

Confidence drains away

The cumulative impact of mistakes by government and entrepreneurs saps confidence in India's economy and business



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India's golden years' – one veteran banker's take on the hopeful second half of the past decade – are receding. At a time when there should be a sharper contrast between panic and irresolution in industrial countries, and strong growth prospects among the BRICs, confidence within India has temporarily drained away.

When Europe and the US were savouring their own golden years in the run-up to the first crisis in 2007, there was widespread recognition of some of the fault-lines that lay beneath the steady growth: excessively cheap money, inflation in asset prices, increasing financial leverage, pro-cyclical fiscal policies, and institutional gaps – like the absence of policy co-ordination in Europe, or in financial regulation worldwide. Taken in isolation, each looked like a potential problem, and each problem on its own had, at least in theory, a solution. But it was the powerful interaction between these different fault-lines, only guessed at beforehand, that turned out later to be so sudden, intractable and dangerous.

It now looks in India as if the sector-specific weaknesses of the boom years, each of them well-understood and not apparently threatening on their own, are cumulating to produce an altogether more worrying outlook for business and the economy.

Among industrial sectors, the weakest spots have been obvious for a long time: real estate, power generation, much of the new retail industry, the recent telecom entrants, airlines, coal and iron ore mining, and infrastructure development. In all these areas and more, ambitions have run far ahead of delivery, and cash flows have lagged far behind capital outlays.

Expectations of investors and lenders had also raced ahead. Companies that were effectively projects on paper were capitalised in 2007-08 at valuations that assumed perfect execution of immensely complex plans. Promoters pledged shares to maximise leverage, and banks reached exposure limits on areas like infrastructure.

The power industry is one of the troubled sectors that have begun to infect other parts of the economic system. Even the most determined promoters have been worn down by delays in land acquisition and environmental permits, failure of coal supplies, declining merchant power prices, poorly drafted contracts, or refusal by some state electricity boards to honour

contract terms. Major infrastructure developers have badly stretched balance sheets, their debts are undermining confidence in banks' loan portfolios, and the overhang of shares pledged against debts is driving down stock prices.

The successive opportunities lost by the UPA government during those 'golden years' to clear away obstacles to growth have accrued in the macro-economic indicators, all of which look poor: inflation running at 9 per cent for almost a year despite high interest rates, fiscal policy undisciplined, the currency weak on poor capital flows. There is always a chance for this government to redeem some of its earlier promise by passing the new land acquisition and mining bills, raising foreign investment limits and getting some of its legislation on the structure of the financial system through. But the timidity of its supply-side reforms must now be paid for through obdurately high inflation and lower growth.

As high financing costs close in on sectors and companies that are long on ambitions and short of cash flow, the focus is turning more from government's mistakes to miscalculations made by entrepreneurs in the boom years. It once seemed enough for promoter groups to assemble teams of aggressive executives who knew how to get things done, give them some capital, and let them loose on a new industry or service sector. There had to be an opportunity, since everything in India was growing, and a promoter group that had delivered success in one business was surely qualified to deliver it in any other.

This fundamental error, of mistaking goals and targets for business strategy, is the subject of a new study that could be a particularly valuable guide to the way forward for Indian business in tough times. Richard Rumelt, professor at UCLA's Anderson School of Management, and a leading consultant on strategy to government and business, suggested in a book *Good Strategy/Bad Strategy* published earlier this year, that there is a growing tendency for business leaders to skip the detailed analysis of challenges and opportunities, and the specific actions needed to capitalise on them. Bad strategy, he says, is a disorder whose symptoms include over-emphasis on ambitious objectives and sheer will power, verbal 'fluff' dressed up as strategic concepts, and failure to analyse what is actually going on. ♦

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