

CONTENTS

	<i>Page</i>
1. ACHIEVING EXCELLENCE THROUGH INNOVATION — <i>CS. N K JAIN</i>	1
2. INNOVATION AND REGULATION — A UK PERSPECTIVE — <i>ROGER DICKINSON</i>	11
3. THE CHANGING ROLE OF REGULATORS IN FOSTERING INNOVATION — <i>N G CHAKRABORTY</i>	15
4. THE OPPORTUNITY IN MID-MARKET PRIVATE EQUITY FIRMS — <i>CS. BALWANT KULKARNI</i>	20
5. INNOVATE AND EXCEL TO SUSTAIN GROWTH — <i>CS. SUTANU SINHA</i>	24
6. INNOVATION — AN ENGINE FOR QUANTUM ECONOMIC GROWTH — <i>V P SHARMA & M A JOSEPH</i>	32
7. SAFEGUARDING INNOVATION — MANAGEMENT OF INTELLECTUAL PROPERTY RIGHTS — <i>DR S K DIXIT</i>	43
8. EMBRACING INNOVATION FOR QUANTUM GROWTH AND THE CHANGING ROLE OF REGULATORS — <i>CS. ALKA KAPOOR & CS. BANU DANDONA</i>	52
9. FINANCIAL INNOVATION — A CRITICAL ELEMENT OF ECONOMIC LANDSCAPE — <i>CS. SONIA BAIJAL</i>	60
10. INNOVATE TO FOSTER EXCELLENCE — <i>ARCHANA KAUL</i>	66
11. DUE DILIGENCE : AN IP PERSPECTIVE — <i>SURYA NARAYAN MISHRA</i>	72
12. EMBRACING EMERGING TECHNOLOGIES FOR PROFESSIONAL EXCELLENCE — <i>CS. SAURABH JAIN</i>	79
13. CORPORATE EXCELLENCE THROUGH INNOVATION — <i>CS. LAKSHMI ARUN & CHITTARANJAN PAL</i>	83
14. UNLOCKING STAKEHOLDER VALUE THROUGH CORPORATE RESTRUCTURING — <i>CS. DEEPA KHATRI</i>	88

ACHIEVING EXCELLENCE THROUGH INNOVATION

CS. N K JAIN*

It is most appropriate in these times to remember Schumpeter and his celebrated "Innovation" that catapults the upturn in the lowest phase of business cycle. As the noted economist who analysed and studied business cycles, he recognized the turbulence and tranquility, the destruction and creativity that underlie their unpredicted surges. Constancy of excellence that a profession yearns stems from innovation, the continual need to innovate.

In the law of contracts, one studies 'the contract of novation'. To 'novate' is to substitute a new contract for an existing contract. The purpose is to make performance possible for either or both the parties to the contract. To transform a contract that has become impossible to perform into a contract full of possibility of performance is the idea behind novation.

Innovation is nothing less than a miracle, "a thing that is impossible to happen, which nevertheless happens", the Shavian idea. Professional, one may say, is a continual process of making impossible things happen, a process that brings into being the latent excellences that normal perception fails to think they exist.

The normal or usual perception of the happenings around is often mechanistic or bureaucratic. It is most likely than not superficial and thus lacks creative possibilities. Edward de Bono introduced the concept of "lateral thinking" that is based on the thought-element "Po" rather than "No"; the latter being the "obvious" result of logical thought processes one learns from childhood. Creativity spurs from dissolution of the ever-demanding and delusive self, which is the greatest hurdle to overcome. It is habituated to creating perceptions that are negative, dangerous to one and others, and quixotically self-perpetuating. They negate the possible, they negate the positive, they negate the creative. Paradoxically, one is inclined to cling to them. A professional who desires and deserves excellence happily remains in a constant process of creative self-denial. This makes her and her profession demandingly innovative.

THE CRISIS

Let us, for example, look at the popular perceptions around the credit crisis created by the Western Financial institutions, causing the Wall Street to collapse spreading gloomy repercussions on the European and Asian stock and money markets. Investors are now perceived to be driving into a fog without headlights. They have developed a firm conviction that there is more uncertainty ahead. They have become super cautious. Large corporates are scrapping dividend and cutting back on their expansion and acquisition plans. Volatility continues on markets. The third quarter of 2008 proved "brutal" for many, particularly the month of September which saw the fall of giants like Lehman Brothers, American International Group, Merrill Lynch and Washington Mutual.

* Secretary & CEO, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

The Reuters Asset Allocation research released on September 30 showed amongst investors, an almost palpable retreat from risk. The world economy is reportedly stumbling. Copper, on commodities markets, lost 29% and oil 25%. Investors were heading into the fourth quarter of 2008 with stock exposure at its lowest since last four and a half years. Bonds holdings, meanwhile, were roughly at average levels. Cash was king. The latest data from fund tracker EPFR Global showed a similar flight to relative safety – relative, because for many nothing looks particularly safe these days. [Jeremy Gaunt, the ET dated October 2, 2008]. Reuters tracked large outflows from global bond and equity funds in the latest week and inflows into US equity funds and money market funds. The findings suggest US investors are repatriating their money to the 'less risky' home shores. "One of the biggest winners in the quarter was VIX Index, the so-called fear index that acts as a proxy for stock market volatility. It gained more than 64%!"

Consider this. Amidst all this volatility, fear and free fall on the Wall Street, J P Morgan Chase worked its way with Ben Bernanke [the Fed Chief], who making use of the least used provisions of the law governing Federal Reserve in getting a backing of almost US \$ 30 billion for its takeover of the investment banker Bear Stearns. Wells Fargo Bank got help of US\$2.16 billion from Federal Deposit Insurance Corporation for its takeover of Wachovia, the FDIC abandoning its standard modus operandi of intervening in insolvent institutions [Bloomberg in the ET dated October 2, 2008]

Failure of Lehman Brothers and other investment banks on the Wall Street is attributed to their high leverage, that is, the ratio of debt to total assets being more than 20:1. Actually, some banks in Europe have even higher leverage. They would not have been allowed to operate if their leverage was not in conformity with regulatory norms. In fact what was wrong with the Wall Street banks was that much was made of the talent at their top levels. It is not the high leverage that mars the performance of investment banker. It is the poor quality of its assets and the poor management of asset risks. What is important is not the financial leverage, but the leverage after adjusting for the risks of various assets. The Wall Street i-bankers suffered from poor quality of assets. Lehman's problem was not that it had US \$ 600 billion in assets with a financial leverage of 20:1. Actually, it had around \$ 80 billion in the form of poor quality assets. They had ventured in a big way into proprietary trading and private equity. Most of the Indian investment banks confine themselves largely to traditional activities like underwriting issues, brokerage, advisory and custodial services. The people at the top of the i-banks of the Wall Street variety came from trading, that hardly requires any formal training and educational background. You only need to create the right impression at the interview. That explains the poor quality of risk management in the fallen i-banks in the U.S. The remuneration the top people in these i-banks drew amounted to US \$ 7 billion a year inclusive of incentives and stock options. It was, in reality, a failure of corporate governance. Governance professionals and, at that, well-trained governance professionals were given no role in promoting business ethics in these finance giants.

Those who have analysed the failures and the effects of the failures of Lehman, Goldman, Merrill, Washington Mutual, Bear Stearns, AIG, etc. have made logical statements of the problem. They predict, almost with unanimity, global economic recession. They point out the crisis and volatility on the stock markets. But, perhaps, volatility on stock markets is not a problem. George Soros and Warren Buffet have made their fortunes by being one step ahead of volatility. Statements of problems sometimes show a grave approach. Let us look at the following statements –

- The measure of the pressure the human activity exerts on the resources of the earth was in 1960s, 60 per cent of the earth's capacity to renew itself.
- It has presently reached 130 per cent of the earth's capacity to renew itself.
- We are no longer living off the earth's revenue account. We are eating into its capital.

Scientists project that if China and India grow the way the West has, within 25 years they will require another whole planet to support them alone. Scientists have, perhaps, looked only at the

evidentiary proof of the earth's physical resources. Mental and intellectual resources of the humankind are immeasurable and infinite. Statements of problems and their logical consequences, sometimes if not always, overlook human creativity. They also overlook the blessedness of the human kind. That blessedness evidences itself in the form of "innovation". Schumpeter stressed the role of innovation and creativity as turners up of the wheels of the economy.

INNOVATION

Creativity at practical levels is called innovation. Innovation may be a process that is a breakthrough or that is incremental in value. Innovation may occur systematically in a company or it may occur sporadically. It is a process by which varying degrees of measureable value enhancement is planned and achieved. The National Knowledge Commission says –

"Innovation" may be achieved by –

- Introducing new or improved goods or services.
- Implementing new or improved operational processes.
- Implementing new or improved organizational/managerial processes to improve market share, competitiveness and quality while reducing costs.

Entrepreneurship and intrapreneurship are products of creative human mind. Schumpeter also looks at entrepreneurship as solution to economic depression. Out of destruction (e.g. of Lehman, etc.) a new spirit of activity arises. Innovation by entrepreneurs is the force that will sustain long term economic growth.

Call it creativity, innovativeness or positivism; it is always manifest in business affairs as it is in social affairs. Look at the benefit the Indian investment bankers are deriving from the collapses on the Wall Street. The Economic Times of October 6, 2008 reports the gain in terms of human potential and experience Indian investment bankers are deriving from the fallen giants like Lehman or Merill Lynch or Bear Steams. Some Indian non-banking financial companies are looking to start or expand businesses in institutional brokerage, investment banking, wealth management, asset management, proprietary trading, private equity, etc., Indian investment banking industry that is pigmy as compared to the fallen giants of the Wall Street is now being peopled by financial and international experts from these vanishing world level mammoths. Indian investment banking industry has definitely shown positive and intelligent attitude turning a grave situation into an opportunity for Asian emerging economies, particularly the evolving future economic leaders of the world, India and China.

CREATION

Creativity and innovativeness is well-entrenched in the Indian mindset. Telling Indians to be creative and innovative in order to achieve excellence is like taking tea to Darjeeling or rice to Kerala. Yet it appears that our growth and leadership as well as industrial, professional and management models are structured towards the fundamentally logical, intellectual and analytical thinking (Western) models. We have perhaps, hardly, looked towards the fundamentally emotive, intuitive and highly subtle models of our miracle-economy neighbour, China or to our own intuitive Upanishadic indescribably emotive self faith models. The reactive economic results stemming from the externalized Western thinking and analytical models giving birth to the rise and fall of the economic and leadership models have always overlooked the "internal reality" of situations. Indeed intellectual logic and analytical understanding of the world have, time and again, resulted in cyclical shocks and depressive reactive actions that we are witnessing now in the present economic upheaval stemming from the US.

The logical and analytical thinking is "externalized", if it can be put that way, as compared to the

“internalization” of the purely emotional, intuitive content of the ancient Chinese, Indian or Japanese way of living and working, approach and attitude.

Even the Westerner Henry David Thoreau puts it as follows:

“What lies before us and what lies behind us are small matters compared to what lies within us. And when we bring what is within us into the world, miracles happen”.

That is what creativity and innovativeness stem from. Let us juxtapose this, and what is drawn in the following paragraphs from the Lao Tzu philosophy, with the US \$ 7 billion per year remuneration drawn by top executive and US \$ 1 billion per year drawn by other executives of the fallen investment bankers.

The Chinese have developed a mature (although this is recent, as compared to the Lao Tzu’s that will follow subsequently) philosophy of “fuzzy logic” – For example,

“Leaves falling

Lie on each other

The rain beats the rain”.

“You can make the sound of two

Hands clapping

Now what is the sound of one hand”.

Vagueness stems from continuum; infinity is extremely vague. The cosmos which has been expanding is getting fuzzier by passage of time. How do you comprehend or explain or clarify by logic. Vagueness is cosmic and therefore it ought to be a strength and not a weakness. In fact too much logic and analysis mars creativity and creates weakness in the system. It also causes losses to one and others triggering a wave of negative reaction, recession and depression.

LAO TZU

May we go further back and deep into Chinese creative and innovative mindset? The revered philosopher Lao Tzu, for example, says, about creativity –

“The one which is not, 's more useful.

Thirty spokes converge at one hub

What is not there makes the wheel useful.

Clay is shaped to form a vessel.

What is not there makes the vessel useful

Doors and windows are cut to form a room

What is not there makes the room useful.

Therefore take the advantage of what is there

By making use of what is not there”.

What is not there, is, in reality, more forcefully, more benignly, without being visible, without being palpable, without being audible, more resplendently there. In fact, the non-existent (apparently) is the source of all creation, sustenance and destruction (creative destruction). It is latent but all powerful. That is why even Schumpeter, the economist, realized and put forth the importance of the latent processes of innovation that cause the upturn in the depressive phase of the business cycle. As history

tells us, realizing the importance of non-existence, Lao Tzu, at an advanced age, was, alone, about to retire into the solitude in maintains, when somebody stopped his chariot and beseeched him to put down his wisdom in the form of poetry for future generations before disappearing into the woods. Fortunately Lao Tzu did it and bestowed his infinite wisdom which is even today driving the Chinese economic miracle and organized gigantic success.

Lao Tzu further points out, the reality of the silent, vast, powerful Truth –

“When the entire world knows beauty as beauty

There is ugliness.

When they know well as good

There, there is evil.

In this way,

Existence and non-existence produce each other

Difficult and easy complete each other

Long and short contrast each other

High and low attract each other

Pitch and tone harmonise each other

Therefore,

Evolved Individuals (creative leaders)

Hold their position without effort

Practice their philosophy without words

Are a part of all things and overlook

Nothing

They produce but do not possess,

Act without expectation

Succeed without taking credit

Since indeed they seek no credit, it

Remains with them”.

Drawing from nature, the highest creative endowment, Lao Tzu tells businessmen (corporate leadership)

“Heaven in harmony with the One

Becomes clear

Earth in harmony with the One

Becomes stable

Mind in harmony with the One

Becomes inspired

Valleys in harmony with the One

Become full

All things in harmony with the world

Become creative.

Leaders in harmony with the One

Become incorruptible". They are not swayed by personal gain or loss, fortune or misfortune, good or bad. He adds –

"Indeed, the highly placed stem from the humble.

The elevated are based on the lowly.

This is why leaders call themselves –

Alone, lonely and unfavoured.

Is it not because they stem from the

Humble and lowly ?

Is it not ?

Therefore, they attain honour without being honoured

Do not desire to shine like jade,

Wear ornaments as if they were stone".

Compare the practical hints of successful creative leadership given in the Chinese philosophy with what happened in Freddie Mac, Fannie Mae, AIG, Lehman, Bear Stearns, Wachovia, Washington Mutual and the like and in the reactive aftermath in the global financial markets. All have been guided and directed by the Harvard and Massachusetts, Cambridge and Oxford graduated finance and management experts ingrained in didactic skills of deductive and inductive logic of the externalized mind.

An externalized mind, the Chinese philosophy or for that matter, the authentic Indian philosophy believes, cannot perceive the internal reality of a situation. The underlying reality of a situation, as Lao Tzu would have us believe, is always glorious and positive, even when the situation is apparently grim. When the going is good the internal reality is even more glorious requiring us to step up the effort. That ushers in creativity.

FEAR & GREED

When the 1987 stock market crash occurred many financial analysts recalled the Great Crash of 1929 and predicted that the late 1980's would witness a prolonged depression of the 1930's variety. Actually, the US economy grew by 4.1% in 1988. The present crisis is also reminding them of the depression of 1930's. In reality, the unemployment rate in the U.S. at present is only 6.1% as compared to the level of 25% to which it had dropped during 1929. In the 1930's the contraction of economic activity had already taken place before the spreads widened in the credit bear markets. The present situation has witnessed credit crisis first before the US economy went into the negative growth trajectory. The policy makers today have started to act pushing liquidity into the economy and cutting interest and discount rates. As Shri Ruchir Sharma, Head, Emerging Markets, Morgan Stanley Investment Management says – "Yet, the truth is that a major market slump and credit crunch are inevitable consequences of a long expansion cycle. Towards the more mature stages of a boom, all sense of proportion regarding risks is lost because of the previous successes.

It is also a natural temptation to draw parallel with the dire events in history during any bear market as fear is often at extreme levels. Following the 1987 stock market crash, many financial observers pointed to the risk of a deep recession. They recalled the experience of 1929, the previous time the market dropped in a similar fashion" [ET dated October 8, 2008].

Coming to the theme as to where from creativity and innovativeness spring, let us notice the

BACKGROUNDER

swayed optimism of the stock markets in the boom times and their melancholic reactivism in bearish credit crisis. Let us look, once again, at what Lao Tzu says –

“Esteem and Fear are identified with the self

There is alarm in both favour and disgrace

What is the meaning of “alarm in both favour and disgrace?”

Favour ascends

Disgrace descends

That is the meaning of “alarm in both favour and disgrace”.

What is the meaning of “esteem and fear are identified with the self?”

The reason for our fear is

The presence of our self

When we are selfless

What is there to fear ?

Therefore, those who esteem the world as self will be committed to the world

Those who love the world as self will be entrusted with the world”.

If you look at the realities behind the present credit crisis in the US, it is not the lack of liquidity that is driving the crisis, it is the loss of confidence that is causing it. Shri Ruchir Sharma points out, “US depository institutions presently hold record cash balances with the Fed, suggesting there is plenty of liquidity in the banking system except that institutions do not want to lend to one another” – for fear the borrower may be the next institution to go bust. On October 9, 2008 the cost of three month dollar loans in London, as indicated by the London interbank offer rate rose to a near three month high of 4.75%.

Thus, despite coordinated interest rate cuts in key markets, banks remain wary of lending to each other. The European Central Bank loaned banks a record of \$ 100 billion in overnight dollar funds, much of it at 5% (on October 8, 2008), sharply down from 9.5%, the previous day. Central banks in Hong Kong, South Korea, Taiwan and Indonesia also slashed interest rates on October 8, 2008 joining the banks in other economies. (ET dated October 10, 2008). The gloom spreads very fast; the good news very slow, if at all. Evolved Individual, as Lao Tzu calls them, become light unto themselves and their creativity can provide powerful lightening amidst gloom of externalized reactive mind. Innovation thus springs from unexpected unassuming quarters.

TECHNOLOGY & GROWTH

A large number of innovative solutions to global problems are worth noticing. In his book “Winning the Oil Endgame”, Mr. Antony Lovins of the Rocky Mountain Institute, has explained how a legion of small, fast and simple micro generation and efficiency project could be an answer to the world’s energy problems. Indian rural side has many examples of community water storage and distribution networks. Micro-credit to rural and urban poor women folks and their self help groups have worked wonders to solve poverty and credit recovery problems. Local energy generation and distribution systems, local food and vegetable growing and distribution networks will make for a sustainable growth in times to come. Prof. David Vogel’s “Market for Virtue” is a marvelous example of eco-friendly, social sustenance through extrovert industry, alert consumer NGO’s, industry-society collaboration and socially responsible behaviour of industry, financial systems and markets.

Thomas Friedman who wrote “The World is Flat” on globalization and the rise of China and India and the new upwardly mobile middle class in those countries, has now come with his researched treatise

titled "Hot, Flat and crowded". Again referring to the growth rates in China and India with some other Asian countries, he has said that both China and India, each, will eventually have three or four Americas within them. Not expecting these new emerging economies to affect their growth, he has pointed out the need for the US to embrace new green technologies. We feel that if America does not innovate in this regard, it will find itself in political as well as economic trouble. The AI-Quaida is a beginning of the political trouble for America because of its super-affluent and negligent lifestyle, Mr. Friedman thinks. Not only the US, India and China which are in the high swing of growth will also have to develop technologies that reduce greenhouse emissions and that are eco-sensitive.

Company Secretaries who are in the forefront on corporate governance and corporate responsibility matters will have to exhibit active awareness of such innovations in technology. This is an area wherein Company Secretaries could exhibit leadership skills in the medium to long term. But they must plan now to develop leadership qualities in corporate governance and corporate social responsibility technologies. Sustainability accounting and reporting will embrace such technological innovations, their activity and financial budgeting and implementation of the budgets will be a good challenge to handle. By the way, sustainability accounting and reporting is a new area where Company Secretaries should show leadership, whether as employed or as practicing professionals.

Videoconferencing and meetings of board and other corporate meetings, through such technology will be another technology area falling within Company Secretary's domain. Countries are now gearing up for Broadband Quality Score increases. BQS is a measure of download and upload speeds – how long data takes to reach a computer. Fiber optic cables are used to connect homes and businesses. Unlike slower broadband connections, this technology allows steaming high quality video to computers and seamless use of videoconferencing software. When new company law comes into vogue in India, meetings through videoconferencing will become an official reality. Upgrading the BQS will be another technological innovation for Company Secretaries to handle. Quantum growth is not possible unless we leverage the use of technology and the urge to innovate. It is innovativeness alone that helps maintain excellence as quantum growth is planned and achieved.

Appropriate technology, efficient technology, green technology, social and organizational engineering, people and process re-engineering, new financial technologies on commodities, currency and money markets are all technological challenges where Company Secretaries may plan to play a visible role. Ability to take on challenges is what distinguishes professional excellence from professional mediocrity.

Thinking differently is what makes the difference and make innovativeness an approach. In fact, times have come when not only marketing and advertising firms but even manufacturing and other service sector companies may now have positions called 'Creative Chiefs'. This is because innovation is no longer limited to technical or technological are not unbounded creativity is demanded today even in unthought-of of areas like organizational behaviour, organizational structures and relationship, marketing, office processes, and what not. The new thinking is that unusual or preposterous may actually be more appropriate. In fact, creativity starts from "resisting the usual". Creativity has often made organizations risk losing core identity.

UNLOCKING VALUE

When we talk of restructuring a corporate, we do not stop only at a corporate. Sometimes we think of the group, of all associated undertakings. In restructuring a different or completely new form of organization may be thought of to hold securities or assets of a body corporate. Various motives may spur the exercise of restructuring. Reverse merger of various varieties has been a great innovation in corporate restructuring creation of a trust to hold high value shares and unlocking the value for large majority of shareholders without loss of promoter control has been a model followed recently. BHP Billiton merger over the UK and Australia's distant borders has been a classic innovation involving various

types of restructuring. Tax Havens like Luxembourg, Malta, Panama, Mauritius, Isle of Man and other jurisdictions are used for cross border restructuring. A high degree of professional care, skill and excellence are required in such structures and Company Secretaries services are distinctly used in such structure planning. Restructuring calls for legal knowledge, applied law, tax laws, transfer pricing rules, procedural laws, finance, documentation, drafting and conveyancing skills, negotiation skill, advance price arrangements and other consummate skills which Company Secretaries possess/can acquire.

IPRs

Inventions and innovations are the breeding ground for Intellectual Property and intellectual property management. IPRs are to be processed, protected and registered in various jurisdictions. Their economic value being enormous, gaining expertise in various aspects of IPRs will enable Company Secretaries to play a critical role in corporate functioning. Research in the law, jurisprudence and global practices regarding IPRs will help in assisting protection of the value of inventions and innovations. After all, innovation is the conversion of profound knowledge of a subject into a creative practicable solution applied to a given situation.

Ideating a practicable solution to a given problem relating to IPRs may become a forte of Company Secretaries who delve deep into IPR related research in India and other countries. IPRs in intangible assets like software source codes, packaged software, designing technology, etc. can become an area of superspecialisation for Company Secretaries. Innovations have always been catalysts of economic revolutions. Hence their identification and conversion into IPRs, structuring their ownership, licenceeship and generating commercial value through such structuring can be areas to generate enormous corporate value. If we look at the present global credit crisis and economic downturn, it found its roots in the US. The US economy found its greatest growth driver in huge investment demand generated by a series of innovations like in assembly line, atomic energy, jet engines, internet, computer operating systems, etc. But the cheap (relatively) manpower from India and China reduced job, service and income opportunities to average Americans. Their reduced income level caused a fall in their debt repayment capacity, their ability to buy consumer durables like cars, etc. This triggered, along with a fall in property values, the sub-prime mortgage crisis. While the American government by its over 700 billion dollar package saved banking system from liquidity crisis, that, by itself, will not build employability, jobs and income levels for American people. Economic leadership through inventions and innovations, may therefore in the most likelihood shift to Chinese and Indian economies whose growth rates are propelled by domestic demand. Thus IPR work and its importance are going to shoot up in Asian countries. Company Secretaries are the ideal professionals to capitalize this opportunity in the medium and long term.

GLOBAL FINANCING

The present liquidity crisis originating in the US and European banks coupled with the growing importance of Asian emerging economies will open up vast global financing opportunities to Indian professionals. Take, for example, the sudden decline (that has become self-sustaining) in demand for cars, houses and consumer durables, in the US. That economy, which was driven by sustaining investment demand, may lose that momentum to economies like India and China, which are driven mainly by domestic demand, especially India which has young age advantage in terms of demography. The petro dollars which were so far flowing to the US and Europe to take advantage of the investment demand there will now have to find new investment avenues. As one is aware, cheap labour from India and China has grabbed jobs from their American and European counterparts in garment industry, software, services and research fields. The giant Asian economies are finding their growth further fuelled by rising income and demand levels. Petro-dollars from West Asia will therefore find investment avenues in India and China more lucrative. In fact, even private equity funds, especially mid-market private equity funds from the advanced Western economies may find greener pastures in India and China and other Asian and African economies. Company Secretaries should, therefore, work to develop industry as well

as finance knowledgebase and expertise and innovate to seize this opportunity. Companies looking for private equity finance, even if they are not listed companies, form Corporate Governance Committees to develop and maintain stakeholder relationships, especially with private equity financiers. As governance professionals, Company Secretaries can develop expertise to work on such committees.

Finance from private equity funds, hedge funds, high network individuals, investment banks and the like, each, has its specialized expertise and nuances. Monitoring of projects/companies financed by such sources and also for each source, is a specialized job. Expertise, networks and knowledgebase should be developed to grab opportunities in these areas. Similarly, wealth management, asset management, portfolio management, net worth monitoring, investment banking and the like are emerging areas in finance where our services can add fantastic value. In fact, after the global credit crisis relatively small Indian funds and finance companies are grabbing expert people and opportunities to surge in investment banking, private equity, hedge funds, fund of funds, HNI asset management, wealth management and similar areas. There are opportunities for Company Secretaries in these areas. They can make financial management simple, intelligible to stakeholders and transparent. The profession can launch a great and sustained effort in this direction. All angles and aspects of finance, stakeholder engagement, communication of value, corporate governance etc. need a hard and probing study and application. When this is done consistently, opportunities in this area are bound to multiply in times to come. Let a few chosen from us change tracks and contribute to the changing paradigms of global finance, lest we miss the bus.

REGULATORY CHANGE

Regulatory environment also needs a constant re-look and renovation in these turbulent times. The US did bring in Sarbanes Oxley legislation to tighten regulatory regime in order to improve corporate governance and protect stakeholder interests. But it failed on the front of large banking and financing industry to protect national economic interests. A keen debate among various regulators from various Ministries, investor associations, consumer fora, NGO's etc. requires to be constantly evoked when we are amidst innovation of the regulatory regime.

Professionals, especially Company Secretaries, have a huge role to play when it comes to reforming the legal, regulatory and supervisory environment affecting the corporate sector. The new Companies Bill that has been cleared by the Union Cabinet to be introduced in the Parliament will, of course, be an area of key focus. Both larger canvas issues and minute aspects of legal and regulatory environment draw valuable contribution from our profession. Ease of functioning for corporate to facilitate faster economic growth, allowing flexibility and innovation in functioning and financing and at the same time protecting and furthering interests of proximate and distant stakeholders, all make for the complexity and perspicacity of legislation and rule making. This exercise needs to encompass, paradoxically enough, the unpredictable future and futuristic rationale. It is a big challenge and we cannot stay away from it as it is not only our bread-and-butter, it is our forte and raison-de-atre.

