Modernising Doesn’t Mean Westernising in Emerging Markets

By Bala Vissa, INSEAD Associate Professor of Entrepreneurship, with Benjamin Kessler, Web Editor

Personal connections still rule in modernising Asian financial markets, despite being taboo in the “Western” sense of a developed market place.

On 24 July 1991, Manmohan Singh, then India’s finance minister, appeared before Parliament to deliver what has been called “the most far-reaching and important budget speech” in the nation’s modern history. In response to an unprecedented financial crisis, Singh laid out a reformist vision designed to free the Indian economy from the government’s grip and kickstart the maturation of the Indian financial sector.

As his speech wound down, Singh made his far-reaching ambitions clear: “As Victor Hugo once said, ‘No power on Earth can stop an idea whose time has come.’ I suggest that the emergence of India as a major economic power in the world happens to be one such idea.” Despite imperfect execution and the nation’s many lingering problems, the effects of Indian economic

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liberalisation have been as sweeping as Singh's rhetoric promised. By 2011, India's GDP had nearly quintupled, per capita income quadrupled, and household savings increased by more than 12 times.

The nation's economic landscape has completely changed since 1991, but has its economic image? Has India's transition to a mature market economy meant development along specifically Western lines, or do local factors continue to have a hand in shaping its economic growth? This question has serious implications for not only India but also the many Asian countries currently making a similar transition.

Bala Vissa, INSEAD Associate Professor of Entrepreneurship, and Guoli Chen, INSEAD Assistant Professor of Strategy, work toward an answer in their recent paper, **Modernising without westernising: Social structure and economic action in the Indian financial sector** (co-written with Raveendra Chittoor of the Indian School of Business). Their findings suggest that even as these emerging markets modernise, they maintain some elements particular to Asian societies – including traits often frowned upon by neo-classical economics.

The Ties That Bind India

"Neoclassical economic theory dictates business decisions should be driven solely by instrumental reasoning," Vissa told INSEAD Knowledge. "Before modernity, social exchange was layered with economic exchange, but [in modern economies] social relations are set aside to make way for cool and calculated decisions by atomistic individuals transacting in the market." That spirit of objectivity prompted the Securities and Exchange Commission (SEC) in the United States to adopt Regulation Fair Disclosure in 2000, prohibiting publicly traded companies from making closed-door disclosures of "material non-public information" to associates such as stock analysts. The rule mandates that they must disclose all material information to such associates at the same time.

But the value system that produced Regulation Fair Disclosure doesn't quite match the picture that emerged when Vissa and his collaborators analysed a sample of 1,552 earnings forecasts issued from 2001 to 2010 by 296 equity analysts in India. The researchers found that forecasts were more accurate when prepared by an analyst with a cultural or social connection to the CEO of the firm in question.

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“There are two things equity analysts fundamentally need to do: Discover new information, and interpret that information. A lot of discovery is happening through private information flows in these social networks,” says Vissa. This matters, because of the influential economic role that analysts play in revealing information on the firms they follow, improving the efficiency of the market where its shares are traded. Although Asian markets are developing, the quality of publicly available information is often poor. High quality information still flows through social ties.

Interestingly, Vissa says that social ties matter as much for the younger, post-economic reform generation of chief executive officers (CEOs) as it does for the older, pre-reform generation; it’s just that the basis for the social ties are different across the two generations. Chief executives who enter the workforce after the economic reforms of 1991 were more likely to transfer private information to analysts that attended the same university as the CEO; whereas the older CEOs were more likely to transfer such information when they shared a language or caste affiliation with the analyst (At least 22 languages are currently spoken in India today, with Hindi and English being the country’s “official” tongues.) “The economic reforms of 1991 accelerated the declining salience of caste and language in economic exchange by significantly increasing the speed and scope of urbanisation and geographic mobility,” Vissa and his co-authors write.

Vissa hastens to point out that he wasn’t privy to any actual clandestine exchanges of information. “To get that sort of data, you’d have to bug people’s offices,” he jokes. Instead their research methodology involved inferring the flow of private information.

The Shadow of the West

Vissa and his collaborators were able to get an even broader picture of the market dynamic by virtue of a historical regulatory artefact that led to some Indian subsidiaries of Western multinational corporations to list on local stock markets. This enabled them to gauge whether CEOs of such subsidiaries tended to adopt more Western norms, i.e. eschewing private information-sharing, or were more influenced by local conditions. As a point of comparison, the researchers analysed forecasts for companies belonging to Indian “business groups”, such as Tata and Reliance. Business groups are also common in other Asian countries, such as Indonesia and Malaysia.

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“Overall, we found that social ties, in general, enabled analysts’ to make accurate earnings forecast… When the CEO was running a business group affiliated company, the effect of social ties gets amplified. In contrast, if the CEO is running a subsidiary of a Western MNC, the effect of social ties gets dampened,” Vissa says. “It appears that there is a distinct difference between, say, a corporation like Hindustan Unilever (the Indian subsidiary of Unilever) and the Ambani group. The latter type of organisation seems to provide a climate where connecting with others based on these kinds of particularistic social ties is legitimate practice. The Unilevers of the world provide a climate where their managers want to engage (even in India) with outsiders based on a more universalistic logic, not based on, ‘He’s my buddy from university.’”

Custom-Tailored Modernisation

In honouring these personal ties, the business group CEOs in Vissa’s analysis, are acting according to their own set of societal norms and values that favour particularistic ties, though they often run counter to Western codes of conduct. So business groups may represent a blend of modern management practices with norms that legitimate particularistic behavioural patterns at the upper echelons. “India is a big country that is modernising, but it’s modernising in its own special way. Sometimes modernisation and Westernisation, which are two distinct concepts, may get mixed up,” he says.

But what of the subsidiaries of Western MNCs? Are they paying a price in Asia for importing a business style that sidesteps the personal? “We haven’t explored this question in our study but it is plausible that Western multinationals are disclosing more information publicly whereas the business groups may not be as transparent,” Vissa says.

As modernisation proceeds apace, Vissa expects the Indian economy will see still more evolutionary change in the medium term with the entry of a new crop of entrepreneurs: “Growth will be to some extent *new* growth – where new represents new actors, new types of organisations and/or industries… The new actors may affiliate very differently from the existing actors – but relationships will continue to be important when doing business in India.”

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