# Eighteen

# Old Money

*The interval between the decay of the old and the formation and establishment of the new constitutes a period of transition, which must always necessarily be one of uncertainty, confusion, error, wild and fierce fanaticism.*

—JOHN C. CALHOUN

Old money has always looked down on new money. Over the centuries, the newly rich have been objects of scorn and derision. Now, perhaps, for the first time in our history, the new millionaires are looked up to with pride and even reverence. For they are a new meritocracy—entrepreneur-professionals who are creating value by innovating in the global knowledge economy. In September 1999, the *Business Standard* published a list of one hundred Indian billionaires, in which eight out of the top ten were first-generation entrepreneurs. Six out of the top ten had made their fortunes in the knowledge industries. They did not inherit wealth, nor did they have a family name. They reflect a new social contract of postreform India where talent, hard work, and managerial skill have replaced inherited wealth. This is one of the most exciting developments of our time. The Internet has also made the marketplace more democratic, so that many more persons with ideas can now become rich. Business is changing so rapidly that those who can foresee the changing needs of the market will not only become rich but also create millions of jobs and transform our poor, hierarchical society.

In 1947, when India became free, the nation's wealth resided with the landed gentry. Talukdars and zamindars lorded over impoverished peasants. There were a few trading and industrial families, to be sure. Some of them had even avidly supported Mahatma Gandhi and the freedom movement. But they were socially inferior to the large landlords. After Independence, the new government took over the princely states, abolished zamindari, and decimated the "old money." The industrial families thought that now their time had come. But their hopes were short-lived because the socialist government shackled them with the most stifling controls and raised tax rates to extortionate levels. Wealth did not shift from zamindars to the business class. It went to finance the public-sector enterprises.

The middle and small landlords, meanwhile, were not destroyed (because we did not fully implement land reforms). When the green revolution came in the 1960s, these farmers in Punjab, Haryana, and western Uttar Pradesh seized the opportunity. They got tractors, put in tube wells, imported Bihari labor, and no one grudged them their new wealth because it was earned through hard work and not from rents from peasants. The rent seekers were a new class of bureaucrats and politicians who were getting rich from the License Raj. By the seventies, Indians started leaving in large numbers for the Middle East and a new monied class of nonresident Indians (NRIs) came up who invested their gains in garish bungalows in Kerala and Punjab. NRIs, green revolution farmers, and corrupt public officials became the "new money."

With the coming of the reforms in 1991, moneymaking again became respectable, and the old business houses suddenly acquired the esteem and power that had eluded them for fifty years. They finally became "old money." However, socialist controls had so emasculated them that they did not know how to respond to the new competitive climate. Like hungry children, they began to set up ventures with foreigners promiscuously, without a thought to their own capabilities. They expanded capacities unthinkingly. When the recession came in 1997, supply was hopelessly ahead of demand and they were in trouble. The joint ventures began to come apart as foreigners realized that their Indian partners were not up to scratch—they had neither the competence nor the capital. The Bombay Club began to clamor for protection.

Ten years after the reforms, "old money" is floundering. It has still not acquired the skills to succeed in the global economy. It continues with a factory mind-set when the industrial age is disappearing. If old businesses are in trouble, fortunately there are new businesses emerging. The 1991 reforms have enabled young Indians to attempt new challenges. The world has also changed to our advantage. Unlike the industrial age, the information age speaks to our strengths. Our bureaucrats and incompetent industrialists may have killed our industrial revolution at birth. "Old money" may have let us down. But "new money" will create millions of new jobs and prosperity in the twenty-first century.

It is becoming increasingly clear that a definite divide has emerged in Indian business. There seem to be two India Incs. One is the new, vibrant world of knowledge-based, globally competitive companies in software, Internet, IT-enabled industries, generic pharmaceuticals, and entertainment. We encountered some of these entrepreneurs in the previous chapter. The second is the world of the old family business houses, which is hopelessly diversified in a vast number of commodity businesses. Its venerable companies are dying, its joint ventures with foreigners are unraveling, and it cries for protection.

