SPEECH

MANAGING COMPETITION : SUCCESS STRATEGIES*

C. Rangarajan

It is a great pleasure to join you here in Bangalore today and it is an honour to have been asked to give the keynote address of your convention. Over the next two days you will be deliberating in some depth about the possible strategic responses in a market environment which is fast becoming competitive and globalised. I thought it might be appropriate for me to take the occasion to speak on some of the policy and firm level concerns from the point of view of India's long-term economic growth.

A. The Changing Policy Environment

Clearly, these are days of transition. A programme of stabilisation and structural reforms was launched as part of the New Economic Policy (NEP) nearly twenty months back. Vigorous market-oriented reforms have been introduced during the period and these efforts have begun to bear fruit. While ensuring a balance between structural continuity and structural change, the effort is towards accelerating the overall growth which is the best answer to the multifarious problems, economic and social, that the country faces.

In the NEP — which comprises the various policy measures and changes introduced since July 1991 — there is a common thread running through all the measures. The objective is to improve the overall efficiency of the system. The regulatory mechanism involving multitudes of controls has fragmented capacity and reduced competition even in the private sector. The thrust of NEP, therefore, is towards creating a more competitive environment in the economy as a means to improving the productivity and efficiency of the system. This is sought to be achieved by removing the barriers to entry and the restrictions on the growth of firms. While the industrial policy seeks to bring about a greater competitive environment domestically, the trade policy seeks to improve the international competitiveness subject to the protection offered by the tariffs. Private sector is being given a larger space to operate in, as some of the areas reserved exclusively for the public sector are also now opened to the private sector. In these areas the public sector will have to compete with the private sector even though the public sector may continue to play the dominant role. What is being aimed is an improvement in the functioning of the various entities whether they be in the private or public sector by injecting an element of competition. The success of this effort will, however, lie in our ability as a nation, to assemble the required blend of public policies and private actions which can find sustainable solutions to the structural problems of the Indian economic system.

B. Productivity Growth

Modern management has become a dynamic process seeking to align a firm's internal resources with the external environment. The extent to which a firm is able to attain its objectives depends critically on its ability to understand the opportunities presented and constraints imposed by its environment and respond with appropriate policies at the corporte and functional levels. This is summarised in the well known strategy of SWOT. Only increasingly the environment that is relevant is not domestic but global. Successful corporate strategy, therefore, rests on the interplay of the competitive advantage of firms and the comparative advantage of nations.

Corporate attention and resources very often are diverted, presumably to more seemingly profitable and short run pursuits. However,

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dangers of excessive preoccupation with transitory phenomenon are not clearly recognised. Perhaps, firms feel that in the long run they find themselves in another short run. The importance of the long-run, therefore, fails to receive due emphasis.

Firms as well as policy makers, however, have to deal with the economy's long-run problems. In the long-run, probably nothing is as important for economic welfare as the rate of productivity growth. Disparities in productivity growth among nations, if they go on only for a very few years, make little difference for the relative productive capacities, but if they persist for any considerable period of time, the phenomenon of compounding makes the things enormous. The "tyranny of compounding" manifests its full powers only in longer periods and that is why the long view becomes crucial. The persistent compounded difference in savings and investment rate such as those reported for the US and Japan can go far in explaining the differences in growth performance.

For long productivity has been measured in terms of capital and labour productivity. But an important advance in economics has been to identify and measure total factor productivity which identifies contribution to increase in output of influences other than increase in factor inputs. Total factor productivity growth thus encompasses the effect not only of technological progress but also of better utilisation of capacities, learning by doing, improved skills of labour etc. It is, therefore, a composite measure of technological changes and changes in the efficiency with which known technology is applied to production. The total output of the United States in the first part of the 20th century grew at about 3 per cent a year. Its capital stock grew at about 3 per cent whereas the labour input grew at about 1 per cent a year. In the capital-labour mix, capital accounted for about one-third and labour two-third. So inputs were rising at about 1.7 per cent a year. Since the total output grew by 3 per cent a year, total factor productivity accounted for 1.3 per cent of output growth. Capital accumulation as a central force driving the process of development is well accepted. However, capital accumulation by itself does not expalin fully the output growth. There are influences beyond the accumulation of capital and labour which are responsible for output increase and that is what is summarised in the term productivity. Between 1960—85, it is interesting to note that in France and Germany total factor productivity accounted for 78 per cent and 87 per cent of the output growth of these countries.