The general opinion about the present global economic meltdown is that it has brought about the unease of impending darkness. That, the situation is comparable to the global depression of the 1930's or, at least, the economic crisis witnessed in 1907. The US and European governments have set aside hundreds of billions of dollars (USD 250 billion by the US alone) to buy shares of banks, to buck up their falling market values. Governance, in general and corporate governance, in particular, appears to have left a lot to be desired. It is in this situation that positive and forward-looking corporate governance professionals, Company Secretaries, should implore, explore, innovate and renovate various aspects of corporate activity and show that the latent seeds of innovation, creativity and positivism do sprout, grow, flower and blossom through hardcore professional approach and attitude. In fact, excellence lies and continues to thrive through all-round creativity and innovation.

INNOVATION AND REGULATION — A UK PERSPECTIVE

ROGER DICKINSON*

The Companies Act, 2006 was finally given Royal Assent following an eight year review process. With 1300 sections, as well as secondary legislation that has subsequently been issued, the Act is the largest ever to go through Parliament in the UK. The changes encompassed by the Act will affect 2 million private businesses and 1 million public sector companies in the UK.

The 2006 Act springs out of a long process of review of company law that commenced in the 1990s and subsequent consultations on the proposals for change arising from that review. In this process company secretaries have played a leading role, not only in the original review process, but in helping to shape many of the new provisions. That influence continues today as company secretaries, many of them working closely with the Institute, participate in consultations on the myriad draft regulations implementing this major piece of legislation. As a member of the advisory group working with the Department for Business Enterprise and Regulatory Reform (formerly DTI), ICSA has played a highly influential role during the implementation process

By introducing the Act, the Department for Business Enterprise and Regulatory Reform (BERR) has made a major attempt at fostering innovation and encouraging entrepreneurship in UK businesses. The Act's 'think small first' deregulatory approach to company law has resulted in a modernised framework for companies. Amongst the Act's key objectives are to make the UK an attractive location in which to do business and to encourage dialogue between companies and prospective investors. Given the size of the Act, BERR has taken the unusual step of implementing it in several stages and the legislation will not be fully implemented until 2009. This approach has allowed BERR to undertake an extensive amount of consultation with businesses and other advisory bodies.

The ICSA has had to ensure that the implications of the legislation are fully understood by its members and other key audiences. The result has been a series of well received guidance notes on certain sections of the Act and there are more planned for the future. The notes are brought about as a result of discussion with various working groups consisting of members, lawyers and other advisers who agree on the wording of each guidance note. Although not a regulator, the ICSA has fostered a much higher level of understanding on some of the more complex aspects of the Act as a result of its guidance.

In a piece of legislation this size it is perhaps inevitable that there should be one or two areas which do not quite work as planned. The complexities of the Act were highlighted early on in the implementation process when between the publication of the White Paper in March 2005 and the Act receiving Royal Assent in November 2006, there was a distinct shift in the wording of the clauses on the company secretary. When the Bill came before the House of Lords it became clear that, should a private company require a company secretary, the Bill would not allow it to register that appointment at Companies

* Chief Executive, Institute of Chartered Secretaries and Administrators (ICSA), London.

House, nor would it give that secretary the automatic powers it enjoyed under the 1985 Companies Act. The secretary would also be unable to file returns at Companies House.

The change meant the execution of documents became a much more convoluted process for a private company. To compensate for this omission from the Bill, a proposed 'authorised signatory' regime was put forward as a means of allowing private companies to register company secretaries as officers of the company at Companies House.

Under this proposed regime, all directors and PLC company secretaries would automatically become authorised signatories. Companies would also be able to appoint anyone as an authorised signatory, and such officers could execute documents (there would have to be two authorised signatories or one plus a witness) and sign any document on behalf of the company. But the Government's argument that this would provide more 'choice' for companies was flawed. ICSA had no evidence of companies wanting a secretary without basic powers, and private companies who did not want a 'document execution' secretary would have been forced to appoint them as authorised signatories.

ICSA submitted two briefings to the Company Law Reform Committee prior to the Commons Committee debate on the clauses relating to the company secretary's role: one on the private company and its secretary, and one on the authorised signatory regime (as it was in May 2006). The briefing on the role of the company secretary had the support of the ICAEW, the Law Society, CBI, ACT and the Institute of Directors. In addition, a letter from ICSA's Chief Executive asking for support in lobbying the Commons Committee was e- mailed to company secretaries in over 2,000 companies, as well as ICSA Advisers, Members and numerous other contacts. As a result, the Commons Committee was inundated with e-mails and letters.

This impressive level of support gave the Conservatives ample ammunition for the debate and this seems, eventually, to have had the desired effect. When the Bill received Royal Assent, it was decreed that private companies who choose to have a company secretary should have one that is fully empowered.

The electronic communications clauses on the Act were introduced early in 2007, and the Institute responded swiftly by publishing a guidance note on this subject. It was the first guidance note to bring together the provisions from both the Companies Act, 2006 and the FSA's Disclosure and Transparency Rules. The first half of the document summarises and interprets the provisions, with the second half focusing on guidance and points of recommended best practice. The most significant aspect of the new provisions is the ability for companies to switch the default communication method from hard copy to website. This method of communication with shareholders continues to be the subject of much debate and the guidance clarified some of the key issues in time for the forthcoming AGM season.

Under the 1985 Act, shareholders could appoint either a proxy or a corporate representative to attend a company's general meetings on their behalf. A proxy could only attend the meeting and vote on a poll, but a corporate representative could effectively exercise all the rights of an individual shareholder – that is, they could attend, speak and vote at a meeting, both on a show of hands and on a poll. So, in many cases, investors preferred to use corporate representatives, particularly if they wished to attend the meeting to ask questions and decide on the way how to vote.

Section 375 of the old legislation referred to a corporation appointing a representative and there was some debate as to whether this could be interpreted to allow more than one representative to be appointed. The 2006 equivalent, S.323, definitely refers to more than one representative being appointed, but introduces a new problem. It appears to say in sub-section (4) that if a shareholder appoints more than one corporate representative, and those representatives exercise their rights in different ways at the meeting, those rights are not validly exercised.

This led to much concern among institutional investors and the custodians which deal with the

practicalities of holding the shares for them. They were keen to make sure that investors could still exercise their voting rights at company meetings, and have certainty that their votes would be allowed in potentially close or contentious issues.

In an attempt to ensure a smooth 2008 AGM season for both companies and investors, a group led by ICSA and made up of representatives from listed companies, various law firms, the three main share registrars, investors and custodians worked to find a solution. The outcome of that work was ICSA's guidance note 'Proxies and Corporate Representatives at General Meetings', which was published in January 2008.

The guidance note identifies the fact that the best way around the problem is for investors to appoint proxies instead of corporate representatives. The note also recommends that the first corporate representative for a particular shareholder who arrives at the meeting be appointed as a designated corporate representative (DCR). This is not particularly straightforward, and more details of the process and the necessary legal wording to make it work are in the guidance note.

In the meantime, the DCR procedure has been tried out and it was found that it did work, although it was time-consuming. All other companies are being encouraged to make the DCR method (particularly appointing the Chairman) available at their general meetings to avoid running into difficulties with their investors. It has been announced recently that BERR is planning to amend the company law regime in 2009 so that it is clear that votes can be split and exercised in different ways where investors employ proxies or corporate representatives. At present, this section of the Act remains confusing, and is clarified only by the ICSA guidance.

Under the Act's provisions, requests for a copy of register of members must include the name and address of the person seeking access, say what the information will be used for, whether it will be shared with anyone else and if so, to whom and for what purpose. The company must either comply with the request within five working days if the purpose is reasonable: however, if it believes it is not, it can apply to the courts for an order allowing it not to provide the register information. However the Act does not give any guidance as to what is or is not a proper purpose. The ICSA Guidance on Access to the Register of Members: the Proper Purpose Test provides advice on what companies need to do to comply with the 'proper purpose' sections of the Companies Act, 2006. These relieve companies of the statutory obligation to allow anyone access to its register of members, and imposes requirements on those that seek access to a particular company's register.

The ICSA guidance identifies several reasons that it believes should be viewed as improper. In addition to gathering information for credit and identity checks, it also identifies obtaining information with intent to commit identity fraud and other unlawful behaviour, intent to harass or intimidate shareholders and any other purpose not related to shareholders' capacity as members of the company.

The guidance emphasises that it is an industry view, and that the legal definition will ultimately be a matter for the courts. Even so, ICSA's view is that it will still provide a useful starting point for companies and their registrars in their assessment of any requests they receive.

On 1 October, 2008, a new duty for directors comes in as part of the second phase of implementation of the Companies Act. The clauses coming into force apply to directors' conflicts of interests and the third party benefit clause which provides that a director 'must not accept a benefit from a third party'. Directors must also declare interest in a proposed transaction or arrangement. These general duties are owed to the company rather than its shareholders and there are civil consequences if they are breached.

In relation to directors' duties, the Act generally codifies common law and equitable principles which directors should already be aware of. However some aspects depart from previous law and require new or revised practices or standards to be exercised. ICSA's guidance note on this section of the

Act assists company secretaries and directors in ensuring compliance with the Act and focuses attention on the decision making process.

Even if the Companies Act is taken out of the equation, a huge amount of regulation is coming across company secretaries' desks these days, and they have to find ways of ensuring that their company can comply with everything. Trying to implement the regulations in a way that is fully compliant, and communicating it in a way that gets the message across, requires quite a lot of innovative thought - especially in today's world where people suffer from information overload. In other words, a company secretary needs to be creative and because of the breadth of their training and experience they are better placed than some other professions to think 'outside the box' and come up with solutions. This is a particularly useful skill at a time when the economy has entered a difficult and troubling phase. As the dust settles on the current crisis, we can be sure that attention will turn again to good governance and the role it can play in helping to prevent some of the extraordinary consequences that the activity in the financial services sector has given rise to recently. It seems certain that, as has been the case over the last 15 years or so, company secretaries, and ICOSA as the leading professional voice representing company secretaries, will rise to the challenge.

THE CHANGING ROLE OF REGULATORS IN FOSTERING INNOVATION

N G CHAKRABORTY*

INNOVATION : MEANING AND RELATION WITH ECONOMY

The term innovation refers to both radical and incremental changes in thinking, in things, in process and in services. It is an important topic in the study of economics, business, technology, sociology and engineering. Innovation is therefore considered a major driver of the economic growth. The factors that lead to innovation are also considered to be critical to policy makers. In the organizational context, innovation may be linked to performance and growth through improvements in efficiency, productivity, quality, competitive positioning, market share etc.

While innovation typically adds value, innovation may also have destructive effect as new developments clear away or change organizational forms and practices. Organizations that do not innovate effectively may be destroyed by those that do. Hence innovation typically involves risk. A key challenge in innovation is to maintain a balance between process and product innovations where process innovations tend to involve a business model which may develop shareholders' satisfaction through improved efficiencies while product innovations develop customer support however at the risk of costly R & D that can erode shareholders' return. This explains the relationship between innovation and organizations.

INNOVATION AND ADAPTABILITY

But what is more important is to find out the answer to the question "Under what circumstances innovations take place?" In short, four conditions are required: (1) demand for the newer idea, process or product, (2) freedom of thought and action, (3) knowledge, and (4) patronization. Innovation is made by one, but the result of such innovation is enjoyed not by all but by many and therefore, it is not that everyone is benefited out of all innovations. The persons who can adapt themselves with the innovated idea, process or product, they can enjoy the benefit, and even survive. Charles Darwin wrote, "It is not the strongest of the species that survives, nor the most intelligent but the one most responsive to change". The developing and the underdeveloped countries are lagging behind not more because of the dearth of capital but more because of their non-responsiveness to change, and absence of those four pre-conditions to innovations.

INNOVATION : KEEPING PACE WITH CHANGES

Now let us look in to those conditions leading to innovations. Demand for innovations is no doubt the key driver. Before, industrial revolution in Europe, the poor financial conditions coupled with newly discovered unexplored markets across the globe made the scientific innovations must rather than possible. Freedom of thought and action is a pre-requisite for innovation. Thought and action of individuals and society is on continuous change due to changes in striking force of economy, politics and religion. To

* FCA, FCS. Institute of Chartered Secretaries and Managers of Bangladesh (ICSMB).

BACKGROUNDER

cope with those changes in life and society, newer thoughts become imminent subject to prevalence of other conditions of freedom, knowledge and patronization. Therefore, innovations and its requisite factors are complementary and counter productive to each other.

INNOVATION AND LAW

Man has, for his own existence and development, formed society, religion and state to reap the benefits of his innovations in the process of discovering the rules of the nature. Society, religion and state again, in the process of advancement, formed various organizations of their own, selected some people having appropriate knowledge to run those, and allowed freedom to the stewards both in thought and action and also patronized them with a view to: (1) keep the process of development unhindered, (2) ensure maximum benefit out of goods and services produced by the efforts, dedication, toiling of all the individuals under their control, (3) induce more innovations to keep the pace of the wheel of progress for further development. Human propensity for more and more consumption encouraged by owning personal property and recognized by those organizations has accentuated intra and inter clash of interest among the individuals and organizations. These clashes have necessitated the enactment of laws and regulations to maintain an equilibrium. With the ever-changing production process, life and livelihood of individuals, this balance tilts left or right. A new equilibrium requires to be fixed and the existing laws and regulations need to be changed and thus it goes on.

INNOVATION AND LAW : OBSOLESCENCE

We know that water hyacinth in the paddy field where standing paddy crops are in the knee-deep water is injurious for the crops and some people used to throw the hybrid hyacinth in to paddy field of others out of animosity. To deter the loss of paddy production, The Water Hyacinth Act, 1936 was promulgated. Days have changed, water hyacinth now-a-days has become scarce. Therefore, the said Act has become obsolete. The same is true for The Arya Marriage Validation Act, 1937; The Famine Insurance Act, 1937 so on and so forth. Again new laws like Micro-finance Regulations Act, Information & Communication Technology Act, Right to Information Act, Intellectual Property laws etc. have now been promulgated to meet the demand of the present day society. Today's laws would become obsolete tomorrow to make way for the laws of the day after to come.

INNOVATION : ROLE OF THE STATE

Society, state and religion suffer from non-responsiveness to any changes. Examples in the history are many. Galileo faced it. Descartes destructed the final volume of his 'Treatise on the World'. Leonardo Bruno suffered a lot and finally sacrificed his life in the inferno. Many men and women toiled for the well being of the masses and even offered their lives for the cause of humanity. They all wanted to bring newer thoughts and ideas, but the powerful group behind these institutions, whom we call regulators did not accept those innovations.

In modern world, the state is run by three basic institutions : legislative, executive and judiciary and the fourth, though not very widely accepted, is the 'media'. All these four are run directly or indirectly by the very powerful people in the respective societies. Their interest as a group is lying on a strong passion 'greed' and self-aggrandizement. This sounds to be very unpleasant but matters much. If all the people behind those institutions play interactively driven by greed in disguise of profit, sufferings of the common people know no bounds. The wars waged so far were sprouted from unbridled greed. This unrestrained greed has caused immense sufferings to the humanity as a whole. In recent history, the war against imaginary bug is the culmination of this human vice. The 'civil society', the most responsive organ of the modern day society across the world though expressed concern over the issue but all these are mostly lost in oblivion.

INNOVATIONS AND REGULATORS : EXAMPLE OF THE FAILURE OF THE STATE RESULTING FINANCIAL CRISIS

The US entered 2008 with a housing market correction and a decline in dollar value. In early month of 2008, Bear Sterns and Global Insight collapsed, recession rose from 25% to 40%. Former Federal Reserve Chairman, Alan Green Span stated in March, 2008 that the 2008 financial crisis in the US was likely to be judged as the harshest since the end of world war II. In the US, GDP went down, unemployment rose, the mortgage lenders like Indymac Bank, Fannie Mae and Freddie Mac were in crisis. Later those were placed in to 'conservator-ship' on September 7, 2008. Deeply engrossed with \$6 bn. loan, Lehman Brothers, an investment bank of 150 years old went bankrupt on September 13. Brokerage institution Merrill Lynch was purchased at \$ 5 bn. by the Bank of America. Insurance giant AIG sought bridge loan from Federal Reserve. A consortium of Banks created emergency fund of at least \$ 70 bn. to deal with the effects of Lehman Brothers' closure similar to the consortium put forth by J. P. Morgan during the stock market panic of 2007. On September 16, Federal Reserve agreed to give AIG \$ 85 bn. as rescue package. The year 2008 as of September 17, 81 public corporations filed for bankruptcy compared to 78 in 2007 in the US. In the meantime, two failed British Banks have been nationalized by the UK Government.

THE RESCUE PLAN

On September 29, the bail-out plan of \$ 700 bn. placed by the US Government to buy mostly soured mortgaged-backed securities from Wall Street firms and banks was however passed by the US Congress. These arcane investment instruments linked to home mortgages, have combined with falling housing prices to ignite credit crisis and therefore, within hours stock market indices across the continents went down, perhaps heading further decline. But no doubt, all these will be a very temporary solution.

The bail-out bill passed by the US Government authorizes the Treasury Secretary to purchase as much securities of such of the failed companies at such a price as may be deemed reasonable to him, of course, with a very powerful five member committee consisted by the Treasury Secretary himself, the Housing Secretary, the Director Home Finance Agency, Chairman of Securities and Exchange Commission, Chairman of the Federal Reserve to oversee the rescue function of the Treasury Secretary. The Treasury Secretary, Mr. Paulson expecting trouble upon taking the Treasury Secretary position last year, said that he was still surprised by the speed and power of the financial 'hurricane' that was descended upon the Wall Street. It would take years for the US financial market to recover the crisis, even if, the bail-out bill is properly implemented. Apprehension is also there that the \$ 700 bn. package would be insufficient because the total deficit of the US financial market will well exceed trillions of dollar when other institutions would surrender declaring themselves bankrupt knowing it fully that there is Federal Government to bail-out.

THE FINANCIAL CRISIS : INTERNATIONAL REACTION

Lu Mingkang, Chairman of the China Banking Regulatory Commission, hit out at the 'dangerous and indefensible' extent to which financial institutions were allowed amass debt, lamented for the lack of 'prudential supervision'. German's Finance Minister Peer Steinbrueck – 'The long term consequences of the crisis are not yet clear. But one thing seems likely to me: the USA will lose its superpower status in the global financial system. The world financial system is becoming multi-polar. ... Stronger international regulation is required to be agreed upon at international level in order to 're-civilize' financial markets so that such a crisis was never repeated.

THE FINANCIAL CRISIS : CAUSE AND EFFECT

All these have happened within a very short span of time. If we look deep in to those cases, we'll find that in case of sub-prime crisis, interest rate of lending was cut down to induce consumption for

housing. This has resulted in allowing loan without considering the ability of the borrowers to repay. When the repayment dates fell due, the housing price began to fall and the lending banks found impossible to recover the money and ultimately failed. In other cases, profits were allowed to be massively inflated year after year which necessitated the creation of 'toxic assets'. Time came when all those companies involved suffered from liquidity. To add fuel to fire, the executives drew a huge amount of salary, and bonus based on the shown false profit.

THE EXPECTED OUTCOME OF THE RESCUE PLAN

To many, the Emergency Economic Stabilization Act of 2008 passed by the US Congress is a cause for qualified sense of relief, even for many conservative policy makers and economists, despite qualms it may be too generous to Wall Street bankers, too weak for struggling homeowners and too costly for taxpayers. Out of \$ 700 bn., \$ 350-400 bn. would be used to write off bad loans not only on housing-related debt, but also for corporate lending, consumer loans, credit cards and student loans. The curbs on executive pay were an essential ingredient to gain political support for the US rescue plan, blunting the criticism that the bail-out would protect the suspect gains of wealthy Wall Street executives. For companies making substantial use of the program, the government would limit the tax deductibility of the executive pay to \$ 500,000, prohibit 'golden parachute' payments to departing executives, and allow the recovery by the financial institutions of bonuses from gains that later prove to have been based on false profit. The provision to recover hefty bonus payments is problematic because the Government would have to prove that an executive had engaged in misconduct, not just poor management.

DILEMMA REMAINS UNRESOLVED

The recent crisis in the global financial market in general and that of the US and the UK in particular, the bail-out bill and nationalization of British Banks all these have put forth several important questions to all concerned. (1) Isn't it unjustified for the tax-payers to purchase the failure or inefficiency (in reality all these have happened due to reckless act of the regulators and regulatees fuelled by unrestrained greed with a view to gain personally) of the management of those failed companies with their hard earned money ? (2) What is the guarantee that no more private institutions would fail in future due to unrestrained greed ? (3) The developed countries and the IMF who always propound for 'market economy' and prescribe 'market force' as panacea for anything and everything going wrong for the third world, while at the same time the developed countries are rescuing or nationalizing the private sector institutions in their countries without allowing market force to work. Who is there to say which one is correct ? (4) What is the guarantee that the proposed Government financing would not be proved again improper in near future ?

INNOVATION AND REGULATORS : THE FUTURE

Financial derivatives have been innovated in a great number and are in use globally to make the financial transactions easy. Cross border financial transactions are taking place under the world's new order of 'globalization' without any corresponding international regulations needed to control the financial market across the globe. At the same time, the existing regulations are not being adhered to in its' proper sense and spirit. Therefore, time has come that the world would soon see a multi-polar system not only in financial sector but also in all other sectors, a new international currency to replace the old, a new war waged against famine, illiteracy, poverty, human trafficking, drugs, arms race.

To make that happen, the difficulty is we don't know how much freedom is required for the innovators to meet the demand of the new world ahead. Therefore, the present day challenge to the humanity is to strike out an effective balance of the factors of innovation where the creators backed by appropriate knowledge and patronization will feel free to innovate and regulators would play their role

BACKGROUNDER

with their appropriate legislations commensurate with the ever-changing circumstances imbued with holistic approach. The world is so eagerly waiting to see that new day! That can only happen when regulators don't innovate and innovators regulate.

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THE OPPORTUNITY IN MID-MARKET PRIVATE EQUITY FIRMS

CS. BALWANT KULKARNI*

The year 2008 has seen an extended market volatility and looming recession in global financial markets. The credit crisis in the western financial giants of the banking, investment banking and insurance sectors has deepened going from bad to worse. The latest failure of Lehman Brothers and the bailed-out American International Group has sent chill down the spine of the global financial sector in particular and the economy in general.

Yet hardcore professionals innovate, create solutions and look for better opportunities even while facing a gloom, a slowdown or a downturn, global, regional or local. That proves their leadership. In fact, such situations do bring out the best in them, drawing assistance from their well-researched studies, mastery over soft-skills and unretrievably optimistic approach.

Rothstein Kass, an American CPA and consulting firm has carried out a study on "Private Equity in 2008" on the background of the credit crisis in the United States, the mild-to-severe economic downturn and the evolving strategies of the hedge funds, the fund of funds, traditional banking, investment banking and private equity funds. The study is based on the experience and researched opinions of the managing partners of a number of private equity funds, their clients and advisors.

When an economic crisis looms large, investment professionals re-evaluate investment strategies and competitive positioning. Such re-evaluation is more intense when top tier institutions face difficulties and sour market sentiments.

During the time that ushers in tightening credit standards private equity community is the most imperiled sector. This sector faces tougher conditions having in recent times experienced strong returns propelling a rapid proliferation of funds encompassing all sizes and strategies. Yet, in this sector, as compared to large and small private equity funds, mid-market funds provide a unique growth opportunity. The Rothstein Kass study finds that mid-market private equity funds occupy an inimitable industry position with keen insight in vertical industry sectors they finance.

"Because of their unique perspective and diverse strategies, mid-market private equity firms – may be more so than the largest firms – can help predict the direction of the economy and the outlook for deal-making". Such firms are normally small players in niche markets. As such, they are among the first to feel the effects of credit market weakness. They are also more "alert to increased competition from larger firms looking downstream for deal-flow". The fund industry has been acutely aware that any extended period of market uncertainty would have an adverse impact on private equity funds. Competition for good companies will become more intense, including from hedge funds and conventional lending organizations. Yet, despite these challenges the individual fund managers Rothstein Kass surveyed were generally optimistic about their own prospects and indicated very aggressive fund raising targets. The survey also showed that mid-market funds will need to be more actively involved in the management

* Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

of portfolio companies and that funds will need to explore more synergies in their holdings in order to maximize returns.

“In this respect smaller and mid-market private equity firms may actually outpace their larger peers. Many of these firms have developed in direct competition with new entrants and established players and have had to adapt and establish niche practices to stand out in the market place. Generally, mid-market firms, accustomed to structuring and executing transactions in challenging markets are firmly entrenched in their chosen practice areas”.

Operations of mid-market firms tend to be more streamlined and efficient, with clearly defined investment objectives. Hence they could be more likely to succeed in the long term perspective inspite of the current weakness in the economy.

THE RESEARCH

In the first quarter of 2008 Rothstein Kass conducted a telephonic interview survey of 323 managing partners of private equity funds. The survey sought their thoughts on how the economic climate and fall out of credit crisis will shape the competitive environment. The survey therefore does not take account of the subsequent afflictions of Lehman Brothers, AIG and Merill Lynch. Yet some of the interviewed managers did predict such worse scenarios. Participating firms had at least one private equity fund - and in many cases several- with a minimum of 50 million dollar, and not more than 300 million dollar, total assets under management.

The survey used a statistical technique known as “cluster analysis” to identify issues having the greatest influence on a managing partner’s outlook. All surveyed respondents agreed that the US was in the midst of an economic downturn, with approximately 29% characterizing the downturn as severe. This, it is submitted, may be considered as an opportunity to canalize such money into Indo-American, if not purely Indian projects in India.

The remaining third were slightly more optimistic about the conditions in the US, maintaining that the US was recovering and, was experiencing only a mild downturn.

The pervasiveness of this view – that the US economy was in downward spiral-dramatically contrast to that of participating in Rothstein Kass earlier survey of hedge fund managers (“2008: Onward and Upward). In that survey a solid one-third of the respondents expected the economy to improve. The perceived severity of the present US economic condition was pivotal factor in how respondents to the private equity survey viewed the challenges facing the industry. While the very large private equity firms are confused, the smaller ones that had proliferated in recent years with their nimble investment strategies and ready access to capital competed effectively with their multi-billion dollar peers. But they had now become more vulnerable to prolonged weakness in credit markets. Thus, the opportunity now lies with mid-market private equity firms in the US.

ISSUES

The survey was conducted to question private equity funds and their executives about four issues:

1. The impact of the recent credit crisis on the private equity business.
2. The fund raising climate.
3. The most pressing competition challenges.
4. The relationship between the economic environment and investment opportunities.

BACKGROUNDER

CREDIT CRISIS IMPACT

The current credit crisis is of the magnitude that threatens the world financial architectures. It may now expand to the extended financial services domain particularly the credit card industry. The credit card payments may also include a component of mortgage payments. The future may now belong to what E E Schumacher had perhaps rightly said "small is beautiful". The credit crisis also subverts the real economy and its production, jobs and price stability.

A strong majority of the Rothstein Kass survey respondents believe that the credit crisis will take a toll on the private equity business. "The harmful impact of the weakened credit markets on the private equity industry was widely acknowledged by survey respondents, regardless of their views on the severity of the downturn. Most respondents were also doubtful of a quick turnaround, with nearly 70% opining that the credit crisis will worsen over the remainder of the year. Still, not all predictions were so dour. Among managers who believe that we are in a mild downturn, only 21% anticipate further deterioration of credit markets in 2008". The US dollar 85 billion loan to the drowning AIG by the Federal Government to abate the crisis of confidence in the American financial markets have proved this prediction. The US Treasury Secretary has proposed to move all the toxic financial assets of tumbling Wall Street Banks to special purpose vehicle. A fund of roughly half a trillion dollars may be created to support a comprehensive effort to deal with troubled assets. [The Economic Times Edit dated September 22, 2008]

RAISING MONEY

In the Rothstein Kass survey, all surveyed managing partners expressed an interest in raising more assets for their funds, including 90 percent of those expecting a severe downturn and 97 percent of those expecting a mild downturn. Life runs on hope after all, both for lenders and borrowers. Despite a strong shared interest in fund raising, there was a marked difference among the survey respondents when it came to forecasting whether raising capital would be easy or difficult. 82% of the partners who expected a severe economic downturn expected difficulty in raising money in 2008, while just 32% of those anticipating a mild downturn felt it would be harder to raise money. "..... a larger majority (of managing partners of private equity funds) indicated interest in raising more money to invest. This suggests that while private equity firms are cognizant of challenges, they are confident in their own competitive standing and generally feel well positioned for aggressive growth". Hope dies hard and is the flame of life activity.