When I first started my consulting work, I met many skeptics who claimed that the economic reforms had been superficial and would not have lasting impact. However, one businessman, Abhijit Sen, catalogued eleven ways in which his telephone cable business had been transformed by liberalization, thereby demolishing the skeptics. Sen said that without the reforms, his business would not even have existed. Until 1991, the government imposed severe licensing obstacles in the manufacture of telephone cable by the private sector. The bureaucrat made the key decisions in the running of the business. These licensing restrictions went away in 1991, and the company rapidly increased its capacity (by five times). Second, he had to split his business before 1991 into three uneconomic units because he did not want his assets in any one unit to exceed Rs 100 crore, which would have made him a "monopoly" company under the MRTP Act and denied him the ability to expand. He merged the companies after 1991 with enormous savings in taxes.

Third, he used to have four full-time people in Delhi to do government liaison; now he had one part-time person because all his raw materials had been decontrolled. Before 1991 he had one person to kowtow to the steel controller, a second to kowtow to the aluminum controller, a third to kowtow to the copper canalizing agency, a fourth to kowtow to the State Trading Corporation for the import of special plastics. Fourth, he no longer needed to get capital expansion approval from the Controller of

Capital Issues. The merchant bankers got it done in less than half the time through the Securities and Exchange Board of India. Fifth, he did not need Joint Controller of Imports and Exports approval for the import of raw materials. Sixth, he no longer needed Finance Ministry approval for loans above Rs 5 crore. Seventh, he did not need Reserve Bank permission to travel abroad; earlier it took a month to get foreign exchange. Eighth, Modvat had been extended to his line of products, which had provided significant tax savings. Ninth, West Bengal had abolished octroi check posts and that speeded up movement of his goods. Tenth, he could travel to most cities in India even at the last minute, without having to rely solely on Indian Airlines. Eleventh, his productivity was up 35 percent because of changed work attitudes. His two thousand workers produced three times more cable than they did in 1991.

This is merely one example, but it illustrates the changed manner in which Indian managers run their businesses. Industrial liberalization has allowed them to expand existing businesses or start new ones without government approval. Hence, they have invested heavily in new capacity, in some cases in world-scale plants (because there is no bureaucrat to decide whether such scale is appropriate). In other cases, they have used the opportunity to leapfrog in technology without the Directorate General of Technical Development telling them which technology is appropriate. Trade reform has made it possible to import raw materials and key components without a license. Tariff reductions have reduced their costs and helped them become more cost-competitive. The freedom to choose between an Indian or foreign supplier has forced Indian suppliers either to improve their products to the standards of the imported ones or to lower their costs in order to compete against cheaper imports. The weaker suppliers have lost significant market shares to imports.

Indian markets have become progressively competitive after the reforms. Even where new competition has not yet emerged, managers are worried that their businesses are under threat from potential rivals. The awareness of competition has finally come to occupy the central place in the mind of the Indian manager. For the first time, companies are having to face tough choices about what products to make, for which markets, and aimed at which customers. They are having to become strategic rather than opportunistic.

Forty years of socialism, I discovered, was not able to destroy India's legendary entrepreneurship, although it had distorted its behavior. Indian companies had real strengths. They had been set up largely by our trading castes with enormous financial acumen, an austere lifestyle, a propensity to take calculated risks, and an ability to accumulate and manage capital. For the past fifty years, the Birla companies had monitored performance of their numerous enterprises across the globe on a daily basis. The Ambanis had single-handedly created the "equity cult" in India by building a base of more than two million shareholders—one of the largest for any company in the world. Because many Indian industries had been under severe price controls in the socialist raj, companies had been forced to become low-cost producers in order to survive. These constituted significant strengths and provided a basis for competitive advantage as India joined the global economy.

Indian companies also had clear and numerous weaknesses. The most important ones were the inability to separate ownership from management; a lack of focus and business strategy; a short-term approach to business, leading to an absence of investment in employees and in product development;

insensitivity to the customer, largely because of uncompetitive markets, but resulting in weak marketing skills; an indifference to technology; and, lastly, poor teamwork. Many of these weaknesses were the result of a closed economy.