Since 1960, growth in productivity has accounted for a relatively small proportion of output growth for most developing countries. The exception is East Asia, where the share is more than 25 per cent. The World Bank data on cross-country evidence of TFP growth for the period 1960-87 revealed that among the developing countries, the TFP growth of East Asia at 1.9 per cent was the highest as against 0.0 per cent for Africa and Latin America. Among the industrial economies, France had the highest TFP growth of 1.7 per cent followed by Germany of 1.4 per cent, United Kingdom of 1.2 per cent and the United States of 0.5 per cent.

C. A Perspective on India's Economic Performance

The current process of change and economic transformation must be seen within the perspective of the last forty years. During the four decades beginning 1950 the Gross Domestic Product of the country has grown at an average annual rate of 3.71 per cent. As population grew more or less at the rate of 2.16 per cent per annum, the per capita Gross Domestic Product increased at an annual rate of 1.55 per cent which had the effect of doubling the per capita income over the period. Significant changes have occurred in the structure of Indian economy. A largely agrarian feudal economy has been transformed into one based on a well developed and a highly diversified infrastructure with immense potential for industrialisation. Foodgrains output which stood at 50 million tonnes in early 50s rose to 175 million tonnes in the very recent period. Income and consumption levels have significantly risen. The contribution of industry to national income has increased perceptibly. We have today a widely diversified industrial and service sector base. The growth of the economy is also reflected in a fairly substantial expansion in educational and health facilities. Literacy rate has gone up from 16.7 per cent in 1951 to 52 per cent as per the Census of 1991 and the educational base has widened. A pool of skilled manpower and professionally trained entrepreneurs is now available. Public health facilities have widened. Incidence of poverty has visibly declined and average life expectancy has increased from 32 to 58 years.

The country has also succeeded in creating a good base for scientific and industrial research. In agriculture, an integrated system involving research institutes, agricultural universities and an extension machinery has been set up. In industry, there is a network of industrial research laboratories. Research and Development divisions have been established in major enterprises and consultancy firms have come up for project consultancy and design engineering. The basis for this advance lies in the rapid expansion of higher and technical education. The ultimate aim of technological progress is improvement in productivity, efficiency in the use of basic resources like water and minerals and increase in income and employment.

The finances needed for development were raised mainly through domestic savings which contributed between 90 and 95 per cent of investment in different periods. The rate of savings increased from an average of 10.3 per cent of GDP during 1951-56 to 21.7 per cent during 1976-81. It, however, declined in the eighties, averaging around 20 per cent. In the last two to three years again, the savings have increased to levels ranging between 21 and 22 per cent of GDP. Household sector continues to be the largest contributor to domestic savings.

Even as one recognises the significant changes that have occurred in the Indian economy there are obviously many failures, shortcomings and disappointments. While the rate of growth of the Indian economy in the last 40 years is significantly higher than what the economy had experienced before Independence, it has certainly fallen short of our aspirations and expectations; it is also lower than what many other countries in South East Asia have achieved. Even the benefits of such a modest rate of growth of the economy have been diluted because of the rapid increase in population. Notwithstanding several attempts made to ensure a more equitable distribution of the benefits of growth, the incidence of poverty is still large. Despite differences on the definition of poverty and how to measure it, even the most optimistic estimate puts the proportion of people below the poverty line in 1987-88 at around 30 per cent. While the ratios of savings and investment in the economy have shown considerable increase, effective use of capital has remained a serious problem. Incremental capital-output ratio rose steadily till the end of 70s and a decline was perceptible only since the early 80s.