COMPETITIVE ENVIRONMENT

The earlier research report of Rothstein Kass pertained, as mentioned earlier to hedge funds. That research showed that the growth of the alternative investments sector had not been slowed owing to market conditions. Institutional investors, in particular, had continued to allocate assets to hedge funds, attracted by a history of superior results in competitive markets. But hedge funds had increased in numbers and in the diversity of their strategies, enhanced competition compelled them to consider new tactics to deliver returns that their sophisticated clients came to expect. This led to greater involvement, the present research shows, in private equity transactions. A prolonged economic downturn would cause more hedge funds to consider this strategy, as investment opportunities in equity markets would likely diminish. This would cause more intense competition to private equity firms of the larger and smaller kind. Almost half of the professionals who characterized the economic downturn as mild expected more private equity funds to be launched in 2008. "While majority of small and mid market private equity managers foresee stiffer competition from hedge funds and established private equity firms, few are expecting the space to become more crowded over the balance of the year. Only 21% of those surveyed suggested that more private equity funds will be launched in 2008". "....with so much uncertainty surrounding the sector, it will be very difficult for new entrants to compete especially with more established players engaged in aggressive fund raising efforts".

BACKGROUNDER

“Less than 25 per cent of funds surveyed expected downward pressure on the fees in the short to intermediate term. When viewed by the economic segment, 27% of the professionals with negative economic outlook and 14 per cent of those with milder economic perspective anticipate having to reduce their management fees”.

INVESTING

After the receipt of the Rothstein Kass research report, worse crisis has happened in the American economy. The Federal Government has taken drastic and out of the ordinary measures to inject liquidity and permitted world reputed investment bankers like Goldman Sachs and Morgan Stanley to become common retail bankers subject to capital adequacy norms. It is believed that injection of fresh liquidity in the economy will not be inflationary as it will substitute the dried up liquidity through big-ticket failures like the AIG, Merrill Lynch, Goldman etc. and can be withdrawn by the Federal Government once the original liquidity is restored.

The Rothstein Kass research report found as follows :

“The most encouraging news that emerges Is that the vast majority of respondents believe that there will not be a decline in suitable investment opportunities this year. Fewer than 15 per cent of all respondents [managing partners of private equity firms] indicated a belief that there will be fewer opportunities in 2008, with little disparity between those predicting a severe versus a mild downturn. As in any crowded marketplace, private equity participants need to offer a clear and unique value proposition to differentiate themselves from the competition. *Fortunately, many mid-market players have been compelled by fierce competition to establish niche investment practices. In many cases their boutiques possess a degree of experience in their chosen areas that far surpasses that found at larger, less specialized firms.* Nearly 70 per cent of survey respondents anticipated that investments will be more strategic through the balance of the year, and more than 75 per cent suggested that it will take longer to sell portfolio companies. Though private equity managers who expect only a mild downturn, were far less likely to agree with these statements, it's clear from our findings that the competitive landscape is shifting. Firms are taking an even more measured approach to the diligence with the understanding that exit strategies could be more difficult to execute than in recent years. In this environment smaller and mid-sized private equity firms are more frequently focused on companies and industries where the experience of their management teams allows them to generate value for longer term portfolio holdings. More than 82 per cent of respondents predicting a severe down turn also suggested that private equity firms will be more involved with portfolio companies than before. A need for increased operational involvement would benefit firms with strong industry concentration and extensive executive management experience. Opportunities in underperforming or distressed sectors such as real estate, financial services and manufacturing could be particularly attractive to mid-market private equity firms. As niche players, these firms often possess the vertical industry and executive management experience required to have a material impact on a portfolio company's bottom line.

It is precisely the prerogative of Company Secretaries to have better exposure and experience in particular industries. This profession is, therefore, particularly poised and positioned to benefit from the opportunities in mid-market private equity firms in the US and other advanced countries. When the giant US economy is withering and the financial centre is tilting towards Asia simultaneously with high rates of GDP growth in the Indian and other Asian economies, Company Secretaries should use their skills and executive experience in industry to seize opportunities in mid-market private equity firms. It is particularly in tough times that those who believe in themselves, their networking and their experience and skills, seize and make the best of latent opportunities. The opportunities in mid-market private equity funding is one such innovative opportunity in international finance, Company Secretaries can seize.

INNOVATE AND EXCEL TO SUSTAIN GROWTH

CS. SUTANU SINHA*

INNOVATION

The word itself indicates something more than its literal meaning. It reminds us of the history of mankind and whenever we study such history, plethora of landmark discoveries and inventions peep into our mind.

When the first man learnt to lit fire artificially by striking two stones, it was one of the greatest inventions the mankind ever had. Invention of wheel sometime between 3200 and 3500 B.C.E was another turning point.

It is worth mentioning that each and every innovation or discovery was the outcome to meet the necessity of the society. King Louis XV of France was lazy to climb stairs to move around different floor of the Castle. In 1743, castle employees created a chair that was controlled by a weight-and-pulley system installed in the chimney, and His Highness could easily move from floor to floor without using stares. Today's elevator is born out of that invention.

In many a cases, however, man discovered a lot of things accidentally. In 1958, Wily Higinbotham created a special visual game to show people the possible paths of nuclear missiles and on that day first video game was born. Wily named that as "Pong".

One of the important aspects of such inventions is community acceptance and absorbing such new knowledge for continuous use through generations until and unless new innovation replaces the old one. This process is now widely known a disruptive innovation.

In this process, human civilizations the world over became enriched through the knowledge gained by their previous generations. Simultaneously, exchange of such knowledge between different civilization further enriched human beings globally. Paradoxically, even war between two communities resulted in acquiring /exchanging of community knowledge developed through innovation or discoveries.

At the point of every discovery or invention there was an upward shift in the Knowledge base of the society and society experienced excellence of such innovation.

Another significant aspect of innovation is sustainability. The day society feels that the innovated product or service has lost its importance, such product vanishes.

The pace of innovation globally remained slow comparing its pace today. For example, eye glasses to solve the far sight problem of eyes was invented in Italy during 1268-1284 by Salvino D'Armato of Pisa and Alessandra Spina of Florence. In 1400, Concave eye lenses was invented to solve near sight problem. After another two hundred years Eye Glasses with arms (i.e. early form of today's spectacles) was invented. In 1775 Benjamin Franklin solved both farsighted as well as near sighted problem by use of single lens.

* Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

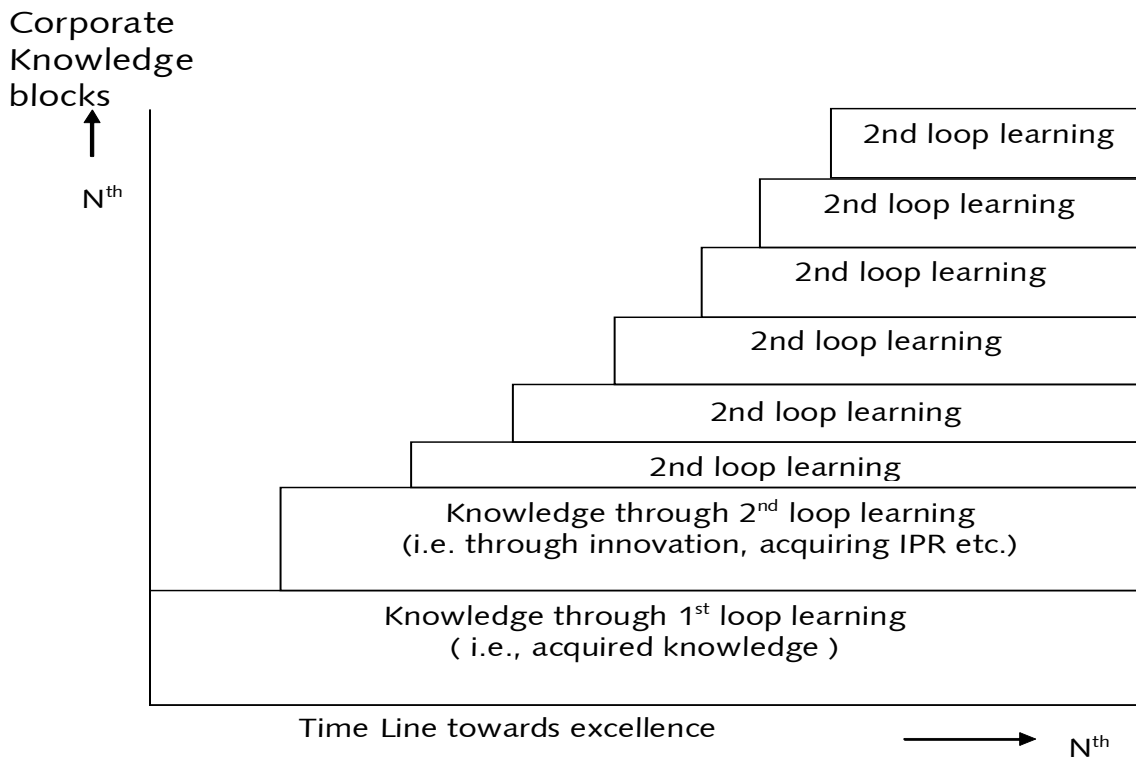
The speed of innovation and its absorption by the society today is very fast. The concept of computer networking materialized in USA during late 60's and early 70's. The pace was amazing. Within a span of about 35-37 years today's world is totally interlinked through internet.

The history of innovation can be segregated into three era, i.e., pre-industrial; post-industrial; and information technology era. Most of the innovations during pre-industrial era were the outcome of individual initiatives. During the post-industrial era, it was combination of both, individual effort as well as collective wisdom. Corporatization of business activities during last two centuries also paved the way to many new innovations of the society. The scenario changed dramatically during last few decades when most of the activities throughout the world resulted from corporate initiatives.

Each innovation leads to knowledge build-up. How effectively one is using such knowledge is most important benchmark of such innovation. Therefore, knowledge has become the key to excellence. It is true for any corporate action. Knowledge gives a corporate that cutting edge which makes it excellent organization. Building of knowledge mass is therefore critical for success and learning is only way to build up such knowledge block.

Acquiring knowledge can be made through two-tier system. Firstly, knowledge can be acquired through learning the existing processes, procedures, experience, etc. both in-house as well as external. This is known as *first loop learning*. Secondly, if an organization wants to excel, it should have some special value driver which will give it the cutting edge. That is possible through extensive research and development in a planned way. By the process, such pro-active organization develops special knowledge domain which keep it one step ahead of others. This process is coined as *second loop learning*. Interestingly, the moment second loop learning process is complete and stabilised, it becomes a part of first loop learning and adds to first loop knowledge block. In order to excel and sustain, organization therefore needs to continue its second loop learning process to remain above the others.

Innovation & Corporate Learning



BACKGROUND

DISRUPTIVE INNOVATION

In 1997, Professor Clayton Christensen in his book "*The Innovator's Dilemma*" (Harvard Business School Press) used the word 'Disruptive Innovation' wherein he investigated as to why some innovations that were radical in nature reinforced the incumbent's position in a certain industry. He analyzed disk drive industry and observed how capacity zoomed up from kilobytes to gigabytes leaving previous versions total obsolete and creating new markets for innovated products. The central theory of Christensen's work is that some innovations will appear as cheaper, simpler and even of inferior quality as compared to existing products, but some marginal or new segment will value it.

Some of the interesting examples of disruptive innovations may be cited as - telephone (disrupted telegraph); semiconductors (disrupted vacuum tubes); steamships (disrupted sailing ships); personal computers (disrupted typewriters).

KEY TO CORPORATE SUCCESS

Corporates - both large and small, are facing increasingly tough competition. There is no guarantee that companies at the top will continue to lead uninterruptedly in long run. Increased market share, sustainable profits and strong organizational results have never been more important. Business success are based on so many factors.

Achieving excellence requires holistic approach. An organization needs to ritually concentrate on the following :

1. *Goal Setting* : Organisation should have clearly defined goals designed in such a way to address stakeholder needs. There should be clearly defined Business Excellence Principles as a framework for strategy and specific targets. Enabling people to execute plan is also equally important and there should be constant monitoring system.
2. *Customer perception* : The major value driver for excellence is determined by the customers. Once confidence of customers is built up, organization never looks back.
3. *Learning, innovation and continual improvement* : Creating an environment of continuous learning, acknowledging new ideas and removing barriers to innovate ideas are essential to excellence. This should be an enduring process. Further, strategically changing old structures/ processes and overcoming barriers to implement innovations would be a winning approach to keep organization ahead of others.
4. *Continuous re-engineering of system to meet stakeholders' need* : The inbuilt process capability of the enterprise be aligned to the targets and corporate performance management be implemented to have real improvements.
5. *Flexibility and response to change* : Adaptability and prompt response to change is one of the most important traits of any excelling organization.
6. *Quality decision making* : Informed and well considered decisions are much more advantageous than decision made out in haste. Corporate Knowledge be used as a resource tool in decision making.
7. *People bring excellence* : Enthusiastic People in a very dynamic and vibrant environment deliver best of their capabilities. Creating proper work environment is therefore essential element to success. World-class companies have best technology and superior infrastructure but key to their success is mostly dependent on human factor – people who actually translate ideas into commercial propositions.
8. *Leaders – the creator of Role models* : Corporate leaders take care of human factors for excellence by creating a climate of trust, building employees' perception, leading improvement, planning

BACKGROUNDER

to increase Business Excellence scores, measuring progress with Business Excellence Principles and rewarding executives for business excellence and creating supportive environment. They become the pioneers to transform an enterprise into an excellent organization.

9. *Corporate citizenship* : Recognizing value drivers and operating under acceptable ethical standards create unparalleled advantage for a corporate. It ensures sustainability of the enterprise.
10. *Value creation for all stakeholders* : Ultimately value creation for all stakeholders without losing focus on best interest of the company is important.

In achieving excellence, an organization has to reach the customers expectation and in process it should develop such a business model which must include “re-learning”. To do things in new ways, a corporate has to forget the old ways of doing things. This is equally applicable for the customer side as well as the company side.

Importantly, sources of value for an organization are mostly indescribable, non-quantifiable and not easily discerned. Stakeholder approach to the business as opposed to the traditional shareholder approach can determine underlying value of the Organisation. Resources are better utilized for long-term value creation which is rightly reflected through stakeholder approach.

Under shareholders approach, value creation is driven by things that have been quantified and measured like financial results. Financial Performance evaluation tends to be more focused with little emphasis on intangible drivers of performance. Under this approach response to change is slow and new ideas are not easily understood and bottom line focus is on earnings.

On the contrary, stakeholder approach is deeper and broader which includes strong value system, sustainable thinking, creativity and innovation, bottom line focus on value, strong IPR strategy, thinking in terms of growing business opportunities around core competencies and so on.

EXCELLING INNOVATION

In order to achieve best of innovations, corporates have to ensure the following:

- (i) Specific strategy
- (ii) Planning
- (iii) Management involvement
- (iv) Knowledge people
- (v) Proper market projection
- (vi) Capability to translate knowledge into product or service
- (vii) Acceptability by consumers / customers
- (viii) Sustainability of the product or service
- (ix) Creation of value that would make the product or service unique

In this direction, it is worthwhile to mention the initiative of Singapore Government which has introduced I-SCORE – a Self Assessment Module to measure innovation scores for business excellence (see format placed as Annexure). This innovation score card for business excellence analyse the organization from the following perspectives :

- (i) Leadership
 - Senior Executive Leadership
 - Organisation Culture

- (ii) Planning
 - Strategy Development
 - Deployment
- (iii) Information
 - Management of Information
 - Comparison and Benchmarking
- (iv) People
 - Human Resource Planning
 - Employee Involvement and Commitment
 - Employee Education, Training and Development
 - Employee Health and Satisfaction
 - Employee Performance and Recognition
- (v) Processes
 - Innovation Processes
 - Process Management and Improvement
 - Supplier and Partnering Processes
- (vi) Results
 - Customer Results
 - Financial and Market Results
 - People Results
 - Operational Results

It is pertinent to mention that most of the drivers above are non-financial and intangible in nature. This exhibits the importance of knowledge resource for an excellent organization.

Innovation alone cannot bring excellence. It is the holistic approach that integrates all the value drivers to bring in excellence. For example, a corporate without putting extra investment in its own research and development activities may also achieve excellence by acquiring knowledge through strategic alliance, tie-up or merger. Similarly, innovative modes of finance can also bring success to a corporate. Off late, Indian corporates are realizing the importance of intellectual property. However, number of patents registered in the country in comparison to that of advanced countries, is still negligible. This indicates that Indian corporates are yet to focus more on intellectual property to have cutting edge over its overseas competitors. More deployment of fund in research and development and/or on acquiring technology, processes and IPRs would definitely create extra mileage.

I-SCORE

**INNOVATION SCORECARD
FOR BUSINESS EXCELLENCE**

Source : <http://www.spring.gov.sg>.

INNOVATION — AN ENGINE FOR QUANTUM ECONOMIC GROWTH

V P SHARMA* & M A JOSEPH**

INTRODUCTION

The international economy is experiencing an unprecedented metamorphosis. In the last couple of decades, the governing dynamics of the global economy have undergone significant transformation. A new world order is emerging where most economic transactions are invisible, borders are mere symbolic references and economic power has started to shift, underlying the growing importance of emerging economies. Innovation and technology are the *sine qua non* for economic growth world over. High-tech innovation in transports and communications has produced a high-speed, networked and increasingly interdependent global economy. Several core conditions enable innovation to encourage economic growth, strong standards and effective enforcement of intellectual property protection, vigorous competition and contestable markets, open trade and investment in a stable economic environment, a strong and sustainable fundamental research and development infrastructure, sound policies and mechanisms to promote the business-innovation interface, efficient and transparent regulatory systems, ethics and the rule of law, and a strong emphasis on education at all levels.

GLOBALISATION - A DOUBLE EDGED SWORD

Globalisation has not been a level playing field, but it has contributed to significant progress. Under the current wave of globalisation, the world economy has experienced one of its most dynamic expansions ever - growing 35% over the last seven years. International trade and investment flows have flourished, allowing developing countries to connect better to the global economy, lifting millions out of poverty. Globalisation has also raised the importance of crucial instruments of development and co-operation, like the Millennium Development Goals, the Kyoto Protocol or the one Laptop per Child project. Research and Development (R&D) have bloomed and spread globally. This globalisation of innovation has been fostered by Internet. With nearly 1.3 billion users, the Internet has opened an ocean of opportunity for millions of people, generating a genuinely global exchange of information, knowledge and ideas. On the other hand, sub-prime crisis, for example, has revealed the remarkable vulnerability of the new financial order. The frantic innovation in finance, like the securitisation of almost any form of debt into a tradable asset, might have been a way to spread risk, but it left the system vulnerable to systemic failures.

ECONOMIC GROWTH AND INNOVATION

The global economy is on its way to achieving a historic growth record. With an annual growth rate of nearly 3.2% since 2000, the world economy grew more in the past five years than in any five-year period earlier. With a projected increase of nearly 5% in 2007, some private think-tanks say global

* Joint Director, The ICSI The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

** Deputy Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

output could be heading for one of its best decades ever. This economic expansion has happened in spite of a number of economic and political shocks: the collapse of the stock market bubble in 2000; the terrorist attacks of September 11, 2001; wars in Afghanistan and Iraq; the escalation of oil and commodity prices; a break-down in Doha round of multilateral trade talks; some worrisome global imbalances and modest performances in some of the traditional engines of growth. Despite all this, the economic wheel is moving forward.

What looked as a recent global economic slowdown turned out to be a "rebalancing" of growth? The slowing pace of activity in the US and Japan, which should remain well contained, is being compensated by an apparently solid upswing in the euro area. Furthermore, and perhaps most surprisingly, the global economy now runs on a new powerful economic turbine: the emerging economies.

China and India, along with other developing nations, are in a position to give the world economy its biggest boost since the industrial revolution. The participation of these countries in global economic flows has been increasing at a remarkable pace, representing now - more than half of total world GDP (if we measure it at purchasing power parity), 43% of world exports and nearly half of the world's energy consumption. In 2006, developing countries have grown at a near record of 7%. During 2007 and 2008 they are expected to grow more than 6% per year, in comparison to a 2.7% GDP growth in developed economies. According to recent analysis by 'The Economist', if these trends continue, "it is estimated that in 20 years' time emerging economies will represent nearly two-thirds of global output (again, at purchasing-power parity)". How has the global economy managed to grow so steadily in a time of international uncertainty and recurring economic threats? Part of the answer lies in one single intangible factor: *innovation, the new arbiter of progress*.

Indeed, a key driver of economic growth has definitely been innovation. The creation, dissemination and application of knowledge have become a major engine of economic expansion. Corporations have come to rely more and more on this precious tool. It is a practice that has moved from the periphery of many corporate agendas right to the center of their strategies for growth and leadership. Most sectors and industries are currently experiencing what is called a "Schumpeterian renaissance": Innovation is today the crucial source of effective competition, of economic development and the transformation of society. It is difficult to agree on one single definition. However, we can argue without hesitation that innovation has proved to be:

- An efficient stimulant for building world-leading organizations (such as Microsoft, Rolls Royce, Apple, etc.);
- A discipline of creativity that attracts the best people (companies such as Dyson, Google, etc.);
- A message that reinforces a corporate ambition (Toyota or Adidas); and
- An instrument to foster leadership.

Innovation has also bred a fruitful collaboration between business and academia in many parts of the world. Turning a novel thought into a profitable product is a hard thing to do. Every great inventor needs a great entrepreneur and vice versa. Very often association between universities and corporations becomes the space where the future is invented. The number of already established university spin-ups like Cambridge or MIT is large, but more and more institutions are pressing forward. Oxford University, for example, is challenging Cambridge as one of the main centers of entrepreneurship and innovation in Europe. Modern economies are built with ideas, as much as with capital and labour. It is estimated that nearly half the US GDP, for example, is based on intellectual property. The EU has set the 'Barcelona target' of increasing R&D to 3% of GDP by 2010 to become "the most competitive and dynamic knowledge-based economy in the world". Look at China: according to OECD estimations, for the first time in 2006 China spent more on R&D than Japan, becoming the world's second largest investor in R&D after the US.

Globalisation itself is a product of innovation. The application of constantly improved technologies to the massive means of transport and communication has produced an unprecedented level of global connectivity and awareness. Economies are becoming more inter-dependent, while cultures are becoming more permeable, transparent and stronger through an intensified exchange of goods, services, ideas, values, experts, problems and solutions.

Today, innovation is facing new challenges. Its own dynamism has produced a world that requires in many ways a rethinking of innovation itself. Strategies like market capitalization, mergers and acquisitions and just-in-time delivery, have to be revised in the light of the Internet, online shopping and digital TV. Companies are hungry for new ideas about new ideas. Thus:

- Innovation takes many forms; it can be a process, product, service, or anything that helps firms to perform better.
- Innovation can originate from anyone. Anyone can innovate, as it requires a mindset that probes perceived boundaries to bring new ideas to fruition.
- Innovation is not creativity alone; it is more than creativity as it begins with an idea and subsequent implementation to produce new value.
- Innovation is more than improvement.
- Innovation pays in quantum amounts. The impact of innovation results in quantum leaps in value creation that encompasses effective results.

ECONOMIC GROWTH AND INNOVATION – ECONOMISTS’ VIEW

Economists define innovation differently and describe the role of innovation in economic growth and development in their own way. Economic growth is the traditional purview of macroeconomics, yet innovation is fundamentally about microeconomics. Sound fiscal policy and stable macroeconomic conditions are certainly important to economic growth but microeconomic concerns such as the role of government to promote innovation relies on addressing market failures that inhibit the accumulation of knowledge and aligning incentives for economic agents to commercialize that knowledge to realize economic value.

Economic growth is most commonly measured using changes in the total value of goods and services produced by a country’s economy or what is known as Gross Domestic Product (GDP). Of course, since the size of countries varies, this number is adjusted for the size of the population which provides a crude measure of the average individual’s well-being. The differences in levels and in trends in economic growth are driven by increased productivity that comes from innovation and technological change. The study of innovation and economic growth began in the late 1950s with the work of Robert Solow for which subsequently he was awarded the Nobel Prize. Of course, like any idea that gains currency the foundations had been provided by earlier scholars, notably Joseph Schumpeter. What was important about Solow’s work was that he empirically demonstrated that 87% of economic growth in the American economy from 1909 to 1949 was accounted for by an unspecified factor or residual that he described as technological change. Other studies have refined these estimates and provided more elegant theoretical models. Most importantly, the largest single factor explaining economic growth is not increase in factor inputs but the ability to extract greater economic value from advances in science and technology. The ability to extract economic growth from advances in knowledge is the essence of innovation.

INNOVATIVE ACTIVITIES

Innovation is a complex development of discoveries and inventions brought into the business and social environment that hopefully leads to diffusion. During the diffusion path, improvements to both the idea and implementation often require further innovation. Successful innovations are often imitated

by other players in the same industry or applied in other industries. Thus, out of several cases, innovation can basically be:

- Product innovation (e.g. new goods or services put on sale);
- Process innovation, which changes the way a given product is produced within the firm or across a supply chain;
- Behavioural innovation, when an organisational routine is replaced with a new one.

Quite often, the innovation turns out to be a mix of all the above three categories, as in the case of introduction of a new product that requires new productive competencies and changes in the organisation. Further, what to a supplier is a product innovation can be a process innovation to a user, as in the case of a new machine that revolutionises the process of manufacturing. In this case, investment is the means by which innovation is spread over the economy.

Although technology is often at the heart of an innovation, marketing and financing organisations can also be sources and multipliers of innovation. In an enlarged meaning, innovation embraces the introduction of known things to new markets or different industries. The environment in which something is said to be an innovation is also relevant. Thus, we can have an innovation simply relative to past achievements of the innovator or to the (local) market or to the world frontier. In the first two cases, it is possible to achieve the innovation just by imitating world-class practices. A useful distinction can be made between radical innovation and incremental innovation. Radical innovations comprise entirely new products, often undertaken by new entrants with a diversified knowledge base. Minor improvements in existing products and processes constitute incremental innovations, often undertaken by incumbent firms with a specific knowledge base.

ROLE OF INTELLECTUAL PROPERTY IN STIMULATING INNOVATION

Intellectual property helped to make possible the conditions for innovation, entrepreneurship and market-oriented economic growth that shaped the 20th century. In the 21st century, IPRs increasingly define these conditions, and dictate the pace and direction of innovation, investment and economic growth around the world. Today, more than ever before, enterprise and intellectual assets drive economic growth and increase standards of living. Innovation is instrumental in creating new jobs, providing higher incomes, offering investment opportunities, solving social problems, safeguarding the environment, and protecting our security. To achieve these objectives, governments must create appropriate incentives for continued growth in innovation and technology development and embrace sound policies for assuring broad social diffusion and access to key scientific and technological advances which enable us, as Newton first observed, “to stand on the shoulders of geniuses”. A critical enabling tool increasingly is intellectual property protection. Intellectual property rights are essential for achieving many of today’s challenges related to innovation and economic growth while providing the foundation on which tomorrow’s societal needs can be met. Their vitality derives from the multiple roles they play. These include the following:

(i) *Stimulating innovation and spurring widespread and sustainable economic growth*

Intellectual property rights are policy instruments that play an increasingly important and positive role in driving innovation and expanding information. By stimulating innovation, information and creativity, IPRs directly influence economic performance to create economic growth through increased productivity, increased trade and investment, and expanded economic activity which enhances consumer welfare. IPRs create incentives for invention and creation, to provide an efficient mechanism to overcome traditional “market failure” associated with public goods, information asymmetry and innovation – especially, the imperfect appropriation of returns and uncertainty with regard to research and investment identified by Nobel-laureate Kenneth Arrow.