A striking characteristic of Indian business is that it is family-owned and family-managed. However, family firms, I discovered, are nervous. They are worried that their family-run business will not be able to cope with the competitive demands of the postreform world. I have tried to reassure them by pointing out the persistence of family businesses in advanced societies. I told them that they had acquired a distorted view of economic history, in which the family firm is regarded as the beginning of corporate evolution. As the firm grows and needs more capital, it employs professionals, goes public, and becomes a giant corporation owned by faceless shareholders.

The reality is that family firms still dominate business life around the globe, and they are especially important in the emerging markets of Asia and Latin America. France, Italy, and capitalist Chinese societies like Hong Kong and Taiwan are dominated by small family-owned and -managed businesses. The success of the Italian, French, and Chinese small enterprises suggests that being a family firm per se is not necessarily a disadvantage. However, a successful family firm must be able to professionalize. It must be capable of recruiting and retaining outside professional talent. In a competitive world, it must be able to get the best person to run the company. If the family member is not the best person, then it must be willing to hand over the management to an outsider. Thus, to professionalize means that the family must make the mental leap and separate ownership and management, and distinguish between the family's interest and the company's interest.

Most Indian companies are in transition today. They are coping painfully with the problem of incompetent or unprepared family members at the top. Rahul Bajaj says, "It is easy to get rid of an outside manager, but how do you get rid of a family member? You must either do what is right for the business or the family. Either way, you will end up with an unhappy family or a weak company." Because of competitive pressures, it is beginning to dawn on Indian businessmen that superior companies are built by superior people; that the success of their company depends on their attitude towards men and women of high ability and advanced training. A businessman of a $450 million company confessed to me: "In the past, I was extravagantly wasteful of talent or myopic in believing that I could do it all by myself." Almost every industrialist I come across says that his biggest challenge is to find men and women of ability to manage crucial positions in his company. This is a profound change in the Indian business world after the reforms.

The inability of Indian business to create large-scale nonfamily organizations, I believe, may not necessarily constitute a constraint on the rate of economic growth, at least at our stage of industrialization. What small companies give up in terms of financial clout, technological resources, and staying power, they gain in flexibility, lack of bureaucracy, and speed of decision making. Throughout the 1980s, the economies of Italy and other family-oriented Latin Catholic societies in the European Union grew faster than Germany's. Max Weber, who argued that the family orientation of China would impede economic modernization, was simply wrong. Indeed, it is likely that small Chinese and Italian family businesses will prosper more than large Japanese or German corporations in sectors serving fast-changing, highly segmented consumer markets. If our objective in India is to maximize aggregate wealth, then we have no particular need to move beyond relatively small-scale family businesses.

However, some sectors of the economy cannot be managed by family enterprises. It is hard to imagine how manufacturers of aircraft, automobiles, semiconductors, or pharmaceuticals, which require huge R&D commitments over long periods, can be managed as family companies. Since some Indian companies have ambitions to become multidivision, multinational enterprises, Japan's example may be instructive. Japan's large corporations also started out as family businesses, but professional managers called *banto* quickly replaced family managers relatively early in the nation's economic development. Public policy specialist Francis Fukuyama tells us that the merchants of Osaka in the eighteenth century made a pact not to turn their businesses over to their children, who they were afraid were too easygoing and would fritter away the family fortune. More recently, Soichiro Honda, founder of Honda Motor Company, was determined not to let his sons enter the business lest it become a dynasty. Many large Japanese firms today forbid their employees from marrying each other, and entry into the firm is strictly governed through entrance exams or university credentials. After 1945, General Douglas MacArthur broke the large family firms (zaibatsu) during the American occupation and purged their top managements. As a result, a new group of young Japanese managers took their place, and Japanese enterprises began to resemble their American counterparts. They became large, multidivision corporations. Without their new-found large scale, it is hard to believe they could have challenged the American auto, electronics, or semiconductor industries. The lesson for Indian companies is that if they want to gain significant global market shares, scale matters, and it can be achieved only by going beyond the family and turning the business over to professionals. Ranbaxy, the leading Indian pharmaceutical company, with operations in more than thirty countries, has learned this lesson. Before its founder died, he turned over the business to professional managers rather than his own sons.

