unilever, together account for only 18% of overall profits. The remainder, some 41% of earnings, are made by firms under some form of family or founder control. This special report will include Tata Sons in this category even though the present fifth-generation boss is likely to be the last family member in charge and most of its shares are owned by family trusts that are meant to be independent.

Capindialism

Within this broadly defined category of family or founder firms it is also possible to find examples of every kind of fresh success. Gautam Adani, a strapping billionaire with a habit of watching share prices on television as he talks, has used brawn and guile to build from scratch an empire of ports, power and coal centred in Gujarat, a western state. In a Mumbai suburb Dilip Shanghvi, a soft-spoken scientist, has turned Sun Pharmaceutical from a minnow into a global generic-drugs firm worth $10 billion. Yet the older family firms, toughened up by 20 years of competition, matured by bitter feuds and splits, and still with remarkable reserves of animal spirits, have at least held their own.

India's economy is one of the world's most dynamic. Some industries, such as media and aviation, are unrecognisable from ten years ago. There has been a fair amount of turnover among the leading firms. But overall, India's form of ownership has barely changed over the past decade. The division of profits made by family firms between those in their first, second and third or older generations has stayed pretty constant. The new kids on the block have made gains but not won the day. Nor has the profit share of family firms overall, of whatever vintage, changed much. The mix of state, blue-chip, foreign and family owners has been remarkably stable.

In the past decade Indian business has not been on a journey towards someone else's economic model, whether Chinese, European or American. It has not been growing out of an immature phase, or shaking off a simpler way of doing things. Instead it seems to have established its own equilibrium-what might be called "capindialism"-in which profits are controlled not by institutional shareholders but mainly by the state, or by entrepreneurs and their descendants. Outside the state firms, the fiddly conglomerate is the favoured form of organisation. This special report will try to answer the big questions ali this raises. Why has Indian business developed in this way? Will it continue to? Can the aspirations it has raised be met? And is this new form of capitalism good for India-and the world? •

Fonte: The Economist, London, v. 401, n. 8756, p. 19-23, 3-5 oct 2011.