A principal source of market failure is the inability of individuals and firms to prevent others from making use of the new knowledge they generate. Without the incentives provided by the temporary exclusivity generated by IPR protection, there will not be sufficient incentives for business to invest in risky R&D and other value-enhancing activities because the benefits from those investments cannot be appropriated fully.

Strong and effective IPR protection is a powerful incentive that permits firms to invest in generating new technology in sectors where the returns to technological or product investment are longer term and involve significant risks, and where the invention may be easy to copy or imitate. Such protection, in turn, is highly effective way to promote the diffusion of knowledge in the long term. Research is only one critical component of innovation. Studies confirm that research constitutes only about 25% of the cost of commercializing a new technology or technique and substantial up-front additional resources are needed to bring most products or processes to the market. The exclusive rights granted to a patent holder for a limited time provide the incentive for encouraging all the up-front investments needed to develop an idea and to generate a marketable product or technology

IPRs promote the disclosure of inventions and pioneering information, which stimulates innovation across industries. Intellectual property rights are not a mechanism for hiding knowledge. They are a powerful market-based mechanism for disseminating knowledge. The diffusion of IPRs, and the bundle of rights that often go with them, can serve as a central policy tool in shaping the knowledge economy. The public disclosure of information is one of the most important functions of IPRs but, often, one of the most neglected by policymakers.

(ii) *IPRs promote risky, uncertain and costly investments*

Forward-looking intellectual property rights protection provides incentives for firms and individuals to invest in generating new technology and new products, including incremental improvements. This is especially important where the returns from investment are longer-term, investment involves significant costs or risks, and the invention or creation may be easy to copy or imitate. IPRs enable technology transfer and increasingly facilitate the operation of markets. Strong and effective intellectual property rights are essential tool for technology transfer. They encourage private and public enterprises to transfer technology not only through voluntary licensing and other contractual arrangements but also through the development of innovative approaches for promoting technological development, direct investment, technology sales and dissemination, and cooperative ventures.

IPRs also help to stimulate and focus the process of knowledge creation and innovation through the necessity of finding legal means to “invent around” or “reverse engineer” patented inventions. By providing exclusive rights to an invention, the patent system frequently spurs others to innovate by developing alternative solutions to technical problems or new and improved inventions. Innovators are stimulated to “invent around” or “design around” the original invention in order to avoid infringing the applicable patent(s). While this may, in some circumstances, lead to “me-too” innovation, it most often leads to the emergence of different technologies and competing pathways that promote competition and spur innovation. The circumvention of existing patents means that new technological solutions put market pressure on the exploitation of existing technologies. History provides a number of examples about inter-industry technology “leaps.” Perfume sprayer mechanisms influenced the development of the carburetor, while various ecommerce innovations have come from the banking industry rather than the computer industry. Such technological convergence among industries is enabled by an intellectual property system which creates a public pool of knowledge, allowing companies to look beyond their own industry boundaries for R&D innovation.

(iii) *Empowering consumer protection in the global economy*

Increase in cross border trade has promoted a growth in trade marked / branded products that also incorporate copyrighted content and patented innovations. As a result, recognition of famous brands exists around the world. Moreover, international efforts to harmonize patent and trademark acquisition procedures have made it possible for companies to seek IPRs in more countries, in turn promoting the introduction of new products into markets around the world. The new global economy increasingly depends on the international recognition and dissemination of IPRs related to branded products. Trademarked brand names, copyrighted systems and patented inventions define the multinational marketplace as products and services are negotiated, shared and transferred with little regard to jurisdictional barriers or related to the country from where they originated.

With increased trade and investment, and the concomitant growth of branded products, IPRs increasingly serve as trade facilitators. Nevertheless, counterfeiting and digital piracy are booming. Innumerable fake products, ranging from pirated software and copied CDs to counterfeit medicines and aircraft parts, plague global trade and harm consumers. Counterfeiting increasingly poses a direct and serious threat to public health and safety. The market in fake pharmaceuticals and healthcare products is thriving in both developed and developing countries, too often putting the health and even the lives of consumers at risk. Counterfeiting also threatens legitimate trade and economic growth. The best estimates suggest that companies are losing more than \$ 200 billion annually to counterfeiting and piracy. In addition to lost sales, counterfeiting damages the reputations of legitimate manufacturers because the quality of fake products usually is inferior and can taint consumer perception of the genuine product. Moreover, counterfeiters pay no taxes or duties, thus costing governments as well. It causes global job losses to the tune of more than 200,000 jobs per year. In this way, counterfeiting, which counts for approximately 5 – 7 % of world trade, threatens economic growth as a whole.

(iv) *Supporting and enhancing competition*

Both intellectual property and competition policy are vital to maintain competition in a market-driven society because each, in its own way, encourages innovation and enhances consumer welfare. In protecting the rights of inventors and allowing innovators and creators to profit from their ideas and inventions, IPRs also depend on a legal and policy framework that ensures competitive markets.

(v) *Securing the benefits of IPRs for the digital economy*

Computers, telecommunications, semiconductors, entertainment and educational content, and other information-based sectors depend on IPRs as the legal and economic backbone of these industries. Intellectual property protection for these sectors - especially digital-related copyrights, software patents and other computer-implemented inventions - are the essential tools which creates new businesses, new jobs and new markets that drive the digital economy.

(vi) *Creating New Technology Markets*

Estimates suggest that more than one-half the store of human knowledge was produced in the second half of the 20th century, more than one-half of all patents have been issued in the last 30 years, and the number of marketable new products, services and innovations has tripled in the last 20 years. An important component of this explosive growth is the role played by IPRs in creating new markets for technology and accelerating the pace of future innovation. The principal reasons for this are the market-oriented characteristics of IPRs-they are tradeable, transferable and transparent.

A number of processes have contributed to the transformation of the global economy since World War II. The opening of national borders has led to a remarkable expansion of international trade and resulted in important efficiency gains in resource allocation. The collapse of barriers to the flow of goods and services, capital and labour has not always been orderly and has proceeded at different speeds in different parts of the world. But it is now virtually universal in scope. Not only has it emerged as an important driver of global economic growth, but greater openness and stronger links with the world economy have imposed on domestic producers everywhere the valuable discipline of international competition and attracted much needed capital and expertise, thus enhancing the prospects for growth through increased efficiency. National competitiveness as the set of factors, policies and institutions determine the level of productivity of a country. Raising productivity, i.e. making better use of available factors and resources is the driving force behind the rates of return on investment which, in turn, determine the aggregate growth rates of an economy. Thus, a more competitive economy will be one which will likely to grow faster in a medium to long-term perspective. To enhance productivity growth, education and training are emerging as key drivers of competitiveness.

As the global economy has become more complex, it has become evident that to compete and maintain a presence in global markets, it is essential to boost the human capital endowments of the labor force, whose members must have access to new knowledge, be constantly trained in new processes and in the operation of the latest technologies. As coverage of primary education has expanded rapidly in the developing world, higher education has gained importance. Thus, countries which have invested heavily in creating a well-developed infrastructure for tertiary education have reaped enormous benefits in terms of growth. Education has been a particularly important driver in the development of the capacity for technological innovation, as the experience of Finland, Korea, Taiwan, and Israel.

THE GLOBAL COMPETITIVENESS INDEX

Different countries, have defined their institutional endowments, current state of policies, and other factors inherent to their stage of development. Sound public finances may be important everywhere for creating the conditions for productivity growth, but they will be less important in countries with a long history of sound fiscal management. On the other hand, a move to better fiscal management in a country is likely to be beneficial for growth. The notion of the relative importance of these factors being a function of a country's endowments and stage of development is explicitly incorporated in the Global Competitiveness Index. The factors themselves will evolve over time, reflecting the rapid pace of change in the global economy. One may look to the growing importance of the latest technologies in enhancing productivity growth through improved processes and management practice, as compared to the early part of the post-war period, when growth in the global economy appears to have been driven mainly by the expansion of resource endowments.

Since 2001, World Economic Forum has been using the Growth Competitiveness Index (GCI) developed by Jeffrey Sachs and John McArthur to assess the competitiveness of nations. Subsequently, Professor Xavier Sala-i-Martin, a leading expert on growth and economic development, has developed a new comprehensive competitiveness model for the World Economic Forum. The GCI, albeit simple in structure, provides a holistic overview of factors that are critical to driving productivity and competitiveness, and groups them into twelve pillars. These pillars are discussed as under:

Basic Requirements

- 1st pillar - Institutions
- 2nd pillar - Infrastructure
- 3rd pillar - Macroeconomic stability
- 4th pillar - Health and primary education

Efficiency Enhancers

- 5th pillar - Higher education and training
- 6th pillar - Goods market efficiency
- 7th pillar - Labour market efficiency
- 8th pillar - Financial market sophistication
- 9th pillar - Technological readiness
- 10th pillar - Market size

Innovation and Sophistication Factors

- 11th pillar - Business sophistication
- 12th pillar - Innovation

The selection of these pillars as well as the factors that enter each of them is based on the latest theoretical and empirical research. These pillars are basically grouped under following three heads :

- (i) Basic requirements sub index group - it covers those pillars which are more critical for countries which are placed in the factor driven stage;
- (ii) Efficiency enhancer sub index group - it covers those pillars which are most critical for countries which are placed in efficiency driven stage; and
- (iii) Innovation and sophistication factors sub index group - it includes the pillars which are critical to countries placed in innovation driven stage.

It is important to note that none of these factors alone can ensure competitiveness. The value of increased spending in education will be undermined if rigidities in the labor market and other institutional weaknesses make it difficult for new graduates to gain access to suitable employment opportunities. Attempts to improve the macroeconomic environment e.g., bringing public finances under control are more likely to be successful and receive public support in countries where there is reasonable transparency in the management of public resources, as opposed to widespread corruption and abuse. Innovation or the adoption of new technologies or upgrading management practices will most likely not receive broad-based support in the business community, if protection of the domestic market ensures that the returns to seeking rents are higher than those for new investments. Therefore, the most competitive economies in the world will typically be those where concerted efforts have been made to frame policies in a comprehensive way, that is, those which recognize the importance of a broad array of factors, their interconnection, and the need to address the underlying weaknesses they reveal in a proactive way. An efficient financial sector is necessary to allocate the resources saved by the nation's citizen as well as those entering the economy from abroad to their most productive uses. It channels the resources to the entrepreneurial or investment projects with highest expected rate of returns, rather than to be politically connected. A thorough assessment of risk is therefore a key ingredient. Business investment is critical to productivity. Therefore, economies requires sophisticated financial markets that can make capital available for private sector investment from such sources as loan from a sound banking sector, well regulated securities exchanges, venture capital and other financial products. An efficient financial sector also ensures that innovations with good ideas have the financial resources to turn those ideas in to commercially viable product and services.

The twelfth pillar, innovation, is particularly important for countries that have reached the high-tech frontier, as it is the only self sustaining driver of growth. While less advanced countries can still

improve their productivity by adopting existing technologies or making incremental improvements in other areas. For countries that have reached the innovation stage of development, there is no longer sufficient scope to increase productivity. Firms in these countries must design and develop cutting-edge products and processes to maintain a competitive advantage. This requires an environment that is conducive to innovative activity, supported by both the public and the private sectors. This means sufficient business investment in research and development, high-quality scientific research institutions, collaboration in research between universities and industry, and protection of intellectual property.

Given the importance of innovation for long-term growth, innovation policy is currently very much at the center of economic policy in many countries. Overall, there is consensus that simply promoting and supporting large, isolated R&D projects has not proven to be a successful strategy. Instead, cumulative small improvements, along with informal innovation, can have similar growth effects to large R&D projects. These small innovative increments also tend to bring about additional spillover effects, such as complementary innovations, the development of specific skills, and additional investment. Thus, rather than focusing on national champions, innovation policies should aim to foster an environment which promotes entrepreneurship and innovation across the economic spectrum.

It may be noted that different key drivers in terms of pillars affect different countries differently. It basically depends on the stage of economic development in which a country is placed. According to GCI, in the first stage (Basic Requirements) i.e. in the factor-driven stage, countries compete based on their factor endowments, primarily unskilled labor and natural resources. Companies compete on the basis of prices and sell their basic products or commodities, with their low productivity reflect in low wages. Competitiveness at this stage of development, hinges mainly on a well-functioning public and private institutions (pillar 1), appropriate infrastructure (pillar 2), stable macroeconomic framework (pillar 3), and a healthy and literate workforce (pillar 4).

As wages rise with advancing development, countries move into the efficiency-driven stage of development, when they begin to develop efficient production processes and increase product quality. At this point, competitiveness becomes increasingly driven by higher education and training (pillar 5), goods market efficiency (pillar 6), labor market efficiency (pillar 7), financial market sophistication (pillar 8), ability to harness the benefits of existing technologies (pillar 9) and market size (pillar 10).

Finally, as countries move into the innovation-driven stage, they are able to sustain higher wages and the associated standard of living if their businesses are able to compete with new and unique products. At this stage, companies must compete through innovation (pillar 12), producing new and different goods using the most sophisticated production processes (pillar 11). Thus, although all twelve pillars matter to a certain extent for all countries, the importance of each one depends on a country's particular stage of development.

Innovation is fundamental to economic growth and development. The ability to create economic value by introducing new products to the market, redesigning production processes, or reconfiguring organizational practices is critical to competitive advantage and growth for firms, industries and countries. The question then becomes how to best organize resources to create, diffuse and sustain innovation and, moreover, how to leverage investments made in science and technology, research and development and related capabilities with the ultimate goal of reaping rewards in terms of wealth creation and increased standards of living.

INDIA'S GROWTH EXPERIENCE - AN OVERVIEW

India is now passing through a period of remarkable change and very interesting times. For half a century before independence in 1947, there was hardly any discernible economic growth in the whole Indian sub-continent. We have come a long way from the growth of 3 to 3.5 per cent growth in 1950s, to around 5.5 per cent in 1980s, 5.8 per cent in 1990s, and most recently to a sustainable growth path

BACKGROUNDER

of around 8.9 per cent plus. But, what is even more striking is the fact that if we take into account the decline in the rate of population growth from 2.2 per cent for 40 years during 1960-90 to 1.8 per cent in the 1990s and further down to 1.6 per cent currently, the growth in per capita GDP has seen a tremendous push from around 1.6 per cent a year in the 1950s to around 7 per cent per year now.

With such a high rate of economic growth that we have now experienced in recent years, progress in the country is now very palpable. The growth is manifesting itself in many ways all across the country: innovation and entrepreneurship are in the air. Exciting changes are taking place in all spheres. Even in agriculture, which otherwise has exhibited low growth over the past decade, a great deal of innovation is taking place. There is need to look at the documentation done by the Indian Institute of Management, Ahmadabad. Changes in public policy over the past couple of decades have indeed freed the entrepreneurial spirit of India. At this juncture, macroeconomic managers are to provide the overall environment for such entrepreneurship, innovation and growth to flourish. What constitutes such an environment? Low and stable inflation is essential, high and uneven inflation enhances risk and is hence inimical to innovation and risk taking. Investment cannot take place without the availability of risk capital, buttressed by the availability of an adequate flow of credit to nurture the investment climate. Furthermore, the cost of money available must reflect appropriately the risk and opportunity cost of lending. Under pricing of risk can lead to excessive risk taking, and over pricing would lead to the converse. For people to take risk, to innovate and grow, to have confidence in the future, the environment of low and stable inflation has to be supported by the maintenance of overall financial stability. Finally, it is the existence of sound financial institutions that is necessary for the appropriate supply of financial resources to take place. It is the job of the central bank and other regulatory institutions to ensure the existence of such an overall financial environment.

The whole process of economic reforms, capital market forms, financial market reforms, banking reforms, and monetary policy reforms have all combined to provide such an environment. There is need to ensure that this kind of growth environment – low and stable inflation and financial stability – is indeed maintained and sustained in the medium to long-term, so that in India entrepreneurship can flower and flourish further.

INNOVATION AND PRODUCTIVITY— INDIAN PERSPECTIVE

The National Knowledge Commission carried out a survey of a wide variety of firms to understand the nature of innovations, the differences between firms across sectors, and the role played by innovations in driving growth in India. The survey covered a total of 137 firms – 58 large firms and 79 small and medium enterprises (SMEs). The survey suggests that innovation is clearly in the air in the Indian business environment. The survey found that innovation gained importance in the decision making processes of firms – both large and small. Firms find that an increasing proportion of their growth in revenue, profitability, reduction in costs and increase in market share can be attributed to innovations. Thus, investing in innovation is being seen as a necessity for business success. Most innovation is incremental, though breakthrough innovations can bring a more dramatic jump in sales, profitability and the like. As might be expected, it is large firms that can hope to do breakthrough innovations, while small firms typically do incremental innovations. Consistent with earlier classification of what constitutes innovation - the survey finds that innovations are well spread across new products, new methods of production, marketing, innovative use of raw materials, and the like. Interestingly, although the intensity of innovation is found to be higher in manufacturing firms, the pace of growth in innovation intensity is higher in service sector firms which are more likely to be highly innovative.

As regards the process of innovation, the survey finds that firms that consciously invest in R&D, have better contacts and collaboration with R&D institutions, universities and government laboratories have a better chance of making innovation. Thus, there is great potential synergy between public investment in knowledge generating institutions and private entrepreneurship. In fact, some of the key

barriers to innovation are the shortage of skills, dull educational curricula and inadequate interaction with public agencies. Correspondingly, within firms, the attention of top management to the importance of innovation is essential. These survey results confirm the view of rising innovation activity and awareness in India and their growing importance in driving competitiveness and productivity gains in an increasingly competitive economic environment.

CONCLUSION

India, one of the largest economy of the world, is moving on high trajectory of economic growth after recording the longest spell (five years) of consistent growth beginning 2003-04 averaging 8.8 per cent GDP expansion including growth of 9 per cent during 2007-08. But the sustainability of high growth rate has become a challenge in the light of various global economic developments - crisis in the world financial markets, impact of phase of recession in US and European economies and world over, oil shocks, bankruptcies of big multinational corporations, soaring commodity prices, infrastructure bottleneck at domestic front. In this situation, for India, innovation in its various forms i.e. production, process, technologies and areas i.e. marketing, finance, communication, may prove an effective mantra to increase the efficiency and productivity and thus sustaining not only a higher and desirable rate of growth but also to achieve a comfortable level of living to its masses.

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SAFEGUARDING INNOVATION — MANAGEMENT OF INTELLECTUAL PROPERTY RIGHTS

DR. S K DIXIT*

Thomas Edison – American inventor and entrepreneur, once said, “the value of an idea lies in the using of it”. Intellectual Property Rights are significant factor in both creating and using ideas that are translated into knowledge and inventions to promote innovation and economic growth. With the advent of an increasingly knowledge-based society, grant of intellectual property rights ensures that innovators and creators have sufficient incentive to bring their works to market and to build on the innovations and creations of others for the benefit of society. As innovation and creativity are essential for sustainable growth and economic development, following core conditions enable the innovation and encourage economic growth:

- Strong standards and effective enforcement of intellectual property rights,
- Vigorous competition and contestable markets,
- Open trade and investment in a stable economic environment,
- Strong and sustainable fundamental research and development infrastructure,
- Sound policies and mechanisms to promote interface between science and innovation,
- Efficient and transparent regulatory systems, and
- Ethics and the rule of law.

Intellectual property protection is one of the central public policy considerations of knowledge based industries and global markets. Rapid changes in key technological, economic and social drivers underscore the importance of intellectual property as it provides an increasingly critical legal and policy instrument for encouraging innovation, stimulating investments needed to develop and market new innovations, and diffusing technology and other knowledge in economically and socially beneficial ways.

Adequate protection of intellectual property is important in safeguarding innovation, stimulating new technology development, artistic expression and knowledge dissemination, all of which are vital to the knowledge-based economy. Intellectual property laws create legally enforceable private rights that protect the form and/or content of information, expressions and ideas. By entitling exclusive rights, the intellectual property laws provide an incentive to pursue scientific, artistic and business endeavours which might not otherwise be feasible. Intellectual property laws confer exclusive rights on owners of IPRs and entitle them to prevent unauthorised use of their intellectual property rights. Accordingly, intellectual property laws confer on holder of the intellectual property the right to unilaterally exclude others from using that property. It allows the IPR holders to maximize its value through trade and exchange in the marketplace. This claim on the rewards flowing from intellectual property enhances the incentive for investment and future innovation.

* Joint Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

GENESIS OF INTELLECTUAL PROPERTY RIGHTS

The concept of intellectual property is not new. A Venetian Law of 1474 made the first systematic attempt to protect inventions by a form of patent, which granted an exclusive right to an individual for the first time. In the same century, the invention of movable type and the printing press by Johannes Gutenberg around 1450, contributed to the origin of the first copyright system in the world. Towards the end of the 19th century, innovative ways of manufacture helped trigger large-scale industrialization accompanied by rapid growth of cities, expansion of railway networks, the investment of capital and a growing transoceanic trade.

New ideals of industrialism, the emergence of stronger centralized governments, and nationalism led many countries to establish their modern Intellectual Property laws. At that time the International Intellectual Property system also started to take shape with the setting up of the Paris Convention for the Protection of Industrial Property in 1883 and the Berne Convention for the Protection of Literary and Artistic Works in 1886.

Over a period of time and particularly in contemporary corporate paradigm ideas and knowledge has become an increasingly important part of trade. Most of the value of high technology products and new medicines lies in the amount of invention, innovation, research, design and testing involved. Films, music recordings, books, computer software and on-line services are bought and sold because of the information and creativity they contain, not usually because of the plastic, metal or paper used to make them. Many products that used to be traded as low-technology goods or commodities now contain a higher proportion of invention and design in their value – for example brand-named clothing or new varieties of plants. Today the value of intellectual property far exceeds the value of assets in companies.

Brand Finance Top 500 Global Brands (2008) shows that some of the world's highest-profile brands display highest proportion of brand value to overall enterprise value: Nike (72%), Dell (45%), Budweiser (36%), McDonald's (32%), American Express (31%), Coca-Cola (31%), L'Oreal (30%), Tesco (27%), Disney (26%), Hewlett-Packard (26%). In the case of Tata, this is 20%.

THE BRAND VALUE – GLOBAL GAIANTS VIS-À-VIS INDIA INC.

India in Global Brands

The Tata group rose 45 places to 57 in Brand Finance Top 500 Global Brands (2008), a widely respected ranking of brands by brand value published by the UK-based Brand Finance Plc. No other Indian brand figures in the top 100. Reliance Industries came at 151 and Indian Oil at 215. Tata's upward rise in the brand rankings is significant because, despite its presence in services such as software, it is largely a traditional manufacturing group. And apart from General Electric (GE), no other traditional manufacturing brand features in the Top 10, which is dominated by US brands: Coca-Cola at 1, Microsoft at 2, Google at 3, Wal-Mart at 4, IBM at 5, GE at 6, HSBC at 7, Hewlett-Packard at 8, Nokia at 9, and Citi at 10.

Brand Strength : In terms of brand strength, the world's strongest brands are Coca-Cola, Microsoft, Google, Gillette, Nike, Apple at AAA+ (iconic) rating, followed by HSBC, McDonald's, BMW, American Express at AAA, or "very strong" rating.

Brand Value vis-à-vis Enterprise Value : The Brand Finance analysis of shifts in brand value by category highlights that Coca-Cola's brand value rose from \$43.1 billion in 2006 to \$45.4 billion in 2007. And its enterprise value rose from \$110 billion to \$147 billion. Pepsi's brand value rose from \$23.9 billion in 2006 to \$24.8 billion in 2007. Its brand value to enterprise value is about 20%, in contrast to Coca-Cola's 30%. In banking sector, the brand value of HSBC climbed from \$33.5 billion in 2006 to \$35.4 billion in 2007. In contrast, Citi's brand value slid from \$35.1 billion in 2006 to \$27.8 billion in 2007, reflecting its impact from the subprime crisis.

Indian brands in India

According to Brand Finance list of India's Top 50 (Company) Brands shows that companies in sectors like telecom, finance and auto have shown healthy signs of growth in the year 2008. Reliance Industries (RIL) once again emerged as the most valuable brand, at Rs 26,801-crore. In the IT-ITeS sector Tata Consultancy Services remained the strongest brand. The TCS brand is worth Rs 19,592-crore. Wipro, India's third largest software services exporter, is worth Rs 12,974-crore. Infosys Technologies has shown positive signs in brand valuation moving from Rs 7,341-crore to Rs 8,334-crore.

In the banking sector, ICICI Bank has gained over Rs 2,000-crore in brand valuation to Rs 11,533-crore, State Bank of India, emerges the most valuable financial services brand valued at Rs 16,595-crore.

In Indian telecom industry Bharti Airtel continues to be the baron of the Indian telecom brands with its valuation jumping from Rs 7,758-crore in 2006 to Rs 9,798-crore in December 2007. Though Reliance Communications has shown negative signs in terms of brand strength, its valuation has grown over Rs 1,400-crore and now stands at Rs 7,440-crore.

In the oil sector, Indian Oil Corporation's brand strength has gone down. Infact, all three PSU oil companies on the Top 50 Brands list have seen brand value erosion, in rupee terms. While Bharat Petroleum Corporation valued Rs 9,395-crore in 2007 as against Rs 11,312-crore in 2006; Hindustan Petroleum Corporation stands at Rs 7,950 crore in 2007 from Rs 9,348-crore in 2006 and IOC is at Rs 17,987-crore in 2007 versus Rs 18,992-crore in 2006.

In auto industry, Tata Motors, remained the country's most valuable auto brand. It stands at Rs 12,950-crore up from Rs 12,096-crore last year. Maruti Suzuki, valued at Rs 5,299-crore in 2007 and Hero Honda at Rs 3,208-crore.

India in the Innovation Mode

India Inc. is in an innovation mode and it is the manufacturing companies that are in forefront in terms of maximum number of patents filed. A Sunday ET analysis of the latest intellectual property rights (IPR) data found that even two PSUs figure in the top 10 companies that filed maximum number of patents during 2006-07 and 2007-08. In fact, the number of patent applications in financial year 2008 was 21% more than financial year 2007. According to the IPR data, Hindustan Unilever, Ranbaxy, Cipla, Tata Steel, Tata Motors, Bharat Heavy Electricals (BHEL) and Steel Authority of India (SAIL) filed maximum number of patents.

Hindustan Unilever (HUL) filed 251 patents in the last two fiscals, Ranbaxy and Cipla filed 208 and 53 patents, respectively, during the same period. Tata Steel filed 45 patents, and most of the Tata Motors' 40 patents are connected to its Rs 1-lakh car Nano. Among the top 100 tech companies in India, almost 89 have not filed any patent applications as yet. India's top two exporters of software services TSC and Infosys Technologies filed 14 and 22 patents, during the year 2007 and 2008 respectively. Corporate India's growing interest in filing patents is a reflection of the country's increasing economic and R&D activities and the realisation that new products are to be IPR-protected.

Though India Inc has come forward to file more patents, the number of patents filed by prominent education and research organisations far exceed that of corporate India. Council for Scientific and Industrial Research (CSIR) has topped the over-all list with 1,741 patents filed during 2007 and 2008, Indian Institute of Technology (IITs) stood second with 90, followed by Indian Council of Agriculture Research's (ICAR) 27.