Whether businesses here can create managerial capitalism depends partly on Indian society's ability to build "social capital." Where strangers spontaneously trust each other and cooperate with each other, there is high social capital. Indeed, Tocqueville regarded this "art of association" as an essential virtue of American society because it moderated the American tendency towards individualism. Trust and cooperation are necessary in all market activity. Social capital can help companies make the transition from small family units to large, professionally run enterprises. High trust can dramatically lower transaction costs, corruption, and bureaucracy. While family capitalism may be successful in Italy, Taiwan, Hong Kong, and France, it seems also to be accompanied by education and a strong work ethic. Otherwise, it leads to nepotism and stagnation. Many large and successful Indian companies have begun to realize that educated, hardworking professionals usually outperform lazy, uneducated nephews. But thousands of small and medium enterprises, which form the core of the private economy, are still struggling with this issue.

A more unique characteristic of Indian business, at least until recently, was that it was managed as a joint family, where brothers and nephews worked and often lived together. An example is the Palanpuri Jains of western India, who have established commercial colonies in the diamond centers of Tel Aviv, Antwerp, Bombay, London, and New York, and who today account for roughly 50 percent of all purchases of rough diamonds in the world. Because of the inherent trust in a joint family, Jain diamond merchants rely on brothers and cousins to keep this highly scattered, specialized, and intrinsically high-risk business together, according to Joel Kotkin in *The Tribes,* a provocative account of tribal behavior in the global economy. It is the family and ethnic ties that give them competitive advantage and partially explain their recent gains in market share at the expense of the Orthodox Jews. Does a joint family business provide a competitive advantage in business? I put this question to Rahul Bajaj, whose family is one of the few surviving joint families in Indian business. His answer was an emphatic no. "Business has to be efficiently managed," he said. "Efficient managers are more likely to be outside the family rather than within. You have no choice but to bring them in to run the family businesses. Otherwise you won't be competitive."

"Does the joint business family have any advantages?" I asked.

"Prima facie, there might be two, but I doubt if they are, in fact, sustainable," he said. "One is commitment, which in a simpleminded way is translated into hard work. The other is continuity. I am not sure about either because I have seen just as much commitment and hard work among professional managers. And I have seen just as many lazy family managers. As to continuity, it seems to be often a liability rather than an advantage when you can't replace a family member who does not perform."

Twenty years ago the majority of large business in India was run by joint families. Today the joint business family is almost dead. The question is, why did the families separate and what is the fallout of the splits to corporate performance and strategy? Pulin Garg, the thoughtful professor at the Indian Institute of Management, Ahmedabad, believed that it was a law of nature that families should break up. He used to say, "Haveli ki umar saath saal [The life of a family is sixty years]." Thomas Mann expressed the same sentiments in *Buddenbrooks,* arguably the finest book ever written about family business. It describes the saga of three generations: in the first generation the scruffy and astute patriarch works hard and makes money. Born into money, the second generation does not want more money. It wants power; and it goes after it with the single-mindedness of a Joseph Kennedy. Buddenbrook's son becomes a senator. Born into money and power, the third generation dedicates itself to art. So the aesthetic but physically weak grandson plays music. There is no one to look after the business and it is the end of the Buddenbrook family.

If there are advantages to life and work in a joint family, why indeed have most of them fallen apart? In unusual cases, where a joint family manages to survive, it is because of the practice of strict equality within the family. Neeraj, Rahul Bajaj's cousin, who runs Mukund Iron & Steel jointly with the sons of Viren Shah, finds many financial advantages to a joint business family, and attributes Bajaj's success in remaining together to the strict equality with which they divide the pie. "We may run businesses of different sizes, but we have the same standard of living. Rahul runs the $850 million Bajaj Auto and Shekhar runs the $80 million Bajaj Electricals, but they get equal salaries and equal pocket money. We travel in the same types of cars, in the same class on airlines; we usually vacation together; thus we minimize differences and comparisons."