The incremental capital-output ratio (ICOR) deteriorated due to a variety of factors. Some of them were the consequences of the very process of development, like changes in the composition of investment (i. e. from engineering to chemical industries) and rising real costs in certain sectors, like irrigation, land and mineral development where the easier opportunities had been exhausted first. The changes in the composition of output do not however fully explain the rise in ICOR. There were other avoidable factors and most of these could be grouped together under the expression "inefficiency in resources use." There were substantial time and cost overruns in execution of several projects. Also, the low level of capital utilisation was due to lack of adequate synchronisation in the implementation of interlinked projects.

D. Need for a 'Productivity' Orientation

The key to India's growth lies in improving productivity and efficiency. This has to permeate all walks of our life. Contrary to the general impression, the natural resources of our country are not large. In fact from the point of view of long range sustainability the need for greater efficiency in the management of natural resources of land, water, minerals etc. has become urgent. In a capital scarce economy like ours, there can be no excuse for underutilisation of capacity. Undoubtedly, improving productivity is the function of many factors. The policy environment has to be correct; the organisational structure has to be appropriate and the attitude to work and work technology right.

The policy environment has undergone a dramatic change under the New Economic Policy. The very objective of the NEP is to create an environment in which firms will be compelled to improve productivity and reduce costs. In a highly protected environment, there is no incentive for firms to cut costs. Very often they operate under a 'high margin-low volume' syndrome. The initiative to adapt and improve technology or to undertake research and development effort also dries up. The NEP seeks to change this regime by imparting a greater element of competition.

Competition however is not the sole answer. It may be a necessary condition, but it is not sufficient. The very fact that some industries are more efficient than others even in the same country indicates that the competitive environment by itself may not be adequate. Firms need to react appropriately. Ultimately an efficient industrial structure can be built up only if the firms provide the necessary response. As has been rightly said, firms, not nations, compete in international markets. In fact nations only negotiate. Indian firms have operated far too long in a protective environment. In any industry, it is said that the nature of competition is embodied in five competitive forces: (i) the threat of new entrants, (ii) the threat of substitute products or services, (iii) the bargaining power of suppliers, (iv) the bargaining power of buyers, and (v) the rivalry among the existing competitors. These factors have played a limited role in the Indian situation. But these forces will begin to assert themselves in a bigger way now. As the competitive environment expands there will be problems of transition. Quite clearly Indian firms also face problems which may not be present in other countries. There are rigidities in the labour market. There are multitudes of controls and regulations at the State and urban levels. Perhaps all these will come down as the process of liberalisation seeps through. In any case, the challenge has to be faced by the Indian industry. It must learn to swim in the tempestous waters of competition.

Productivity increase is normally associated with manufacturing industries, but it equally applies to the services sector such as banking. Steps are being initiated to bring about an improvement in the productivity and efficiency of the financial system. Indian financial system today comprises an impressive network of banks and financial institutions and a wide range of financial instruments. All the indicators of financial development have significantly increased, implying the growing importance of financial institutions in the economy and growth of financial flows in relation to economic activity. The extension of banking and other financial facilities to a very large cross section of the people stands out as a significant achievement of the Indian financial system. Despite the overall progress made by the financial system, there has been a growing concern about operational efficiency of the system. It is to this issue that the financial sector reform addresses itself. Financial services constitute an important part of the infrastructure required for rapid industrial and agricultural development. An improved functioning of the financial sector is, therefore, a necessary pre-requisite for the overall improvement of the economy. Financial sector reform once again seeks to bring about improved customer service and the narrowing of the differential between cost of raising funds and the rate of return on assets through imparting greater degree of competition as well as by strengthening the capital base and the resource position of banks. Even as external constraints such as pre-emption in the form of reserve requirements are eased the financial institutions must act as business units with full autonomy and transparency in operations and by the same token become fully responsible for their performance.

The time has come for the Indian firms to respond adequately to the positive changes ushered in by the New Economic Policy. Entrepreneurial spirit of the Indian industry must rise to the occasion. Companies and economies grow and flourish not in a docile environment but because of the pressing challenges and new opportunities. Let us note that progress comes from change and not from a static environment.