SOFTWARE PIRACY A MAJOR THREAT TO INNOVATION

Safeguarding intellectual property is crucial to the sustainable long-term growth and performance of any business enterprise and the overall development of a nation. Innovation being at the centre of

intellectual property, its protection assumes paramount importance as IP theft in various forms has assumed high proportions. According to global PC Software Piracy Study (2008) the industry losses due to software piracy in India rose to US\$2 billion in 2007 as compared to US\$1.28 billion in 2006. The key findings of the study indicate that because the worldwide PC market grew fastest in high-piracy countries, the worldwide piracy rate increased by three percentage points to 38% in 2007. In Asia, the highest-piracy countries were Bangladesh (92%), Sri Lanka (90%) and Vietnam (85%). Among the lowest-piracy countries were Japan (23%), Singapore (37%) and Taiwan (40%).

Global Piracy Perspective

Business Software Alliance (BSA) Fifth Annual Global Software Piracy Study (May 2008) pointed out that although piracy of software on personal computers (PC) declined in many countries in 2007, fast growing PC markets in some of the world's highest piracy nations caused overall numbers to worsen—a trend that is expected to continue. Moreover, dollar losses from piracy rose by \$8 billion to nearly \$48 billion.

Software piracy negatively affects much more than just the industry. It also puts a strain on technology companies' ability to invest in new technologies; harms local resellers and services firms; lowers government tax revenues; and increases the risk of cyber crime and security problems. A recent IDC study conducted for BSA found that reducing software piracy by ten percentage points over four years could deliver billions in economic growth and hundreds of thousands of new jobs. A list of countries with highest/lowest piracy rates is given below :

	<i>Countries with Highest Piracy Rates</i>		<i>Countries with Lowest Piracy Rates</i>		
	2007	2006		2007	2006
Armenia	93%	95%	United States	20%	21%
Bangladesh	92%	92%	Luxembourg	21%	--
Azerbaijan	92%	94%	New Zealand	22%	22%
Moldova	92%	94%	Japan	23%	25%
Zimbabwe	91%	91%	Austria	25%	26%
Sri Lanka	90%	90%	Belgium	25%	27%
Yemen	89%	--	Denmark	25%	25%
Libya	88%	--	Finland	25%	27%
Venezuela	87%	86%	Sweden	25%	26%
Vietnam	85%	88%	Switzerland	25%	26%
Iraq	85%	--	United Kingdom	26%	27%

Key findings of BSA Study

The key findings of BSA Fifth Annual Global Software Piracy Study (2008) are given below :

- Russia led the way with a one-year drop of seven points to 73%, and a five-year drop of 14 points. Russia's piracy rate is still high, but it is decreasing at a fast pace as a result of legalization programs, government engagement and enforcement, user education, and an improved economy.
- United States (20%), Luxembourg (21%), and New Zealand (22%) were three lowest piracy countries.

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- Armenia (93%), Bangladesh (92%), and Azerbaijan (92%) were three highest piracy countries.
 - Piracy rates dropped slightly in many low-piracy markets where rates have been stagnant for several years, including the United States (-1%), United Kingdom (-1%), and Austria (-1%). Many other developed economies experienced a continuing gradual decline, including Australia, Belgium, Ireland, Japan, Singapore, South Africa, Sweden, and Taiwan.
 - Market factors contributing to increasing piracy rates include:
 - (i) dynamics in the PC market where the fastest growth is in the consumer and small business sectors; these are the hardest sectors in which to lower piracy; and
 - (ii) expanded Internet and broadband access. With approximately 700 million people expected to go online for the first time between 2008-2012, 76% of them will be in emerging markets. Access to pirated software will continue to shift from the streets to the Internet.
 - Market factors contributing to decreasing piracy rates include:
 - (i) increasing globalization among countries in emerging markets;
 - (ii) technologies such as technical protection measures like digital rights management (DRM) which software developers are building directly into their products;
 - (iii) new software distribution models such as software-as-a-service.

Road map for reducing software piracy

BSA's study suggested following five-point "blueprint" for reducing software piracy and reaping the economic benefits :

- Increasing public education and awareness of the value of intellectual property and the risks of using unlicensed software;
- Updating national copyright laws to implement World Intellectual Property Organization (WIPO) obligations in order to enable better and more effective enforcement against digital and online piracy;
- Creating strong enforcement mechanisms as required by the World Trade Organization (WTO) Trade-Related Aspects of Intellectual Property Rights Agreement (TRIPS), including tough antipiracy laws;
- Dedicating significant government resources to the problem, including national IP enforcement units, cross-border cooperation, and training for local officers and judiciary officials; and
- Leading by example by implementing software management policies and requiring the public sector to use only legitimate software.

PROTECTION OF INTELLECTUAL PROPERTY – GLOBAL INITIATIVES

The International Intellectual Property System is in fact a system of accumulated practices rather than a set of fixed rules. It is the practice of international relations in the matter of legal protection of invention and literary and artistic works, resulting from and governed by both national legislation defining the treatment to be granted to foreigners and international treaties concerning such treatment. It may be emphasised that a country's laws defining the rights of the foreigners form part of the international system even when, the country is not party to any international treaty on the subject, for such laws form the basis upon which in practice intellectual property is protected in more than one country. There

are number of International Treaties/Conventions which deal with the various aspects of intellectual property and industrial property. These Conventions are administered by World Intellectual Property Organisation, popularly known as WIPO.

Protection of Intellectual Property under TRIPs

The WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs) is based on the recognition that increasingly the value of goods and services entering the world trade resides in the know how and creativity incorporated into them. The TRIPs Agreement provides for minimum international standards of protection for such know-how and creativity in the area of copyright and related rights, trade marks, patents, geographical indications, industrial designs, layout designs of integrated circuits and undisclosed information. It also contains provisions aimed at the effective enforcement of such intellectual property rights.

Enforcement of Intellectual Property Rights under TRIPs : TRIPs agreement requires the member states to ensure that intellectual property rights are enforced under their laws, and that the penalties for infringement are tough enough to deter further violations. The agreement requires that the procedures must be fair and equitable, and not unnecessarily complicated or costly. They should not entail unreasonable time limits or unwarranted delays. People involved should be able to ask a court to review an administrative decision or to appeal a lower court's ruling.

The agreement describes in some detail how enforcement should be handled, including rules for obtaining evidence, provisional measures, injunctions, damages and other penalties. It says courts should have the right under certain conditions, to order the disposal or destruction of pirated or counterfeit goods. Willful trademark counterfeiting or copyright piracy on a commercial scale should be criminal offences. The agreement further requires the member states to ensure that the owner of intellectual property receives the assistance of customs authorities to prevent imports of counterfeit and pirated goods.

PROTECTION OF INTELLECTUAL PROPERTY IN INDIA

Until recently, the law relating to intellectual property in India were contained in Patents Act, 1970, Trade and Merchandise Marks Act, 1958, Copyright Act, 1957 and Designs Act 1911. India being a member of the WTO is under obligation to give effect to the various provisions of the TRIPs Agreement of WTO. The Government with a view to meet the time frame provided under TRIPs agreement, expedited the process of harmonization of Indian Intellectual Property Law with that of TRIPs agreement and amended the Patents Act in the years 1995, 1999, 2002 and 2005; and the Copyright Act in the years 1994 and 1999. The Government has also enacted following new legislations in the area of Intellectual Property :

- Trade Marks Act, 1999
- Designs Act, 2000
- Semiconductor Integrated Circuits Layout Design Act, 2000
- The Protection of Plant Varieties and Farmers' Rights Act, 2001.
- The Geographical Indications of Goods (Registration and Protection) Act, 1999

It can be said that with the amendment of Patents Act in 2005, the process of harmonization of intellectual property laws in india has been completed. And now the Indian system of protection of intellectual property can be benchmarked against global standards. Global PC Software Piracy Study (2008) findings that the piracy of software on PCs falling to 69% from 71% in the year 2006, in india, tells the challenges ahead for regulatory authorities in the effective enforcement of IPR laws to safeguard the innovations and to encourage innovative activities in India which was witnessing rising trends.

MANAGEMENT OF IPRs

In an increasingly knowledge-driven economy, Intellectual Property (IP) is an important key consideration in day-to-day business decisions. New products, brands and creative designs appear almost daily on the market and are the result of continuous human innovation and creativity. Generally, the small and medium companies in India either do not understand the value of their intellectual property assets or are not aware of the intellectual property system or the protection it can provide for their inventions, brands, and designs. As the Intellectual Property forms an important part of companies assets, its adequate protection is crucial in deterring potential infringement and in turning ideas into business assets with a real market value. Infact, the Intellectual Property system enables companies to profit from their innovative capacity and creativity and enhance their competitiveness.

Companies that dedicate time and resources to protecting their intellectual property can increase their competitiveness in a number of areas, as it prevents competitors from copying or closely imitating a company's products or services; avoids wasteful investment in research and development (R&D) and marketing; creating a corporate identity through a trademark and branding strategy; negotiating licensing, franchising or other Intellectual Property based contractual agreements; increasing the market value of the company; acquiring venture capital and enhancing access to finance; obtaining access to new markets and most important a careful search for conflicting existing Intellectual Property rights, and the examination of application by offices can help an enterprise to avoid conflicts and unnecessary litigation.

Strategies for Effective IPR Management : The effective management of intellectual property assets requires implementation of a comprehensive asset management plan. In this process one of the most important step is to review the existing intellectual property assets, so as to identify and locate the company's key intellectual property assets such as patents, patentable subject matter, copyrights, trade marks, designs, trade secrets, domain names, mask works, inventions, works of authorship, hardware and devices, depending upon the nature of business. Once the intellectual property assets are identified, it becomes important to determine nature and scope of the company's rights in intellectual property assets, which may range from outright ownership to a license- including contingent rights in intellectual property to be developed in future.

The capitalizing on intellectual property assets so identified require a most constructive approach keeping in view, among others, type of intellectual property assets, the type of business claiming ownership of intellectual property assets, long term and short term goals of the business organization including intended/possible use of intellectual property assets.

Intellectual Property – Risk Management : The ownership and control of intellectual property also attract certain risks and this requires strategies and plans to mitigate those risks. The most important among others being the infringement of rights in intellectual property, the risk management strategy should take into consideration the situations where company's own Intellectual Property Rights (IPRs) may infringe the IPRs of a third party; the company has a valid claim of infringement against a third party. It is also important to analyse the scope of any grant of rights in intellectual property assets, which may include licenses, distribution agreements, reseller arrangements and any other agreement or transaction involving transfer of IPRs that may impact its value.

One of the most important IPR risk management techniques, particularly in respect of trade secrets, is to put in place a system requiring all new employees and consultants to execute a confidentiality agreement. It indeed allows company to establish ownership in IPRs developed by the employees during their employment and also help company to effectively contest infringement in case employee leaves the organization and disclose the same to new employer.

In nutshell, effective management of Intellectual Property enables companies to use their intellectual property to improve their competitiveness and strategic advantage. Acquiring Intellectual Property

protection no doubt is crucial but its effective management provides much more than just protection to an enterprise's inventions, trademarks, designs, copyright or other allied rights.

Effective intellectual property management requires a company to commercialize its inventions and effectively monitor and enforce its intellectual property rights. Indeed, a company's portfolio of Intellectual Property must be viewed as a collection of key assets that add significant value to the enterprise. Thus, effective management of intellectual property may be seen as critical business strategy to maintain sustainable corporate growth and maximisation of shareholder value resulting into the economic growth.

CONCLUSION

Lack of intellectual property protection deprives the innovators and creators of their rightful reward for hard work and innovation, and weakens the incentives to invest for researchers. Counterfeiting and piracy jeopardizes healthy competition in an economy and distorts economic growth. As illegitimate operators save millions on research, development and marketing costs, legitimate companies struggle to compete with counterfeiters in a price-sensitive market. It deeply affects the knowledge-based sectors, for which innovation is the essence of their success, survival, and growth. Companies abroad seldom transfer advanced technology or invest in production or R&D facilities in countries where their products are copied or technology is stolen. Integration of a strong IPR regime into the international intellectual property system ensures that innovations are safeguarded against unauthorised use and treated as an invisible asset. At the organisation level, it is necessary that effective IPR management strategies are in place to safeguard against unauthorised use of intellectual assets.

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EMBRACING INNOVATION FOR QUANTUM GROWTH AND THE CHANGING ROLE OF REGULATORS

CS. ALKA KAPOOR* & CS. BANU DANDONA**

*"The Stone Age didn't end because we ran out of stone,"
– Thomas Friedma*

Empowered Organizations **ATTAIN** dominance by **Achieving Through Technology And INnovation**

Over a century ago, Adam Smith theorized that profit was a function of three factors of production: land, labor, and capital. By bringing these together in the right combinations, companies create value and return a profit.

But in reality, profit doesn't come from the factors of production themselves. It comes from the way those factors are brought together - the design and structure of the company and of the people and resources it uses. What makes one thing different from another is the way its parts are arranged. Bring together the elements to form simple cells, and life is born. Merge simple cells with one another to form complex ones, and thought is born.

Companies are living systems. They flourish on very same principles that foster sustainability in nature. Companies create value, using the same principles that drive innovation and value creation in nature. One need not re-invent the wheel, what one needs to do is to find newer and newer ways to use the wheel. That is innovation.

Innovation calls for passion. Most technology breakthroughs were possible because people who had the passion to experiment developed their ideas to fruition. Companies are also differentiated because of this passion. Some of the companies define passion in technology: Apple, or Google, for that matter. It is the passion in people that makes the fundamental difference to the results.

The idea that creativity is a predetermined personality trait gives people the excuse for not innovating or initiating change. The real challenge or barrier to innovation is doubt, the fear of criticism and the fear of failure. The real reason for failure is the lack of courage to embrace change or take a long-term view of their businesses.

The integration of constituent skills that is the distinguishing mark of a core competence, is achieved and sustained through developing strong dynamic capabilities, particularly in a world of innovation based competition.

* Joint Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

** Assistant Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

Robert B. Tucker in his article titled **Innovation: Core Competency for the 21st Century** writes –

“Winning firms will embrace the following four essential principles of managing innovation in the new century:

Principle No. 1 - A company’s approach to innovation must be comprehensive.

Innovation cannot be confined to one or two departments or farmed out to an elite group of star performers. Instead, it must permeate the entire company, and it must encompass new products, new services, new processes, new strategies, new business models, and the pursuit of new markets. It must be comprehensive.

Principle No. 2 - Innovation must include an organized, systematic, and continual search for new opportunities.

Firms that make innovation a core competence, specific systems and practices are in place that promote a deeper understanding of social, demographic and technological change.

The pace of change today requires broader participation. Successful innovation means more than just hatching ideas. It means being able to move on those novel solutions and champion them into specific results that create tangible customer value, improve processes, and build new opportunities. Creativity and passion are required at the inception and during each phase along the way to deal with bureaucracy and inertia. From the smallest improvement to the “*bet the company*” mega-product, ideas depend on people’s commitment to bringing them to fruition.

Principle No. 3 - Organizations must involve everyone in the innovation process.

Companies don’t use even half their brainpower. More than 70 percent compared their organizations to a “slow moving truck” blaming the condition on a failure to involve employees in decisions and a lack of training or rewards. Many jobs have actually been designed to eliminate the thinking component altogether and not just entry level jobs either. Then, in the midst of a crisis, employees are asked to suddenly be creative, to “think outside the box,” and management is underwhelmed by the results.

Akio Morita, the founding chairman of Sony, believed that a company would never rise to its potential if all the thinking was left to management. “Everybody in the company must contribute,” Morita wrote in his book, *Made in Japan*, “and for the lower-level employees their contribution must be more than just manual labor. We insist that all of our employees contribute their minds.”

Not all ideas that people come up with will be useful. Many will be redundant, self-serving, and absolutely useless. But not to have an organized method for harvesting ideas tantamounts to erecting a billboard at the entrance to your company announcing, “If we had wanted your ideas, we would have asked for them.”

Principle No. 4 - A company must work constantly on improving its climate for innovation

Culture is generally used to describe a company’s values, traditions, priorities, and paradigms. A company’s culture may be centered on spreading its service ethic, “going the extra mile for the customer,” or its fierce commitment to quality, or engendering loyalty to “the company way,” while its climate may stifle innovation by fostering too much loyalty and an unwillingness to make a mistake or take a risk.

There are at least three possible responses to a “failure.” You can: a) cover up the failure and refuse to acknowledge it. You can, b) acknowledge the failure, assign blame, or c) you can acknowledge the failure, make every effort to learn from it, and share the learning broadly. Innovative companies are

above all, learning organizations. They realize that the degree of learning is directly related to the degree of open acknowledgement of the failed effort, and what happens to those associated with the "failure" says everything about who ventures forth in the future.

Whilst there is no sure fire route to commercial success, these processes improve the probability that good ideas will be generated and selected and that investment in developing and commercializing those ideas will not be wasted."

CREATIVE DESTRUCTION

However, successful innovation is normally a source of temporary market power, eroding the profits and position of old firms, yet ultimately succumbing to the pressure of new inventions commercialized by competing entrants.

This is very similar to the trinity of Brahma- Vishnu – Mahesh. The creation, the preservation and the destruction. It is the very order of nature. The creation is driven by ardour and enthusiasm, the preservation provides the continuum to the creation while the destruction is to be viewed dispassionately. The destruction here is the creative destruction. Economist Joseph Schumpeter popularized and used the term to describe the process of transformation that accompanies radical innovation.

Companies that once revolutionized and dominated new industries – for example, Xerox in copiers or Polaroid in instant photography – have seen their profits fall and their dominance vanish as rivals launched improved designs or cut manufacturing costs. The cassette tape replaced the 8-track, and was replaced in turn by the compact disc, itself being undercut by MP3 players. This is the process of creative destruction.

Is creative destruction the death knell of old order ?

Sustainable success in development relies on the ability of individuals to adapt solutions to their own unique needs, whether in parallel with others or by building upon what's been proven to work elsewhere. They only need to know their options, and the key to enabling the exponential growth of their opportunities are the networks of development, of innovation and of knowledge available to them. In the end, the best paths to a better future run alongside the networks of individuals that create them. It is, after all, all about their own ability to improve their own lives.

An example of this is the humble time piece, the watch has seen so much innovation since its invention. Before the inexpensive miniaturization that became possible in the 20th century, most watches were pocket watches, which had covers and were carried in a pocket and attached to a watch chain or watch fob. This gave way to wrist watches which can be worn around the wrist, the technology was the same i.e. winding. Further innovation saw the use of quartz and the need to wind the watch was obliterated, now the basic use of a wrist watch i.e. to show time is just incidental. It is more of an accessory, a fashion statement since there are other gadgets like the mobile phone which not just shows time but organizes the schedule of the user. Here the wheel was not re-invented it just found a new use.

Creativity is unbridled and free spirited; one requires to harness the creativity leading to innovations. To restrain creativity is to kill it, however certain situations require that creativity is to be restrained to have a certain amount of semblance in the civil society. This is to be achieved not by a hammer and tong approach. Creativity is like a wild and raging forest fire and how is a forest fire contained? Either the forces of nature quell the fire or trees on the other side is deliberately burnt down, so that the forest fire has nothing to feed on and it dies down. This is a creative solution. In business situations also unchecked practices are restrained either by the forces of the market or the creative and innovative ideas of the regulators.

THE CHANGING ROLE OF REGULATORS IN FOSTERING INNOVATION

Regulators and legislators tend to think in bulk- if ten rules are good, 20 rules must be twice as good, and 40 rules even better, and.....

Which is why we get hundreds of poorly enforced regulations

Posted by : Save-the rustbelt at Sep 14, 2008

As mentioned in preceding paragraphs, in this globalised and highly competitive business environment innovation has become the mantra for success. The Governments the world over recognize that decades of economic growth has been the result of innovations brought about by companies in technological, financial and other systems. It is widely acknowledged that companies have become the centre of or even the driving force behind the emergence and growth of modern global economy. Therefore, to ensure that companies continue to play their role as an engine for economic growth, there is an international drive to review, reconstruct and reorganise the laws governing companies so to ensure that corporate activities function within a modern, and forward looking regulatory framework that supports and sustains the economic growth. And regulators across the world are shifting from their traditional role and reconsidering their regulatory framework and approaches. They are constantly innovating and bringing out forward looking and progressive legislation, by adopting a flexible approach towards changing business environment and ethos. Additionally, the reforms are aimed at cutting back on overly regulatory intervention thus providing companies with operating flexibility to function in conformity with changing environment.

Role of regulators goes beyond governance. Realising this regulators across globe are moving towards corporate stewardship to support innovation driven growth and address key global competitive challenges. Strategic innovative partnerships among Government, private sector leaders, Academia and Labour are emerging to enhance competitiveness.

The need to achieve high standards of international prudential regulation and transparency have also become critical objectives for various regulators of the world.

Despite the current financial crisis which has exposed major flaws in the system, some of the world's brightest economic minds - Nobel Laureates, disagree about the role of the regulators should play in preventing a repeat. At an Annual Gathering of Economic Laureates in Germany, recently, three winners of the Nobel Prize in economics and one peace prize winner lamented the excessive risk-taking, lax management and impenetrable complexity at the heart of the financial system's current turmoil.

'A rush to regulation could have dire consequences', warned laureate **Myron Scholes**, who received a Nobel Prize in 1997 for a method of valuing derivatives. Scholes, who also co-founded **Long-Term Capital Management**, a hedge fund that collapsed amid the East Asian and Russian financial crises of the late 1990s, said, "sometimes, the cost of regulation might be far greater than its benefits." One example, he quoted was the **Sarbanes-Oxley accounting rules** implemented after Enron's collapse earlier this decade. The rules have been criticized for undercutting the U.S.'s attractiveness as a base for investment.

Joseph Stiglitz, a professor of economics at Columbia University who won the Nobel in 2001, suggested that the misguided innovation itself caused the current turmoil.

To prevent a repeat of the turmoil, a idea that emerged at the gathering was setting up of a Commission that would vet financial products before their release, akin to the **Food and Drug Administration's** evaluation of drugs before they are released to the market. **Daniel McFadden**, who won the Nobel memorial economics prize in 2000 for research focused on modeling individual's decision making processes, suggested, "we may need a financial-instrument administration that tests the robustness of financial instruments and approves only the ones which can do no harm."

The rationale for regulation as well as regulatory approaches are typically influenced by the level of competition and maturity of markets.

In order to achieve policy objectives, regulators around the world increasingly recognize the importance of developing the necessary instruments and regulatory tools to deal with the complexities of competition issues and facilitate the development of effective competition in relevant markets. Regulators and policy makers also recognize that increasing competition in a market can change the nature of regulation and the role of regulators. The greater the level of competition, more the market forces can be relied on to achieve certain policy goals.

Role of Regulators in Changing Financial Markets

Let us have a quick review on the basic objective in the formation of financial market's regulatory agencies which primarily include, investors' protection, maintaining fair, orderly, and efficient markets, and facilitating capital formation.

But while globalization is moving apace and technological advancements are making it easier to engage in cross-border trading, there are many hurdles to achieving a truly global marketplace. Some of these hurdles are a result of securities market regulation that is national in nature. In a globalized, fully electronic trading world, maintaining national standards presents challenges. It can impose duplicative costs and regulatory compliance burdens that, in some cases, do not necessarily offer meaningful additional protection to investors. This regulatory friction and overlap can be a real impediment to cross-border trading, standing in the way of investors realizing the benefits that true cross-border access can offer.

Further, in case of developing financial markets, regulatory or enforcement agencies remain more vigilant as with experience they learn from their counterparts in the developed or matured markets. This cautious approach sometimes attracts criticism from MNCs and big international financial houses or FIIs as an interference and an obstacle towards liberalization in the free markets. The argument here lies, 'Let the markets find their own course'.

Peter Mandelson, the European Union trade commissioner, has called for a far-reaching reform of global financial and regulatory systems to reflect the vital role of emerging economies in restoring the world's economy to health in the wake of the credit crunch.

His comments, at a World Economic Forum conference on "new champions", have found an echo among all political leaders, bankers and regulators across the globe, who are demanding stricter international rules on regulation of financial institutions. Further, 'prudential supervision,' is being stressed upon. The role of rating agencies is also being questioned by many investors, which is an area where regulators role needs to be looked into.

Mandelson argued "an international system in which not just the G7 or G8 and OECD will be reaching out and inviting so-called emerging economies in for a cup of tea every now and again or a coffee to hear their views and then politely ask them to leave as we take the decisions". Insisting that the global capital market system is not "fundamentally flawed", he said: "We are now looking to the larger, faster-growing economies to take up the slack. We need them to be the source of liquidity, of demand, of investment, of confidence in the global economy."

Changing Approach of Regulators on Outsourcing

As more financial services companies look to outsource core parts of their operations to external suppliers, managing adherence to compliance is paramount, says Peter Fawcett.

There is a common misconception that outsourcing certain functions will result in a substantial reduction and transfer of risk from the client to the service provider. This view is a direct result of the

faith and reliance that tends to be placed on detailed contracts, work orders, Service Level Agreements and the general due diligence and care spent on deciding which service provider to engage with. Often, executives are blinded by the benefits of such an arrangement and hence pay less attention to ultimate risk exposure and risk management.

Control over outsourcing is now high on the agenda of regulators and they are forcing the issue by cracking down on outsourcing arrangements driven by a number of powerful trends.

Firstly, outsourcers are taking on more of the core of firm's operations. Secondly, the number of data and control risk failures appears to be increasing as technology advances and firms handle increasingly sensitive data. For example, memory sticks can now hold vast amounts of sensitive data, yet can easily be lost or stolen.

In UK the Financial Services Authority (FSA) is clear that the ultimate responsibility for a control failure remains with the client and not the outsourcer. Yet what is surprising is that many arrangements do not have the control processes in place to prevent failures such as data leakage. The FSA has been handing out fines to outsourcing service providers who are failing to adhere to IT security regulations. For instance, Liberata was slashed with a £525,000 fine in April for failing to cope with the number of messages generated by its computer system. This error resulted in life and pension policy holders losing £17,584 in their investments.

In December 2007 *the FSA fined Norwich Union Life* £1.26m for various shortcomings in information security and fraud prevention. This penalty broke the record fine imposed by the FSA on the Nationwide Building Society in February 2007 for information security breaches following theft of a laptop containing confidential information.

For the penalised firms, it's not just about fines. It's the damage to their reputation that has the greatest impact. These high impact incidents seriously harm the reputation of the core firm, even when the root cause occurred within an associate, subsidiary, third party or outsource service provider.

Many firms subject to the US *Sarbanes-Oxley* regulations place comfort on the SAS70 audit provided to them by their service provider. However, it is not necessarily the case that having a SAS70 means a firm should sleep easy, as having such a report does not necessarily imply that your risks are mitigated.

The role of regulators is increasing for those firms failing to check the IT controls of their outsourcers. They are making it clear that client firms are not only ultimately responsible for the services delivered by their outsourcer, but are also responsible for ensuring on an ongoing basis that they have the right people, processes and controls in place to provide effective management and monitoring of the supplier.

However, there are a number of ways in which firms can work with their suppliers to gain control over their risks. From the beginning they should work closely together to ensure they are able to meet all regulations and that their risk exposure is managed. This is vital for those firms in the financial sector who are considering or have outsourced or offshored business or IT processes that are core to their operations.

Principles – Based Regulation

The global echo today is the need for principles based regulation - An approach to regulation which is focused principally on getting the right outcomes, both for firms and for consumers. From firms a stronger focus is expected on the outcomes that really matter - better outcomes for consumers, investors and markets.

Global markets are constantly changing. It is, therefore, essential that regulation keeps pace with this. Continuous innovation and new product developments are important ways in which the industry

generates benefits for markets and consumers. At the most basic level it is neither practicable nor desirable for regulation to seek to respond to each market development. However, regulatory approach that focuses on outcomes rather than prescriptive rules is more likely to encourage and respond to market innovation and development. Thus a principles-based approach is more durable in the longer-term.