A Birla scion says, "In a sense, life in joint families is a bit like life under socialism. They do not work in the long run in the same way that socialism does not work. Joint families require strict equality. Because human beings are unequal and need material incentives to perform, joint families break down.” A member of the Murugappa family says that “young Vellayan, who runs the TI group of companies, was refused an air-conditioned car some years ago; if the old patriarch, M. M. Arunachalam, did not have an air-conditioned car, how could Vellayan?”

The family splits have reduced the advantage of the combined group to borrow money or to negotiate common purchases. In a few cases, they have had a positive fallout in making the businesses smaller and more manageable, especially where the families split businesses logically along industry lines. This has helped make the businesses more focused and strategic. In most cases, however, the families ignored business synergies and split the assets in a manner that only served the family interest. In the latter case, the next generation is grappling with the issue of divesting unrelated businesses which lack critical mass.

In the new environment, mediocre children will not survive on the basis of inherited wealth. Since gifted entrepreneurs are a tiny part of the population in any society, most heirs are bound to fail. Their companies will eventually die, destroying in the process the careers of hundreds of managers and workers. So the best course open to them—and this is the advice I have given to several companies—is to sell out and enjoy a life of ease and luxury. Both their family and their company will be happier. This is what the industrial families have done in the United States for a hundred years. However, this is precisely what they do not wish to hear, and in all the cases my advice was ignored. In fact, the families compounded the sin by dividing the companies among their children in a democratic manner, and this weakened the entire business group. What they ought to have done is to have given their children equal shares in the entire business, and had the most talented family member or an outside manager run it.

Swaminathan Aiyar, the consulting editor of the *Economic Times,* suggests a reason why they chose not to do so. According to him, it is because of bad habits acquired during Indira Gandhi’s rule, when income tax rates were 97 percent and industrialists could either pay taxes and go broke or operate in the black economy. They chose the latter. This meant that each family member needed a company to generate black money in order to survive. High tax rates also hastened family quarrels and splits because most of the profits were off the books. As no one knew who was making how much, each heir wanted his own company.

The bigger failing of Indian companies, I find, is that they want to do everything. Whether it is the Tatas, the Birlas, Singhanias, Modis, or Thapars—the vast majority of big business in India lacks focus. The average business house is engaged in eighteen different businesses. Reliance, in refreshing contrast, makes only a few products (all from petrochemicals) and does it well. Ranbaxy makes only generic pharmaceuticals; Infosys only creates software.

Whereas companies overseas have been shedding unrelated activities, Indian companies seem to have gone the other way. Among the fifty leading Indian companies studied by Dr. Freddie Mehta in 1993–94, there was a specific mention of starting a finance company in the majority of the chairmen’s statements. The 1994–95 chairmen’s speeches proclaimed their interest in the power sector. The 1995–96 reports showed a strong desire to enter telecommunications. It takes decades to master the fundamentals of an industry through painstaking attention to detail—building suppliers, creating distribution networks, understanding customer needs. Yet Indian business treats the serious decision of entering a new and unrelated industry as though it were a "flavor of the year." It is difficult to have sympathy with the Bombay Club when some of its members behave in this amateurish, drawing-room manner. Particularly in infrastructure, the stakes are very high, and Indian companies do not have the business fundamentals or the funding capability.

Having said that, there are many responsible businessmen who are questioning their basic strategy and have asked themselves, "What is our core competence?" and "Where can we create competitive advantage?" They have brought in consultants like McKinsey to help them restructure their businesses. The laws governing buying and selling companies have also made mergers and acquisitions easier. Thus, the diversified house of Tatas has divested itself of Tata Oil Mills and Lakmé toiletries. The Thapars are getting rid of all businesses other than chemicals and paper. And so on.