Commissioner McCreevy's 6 principles of Regulatory Convergence in a global world

In New York Commissioner McCreevy set out Six Principles for Building a Transatlantic Market. In shortened form, these were:

- Do no harm: regulators should attempt to stay out of the line of play as much as possible: to observe closely, to step in when needed, but only to do so when absolutely necessary.
- Act in a co-ordinated multilateral manner, rather than try to build the foundations of the new order on a 'thicket of bilateral agreements'.
- Remove regulatory duplication as far as possible. If another regulator offers an equivalent standard of regulation and equivalent enforcement, have the courage to rely on them.
- Equivalence recognition should be based on global understandings and global standards.
- Transatlantic markets should serve as the laboratory of globalisation.
- Underneath these principles, there needs to be consistent implementation, information sharing and enforcement at a technical level between individual jurisdictions.

These are the principles on which one needs to move forward in the international borders/ discussions.

NEED OF THE HOUR

- Building Innovation Partnerships : To build effective Partnerships between Government, Industry, Academia, and Labour to enhance competitiveness.
- Building a co-ordination between Regulatory activity and Competition policy, which can ensure that basic regulatory principles are implemented across different sectors of the economy in a uniform way.
- Nations to work together to build a greater global consensus on how all Nations can benefit from the opportunities arising in the fast growing International Business/Service Industries.
- Setting-up of International Standards and accessing how International Organisations can facilitate the process of Globalisation.
- The need to achieve high standards of international prudential regulation and transparency and accountability by various Countries of the World.
- Moving beyond governance and making co-ordinated efforts by adding insights into regional and global trends.

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FINANCIAL INNOVATION — A CRITICAL ELEMENT OF ECONOMIC LANDSCAPE

CS. SONIA BAIJAL*

INTRODUCTION

Financial innovation, like innovation in businesses and elsewhere, is an ongoing process, responding to both immediate and gradual changes in the economy. The financial innovation has been a critical part of the economic landscape over the past few centuries. The literature on financial innovation from a wide variety of disciplines, finance, economics, history, law, and industrial organization shows that the sophistication of financial innovation increases, with the growth of volumes. As the financial markets have continued to produce a multitude of new products, including various new forms of derivatives, alternative risk transfer products, exchange traded funds, and variants of equity, there have been instances to show that innovation flourished, failures took place, and public and regulatory sentiment led to temporary anti-innovation feelings, similar to those being experienced now. Yet the financial innovation continues, the latest on the list being Green Finance and Carbon Credits Trading.

GREEN FINANCE – A NEW FINANCIAL INNOVATION

With global financial markets in deceleratory mode, “green financing” is emerging as a key driver to stimulate sustainable global economy. Record-high oil prices, inflation and demand from international community and the governments to deal with dangers of global warming are attracting huge investments in innovative projects. Financial institutions, venture capitalists, investors and traditional non-green businesses are pouring money into clean, renewable-energy technologies.

The year 2007 was a great one for green IPOs and stock offerings as clean-energy companies raised \$27 billion on the world’s public markets, more than double the preceding year. The highlight was \$7.2 billion offering for Iberdrola Renovables, a wind-energy spin-off from Spanish power giant Iberdrola. It was the second-largest IPO of 2007 and the biggest Spanish IPO ever.

John Challenger, CEO of Challenger, Gray & Christmas, a global outplacement and research firm, says that “Companies researching and developing alternative sources of energy, which once found it difficult to secure funding, are now the favorites of venture capitalists.” Developers of wind, solar, biofuel, biomass and waste, energy-efficient technologies and other emerging energy options are securing funding where it was once hard to find.

According to London-based energy research firm New Energy Finance, total global investment in clean-energy technologies jumped 60% in 2007 to \$148.4 billion. Wind-power technology attracted 43% of new investment, solar 24%, biofuels 17%, and biomass and waste 9%, with the other 7% divided among other renewable fuels, low-carbon technologies and energy efficiency.

A report produced by New Energy Finance on behalf of the United Nations Environment Programme, expects a slight increase in total clean-energy investments amid challenging capital markets. However,

* Assistant Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

“investment levels are on track to reach \$450 billion a year by 2012 and \$600 billion a year in 2020”. Global venture capital and private equity investments in clean-energy technology rose sharply to \$4.7 billion in the second quarter of 2008, from \$2.5 billion in the first quarter of 2008 and \$3.5 billion in the second quarter of 2007.

A report from Cleantech Group San Francisco-based market-research firm focusing on venture capital in North America, Europe, China and India alone shows that venture investors poured a record \$2 billion into clean-technology companies (“cleantech”) in this year’s second quarter. That’s up 58% over the year-ago period and 48% higher than the first quarter. In this context, John Balbach, managing partner of Cleantech Group says that “Interest in cleantech continues to show robust growth, despite the impact of economic headwinds and continued credit market constraints”, “The combination of a strengthening pipeline of promising new innovations, steady progress in scaling growth-stage companies and improving demand-side pull are leaning toward 2008 outperforming the banner 2007 record performance.”

CARBON CREDITS TRADING

The concept of carbon credits came into existence as a result of increasing awareness of the need for pollution control. It was formalized in the Kyoto Protocol (1997 World Earth Summit – United Nations Framework Convention on Climate Change), an international agreement between 169 countries. Carbon credits are certificates awarded to countries that are successful in reducing emissions of greenhouse gases.

For trading purposes, one credit is considered equivalent to one tonne of CO₂ emissions. Such a credit can be sold in the international market at the prevailing market price. There are three exchanges for carbon credits: the Chicago Climate Exchange, the European Climate Exchange and MCX (Multi-Commodity Exchange of India) with a license to trade in carbon credits.

The Kyoto Protocol provides for three mechanisms that enable developed countries with quantified emission limitation and reduction commitments to acquire greenhouse gas reduction credits. These mechanisms are Joint Implementation (JI), Clean Development Mechanism (CDM) and International Emission Trading (IET).

Under JI, a developed country with relatively high costs of domestic greenhouse reduction would set up a project in another developed country that has a relatively low cost. Under CDM, a developed country can take up a greenhouse gas reduction project activity in a developing country where the cost of greenhouse gas reduction project activities is usually much lower. The developed country would be given credits for meeting its emission reduction targets, while the developing country would receive the capital and clean technology to implement the project. Under IET, countries can trade in the international carbon credit market. Countries with surplus credits can sell them to countries with quantified emission limitation and reduction commitments under the Kyoto Protocol.

How buying carbon credits attempts to reduce emissions

Carbon credits create a market for reducing greenhouse emissions by giving a monetary value to the cost of polluting the air. This means that carbon becomes a cost of business and is seen like other inputs such as raw materials or labour.

By way of example, assume a factory produces 1,00,000 tonnes of greenhouse emissions in a year. The government then enacts a law that limits the maximum emissions a business can have. So the factory is given a quota of say 80,000 tonnes. The factory either reduces its emissions to 80,000 tonnes or is required to purchase carbon credits to offset the excess.

A business would buy the carbon credits on an open market from organisations that have been approved as being able to sell legitimate carbon credits. One seller might be a company that will plant so many trees for every carbon credit you buy from them. So, for this factory it might pollute a tonne, but is essentially now paying another group to go out and plant trees which will, say, draw a tonne of carbon dioxide from the atmosphere.

As emission levels are predicted to keep rising over time, it is envisioned that the number of companies buying more credits will increase, pushing the market price up and encouraging more groups to undertake environment friendly activities that create for them carbon credits to sell. Another model is that companies that use below their quota can sell their excess as 'carbon credits.' The possibilities are endless hence making it an open market.

Carbon Credits Trading in India

Companies such as ITC, Tata Steel, ACC, Birla Corp, RIL, JK Cement, etc. are minting millions of dollars each year through Carbon credits trading. ITC has endeavoured to reduce CO₂ emissions both within its operations as well as on sequestration basis i.e. through extensive afforestation projects. ITC's hotel ITC Sonar Bangla, Kolkata became the first hotel in the world to get and sell carbon credits by using energy conservation projects.

A Kerala-based NGO, Anthyodaya, has become the first Indian entity to become a member of Chicago Climate Exchange (CCX). Anthyodaya's project involves 2000 rural households that use biogas for cooking. The methane captured and burnt would earn the NGO allowances which it can sell through CCX to entities in the US. The rate at which allowances are sold is fixed by CCX at \$4 per allowance.

At present, Anthyodaya has around 16,000 biogas plant owners signed in for the carbon credit programme. On an average, each of them get around Rs. 1,000 annually.

Having discussed the new financial innovations, the following paragraphs elaborate the concept, classification and technology driven financial innovations besides, the processes of introduction of new financial innovations in the market.

CONCEPT OF FINANCIAL INNOVATION

The theoretical and empirical work in financial economics considers a highly stylized world in which there are few types of securities (debt and equity), and perhaps a handful of simple financial institutions (banks or exchanges). However, in reality there is a range of financial products, types of financial institutions and a variety of processes that these institutions employ to do business.

Webster's Collegiate Dictionary defines "*innovative*" as "to introduce as or as if new". The Concise Oxford dictionary defines "*innovate*" as "to bring in new methods, ideas etc." The word has its origin from the Latin word "novus" or new. Broadly speaking, financial innovation is the act of creating and popularizing new financial instruments as well as new financial technologies, institutions and markets. The "innovations" are sometimes divided into product or process innovation; product innovations may be exemplified by new derivative contracts, new corporate securities or new forms of pooled investment products, and process improvements can be exemplified by new means of distributing securities, processing transactions, or pricing transactions. In terms of financial innovations, securities innovations include wide range of instruments such as debt, preferred stock, convertible securities, and common equities. They serve the purpose of reallocating risk, increasing liquidity, reducing agency costs, transactions costs, taxes and sometimes circumventing regulatory constraints.

Briefly, the financial innovations help in moving funds across time and space; pooling of funds; managing or reallocating risk; extracting information to support decision-making; addressing asymmetric information problems; facilitating the sale or purchase of goods and services through a payment system; reducing agency cost, and enhancing liquidity.

INNOVATIONS IN FINANCIAL PRODUCTS

The worldwide financial industry is full of innovation in product design. New financial products become popular because people find them useful. A look at stream of new products like index funds, index futures, index options, etc., shows that these products become internationally successful because they fulfill basic economic objectives of people in the economy.

The economist Robert C. Merton has coined an evocative phrase "the spiral of innovation" to describe the dynamics of this process: "As products such as futures, options, swaps and securitised loans become standardised and move from intermediaries to markets, the proliferation of new trading markets in those instruments makes feasible the creation of new custom-designed financial products that improve "market completeness"; to hedge their exposures on those products, their producers, financial intermediaries, trade in these new markets and volume expands; increased volume reduces the marginal transaction costs and thereby makes possible further implementation of more new products and trading strategies by intermediaries, which in turn leads to still more volume. Success of these trading markets and custom products encourages investment in creating additional markets and products, and so on it goes, spiraling towards the theoretically limiting case of zero marginal transaction costs and dynamically-complete markets."

In India these linkages can be illustrated in the relationship between the underlying spot market, index funds, index futures and index options:

- The prerequisites for an index fund are (a) program trading facilities and (b) an index where all components are liquid and convenient to trade. Index funds fulfilling these conditions have now come to exist in India.
- Index funds make it possible for people to sell options on the index while being covered this could happen on exchanges which trade index options or over the counter.
- Index futures make the implementation of index funds easier.
- Index funds generate an order flow for index futures markets, and help make them more liquid.
- Index futures markets enable index options markets.
- Access to index futures and index options makes index funds more attractive, since users can couple their investments in index funds with risk management using the futures and options.
- Index options make possible innovative new products like 'guaranteed return funds'.

Starting from simple pre-deducted interest loans, hundies and gold receipts, the 20th century witnessed major developments in the financial products. The new instruments changed the age-old belief that capital is not mobile, thus shaking the very edifice of classical theories. Needless to say, innovations in financial products were hastened by rapid developments in accounting and the emergence of newer techniques alongside.

Technology Driven Financial Innovations

Information Technology and improvements in telecommunications have facilitated a number of innovations, including new methods of underwriting securities, assembling portfolios of stocks, new markets for securities and new means of executing security transactions. New intellectual technologies, such as derivative pricing models, are credited with stimulating the growth and popularization of a variety of new contracts. Many new forms of derivatives were made possible because business people could have some confidence in the methods of pricing and hedging the risks of these new contracts. Various forms of innovations such as new risk management systems and measures, on-line retirement

planning services and new valuation techniques were clearly facilitated by both intellectual and information technology innovations.

CLASSIFICATION OF FINANCIAL PRODUCTS

The broad classification of the Financial Products include the following :

Payment products include retail, corporate and trade-related products, and financial/securities products.

Trade finance includes bills of exchange, collection bills, letters of credit, factoring, forfeiting, performance/bank guarantee, and export and import bills.

Commercial lending comprises overdrafts, cash-credits, open loans, goods loans, hypothecation of stock-in-trade facilities, medium-term loans, syndicated loans, financial guarantees, acceptance instruments, etc.

Structured finance includes commercial and real-estate finance, project and start-up finance or equity loans, buy-outs of management or leveraged buy-outs, subordinated debts, etc.

Equipment finance consists of project loans or long-term acceptance bills, leasing and hire purchases. It could be financial or operational or a combination of both and sellers-participated loans. There could be even long-term quarterly/half-yearly equated bills acceptance arrangement.

Money market products include certificate of deposits, commercial paper, treasury receipts/bills and repurchase agreements and also, money market mutual fund units.

Capital market products include bonds and debentures, government bonds/gilt-edged securities, equities of all types, including preference and ordinary.

Derivative products, Risk Management projects include foreign exchange forward covers, rate agreements, financial futures swap and options. They are also known as risk-management products, as they cover the risk in exchange markets.

Consumer products are personal loans, housing loans, white goods, car loans, hire-purchase and lease arrangements, and mutual and pension-related funds. Credit/debit cards and other types of cards (known as plastic money) also fall under this category.

Indigenous products include both local and ethnic financial products such as chit funds and benefit funds. They offer credit off-takes through local and indigenous arrangements.

Postal products in the Indian context include National Saving schemes, where one can have both loan and withdrawal facility and also enjoy tax benefits.

Development of New Instrument - Experimentation Process

Typically, when a new product is being developed, there is an initial experimentation phase in which market participants learn about the product's performance and risk characteristics. This involves gathering and processing information and modeling the performance of the product in various scenarios and under different market conditions. Subsequently, market participants take time to understand as to what, exactly, they need to know to value a product. The investment in gathering, processing, and evaluating information often leads to greater standardization of products and contract terms, which in turn enhances the liquidity of products as the markets mature.

In the initial experimentation phase, the terms and characteristics of a new product are adjusted in response to market acceptance. During this period, market participants seek and provide information so that they can properly value the product, judge its potential for risk and return, assess its market

acceptance and liquidity, and determine the extent to which the risks of the product can be hedged or mitigated.

CONCLUSION

Preceding discussion makes it clear that financial innovation is a continuous process and will continue as in the past, despite failures and negative public sentiments about financial innovation. This may be exemplified by the fact that on the one hand the sub prime crises has engulfed the world market to drive towards deceleratory trend, on the other hand new financial innovations such as Green Finance and Carbon Credit Trading are becoming popular. What is more important is to learn lesson from the past. Recent market events have underscored the need for better market information about new products, due diligence to verify information, and risk-management strategies to utilize the information in decision making.

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INNOVATE TO FOSTER EXCELLENCE

ARCHANA KAUL*

"Genius is seeing what everyone else sees and thinking what no-one else has thought."

Albert Szent-Gyorgy

INTRODUCTION

There has been a sea change in the economic, political and technological environment the world over. Age old attitudes and mindsets are being discarded everywhere. India has been no exception; its economy has been unshackled and the forces of competition have been unleashed. A new vision of India as a major player in the global setting has been articulated. The wave of change sweeping the country and the world has thrown up myriad opportunities and challenges. To encounter such challenges effectively, we have to be more adaptive, flexible and responsive to global realities.

While a glorious future certainly beckons us, our ability to actually realize its promising potential, depends entirely on the efficacy with which we are able to overcome the external and internal challenges that we face today. Globalization is a phenomenon that we cannot wish away and its politico-economic impact on our business needs to be clearly understood.

Corporate throughout the world have had to cope with responsibilities and expectations which have been changing with the increasing speed. Change is not just about the creation of new policies and procedures to implement external mandates. It is also about the development of personal strategies by individuals to respond to, and seek to influence the impact of structural and cultural change, personal change as much as organizational change.

Offering just superior services and products does not suffice to become a strong player in the present competition-based market. Real difference comes out when adapting to the dynamics of change, and becoming a part of change becomes the approach adopted by all of us. This dynamics is only activated when fed by innovative thinking and when each one of us revitalize our innovative thinking, expose it, put on strong foundations and transform it into a state where it could be translated into action plans. The major challenge for corporate leaders in the global competitive environment is to address continuing challenges of change and organizational adaptation, and those professionals with the skills to steer change effectively are in high demand.

WHY INNOVATION

Today, we see a new era that has been created by the revolutionary advances that have been made in the use of technologies in the fields of science, communication, transport, and 'Information Systems'. It is technology that has radiated visions of possibilities, generated new hopes and given rise to new

* Assistant Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

business risks and temptations. One cannot be allergic to radical reflection, and the radical revision of confrontational attitudes and mindsets.

The image of an organization among customers, general public and in its own industrial and commercial fields gets very much elevated through product development, process development, or value addition thereof through new creation, new innovation and new application.

Creativity and innovation are important keys to success in today's rapidly changing global marketplace. Process improvement, problem solving, recruiting, retaining and motivating employees, decision making, dealing with limited resources, satisfying customers, and rapidly changing technology are all examples of business realities that require creative solutions. In fact creativity and innovation are the important factors that compel businesses to become increasingly innovative to gain a competitive edge. Companies are now focusing on innovation to insure continuous harvests. Innovation becomes one of the critical factors for ongoing growth. It may be pointed out that a recent survey of top executives from Fortune 500 companies throughout the United States ranked creativity more important than intelligence for success in business today.

WHAT INNOVATION MEANS

What does innovation mean? Generally we say 'successful exploitation of new ideas'. If we look at the meaning of the word "innovate" in any dictionary we will find something like this: To innovate is "to introduce something new." It does not say you need to be a creative genius.

In the simplest form, it means coming up with new ideas and putting them to work in our businesses and industries. Making a product or offering a service that no one had thought of before.

INNOVATION - A BUSINESS SURVIVAL TOOL

The increasing interconnectedness of complex international challenges and our increasing reliance on each other around the globe, has placed international development high on the agenda of innovation and change. Recent studies point to the increasing recognition by CEOs that innovation will be a key strategic imperative for long-term growth and survival.

We all know that human mind is an energy field with unlimited capacity and intelligence. It has a creative capacity to solve any problem and bring forward new forms and fancies. Research has shown that regardless of age or education, everyone has the capacity to become more creative. Yet, innovative thinkers are often tough to find today.

Innovation is everybody's business. We as professionals need to realise our potential as a creative human being. We ignore our creativity because we are too focused on our existing work that is right in front of us. Most of the professionals are too busy with so much of work load than they have hours in the day. With so much deadline-driven stuff to do, they have no time to be creative. However we fail to realise that beyond the narrow vision of our existing work is a world rich with creative possibilities. It contains ideas that could revolutionize our work, career and even our personal life, if we would only find time to seek them out and explore them.

The demand for professionals who will be driving the destinies of the organisations with innovative capabilities is on the rise. In the changing global environment, organizations need ideas and it is the professionals with creative and innovative capabilities who can propel such organisations forward in a competitive marketplace. Therefore, learning to think creatively is the best business survival tool for professionals like Company Secretaries. We as professionals must learn how to develop an innovative approach, enhance our creativity and stimulate creativity with our co-professionals at the work place. It is to be realized that just as the market is expanding for the products, so it is opening up new opportunities for the professionals who are skilled as well as innovative in their approach.

There are countless examples where creative thinking of the persons has helped the organizations not only to gain a competitive edge but also achieve a good market reputation. Take the case of Henry Ford. He was not just an inventor. He was a visionary. Unlike other car makers of his time, he saw the future of his company lay in producing affordable cars for a mass market. He also had rather radical beliefs on how to run a company. Ford's legacy of creative thinking still guides the organization.

INNOVATION AND COMPETITION

Technical progress is the key driver of growth and development. Growth accounting exercises that seek to separate the contribution of input expansion and productivity increase have shown that the latter accounts for a substantial part of output increases, both at the micro and the macro level. Hence public policies to promote research, innovation and access to technology are at least as important as human resource and capital market development for promoting growth.

The present economic scenario is governed by the philosophy of competition. In a regime of competition, this means that every nation has to acquire and retain sufficient competitiveness to be able to survive and prosper in world markets. As we look forward, we can foresee business opportunities expanding as never before. The Indian economy is growing at a very rapid pace. Disposable income in the hands of consumers has more than kept pace. The result is that our domestic market has been expanding at a pace that occasionally surprises even the optimist. An expanding market inevitably attracts increasing competition. Today, every product category sees new entrants in our business. Competition may be from existing companies entering new categories or from new companies. Enhanced competition and proliferation of imported brands on our Indian retail shelves is a reality that we will have to embrace. Innovative technologies, creative ideas and new products that emerge on the global horizon are swiftly making a beeline for the Indian market. It has, therefore, become a national necessity to acquire competitiveness.

For mature economies like the UK innovation is regarded as the major source of competitive advantage. China is not content to serve as factory to the globe. Call it economic foresight, or cultural pride, but despite the stratospheric growth of its economy – 10.7% last year – China knows that cheap labour alone cannot sustain the boom. While a flurry of activity has stressed scientific and technological innovation, look a little closer and you will see that creativity in art and industry – in design, fashion, media, and the like – is fast becoming a driving national mission.

With the opening up of economy, in the current global scenario, one needs to integrate one's operations in the context of the emerging global market. In the overall global corporate and economic scenario, whether a profession is big or small, old or new, its well-being depends on its ability to adapt. Corporates throughout the world have had to cope with responsibilities and expectations which have been changing with the increasing speed. The major challenge for corporate leaders in the global competitive environment is to address continuing challenges of change and organizational adaptation, and those professionals with the skills to steer change effectively are in high demand.

DRIVERS BEHIND INNOVATION

Two major drivers behind innovation are creativity and existing ideas. Creativity involves risk and the acceptance of failure while ideas are usually a function of watching and learning from others, finding ways of how you can apply and fit the best ideas of others into your business.

The great innovators did not take the traditional view to develop existing ideas. They took an entirely different view and transformed society. Picasso took a different view of painting; Einstein imagined a new approach to physics; Darwin conceived a different view of creation. Each of them looked at the world in a new way.

Another powerful driver behind innovation is comparing what you are doing against others. Study the ideas of your competitor's, other companies, monitor business innovation on a large scale and see how you can adapt it to your organization. The best ideas that fuel innovation usually come from existing ideas. This is how the Japanese captured market share in the United States. In today's fast changing business scenario. So institutionalization of creativity awareness and extending its advantages to sustainable business strategies, and landscaping of creativity must be an agenda for corporate growth to be built into appropriate policies, goal congruence and vision development. Corporate creativity is a very complex process and depends to a large extent on the inter play of three inter-dependent variables—organizational characteristics, group characteristics and individual characteristics. How the organization behaves, its attitude and encouragement, its perceptions and values towards creativity determine the organizational characteristics. Group characteristics are determined by the collective behaviour of the people included in the group. Individual characteristics are the functions of several variables, which influence the thinking process, attitude towards work and integrity. Corporate creativity is the outcome of the totality of these three factors that operate within a company but do not follow any rigid formulae.

A tension free relaxed frame of body and mind is the first prerequisite to enable a person to think logically, behave rationally and decide correctly the way a problem is to be solved or a new idea to be developed. Common sense also is very vital and if applied properly to analyse a problem with reference to the conditions and circumstances that have created the problem, some idea, not thought earlier, might click which could solve the problem. Intelligence is described as the mother of creativity but it is just not true that the more intelligent person is necessarily the more creative one. Age and sex rarely influence creativity. But curiosity, initiative and experience are the three basic qualities of a creative individual. They are creative job skills. Qualitative experience is more important than its quantitative part. These basic qualities influence a person to challenge the existing one and search for a new solution for its betterment.

Creativity does not expect us to pluck flowers out of the empty sky. Real creativity can be brought forth only on the background of the best in the tradition and the existential knowledge base. As members of a great professional body, we already carry the grain of quality, both in terms of knowledge, compliance ethos and corporate skills. Yet, we have to always look to competing for the future. The expectations of the regulators, the corporate world and of various stakeholders that carry the right to expect better and better from professionals are growing so fast that we have to constantly think and rethink in order to upgrade the quality of our services on a continuous basis.

HOW TO CREATE INNOVATION

Peter Drucker, the father of modern management once declared that the one core competency every organization must have is the ability to innovate. One of the reasons innovation is so critically important is because of change. With change, you are forced to innovate and you can elect to be reactive, forcing yourself to innovate (change what you are doing) or you can be pro-active, purposely seeking to innovate so as to control the changes forced upon you. As you might expect, the latter, the deliberate pursuit of innovation is the "value added" option.

So how do we create innovation? Start by fueling innovation through ideas. Ideas bring about innovation and ideas are fueled by creativity. Creativity emerges from people with varied skill sets, working together to spark innovation from one another. One ingredient behind creativity is having the right environment. People need to feel they can raise questions and take initiatives for innovation. The combination of competent people and the right environment is a powerful driver for creativity and innovation.

One common approach to innovation is through new product development. There's nothing wrong with redesign of products and services. However, you should not confine innovation to this single area. For example, innovation can take place by changing the customer mix, adjusting the business strategy,

rethinking how you apply your core competencies and managing complex differently. There are numerous areas where innovation can take place.

The timing of innovation can be important. The best time to pursue innovation is when you least need it! Since innovation is not easy to come by, it is best to pursue innovation when all is going well. You do not want to find yourself trying to force innovation during bad times or especially, during a crisis. You need time to test alternatives, run pilot programs, and discuss “lessons learned” before full-scale implementation of new ideas can be launched.

CREATING A CLIMATE FOR INNOVATION

Arthur B. Van Gundy in his book *Idea Power : Techniques and Resources to Unleash Creativity in Your Organization*, very succinctly outlines seven important factors for creating a climate for innovation:

1. *Risk Taking* – Any change requires some acceptance of risk.
2. *Autonomy* – Creative ideas are best generated when there is some degree of freedom of thought.
3. *Performance / Reward* – You must link rewards to specific performance.
4. *Tolerance of Differences* – An innovative climate recognizes that everyone is not alike and innovation works when everyone can express their ideas.
5. *Top Management Support* – Creating an innovative climate begins at the top, not at the bottom.
6. *Initiating and Encouraging Ideas* – Innovation requires a continuous flow of ideas – lifeblood of the organization.
7. *Positive Response* – Innovative ideas should receive strong positive response, not just passive encouragement.

STRATEGIES FOR INNOVATING IN THE CURRENT GLOBAL ECONOMIC DOWNTURN

Experts based on their experience as well as conversations with global customers and executives have given following suggestions that CEOs could implement to drive shareholder value in a recessionary economy:

Drive the innovation agenda : CEOs must be committed to setting and driving the innovation agenda as well as monitor success on an ongoing basis, especially during a slow economy. Admittedly, innovation is still a grassroots movement. Yet, successful innovation initiatives almost always start at the top. At companies such as Unilever, BP and Samsung, innovation initiatives start out as small projects and expand as teams begin to replicate that success across the enterprise. Rather than slashing R&D budgets in a recessionary economy, CEOs should encourage management and teams to deliver market-leading products.

Encourage new product development and enhance existing products : Companies need to continue investing in new product development as well as reengineer existing products for new markets. In the academic world, the saying is ‘publish or perish’. In the manufacturing world, it’s “create or perish.” While creating new products is critical to the bottom-line, so is reengineering existing products.