The disease of diversification goes back to the origins of Indian business, to the managing agency system that prevailed during the British days, when a single management oversaw varied business activities—tea, jute, textiles, cement, shipping, etc. The typical British company in India was a managing agency which raised capital in England and invested it in half a dozen business activities in India. Since managerial talent was scarce, a small group of managers oversaw diverse activities. When the British left, Indian businessmen took over these managing agencies. Meanwhile, the managing agency had become the model for Tatas, Birlas, and other Indian houses. After Independence, the licensing system and inefficient capital markets reinforced diversification. Since a businessman did not decide what he should produce and depended on what licenses were available, there was a mad scramble for these, and business houses ended up producing all manner of unrelated products. Although licensing was unique to India, diversification is not. The Japanese zaibatsu and Korean chaebols were similarly diversified. However, the Japanese have realized that the success of Toyota, Honda, Sony, Panasonic, and Toshiba depends on focus. Indian firms are now learning this lesson painfully. Soon after 1991, they went on a spree, forming ventures with foreign companies. These joint ventures had no relationship with one another, ranging as they did from automotive components to fast food and fashion garments. Many of them unraveled after a few years.

Another flaw in most postreform joint ventures was that they were hopelessly unequal. The Indian partner was far weaker than his ownership share in the joint venture. It did not take long for the foreign partner to realize that he was "carrying" the venture, and he resented the Indian partner taking a free ride. This led to trouble. In a typical venture, the foreigner brought technology or the product and the Indian brought market access—that is, a distribution network and skills in managing labor and the government. This seemed to be a reasonable basis for collaboration. The trouble began when the Indian partner insisted on (and got) majority equity without realizing the inherent inequality of the situation—namely, that the venture could not exist without the foreigner's product or brand name. The Indian government's bias also encouraged the inappropriate equity structure. After some time, the foreigner discovered the Indian partner's weaknesses—the distribution network was weak or nonexistent, government contacts mattered less after the reforms, and shockingly, the quality of the Indian partner's managers was second-rate. To be fair, some joint ventures have been successful and many Indian partners overdeliver. However, these are exceptions, and my guess is that a large number will come apart.

Under the circumstances, the best that Indian industrialists can do is to concentrate on learning whatever they can from the foreign partner. These joint ventures represent a window of opportunity to absorb technology and management practices and to upgrade their skills. Historically, India is at the stage where Korea and Taiwan were twenty years ago. These two East Asian nations concentrated on absorbing technology with a passion. "The joint venture is one of the most efficient ways to learn," said Anand Mahindra, managing director of the automotive major Mahindra and Mahindra, recently. "It is a membrane for technology to pass between a developed and a developing country, and it is the responsibility of the joint venture to ensure that the membrane is truly porous." Samsung did not learn as much about making aircraft from Boeing as it did about Boeing's legendary project management skills, which it later applied to its electronic assembly operations. Ownership matters less to Indian society. What matters is that knowledge and skills are transferred to Indians.

Competitive markets are forcing other changes on companies. An important failing of Indian business has been its short-term focus. Companies have invested too little in employees. The lack of attention to human capital begins with lack of attention to recruiting new employees. I recall that when Procter & Gamble used to recruit its trainees at the campuses of the Indian institutes of management, we competed mainly with foreign companies like Citibank, Lever, and Nestlé for the best graduates. There were few Indian companies—Asian Paints was one of them. Exactly the opposite situation prevailed in Japan at the time, where foreign firms found it difficult to get the best graduates from top institutions, such as the University of Tokyo, because of fierce competition from Japanese companies and the prestige and rewards attached to working for a home firm.

If the success of a firm rests on the quality of its managers, why do Indian companies not recruit from the best at the IIMs and IITs? Indian industrialists say that IIM and IIT graduates are not culturally suited for their businesses. If the products of the premier schools are culturally unsuited, the industrialists should have put in place recruitment programs from other colleges. Their solution to hiring is to "place a wanted ad." Mukesh Ambani of Reliance expressed his allergy to the Westernized, "tie-wallah golf-playing" executive. The issue he should have addressed is why the best products of Indian colleges are reluctant to join Indian companies and prefer foreign ones. The main reason is that the Indian business world is still largely feudal with the owner centralizing decisions. Some owners treat their employees no better than they treat domestics. In fact, I once heard an industrialist refer to his finance manager as a "servant" within the earshot of his foreign collaborator. Employees feel more respected in the professional environment of a foreign company. Therefore, even when Indian companies are able to hire a good manager, they are often not able to retain him.