Invest in technology to drive repeatable innovation: The process of innovation should be sustainable not accidental, especially during a recession. Though the concept of sustainable innovation is emerging, best-in-class companies are 36 percent more likely to implement a predictable, repeatable innovation process, according to a recent Aberdeen Group report. Granted, innovation is an overused word and conjures up images of people sitting in a room, brainstorming on ‘hit or miss’ ideas. Innovation is about

generating breakthrough ideas or concepts that result in cutting-edge products. With the right technology, many companies have made innovation a repeatable process vs. that one time 'aha' moment. Companies do not have to reinvent the wheel, but rather they need to successfully leverage internal and external knowledge. Nestle, Pratt & Whitney Rocketdyne, and Schneider Electric are examples of companies that have invested in technology to help sustain the innovation process.

Track return on innovation closely : In a sluggish economy, CEOs have no room for error. They are pressed for funds and resources. Therefore investments in product innovation have to yield high returns. Innovation is about turning ideas and concepts into commercial, market leading products. CEOs have to be confident that ideas for product design and product development will yield results that meet customer demand, increase revenue growth and keep costs low. This means that almost every idea or concept has to become a reality, the first time.

CEOs can successfully navigate companies through a recession by encouraging product innovation, fostering generational transition and investing in technology that will translate ideas into commercial products, consistently thereby resulting in increased top-line growth and market capitalization, even in a recessionary economy.

CONCLUSION

In this race of growth and prosperity of the corporate world, human capital has been gradually recognized as the most powerful and valuable strategic weapon. Traditional factors of production of land, labour, capital and organization are being replaced by knowledge, which is considered to be the key to formation of intellectual capital. People have an inherent capability for improvement and progress. A company is as good as its people. Knowledge, creativity, innovation and ideas could make or break a company. These, intangible intellectual capitals are to be leveraged to improve performance and profitability to achieve sustainable growth and excellence. To achieve this, a company has to pursue a long-established strategy of innovation to encourage its people to think and come up with new products from the company's core competence. One should bear in mind that creativity not only helps in solving immediate problems but also provides requisite momentum to adapt innovative and imaginative behaviour as part of the work culture, and to develop a conducive environment in the organization.

During the 1970s and early 80s, companies focused on advertising and promotion to build brands. In the late 1980s and 90s, they focused on productivity savings to increase margin. Now, companies are forced to compete on a global scale, finding resources and insights worldwide to grow their businesses. It is complex and difficult, but the only long-term insurance policy is to maximize the company's roots — the potential of the people in an organization — by providing the leadership, the skills and an environment that supports innovation.

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DUE DILIGENCE : AN IP PERSPECTIVE

SURYA NARAYAN MISHRA*

INTRODUCTION

The integration of the corporate sector and the alignment of corporate ownership and structures are driven by the Merger and Acquisitions. There is lot of implications of mergers and acquisitions on the market for corporate control for value creation. Three main value drivers in mergers are : the existence of synergies between the target and the buyer, the importance of value investing and the key role of management involvement. Synergies through either one product market, the development of economies of scale, cost reduction or the elimination of duplicate activities are almost always mentioned as the justification for a merger.¹

The corporate objective is value maximization be it the acquirer or the seller. In integration process the target firms' intellectual property (IP) plays a pivotal role for future growth. A firm cannot maximize the value if it ignores the IP. There is a great correlation between Intellectual Property (IP) Protection and due diligence and value maximization.

INTELLECTUAL PROPERTY (IP) DUE DILIGENCE

Intellectual property is an important part of any business. In this competitive environment every business looks towards and requires innovation engine to generate novel ideas and materialise the same that will drive the business forward into the future. As the innovations are the key to success, so all innovations, which in turn create intellectual property (IP), must be managed properly.²

Intellectual property (IP) due diligence is a component of nearly every M&A and private equity transaction. When acquiring or investing, a buyer's primary interest in a target company is often the perceived value of its IP portfolio. Even when the buyer isn't initially targeting IP per se, the IP portfolio always forms a material part of the transaction, especially given that most authorities peg the value of intangible assets at anywhere from 25% to 80% of the average company's total valuation.

Because of the expense of patent litigation and the increasing activity of the IP market makers, the deal can hinge on high-quality IP due diligence. The goal is to accurately map out the territory that the target company has procured for itself in a volatile IP landscape, and identify the soundness of the assets being purchased and potential risk.

The increased profile, frequency, and value of intellectual property related transactions have elevated the need for all corporate professionals and IP owner to have thorough understanding of the assessment and the valuation of these assets, and their role in commercial transaction.

Intellectual Property due diligence generally provides vital information specific to future benefits, economic life and ownership rights and the limitations of the assets all of which affects final valuation.

* Assistant Director, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

Therefore due diligence is prerequisite to the valuation process, regardless of the methodology used. IP Due diligence is the process of investigating a party's ownership in the IP, right to use, and right to prohibit others from using the IP rights involved in sale or merger -the nature of transaction and the rights being acquired determines the extent and focus of the due diligence exercise.

The IP Due-diligence should reveal-

- Who owns the rights ?
- Are the rights valid and transferable and enforceable ?
- Are there any agreement or restriction that prevents the party for granting rights to other ?
- Is the property registered in the proper office ?
- Any shortcoming or default on payment ?
- Any past or potential litigation ?
- Has the property being misused in the past rendering right unenforceable ?
- Any encumbrances ?

It should also evaluate agreements material to the company's business that may be affected by change of control, agreements that may vest rights in intangibles, and company policies and practices.³

SCOPE OF IP DUE DILIGENCE

The scope of Intellectual property due diligence is determined by a number of factors such as party's aspiration in the transaction such as market share, product/service offered, capital contribution, assets transfer, security of loan, or internal assessment of its own. It is also influenced by budgeting, available human resources, the size and complexity of target company and its intellectual property portfolio among other such issues.

Buyer having done the preliminary due diligence with respect to current status of intellectual property portfolio, it should evaluate the portfolio with respect to following function strategy:

Ownership Strategy : The due diligence team must see the IP ownership right of the buyer and the seller. List out the possible integration of the both in terms of the primary product lines, business environment and future plans of the enterprise to remain focused on the IP assets that are relevant to the business. The identification and locating the intellectual property assets of the target company is the next critical step in predicting the future value of a business. Practically speaking, a checklist should be prepared to enumerate all IP assets associated with the business. This list may be incredibly varied depending on the nature of the business, but could include patents and/or patentable subject matter, copyrights, trademarks, domain names, trade secrets, inventions, works of authorship, hardware and devices. As part of this process, it is important to consider which stage of evolution the business is at.

Protection Strategy : After going through and listing out the ownership of various IP, the next step is to see how these are protected like the patent issued or in application stage, process patents are there or not or there is chance of infringe at the process. Whether or not Intellectual Property rights are protected under respective laws? It must be carefully list out that all the IP are properly protected.

Exploitation Strategy : Most importantly, the diligence team must verify exploitability of IP assets. This includes verifying the ownership of each IP right and their validity. For that it is extremely important to examine all agreements, registrations, filings and other documents to ensure that they are valid. A further aspect involves assessing any on-going litigation in that company and making a reasoned determination of how that litigation will affect the IP rights at issue. The due diligence should also

include evaluation of all potential claims of IP infringement including analysis of situations where the targets IP assets may infringe a third party's rights, and the target has a valid claim of infringement against a third party. Either circumstance has the potential to seriously disrupt the operation of the business.

Enforcement Strategy : Finally, it is necessary to analyze any grants of IP rights made by the target to third parties. This analysis would include licenses, distribution agreements, reseller arrangements and any other transaction by the target that involves a transfer of rights in the IP assets that may impact the value of those assets.

Every business transaction has its unique issues, whether due to the particular technology, the geographic market, the level of competition, or the litigious nature of the industry. The due diligence exercise must assess how the unique aspects may ultimately affect the resultant corporate structure and its place in the market. It is also important to examine how the encumbrance to the IP can be stop.

Disclosures in the IP due diligence process might provide the grounds to renegotiate the price or other key terms of the transaction. For example, the buyer might learn that the seller uses but has not registered a key trademark that the buyer intends to continue using after the acquisition. In such a situation, the buyer should evaluate whether it will be able to use the mark without infringing third party rights and perhaps demand suitable concession from the seller.

Target Company should make a preliminary assessment of the current status of its intellectual property portfolio and management including:

- (a) Current holding and their status,
- (b) Goals for the portfolio,
- (c) Historical and prospective investment in Intellectual Property (IP) and,
- (d) Acquisition, protection and exploitation of the IP.

In the IP due diligence process the most significant provisions of the agreement are: definitions of assets and IP; the scope of the transfer; and Representations and warranties. The representations and warranties, indemnification provisions should also be taken care of in the exercise. Disclosure schedules are also critical because typically the seller is not liable, unless the purchase agreement otherwise provides, for any monetary damages resulting from disclosed events.

DUE DILIGENCE FOR DIFFERENT IP ASSETS-CHECK LIST

The nature and extent of the due diligence exercise depends on the type of intellectual property rights involved. Generally, intellectual property rights can be broken down into four main categories: patents, trademarks, copyrights, trade secrets and domain name. Each class of intellectual property rights necessitates the use of different methods of review.⁴ However, before undertaking due diligence exercise, a confidential agreement must enter between the company and due diligence team.

Patents

- Review all issued, pending and abandoned patent applications and patents in the country and in foreign countries. Such review should include not only those patents owned by the target but also those previously owned or licensed by the target.
- Examine all patent searches conducted by or on behalf of the target in relation to the inventions of the target.
- Confirm that all issued patents are being properly maintained and that the target is current with all maintenance fees.

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- Review and evaluate all threatened or pending interferences.
 - Evaluate the scope and nature of any transfer of rights by evaluating all relevant agreements including licensing and manufacturing agreements.
 - Review all invention disclosures related to the business assets being transferred that are either awaiting disposition or are to be the basis of a patent application.
 - Review all technologies that are material to the business assets being transferred, together with a description of how each such technology was developed or acquired and copies of all documents evidencing any such acquisition.

Trademarks

In trademark due diligence the buyer company should have clear view as to why he is interested in the deal and its brand strategy after the completion. Then a due diligence plan should be crafted which includes identifying and verifying whether the trademarks and Internet domain names are owned by the target. The relative strength of the Trademark Rights has to be assessed vis-a-vis third party rights. Trademark rights would be weak due to the number of third parties using the same mark. Further, the team should:

- Review all trademarks and service marks registered or used by seller anywhere in the world, whether as owner or as licensee. Examine both the geographic area of use and the date of the first use of the mark in the given territory.
- Scope of Rights- exclusive/non-exclusive right.
- Examine the prosecution files for any registration of pending applications and examine all trademark searches performed in connection with such pending applications.
- Review all quality control manuals / files or guidelines relating to goods or services sold under the marks.
- Review all trademark licenses, not only through trademark license agreements but also through all other types of agreements that include trademark licenses, including, for example, co-branding agreements and marketing and distribution agreements.
- Review specimens of each use of such mark for each jurisdiction in which the mark has been used or registered.
- Review that the assignments and registrations are in proper order.
- Review that there is no encumbrances and liens.

Copyrights

- Review all copyrighted works that the target has created, commissioned or to which it has acquired rights. If seller does not own a copyright in such works, review who owns the copyright and the nature of seller's right to use the works.
- Scope of Rights - exclusive/non exclusive right.
- Evaluate all work-for-hire agreements and contracts relating to consulting services and development work.
- Review all documents concerning copyright registration, including applications, correspondence, transfers and security interests.
- Review all licenses related to copyrighted works used by target and assignments.

- Review and evaluate the target's policy for identifying and protecting its copyrights in works it develops or developed for it.
- Review and evaluate the efforts undertaken by the company to avoid claims of copyright infringement and obtain proper copyright clearances.
- Identify and evaluate all actual or pending claims of copyright infringement asserted against the target.
- Review that there must not be any encumbrances and liens.

Trade Secrets

- Obtain an inventory of all material trade secrets utilized by the target.
- Review the Confidentiality/Security precautions and procedures of the target.
- Proper marking of the legends made or not.
- Determine whether non-disclosure agreements have been executed with key employees, consultants and other individuals or entities having access to the target's confidential information.
- Determine whether non-compete agreements have been executed between the target and its key personnel.
- Review employment records of key personnel.
- Consider the impact of recent arrivals and/or departures of key personnel.
- Evaluate the adequacy of exit interviews.
- Evaluate security policies including physical, technical and administrative security procedures employed by the target.
- Review and evaluate all relevant agreements including know-how licenses and technical assistance agreements.

Domain Name

- Obtain an inventory of all domain names utilized and issued by the target.
- Review and verification of record owners.
- Review the assignments and registrations.
- Status of various registration and renewal.
- Proper marking of the legends made or not.

Specific Issues that needs to be examined with respect to Trademarks & Service Marks

- Definition of Rights
 - Registered marks
 - Pending applications
 - Trademarks exploited by Target Company but not subject of registration
 - Ownership
 - Marks created by Target Company employees
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- Marks created by independent contractors
 - Marks assigned to Target Company by third parties
 - Liens and other mortgages
 - Third Party Rights
 - Concurrent use and consent agreements
 - Licenses from third parties
 - Freedom to use-Protection/Registration
 - Status and scope of registered marks
 - Status and scope of pending applications
 - Non-registered marks (marketing/registrability)
 - Proper use of markings
 - Exploitation
 - Inventory of products/services on or in connection with which marks are used
 - Licensing practices
 - Inter-company licensing practices
 - Internet use/licensing
 - Nonuse
 - Enforcement/Disputes
 - Pending actions against third parties
 - Pending actions against Target Company
 - Summary, Conclusions, General Comments
 - Examine and evaluate opinion letter and cease and desist letters.⁵

IP due diligence may be custom-made to the target. Businesses' dependence on technology and branding varies significantly. On the other hand, virtually every business uses computer software and owns trademarks, meaning that some IP due diligence must be done.

The Mergers and Acquisitions, Private Equity Investment and Venture Capital transactions require due diligence before signing the deal. Due diligence provides the practical tools to conduct thorough, cost-effective intellectual property investigations. It covers both business strategies and the complex law and regulations relating to intellectual properties. The due diligence exercise must be done by specialists from various areas. Specialists including Company Secretaries need to be involved in the due diligence process. If any part of IP is ignored then the business may get a serious setback from any corner. When purchasing IP, one should work closely with IP counsel/Company Secretaries.

An IP due diligence involves numerous factors that must be specifically designed to the transaction at hand. A proper IP due diligence thus maximizes the value of the business and enhances the stakeholder confidence.

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EMBRACING EMERGING TECHNOLOGIES FOR PROFESSIONAL EXCELLENCE

CS. SAURABH JAIN*

Gone are the days when we wrote letters by hand and waited a week or two for the reply. We no longer visit the bank to check our account balances nor do we queue up to pay our utility bills any more. All this and more has been made possible due to the advent of information technology. The service sector today is highly dependent upon information technology for timeliness, speed and accuracy in delivery of services. The individual consumer has broadband access to the Internet through cable, phone or wireless networks. The Personal Digital Assistants (PDAs), cell phones, cameras of today are no more mundane objects of desire instead they are multifunction devices that can be used for reading and replying to emails, surfing the web and sending instant messages. Researches are on to determine the viability of using the rail networks as a means of providing broadband internet access.

Convergence of technologies and functionality to build more power packed multifunctional devices offering ease of handling, cost effectiveness and reduction in time required to accomplish a task is what research teams worldwide are working upon. These new technological wonders would not only make the work of professionals like Company Secretaries much easier but would also open up a challenge of keeping abreast with the latest technologies along with the ability to operate such devices. The “survivor” in this race would be the one who is able to put the technology to his best advantage to keep himself “steps ahead” and not a step ahead of other professionals.

Prototypes of smart clothing (which would react to weather with the help of sensors), wearable computers and video lenses are already being tested worldwide to make them commercially viable in the near future. The time is not too far when the real estate vendor would supply telephony services, television, cable, radio, personal computing, internet access, power, day planners and even room lighting bundled into one product in the home or flat we purchase. This would increase the responsibility of the professionals in guiding the regulators on policy matters relating to competition/monopoly, ethical standards, licensing, etc. as each of these services is governed by a separate set of rules and guidelines at present. With one vendor providing all the services, the challenge before professionals would be to help their client (“the vendor of multiple services”) in obtaining an umbrella licence under which to provide a plethora of ‘converged’ services.

The plethora of technologies being developed and the quantum of data that would be generated through such technologies cannot be determined as yet. For instance, the nearby departmental store which supplies hundreds of our daily needs uses different technologies to keep track of the items in its stores, sales, theft prevention, item identification, customer identification, customer behaviour study, consumption patterns, etc.

Let us take each one of them individually.

The stores now-a-days make use of radio frequency identification (RFID) tags to keep track of their inventory in the stores. Similarly they may make use of Global Positioning Systems (GPS) to track the

* Education Officer, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

movement of their inventory from the manufacturer to their stores. For easy identification of the individual items at the point of sale they are marked using distinctive bar codes which contain all the requisite information such as product details, size, weight, maximum retail price, date of manufacture, date of expiry, etc. For theft prevention, the stores make use of surveillance cameras and digital scanners at the exit points. The stores issue loyalty cards to their customers in order to achieve customer loyalty in exchange for some rewards or gifts. For the purpose of identification of the customer, the store may make use of biometrics which make use of automated tools to recognise a person by a relatively static pattern of a body part or from a person's behaviour. Examples of biometrics include fingerprint, face, iris and keystroke recognition. At the point of sale the business may collect cash for the goods sold or receive payments through plastic cards (credit/debits cards) which can be swiped in the swiping machine which reads the information recorded on the magnetic strip on such cards. For sales forecasting the business may make use of consumer spending patterns, differentiating between fast moving, slow moving and non-moving goods, etc.

All above mentioned technologies produce data in a different form, the challenge before businesses is thus to have convergence of data collected from various sources to provide the desired inferences. For example, the data provided by RFIDs is different from that provided by biometric systems. Moreover, each of these systems has its own set of advantages and limitations over the other. The professionals need to have an understanding of all these emerging technologies in order to be able to advise and guide their clients about the available technologies which can be put to the most productive use to manage their business processes effectively.

Another challenge thrown open by such technologies before the policy makers and regulators is that of maintaining privacy and anonymity. For instance, the 'retina scan' used in biometric systems can be used to determine the health status or medical conditions. With respect to privacy and security, important choices need to be made before implementation regarding what other types of data will be linked to biometric data. The professionals need to understand the legal issues arising out of the use of such systems and technologies and how such issues can be addressed by the businesses. The professionals need to keep themselves abreast of the policies followed world wide to address such issues.

Similarly, the RFID tags and GPS systems that are currently in use to track inventories are increasingly finding use in tracking the workforce. For instance, the GPS system may be used by the fire fighting department to track its personnel who have entered a huge business complex or a factory in case of fire. But the same GPS system may also be used to track a persons movement when he is off duty. Such unauthorized tracking of personnel is an invasion upon their privacy. Thus, professionals need to exercise care while advising their clients about the use of such technologies.

The surveillance cameras installed by businesses to keep an eye on unauthorized access to its premises and equipment and to stop theft are getting smaller and being embedded in such everyday items as cell phones or badges. Further, the rapid advancements in technology have made the memory for storing photos and videos dirt cheap and easily accessible. The data produced by such devices being rich in content is considered to be more invasive than other information. Various countries have enacted legislations to deal with use of camera phones in public places as gyms and court rooms. With cameras becoming tinnier by each passing day, it may so happen that some day a camera becomes small enough to look like a dust particle yet capable of capturing and transmitting high quality images at mind boggling speed over the internet. Undoubtedly, images captured by such cameras would come handy in solving many of the crimes and drawing public attention to societal issues. Privacy and anonymity would be threatened. Businesses would need to establish adequate security measures in regard to data collected by their surveillance cameras. Thus, the professional is required to have in-depth knowledge of such technologies and the uses to which it is being put, the safeguards required in the implementation of such technologies and the regulatory measures that need to be complied with in the use thereof.

Further, the enormous amount of data generated through the use of such technologies has another dimension - sorting, categorizing, storing, retrieving, analysing and finally destruction of data after it has met the purpose for which it was gathered. It has to be ensured that the data is destroyed in a manner rendering its retrieval impossible at a later stage.

With the electronic devices becoming smaller and more light weight, the trend is towards wireless devices. Consequent to these advances, a need is increasingly being felt for alternative sources of power that are also light weight, mobile and long lasting. The use of alternative sources of energy would bring with it environmental issues such as pollution due to use of hazardous substances, excessive use of natural and non-renewable resources, cross border issues in regard to technology transfers, etc.

Corporates around the world have always been looking at efficient modes of communication. Meetings through teleconferencing and videoconferencing though of a recent origin have caught the fancy of the corporate sector for holding meetings worldwide without the hassle of arranging for travelling by their executives. Although such meetings are taking place in a big way in almost all big corporate houses, there is still no statutory recognition for such meetings.

E-allotment and e-transfer of securities in demat form have heralded a new era in the way dealings in securities take place. The financial markets through out the world are now more electronically connected than a decade ago. The Internet is profoundly reshaping financial services market. It has empowered us with faster and more efficient access to information and transactional capability. The combination of easier access and reduced costs for online financial services has intensified investment activities.

The next on the anvil are e-prospectuses and e-offer documents. The policy makers in developing countries are considering allowing presentation and promotion of prospectuses in an electronic format, reducible or revertible to the printable form. Professionals like Company Secretaries would be required to ensure that the electronic prospectus satisfies the provisions of the Companies Act relating to issue of prospectus, so that the investors can take informed decisions based on the information contained in the prospectus relevant to the securities on offer. Investment advisory services over the internet would not be something unheard of in the near future.

The Insurance sector has started selling insurance policies online without the insurer and the insured meeting physically in the entire process. In such cases the insurance companies rely on documents submitted to the company by the insurer. With the increase in online business, time is not far when such companies would rely on documents which have been pre-certified by professionals like Company Secretaries. As the insurance policies bought and sold over the internet involve e-contracts, professionals need to have an understanding of the enforceability of such contracts and that of essential ingredients of an insurance contract.

Computers have started responding to vocal instructions issued by the user, the keyboard is no longer needed to type documents, a simple dictation is converted into a digitized text document within a matter of seconds by the PC. This has been made possible by the use of "voice recognition" technology. The professionals can make use of this technology to enhance their efficiency in service delivery, improve customer satisfaction and increase operational effectiveness.

The regulators have kept abreast with the rapid advances in information technology. The role of the regulator has undergone a paradigm shift from that of a controller to a facilitator. The MCA21 project is a successful example of an e-governance initiative of the government. Professionals need to keep themselves updated on the policy changes introduced by the government and also suggest positive measures to the government to streamline the systems so as to make it more user friendly and effective. This would not only improve the level of compliance but would also reduce the risk of non-compliance faced by corporates.

To conclude, let all professionals pledge to keep pace with speed of change. We need to have a clear vision for convergence of technological advancement and service delivery. An understanding of where we are today and where we want to be in the future is highly essential. Before executing any plan for the future there is need for impact analysis using the predictive model on how the existing models can be integrated with IT enabled systems faster, better and at reduced costs. In nutshell, there is need to examine the practice areas and identify hot spots where improvements will have the greatest pay off – areas to focus on, to improve, areas to outsource; areas to divest, etc. Develop a service oriented architecture. Look at the existing systems for opportunities to improve or update them.

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CORPORATE EXCELLENCE THROUGH INNOVATION

CS. LAKSHMI ARUN* & CHITTARANJAN PAL**

Every success story is backed by innovative initiatives. Innovation and growth is a systematic and complementary process. It is about creating a transformational change in the way we live, we work and we perform.

Successful business innovations that drive growth are guided by certain principles such as Vision to create new products, systematic processes, reward and recognition system, focus present and future needs and growth-oriented leadership etc.

Innovation or creativity is not confined to a particular product or process, but is applicable to all functions of an organisation. It may be service innovation, strategic innovation, customer-oriented innovation, technical innovation, financial innovation, sales promotion innovation and so on.

Mukesh Ambani, Chairman of Reliance Industries Ltd said that “Innovation only in technology is not enough. You need that more in management practices, where the RoI is greater”. Innovation is required in every interface with the stakeholders, to make a difference and distinguish an organisation that desires to excel. Innovation has to be pervasive. Everybody should have an opportunity and incentive to innovate. In every function, be it finance, software, quality, HR, or investment, people should constantly look for innovation. Innovation has to become part of corporate DNA and strategy. Valuable ideas should come from every level in the organisation.

EXCELLENCE THROUGH INNOVATION- CRITICAL AREAS

Enduring corporate excellence is the ability of a company to consistently outperform competition over long period of time and deliver long-term stakeholder value. Critical areas that facilitate the company to achieve excellence may be business process re-engineering, growth, sustainable development, core-competence, resource utilization, stakeholder satisfaction etc. For achieving every such factor innovative skills are essential ingredient. To be more precise,

Innovation in Business Process : As business scenario is fast changing with each passing day and to meet the ever-changing demands of the market, organizations need to restructure and redesign their Business processes. They have to reinvent the way the businesses are carried to ultimately engender corporate excellence.

Sustainable growth : Many organizations are growing at a rapid speed, but they failed to develop consistently. Hence, the companies need to redefine their objectives towards sustainable development.

* Education Officer, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

** Assistant Education Officer, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

Core Competence : Achievement of unique strength either in technology or in the processing of functional areas, that an organization enjoys exclusively leads to Core Competence. This unique strength helps the company to get competitive advantage over a long period of time, which in turn facilitates the company to excel. This of course requires innovative skills.

Resource Utilisation : Excellence in organization can be achieved through proper utilization of the basic Human, Physical and financial resources. New and advanced technologies have to be adopted in innovative manner in all the functional areas like production, marketing, finance, HRD, of the organization.

Stakeholder Satisfaction : In the process of achieving corporate excellence in the present day highly competitive market, the organizations' ability to compete depends on its relationship with its stakeholder. The basis for continuity of relation between the corporates and the stakeholders, over the period of time is value maximization to them. This cannot be achieved without innovative skills.

Thus, embedding innovation in an organization at every level is essential. When every employee becomes an innovator and every process is open to innovation, the innovation becomes a habit in the organization. Innovation then does not remain a one time radical breakthrough; it becomes dynamic.

CORPORATE EXCELLENCE – INDIAN PERSPECTIVE

Though there is a temporary global recession, the growth in Indian economy especially in the last one decade, is fueling entrepreneurship, innovation and creativity in every industry. This growth is even attracting MNCs to establish their R&D, manufacturing and entrepreneurship centers in India.

As regards innovation and creativity, India as a country has been able to attract a number of global players in software. Microsoft has built its largest development centre outside the US in Hyderabad, almost 20% of the development activities of SAP are done in India, the Bangalore development centre of Philips contributes in every product of the company that has software in it. Hewlett Packard is conducting all its high level research on futuristic technologies for emerging markets in India. In fact, the growth of innovation in India is witnessed by pharma, healthcare, autos, equipment, manufacturing, financials, retail, education etc.

INNOVATION FOR SUSTAINABLE DEVELOPMENT

Sustaining a position in the stakeholder' mind is an on-going battle and victory can be taken away at any moment by a competitor. This position has necessitated the corporates to innovate constantly. Very few companies are successful in sustaining their dominant position and those that are, continuously innovate. Continuous innovation and self-attack are at the core of competitive strategy for the 21st century companies. A number of companies in India also, who are also market leaders in their respective industries and maintain a dominant position in the market place, have embraced these strategies. For example, Hero Honda, the successful two-wheeler company in India knew the importance of change and continuous innovation and attacked itself with better and new products, without any fear of failure. They have mastered the art of consistently generating revenues and doing better than all other competitors, i.e., they knew how to create the demand for new products and grow revenues even in recessionary times.

CORPORATE INNOVATION - INTERNATIONAL SCENARIO

Corporate Innovation at international level may be better described by referring to Innovation Index. The Innovation Index is a compilation of the Top 20 Innovators in North America. Most of these Innovators are prestigious companies including Apple, GE, 3M, HP, IBM, and Proctor & Gamble who have created numerous innovations and shaped our lives over the past fifty plus years.

Companies like Apple Inc., GE Healthcare BMW, Proctor & Gamble etc adopt certain common mechanism that has lead to innovation. These innovators consistently and successfully bring to market

BACKGROUNDER

winning innovations, achieve profitable new growth, and reinvent their business for the future. For example, the strategy at GE emphasizes sound business processes driving creativity and innovation, and is rooted on the three pillars viz. 1. Focus on key technologies: 2. Growth-oriented leadership: and 3. Business portfolio. There are similarities between the Innovation strategies of GE and P&G. For instance both companies have divested non-core businesses. Both emphasize on strong leadership and innovation accountability. Both are focused on new products driving current and future growth. The strategy at P&G is made of three pillars driving new innovations viz 1. Brand mix; 2. Global top team; 3. New products.

INNOVATION FAILURES THAT LED TO SUCCESS

“Failure is our most important product”-R.W.Johnson Jr., Former CEO, Johnson & Johnson

‘Our Company has, indeed, stumbled onto some of its new products. But never forget that you can only stumble if you are moving’-Richard P Carlton, Former CEO, 3M Corporation

3M and Johnson & Johnson are the typical examples of corporate innovation through failures. Johnson & Johnson had many failed ventures such as foray into Kola stimulants, colored casts for children, heart valves, kidney dialysis, and ibuprofen pain relievers - the list is quite big. The failures result at J & J from the fact that the company emphasizes placing bets on many potential opportunities—most opportunities possibly fail, but the ones that do succeed, they succeed big. The bets, or the experimentation, are an essential price to pay for successful Innovation and long-term growth.

3M is best known for its household brands such as Post-It note, Scotch tape, etc. 3M initially failed in its mining business, and eventually stumbled onto most of the successful innovations. 3M created the mechanisms and management practices to encourage individual initiatives and experimentation. “Golden Step” award is being given to those creating successful new business ventures originated within 3M. More mechanisms were created to stimulate internal entrepreneurship, test new ideas, create unplanned experimentation, share new ideas, develop new innovation etc.

Another example, Honda Motor Company entered the US market in 1959 with its range of low-powered motorcycles. It endured failure after failure as it learned the hard way that little motorcycles popular in the Tokyo suburbs were not well received on the wide open roads of the USA. They eventually brought out a range of high powered bikes that became very popular. Like this there are many corporates that has excelled after going through failures.

OBSTACLES TO CORPORATE INNOVATION AND REMEDIES

Obstacles

The following are the some of the common obstacles to innovation and creativity that are being faced by any corporate.

- Lack of skillful brainstorm facilitation
- Constantly shifting priorities
- Risk aversion
- Fear about failure
- Inadequate systems and processes
- Assumption that innovation is related to R&D
- Short term thinking
- Lack of focus
- Lack of reward

- Inadequate training
- Unfriendly corporate culture
- Lack of shared vision
- Unwillingness to change etc

Remedies

The following measures might act as effective tool to unblock creativity.

- Open Communication
- Effective training
- Conducive work atmosphere
- Employee friendly culture
- Proper rewards and appreciation
- Curtailment of internal politics
- Introduction of group activity
- Job rotation
- Availability of resources, time and systems for creativity and innovation
- Free hand for experimentation
- Hiring of persons with diversified qualifications and experience etc.

Cultural Aspects

Corporate culture is made up of a complex mix of employee and corporate beliefs, attitudes, values, rituals, and behaviors that permeate a company and give it its unique personality. It has surfaced as one of the most compelling factors in characterizing, leading, and managing any organization. It is a set of specific belief, methodology and characteristics unique to an organization, where the organization becomes the microcosm under scrutiny, hence the way of its constituents.

Culture can attract the best employees and maintain their loyalty and integrity. Sometimes, corporate culture is not given sufficient importance as it is difficult to measure.

According to Management expert Peter Drucker knowledge workers do not respond to financial incentives, orders, or negative sanctions. He refers that the key to managing these workers is to treat them as people whose commitment is highly contingent and whose motivation comes largely from within. In order to generate genuine inspiration or passion naturally, a company has to start at the core.

The employee-friendly, uninhibited, value-focused culture is a direct product of the personalities, visions, and efforts of the company's founders and leaders.

If an organization values innovation, it will require team with fresh mind and inspiration more than just ideas. It will need to establish the right kind of culture that is conducive to sustainable innovation. Creating this kind of employee-friendly culture is not accomplished overnight. This is achieved through consistent/regular informal talks, incentives at proper time, appreciative remarks, conducive working environment etc. Further, counter-productive politics and territoriality needs to be addressed. People need to enter into new kinds of dialogues and debates.

It is worth referring a case study that describes how the organizational culture improves/hinders innovation.

A February 2007 working paper, *Innovation in Firms Across Nations: New Metrics and Drivers for Radical Innovation*, describes a global research effort that looked at 759 public companies from 17 of the largest economies and most populous countries in the world. The companies came from a set of nations that included developed nations such as the United States, Germany and Japan, and developing nations such as China and India, providing a cross-cultural look at the factors that drive innovation.

They claim, the most important factor driving innovation is the internal culture of the company. Specifically, the researchers found that a future market orientation, a willingness to cannibalize and a tolerance for risk are three elements that have a particularly strong relationship with radical innovation. Organizational tools such as incentives and product champions are also important, though less so. The only other factor that the authors found to be significant is R&D spending, but even that is not as strong as company culture.

CONCLUSION

Creativity generates Ideas. Ideas generate Innovations. Innovations generate revenues to the organisation. Creativity has to become ones' profession, instead of bringing in creativity into one's profession. As innovation is not confined to R&D department/ production, Company secretary has wider role to play in achieving corporate excellence. As a Company Secretary, Innovation and creativity lies in better compliance management, guiding in optimum finance mixture, drafting of important corporate documents like joint venture agreements etc.

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UNLOCKING STAKEHOLDER VALUE THROUGH CORPORATE RESTRUCTURING

CS. DEEPA KHATRI*

Corporate Restructuring is vital for survival of a company in the competitive environment. Success in business goes with the changing of methods of doing business, and to succeed in business, requires Restructuring. The judiciary has been generally espousing a liberal and pragmatic approach towards corporate restructuring. In *Ion Exchange (India) Ltd., In re.* [2001] 42 CLA 302 (Bom), Justice Dr. Dhananjay Chandrachud emphasised: "Corporate Restructuring is one of the means that can be employed to meet the challenges and problems which confront business. The law should be slow to retard or impede the discretion of corporate enterprise to adapt itself to the needs of changing times and to meet the demands of increasing competition. The law as it has evolved in the area of mergers and amalgamations has recognised the importance of the High Court not sitting as an appellate authority over the commercial wisdom of those who seek to restructure business. The need for this restatement is all the greater today where the interplay of competition and the forces of the market demand efficiency; cost effectiveness and high levels of productivity."

OBJECTS OF RESTRUCTURING

The ultimate litmus test for any organisation is its financial health, and the financial benefits have to be maximised in order for the firm to survive. The application of any concept in finance/strategy/HR to the organisational restructuring has to be driven by one single goal, viz. maximisation of the shareholder value. Taking care of this would automatically ensure that the other concerns of the firm are taken care of. Running a business without the proper support of the employees is simply not possible. Hence, the employees have to be given their part of the value. Likewise, the other stakeholders including customers and suppliers have to be satisfied. It is only after all these stakeholders are taken care of, that the residual value can be appropriated by the shareholders. If the residual values can be maximized, it means that the other stakeholders are also happy.

The motivation to restructure is driven by how organizations are performing in the marketplace and what they want to do. Often they want to acquire a new technology, enter a new market, or extend a product line. In sum, corporations are focused on bottom-line issues; they use mergers and acquisitions as a component of strategic growth. Rather than starting from scratch to build a product or to maximize intellectual property, a company can go out and acquire these capabilities. The main objects of corporate Restructuring can be identified as follows:

- Business strategy to focus on core strength, operational synergy, efficient allocation of managerial capabilities and infrastructure. Core competency is a bundle of a company-specific knowledge; skills, technologies, capabilities. The concept of 'core competency' is central to the resource-based perspective on corporate strategy. The resource-based view of strategy is that sustainable competitive advantage arises out of a company's possessing some special skills, knowledge, resources or competencies that distinguish it from its competitors.

* Assistant Education Officer, The ICSI. The views expressed are personal views of the author and do not necessarily reflect those of the Institute.

BACKGROUNDER

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- Consolidation and economy of scale by expansion and diversion to exploit extended domestic and global markets.
 - Revival and turning around a sick unit by adjusting losses of the sick unit with profits of healthy company.
 - Acquiring constant supply of raw material and access to scientific research and technological developments.
 - Capital Restructuring by appropriate mix of loan and equity funds to reduce the cost of servicing and improve return on capital employed.
 - Corporate restructuring is necessary when a company needs to improve its efficiency and profitability and it requires expert corporate management.
 - New geographical markets, maximize shareholder value, increase/ protect market share, acquire new products/services, gain control over supply chain, economies of scale.

REGULATORY FRAMEWORK FOR RESTRUCTURING

The term 'corporate restructuring' is quite wide and varied. Depending upon the requirements of a company, it is possible to restructure its business, financial and organisational transactions in different forms. The often-used tools are amalgamation, merger, demerger, spin-off, slump sale, acquisition, buy-back of shares, issue of shares with differential voting rights, de-listing, joint venture, strategic alliances, and franchises, etc.

Restructuring under Companies Act, 1956

Sections 391 and 394, which is a statutory device to facilitate mergers, de-mergers, amalgamations and other schemes of corporate restructuring provides for easy and quick corporate restructuring in the current era of global competition.

Chapter V (sections 390 to 396A) of the Companies Act, 1956, is a complete code in itself. It provides for the law and procedure to be complied with by companies for giving effect to restructuring schemes based on compromises, arrangements, and reconstruction. The term amalgamation and merger are synonymous under the Act. Any scheme of compromise, arrangement with shareholders or creditors or reconstruction falls within the provisions of sections 391 to 394.

The Companies (Court) Rules, 1959 ('Rules') lay down the court procedure for the approval of schemes of amalgamation, merger and demerger. The Rules provide for the approvals of shareholders, creditors, Central Government, official liquidator and sanction of the company court. Two companies can file a joint application for the approval of a scheme to the same High Court, if the registered office of the companies is in the same State. Moreover, in case of a holding company merging with its wholly owned subsidiary company, only one application has to be filed by the wholly owned subsidiary company for seeking the necessary sanction from the High Court where the registered office of the wholly owned subsidiary company is situated.

Judicial view on Restructuring

It is well settled that sections 391 and 394 vest in High Court very wide powers with respect to sanctioning schemes of corporate restructuring. Section 396 empowers the Central Government to provide for amalgamation of companies in national interest. The court and Central Government have supervisory powers in approving schemes of compromises, arrangements and reconstructions by companies. The Supreme Court in *Miheer H Mafatlal v. Mafatlal Industries Ltd.* [1996] 23 CLA 1 (SC) has ruled that the High Court in sanctioning any scheme of merger or amalgamation has no jurisdiction

to act as a court of appeal and sit in judgment over the informed view of the concerned parties to the compromise as the same would be in the realm of corporate and commercial wisdom of the concerned parties. The High Court has neither the expertise nor the jurisdiction to delve deep into the commercial wisdom exercised by the creditors and members of the company who have ratified the scheme of merger by the requisite majority. Consequently, the company court's jurisdiction to that extent is peripheral and supervisory and not appellate. Justice S.B. Majmudar observed that "While deciding the issue of amalgamation or merger, the company court acts like an umpire in a game of cricket who has to see that both the teams play their game according to the rules and do not overstep the limits. But subject to that, how best the game is to be played is left to the players and not to the umpire."

The Supreme Court ruled that the company court can not, undertake the exercise of scrutinising the scheme placed for its sanction with a view to finding out whether a better scheme could have been adopted by the parties. This exercise remains only for the parties and in the realm of commercial democracy permeating the activities of the concerned creditors and members of the company who in their best commercial and economic interest by majority agree to give green signal to such a compromise or arrangement.

Restructuring under the Competition Act, 2002

The Act regulates the various forms of business combinations through Competition Commission of India. Under the Act, no person or enterprise shall enter into a combination, in the form of an acquisition, merger or amalgamation, which causes or is likely to cause an appreciable adverse effect on competition in the relevant market and such a combination shall be void. Enterprises intending to enter into a combination are required to give notice to the Commission. But, all combinations do not call for scrutiny unless the resulting combination exceeds the threshold limits in terms of assets or turnover as specified by the Competition Commission of India. The Commission while inquiring into a 'combination' shall consider the following factors :-

- Actual and potential competition through imports;
- Extent of entry barriers into the market;
- Level of combination in the market;
- Degree of countervailing power in the market;
- Possibility of the combination to significantly and substantially increase prices or profits;
- Extent of effective competition likely to sustain in a market;
- Availability of substitutes before and after the combination;
- Market share of the parties to the combination individually and as a combination;
- Possibility of the combination to remove the vigorous and effective competitor or competition in the market;
- Nature and extent of vertical integration in the market;
- Nature and extent of innovation;
- Whether the benefits of the combinations outweigh the adverse impact of the combination.

Important Laws/Regulations Affecting Restructuring

The Foreign Exchange Management Act, 1999 and the Income Tax Act, 1961 are other major laws affecting the restructuring. Besides, the Securities and Exchange Board of India (SEBI) has issued guidelines

to regulate mergers and acquisitions. The SEBI (Substantial Acquisition of Shares and Take-overs) Regulations, 1997 and its subsequent amendments aim at making the take-over process transparent, and also protect the interests of minority shareholders.

SIX KEYS TO SUCCESS OF RESTRUCTURING

According to the survey conducted by KPMG Global Research Report 1999 on Mergers and acquisitions, there are six 'keys' which successful companies use to unlock value. These six keys are categorized in two parts Hard Keys and Soft Keys.

Hard Keys

The successful companies achieved long-term success by prioritising three key activities in the pre-deal phase (the so called hard keys) which had a tangible impact on ability to deliver financial benefits from the deal. They are:

- synergy evaluation;
- integration project planning; and
- due diligence.

Using the benchmark, a quantifiable benefit could be accorded to each one. Each one in its own way contributes to deal success; however there is overlap between them. They can therefore have greatest impact if brought together in a single pre-deal process which gives the acquirer essential intelligence about risks, benefits and operational issues. This information helps in deal negotiations and shape the post-deal integration programme to ensure that shareholder value is increased.

Soft Keys

People and cultural issues are important in determining deal success, the stress in the survey was given to drill down and understand the impact of different decisions and timescales relating to soft keys on deal outcome. The results highlight three soft keys:

- selecting the management team;
- resolving cultural issues; and
- communications.

The power of the hard keys with soft keys combination

The relative impact of the keys on success rates was investigated and found that it would be wrong to leave an impression that any one activity is sufficient in its own. The acquirers who achieved best results were those who recognized the importance of both sets of keys.

A brief analysis of hard and the soft keys

Synergy Evaluation

Synergy evaluation – 'what' Synergies are vital to the success of any merger or acquisition, most companies now realise that without them, an M&A is unlikely to result in any significant additional growth in shareholder value.

Pre-deal synergy evaluation emerged from the survey as the prime hard key to deal success; one which can enhance chance of success to 28% above average. Only by gaining a clear understanding of what and where value can be obtained from a deal, the companies can hope to avoid 'bad' deals and be in a position to work out how, during integration planning, this value extraction will be achieved.

While the concept of 'synergies' is now something of a cliché – and one commonly trumpeted during public merger announcements – too few companies are moving beyond these statements of intent to work out how and indeed whether they can actually be achieved. To do this requires a thorough process of synergy evaluation, beginning as soon as possible in the pre-deal phase. Such a process involves detailed work with operational managers to confirm the 'deliverability' of synergy assumptions and provide the reassurance during negotiations that the identified benefits are robust. The survey confirms that companies target synergy benefits through revenue enhancement as well as direct operational cost reductions.

The Key areas targeted for synergies are:

- Revenue benefits
- Indirect, overhead cost reductions
- Direct operational cost reductions

Integration project planning - the 'how'

Integration project planning goes hand in hand with synergy evaluation as a key to merger success. It is critical to work out the mechanics of how synergies will be attained, and also how the combined business will be stabilised to preserve current value and ensure that one plus one does not make less than two. The survey confirms, through its objective benchmark, that the chances of merger success are increased if the process of working out 'how' is started well before the completion of the deal. Those companies that prioritised predeal integration project planning were 13% more likely than average to have a successful deal.

According to survey, there is no substitute for pre-deal planning. Company management have a 'honeymoon' period of some 100 days after deal completion to take hold of the business and begin delivering benefits. Unless they are in a position to start implementing the hard mechanics of their M&A aims by this stage they will lose value from their acquisition. If stakeholders do not see results, and see them quickly, then their support will be lost and the project will be derailed. Companies that invest time and effort in pre-deal planning will be in a much better position to meet stakeholder expectations and unlock value from the deal.

Due diligence – a springboard to the 'what' and the 'how'

The survey showed that due diligence is the most important of the non-optional pre-deal activities. Companies which prioritised this were 6% more likely than average to have a successful deal. This contrasts with the acquirers who focused their attention instead on arranging finance or on legal issues and were therefore 15% less likely than average to have a successful deal. This evidence highlights the power of due diligence if used to full effect.

Sophisticated and forward-looking acquirers use a 'springboard' approach to due diligence which often encompasses a range of investigative tools designed to systematically assess all the facts impacting on value. This can include market reviews, risk assessments, and the assessment of management competencies, as well as areas to concentrate on for synergies or operational impact.

The power of an integrated approach

When viewed separately, synergy evaluation emerged as the hard key which had greatest impact on deal success. Implementation planning and due diligence also have a positive influence on success levels, though on face value appear less important than synergy evaluation. However, it would be misleading to view each area in isolation as there is inherent overlap between each of these hard keys. By bringing the three activities together within a single process, the acquirer can maximise the value of

predeal investigation work. When handled in this way as an holistic approach, the process provides the necessary intelligence to influence price negotiations and plan for the post-deal integration which ultimately unlocks shareholder value.

Soft Keys

Hard factors alone are not enough, and acquirers must devote effort to the 'softer' aspects of their transactions if they are to deliver ultimate benefit to shareholders. Three soft keys which have significant impact on deal success includes selecting the management team, resolving cultural issues and communication. Planning for the mechanics of M&A value extraction is worthless unless company employees are both willing and able to implement them. It is not surprising that the survey found a strong correlation between these 'softer' areas and overall deal success. People issues are historically the most difficult to resolve. Staff cannot be forced to cooperate, to drive forward merger objectives, or to change their business behaviour. They must be motivated and given incentives to do so. This requires careful planning, and resourcing.

Selecting the management team

To be successful, a merger or acquisition requires exceptionally strong leadership from the board downwards, to drive forward a complex programme of value realisation. Hasty decisions may prove to be wrong and the need to move quickly must be offset by legal compliance considerations. Yet, if the selection process is too slow, uncertainty can lead to a damaging drop in morale and the exodus of key talent. This can have a devastating effect on the combined business.

Resolving Cultural Issues and Communications

Culture encompasses the way people communicate with each other; the way they resolve conflict; how they celebrate, reward, lead, manage, do their work, break down and assign work, and relate to each other. It is the core of the company's belief system.

It's very challenging to address culture as part of mergers and acquisitions. But organizations that engage in M&A without considering culture do so at their own peril. It is often heard that mergers don't work due to a clash of cultures, which has a lot to do with people—the inability of people to think of themselves and their organizations in different ways. They get tracked in one way of doing things, and get very resistant to any kind of change.

In the integration process, what is the objective is to bring the best of both entities together to create something new. It takes an extraordinary amount of skill and patience. It can be hard to find the energy and focus for this after an intense negotiation process. Integrating staff after a merger is far more of an art than a science. As such, there is no definitive "checklist" for how to get it done. Success depends heavily on awareness of what the staff's concerns, feelings, and challenges are, and on communication.

Communication is the key. It is needed to communicate how the strategic intent of the deal translates to people's day-to-day goals and objectives. This is key to making sure that staff are on board and are aligned with the new organization.

One thing that works well is to have an executive sponsor, someone who has been through deals in the past and can ensure successful integration. This serves as a champion of the integration and can help the acquired company through — making sure they have a sense of voice and purpose, are being listened to, and are getting the resources they need to ensure the success of the deal. The champion should be a decision-maker who has authority and credibility with both organizations. They need to have great communication skills, as well as leadership skills.

Despite vast differences in scale, intent, and even process in terms of merger integration the bottom line for success is the same—it's critical to focus on the people and on frequent, clear, and honest communication. When it comes to achieving success, the similarities outweigh the differences. The following qualities and actions of the champion support successful integration:

- Having a vision, the focus and conviction to realize it.
- Explaining the change and why it was necessary.
- Keeping everyone focused on the mission.
- Having a plan for integration and communicating it broadly.
- Showing respect for the old organization, but creating a new organizational culture.
- Being an excellent communicator—a master at listening as well as persuading.
- Communicating honestly, clearly, concisely, and frequently.

Other qualities of the Champion include:

- A positive attitude: Modeling a forward-looking and mission-oriented attitude.
- Acknowledging, absorbing, and attending to the emotions of the staff, while keeping the organization's clients and the community served as the ultimate focus.
- Naming and dealing with staff resistance when it emerges.
- Knowing when to be patient and when to move quickly.
- Looking for "quick-wins" and celebrating these.
- Securing the buy-in of those who must directly implement the change, while gradually expanding to others throughout the organization.
- Get people involved, especially across the lines of the former organizations

In addition to the key role of the leader, integration is best effected when there is a plan and an integration team composed of staff and board (and volunteers) from the former organizations. The composition of the integration team is critical; if it appears to be unfairly dominated by one of the former organizations, this may create a roadblock to smooth integration.

MEASURING SUCCESS IN RESTRUCTURING

The success of a deal is usually measured in terms of return on stakeholders value. Successful companies are those that have both short-term and long-term goals and timetables, and that have the ability to adjust these to accommodate changes, such as the changes in business climate that may occur between the time you announce, the time you close, and throughout the integration process. It's important to keep people on track, and to ensure that people aren't trying to sabotage the process. They explore as many solutions as possible to make the merger a possibility. In the end, though, success in merger negotiations may be the decision that a merger would not work right now, that it's just not viable or would cost too much.

It may sometimes happen that the resistance is often greater than the momentum. "Getting the word out is challenging — but you need to. That's really the key to making sure it works. It's important to keep people on track, and to ensure that people aren't trying to sabotage the process." you have to constantly drive the momentum; it rarely takes on a life of its own.

RECENT MERGERS AND ACQUISITIONS

Mergers and Acquisitions have been very common incidents since the turn of the 20th century. These are used as tools for business expansion and restructuring. Through mergers the acquiring company gets an expanded client base and the acquired company gets additional lifeline in the form of capital invested by the purchasing company. The recent mergers and acquisitions authenticate such a view.

The Long Success International (Holdings) Ltd merged with City Faith Investments Ltd on the 8th of April 2008. The value of the merger was US \$3.2 million. The agency in this instance was Bermuda Monetary Authority, Hong Kong Stock Exchange.

Novartis AG acquired 25% stake in Alcon Inc. This acquisition was worth 73,666 million common shares of the company. They bought this stake from Nestle SA for \$10.547 billion by paying \$143.18 for every share. It was a privately negotiated transaction that needed to have a regulatory approval. Simultaneously, Novartis AG also received an offer of 52% interest that was equivalent of 153.225 million common shares of Alcon Inc

Kinetic Concepts acquired each and every remaining common stock of LifeCell Corp for \$51 for each share. Their total offer was \$1.743 billion. The deal was done in accordance to regulatory approvals and the conventional closing conditions.

Kapstone Paper & Packaging Corp acquired the kraft paper mill as well as other assets of MeadWestVaco.Corp. They paid them \$485 million. The deal was conducted as per the regulatory approvals, receipt of financing and conventional closing conditions. This deal included a lumber mill in Summerville, hundred percent interest in Cogen South LLC. The Chip mills in Kinards, Elgin, Andrews and Hampton in South Carolina are also parts of this deal.

Petrofalcon Corp acquired the remaining shares of Anadarko Venezuela Co from Anadarko Petroleum Corp. The deal was worth 428.46 million Venezuelan bolivar or US \$200 million. The deal was completed as per the regulatory approvals.

WNS (Holdings) Ltd from India, took over the total share capital of Chang Ltd. The deal was worth 9.6 million. Of this amount 8 million was to be paid in cash and the rest was to be paid in payments related to profits

Spice PLC took over Melton Power Services Limited. The deal was worth 4.5 million. 2.5 million was paid in cash and the rest was to be paid from the profits made by the company. Spice PLC also got Utility Technology Ltd., GIS Direct Ltd, and Line Design Solutions Ltd as part of the deal.

Atlas Iron Ltd. took over a 19.9% stake in the Warwick Resources Ltd. This was equivalent of 15.124 million new common stock of the Warwick Resources Ltd. They paid A\$ 3.781 million in a transaction that was privately negotiated. The transaction was executed as per the approval from the shareholders. The selling price of the shares was A\$ 0.23 and it was based on the value of each share that stood at a\$ 0.25 on 4th of April 2008.

Republic Gold Ltd of Australia took over the remaining stocks of Vista Gold (Antigua) from Vista Gold Corp. The deal was worth \$3 million. Republic Gold also got the Amayapampa project in Bolivia as a part of the deal. Manpower Software PLC took over Key IT Systems Ltd. The deal was worth 0.83 million. 0.375 million was paid in cash and the rest is supposed to be paid from profits.

Thomas Cook Group PLC acquired Elegant Resorts Ltd from Barbara Catchpole and Geoff Moss. Australian Social Infrastructure Fund merged with API Fund. The deal was subjected to regulatory approvals and shareholder. Greenbier Cos Inc took over Roller Bearing Industries Inc., from AB SKF. Fijian Holdings Ltd has took over 50.2% interest in RB Patel Group Ltd. Honeywell International Inc has

acquired Norcross Safety Products LLC from Odyssey Investment Partners LLC. The deal was worth \$1.2 billion. It was subjected to various kinds of regular closing conventions and regulatory approvals.

When it comes to mergers and acquisitions deals in India, the total number was 287 from the month of January to May in 2007. It has involved monetary transaction of US \$47.37 billion. Out of these 287 merger and acquisition deals, there have been 102 cross country deals with a total valuation of US \$28.19 billion.

Hindalco acquired Canada based Novelis. The deal involved transaction of \$5,982 million. Tata Steel acquired Corus Group plc. The acquisition deal amounted to \$12,000 million. Dr. Reddy's Labs acquired Betapharm through a deal worth of \$597 million. Ranbaxy Labs acquired Terapia SA, the deal amounted to \$324 million. Suzlon Energy acquired Hansen Group through a deal of \$565 million. The acquisition of Daewoo Electronics Corp. by Videocon involved transaction of \$729 million. HPCL acquired Kenya Petroleum Refinery Ltd., the deal amounted to \$500 million. VSNL acquired Teleglobe through a deal of \$239 million.

The sectors attracting investments by corporate India include metals, pharmaceuticals, industrial goods, automotive components, beverages, cosmetics and energy, in manufacturing sector; and mobile communications, software and financial services in services sector.

CONCLUSION

Globalisation gives the consumer many choices - technologies are changing, established brands are being challenged by value-for money products, the movement of goods across countries is on the rise and entry barriers are being reduced. As markets consolidate into fewer and larger entities, economies become more concentrated. The second-generation economic reforms in India have accelerated the trend of corporate restructuring. Indian companies are building up global size operations. The underlying object of corporate restructuring is efficient and competitive business operations by increasing the market share, brand power, operational synergy, and unlocking stakeholder value.

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