The weakness in recruiting is compounded by the lack of attention to training. Companies hire a young person and just throw him or her into the job. Multinational companies, on the other hand, prepare detailed training plans for their young managers and closely guide them for the first two years. They reward senior managers not only for the results they produce but also for the on-the-job training they impart to their subordinates. Amiya Kumar Bagchi, director of the Centre for Studies in Social Science, Calcutta, attributes the lack of attention to human capital to our feudal social structure. "As a result, the owners are arrogant and the managers are servile," he says. "In East Asia, the owner will happily sit down with an employee for a meal. It is this attitude which has helped them succeed, create universal education, and wipe out poverty. India, in contrast, is like the Philippines, which is a relative failure in East Asia because it shares our social structure."

Indian companies are in a state of transition after the economic reforms. One of the potent effects of the new competitive environment is a mad scramble for talent. Dozens of companies have created outstanding recruiting and training programs. Some companies are seriously attempting to globalize. A number of examples are available, but I shall illustrate with two. Sundaram Fasteners of Madras quickly responded to the reforms by bidding and winning a contract to supply radiator caps to all General Motors plants in the United States in competition against twelve global suppliers. Within six months, it installed a used GM facility from the United Kingdom—it would have taken years to do so before the reforms. Now it is electronically linked to all GM plants via its warehouse in Detroit, and it has not missed a delivery in five years. Within forty-eight hours, it can turn around a new shape for a cap. Against a standard reject rate of 150 parts per million, it has achieved 6 parts per million.

After building the largest pharmaceutical company in India, Ranbaxy made a big push into the international market. It now sells its products in forty-five countries, manufactures in eight countries, including the United States and China, and half its total revenues come from outside India. In 1998, its turnover was $450 million and it expects to cross a billion dollars by 2003. It is vigorously engaged in R&D to bring low-priced generic drugs to the global market under the Ranbaxy brand name—thus tapping into the worldwide trend of containing health-care costs through generics. It spends 5 percent of sales on research, making it the second-highest spender among all industries in India. Its research recently paid off when Bayer, the German drug company, agreed to pay $67 million plus royalties for the rights to a new dosage form of the drug ciprofloxacin; Ranbaxy scientists had discovered a way to deliver the drug in a more consumer-friendly way. Its strategy is based on three advantages enjoyed by Indian pharmaceutical producers: (1) low-cost but excellent R&D scientists; (2) extremely low manufacturing costs achieved by Indian producers due to tough price controls, which pushed them to continuously lower costs for twenty years; (3) the experience of reverse engineering of drugs because of low patent protection in India; thus, Indian scientists became experts at cracking new drug molecules.

These two examples illustrate that Indian companies are capable of acquiring a global mind-set. To do so, they have to focus on a single area of competence—Sundaram in auto components, Ranbaxy in generic drugs—and not be hopelessly diversified. Second, they have to initially win in the domestic market and then leverage their economies of scale overseas. Third, they have to be able to capitalize on global trends. Sundaram tapped into the desire of Detroit's automakers to outsource their components rather than produce them in-house. Ranbaxy is taking advantage of the global shift to generic drugs as a way for all societies to contain health-care costs. Fourth, they cannot ignore quality even when they are pursuing a low-cost strategy. For this reason, Sundaram was one of the first in India to obtain ISO 9000 quality rating. Fifth, they must be able to overcome our historical phobia about investing in product development.

There are only three ways that a company can create competitive advantage. It can compete on the basis of superior cost or a superior product or superior service. India's best companies have largely adopted the superior cost strategy. Pursuing a clear-cut strategy is in itself an advance over the past, when Indian companies were ad hoc and opportunistic and exported undifferentiated products based on factor advantage. Firms are realizing, however, that to compete as a cost leader does not mean that they can ignore quality. On the contrary, world-class quality is a given for any company that aspires to compete in the world market. It means, however, that on an ongoing basis one does not differentiate oneself on the basis of quality but on the basis of cost.

It is unrealistic to expect Indian companies to become technology leaders. This is not because Indian scientists are not capable, but because Indian companies will take time to mobilize the power of science and become a technology-driven culture. The companies of Korea and Taiwan still do not have a technology edge.

The essential question is whether Indian companies can realistically adopt another strategy besides cost leadership. A cost strategy is vulnerable to exchange rates of competitors and rising labor costs of domestic employees. I find it surprising that Indian companies have not directed their energies to a strategy based on superior service. Not only because it is more enduring but also because it builds on the proven capability of Indian traders in the competitive bazaar economy. Anyone who has shopped in a saree store or eaten in a Udipi restaurant knows the Indian traders' ability to deliver superior service.

A strategy based on superior service can be especially powerful where the value added is high. Superior service delivered by highly trained "knowledge" workers—scientists, engineers, market researchers, lawyers—provides a powerful insulation against competition. Not only can knowledge workers harness the power of information technology, they can also be trained to benchmark their deliverables against competition and against customers' needs. Commitment to this strategy implies that one hires new employees on the basis of their attitude and trains them in business skills. Most companies do the opposite. It is an attractive strategy because it is practically "free" compared to the other two. Yet I am not aware of a single Indian company with global ambitions which is seriously and strategically pursuing it.

The competitive advantage of a firm arises from its distinctive capabilities. These capabilities are generally based on the stability and continuity of relationships which the firm builds with its suppliers, customers, and employees. Its competitive advantage is thus the product of history and is not easy to duplicate. It emerges from within the company, from a recognition of its strengths, and is never imposed from the outside by consultants or created by corporate communication programs. These relationships are uniquely different and the search for generic strategies or recipes for corporate success is doomed to failure.

Creating competitive advantage takes years of painstaking effort and few Indian companies have had the patience or the inclination to do so. It requires the ability of the top management to penetrate into the messy details of the business, without losing sight of the big picture. Most Indian businesses have found themselves hopelessly unequal to this task. Until 1991, their talents and their attention were misdirected by the socialist raj. While they were busy negotiating the shoals of our byzantine bureaucracies, their competitors in other countries were carefully crafting relationships with suppliers, distributors, and customers. Honda, in the 1960s, captured a third of the U.S. motorcycle market in less than five years. It had no great vision; it simply did what it did best—making a simple, inexpensive motorcycle. However, the crucial ingredient in its success lay in its unglamorous attention to building long-term ties with its distributors.

The lesson for Indian companies with global ambitions is that success will come not from merely imitating the successful but from identifying and nurturing their own distinctive capabilities.

Can the old Indian companies deliver the goods? The Indian stock markets in 1999 and 2000 did not think so. The market capitalization of the old family companies on the Bombay Stock Exchange had plummeted to 15 percent of the total in February 1999. Although the old family houses still accounted for two-thirds of *Business India*'s top hundred companies as measured by sales, in terms of market capitalization forty-five companies had been forced out of the list of the top hundred, according to *Business World* on 22 August 1998. Although the old houses have begun to change, they continue to resist the shift from "family wealth" to "shareholder value." Only a few are comfortable with the idea that today wealth, status, and power do not derive from controlling the management of the companies that their ancestors promoted. It comes from the rising value of their equity from competitive and professionally run companies. Parvinder Singh of Ranbaxy sent the most powerful signal to "old money" in March 1999 when he announced that his company would pass into the hands of a professional manager rather than to his sons. He was suffering from cancer, and he jolted a number of old houses into realizing that shareholder value is a better way to create wealth.

Most of the debate on the Indian economic reforms has centered on what the government needs to do. Little attention has been paid to what Indian industry and business need to do to respond successfully to the reforms. Clearly the future of the Indian economy after the reforms increasingly depends on the success of Indian industry and business. The historical performance of Indian business is weak. Certainly it has not succeeded in bringing about an industrial revolution in the country. Before 1947, it could blame the British Raj; after 1947, it could blame the overregulated License Raj. Now, after the 1991 economic reforms, it has no one but itself to blame.