Limits to Corporate Growth

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Since the publication of the Monopolies Inquiry Commission Report in 1965, there has been an increasing public concern with the growth of big business which is normally associated with concentration of economic power. The growth of Indian corporate enterprises is highlighted from time to time in that context. The MRTP Act notwithstanding the growth of corporate enterprises has continued unabted over the years. The total assets of the 101 top private sector companies-the corporate giants-grew at a faster rate in 1980-81 than in the previous year in terms of total assets, net worth and net sales. The growth of total assets was 18. 8 per cent in 1980-81 as compared with 15. 5 per cent in 1979-80. Sales (net of excise duty) recorded a higher growth rate of 20. 3 per cent in 1980-81 as against 15. 5 per cent in the previous year.[1] Many of the companies designated as corporate giants have obviously attained giants proportions over years through well thought out strategies, availing of opportunities that came in the way. Let us take the case of Reliance Textiles, manufacturers of quality fabrics well known by the brand name Vimal, using 1979 as a base, its gross fixed assets increased in value at a compound rate of 61 per cent every year; Owners' equity (share capital and reserves) increased at 59.8 per cent per annum till 1984.[2] While the growth of Reliance Textiles during the last six years is impressive enough, those of other giants have been continuing over a longer period of time. Indeed there are numerous instances of firms which started business on a meagre scale but achieved phenomenal growth over time. To cite one instance, the Transport Corporation of India (TCI) which started transport operations in a small way in 1958, now operates 1360 trucks that haul 13,600 tonnes of frieght over 5,25,000 kms of road every day. With a modest turnover of Rs. 18 lakhs in

the first year of operation, the company's turnover has grown at an average rate of 20 per cent per annum to its present level of Rs. 53 crores.

Even though public opinion in India has looked upon big business with alarm and Government policy has been based on the ideology of regulated growth, expansion of business happens to have been a creed with many corporate executives in recent years. But, is it possible for a company to grow exponentially for an indefinite period of time? To put it differently, are there recognisable limits to growth? Further, is growth an unmixed blessing? Do companies pursuing growth strategy always succeed? There are research studies which have thrown considerable light on these questions even as there are studies evidencing the compulsions underlying corporate growth and the benefits thereof. Let us consider these aspects first by reference to the factors which necessitate corporate growth.

One of the basic reasons underlying the phenomenon of growth is that it is often a cherished cultural value. A company that is not expanding is said to be falling behind. Failure to grow is considered to be a stigma. On the other hand, a growth company is better known and attracts better management. It is a source of strength. Secondly, in industries which are subject to frequent changes in technology and other external conditions, growth is necessary for survival. Opportunities must be availed of, and threats must be overcome, so as to survive. In volatile industries, a firm which does not keep pace with the changing conditions is bound to be left high and dry sooner or later. Thirdly, growth strategy is associated with strong managerial motivation in its favour. Expansion is a rewarding phenomenon in several ways. Larger size means higher executive compensation. It is also conducive to the satisfaction of their power and recognition needs.[3] To seize market share from competitors or to enter challenging new fields is not only exciting and satisfying but also leads to a sense of achievement.[4] Besides, growth is often perceived as an index of effectiveness which has greater news value than stability. In more recent times, the growth objectives of companies have also derived support from the experience curve theory, which on the basis of empirical verification suggests that value added net production costs tend to decline 25 to 30 per cent each time the production volume (i.e total accumulated experience) is doubled.[5]

The nature of conditions in which growth strategy may succeed and the outcome of such a strategy have been the subject of enquiry in a number of research studies in the United States. Buzzell, Gale and Sultan in their study found a positive correlation between growth and effectiveness as measured by profitability and other indices [6] In a study of 53 leading growth companies in the United States, Peter Gutman found that growth rates ranged upto 76.7 per cent annually. Firms with the highest growth rates were those which (a) chose industries where sales increased more rapidly than the economy as a whole; (b) concentrated on market segments within the industries which grew more rapidly than the industry; (c) entered the market earlier than competing firms, and (d) operated in multinational markets.[7]

The study of Chevalier and Catry which included three U. S. industries revealed that some growth strategies were more effective than others.[8]

Going by the experience of executives who have been on the look out and capitalised opportunities for growth, as well as the success attained by companies pursuing continuous growth as their primary objective, it would seem that growth is always preferable to no-growth or zero growth. But even if it is preferable, can a high growth rate be sustained over an unusually long period of time? This is a doubtful proposition, for there are compelling reasons which are bound to set the limit to growth sooner or later First, there are what may be called self-imposed limits. Growth strategy is one of the most difficult to manage. Once a company has reached what E. A. G. Robinson called the managerially optimum size, its effectiveness is bound to slow down with further expansion. Growth often hides serious underlying problems which do not come to light until the growth rate stops or a decline is experienced. The research findings of Easton and Wittenburt support this contention. The study of Wittenburt showed that as the rate of growth accelerated, there sets in a corresponding decline in profitability.[9] Easton found that beyond a certain size, the relationship between size and profitability tended to deteriorate.[10] In other words, companies which show impressive growth in their number of employees, products and sales do not always improve their profits. Citing the experiences of four companies that sought and achieved impressive growth through diversification and acquisitions, Lauenstein has shown how the problems resulting from expansion outweighed the opportunities.[11] The impressive growth rates of the giant companies in India that we mentioned earlier in terms of assets, sales and net worth, did not result in commensurate increases in profits or any significant rise in profitability ratios in 1980-81 as compared with the results of 1979-80. Gross profits increased by 14.3 per cent in 1980-81 against 19.3 per cent of 1979-80; pre-tax profits recorded a rise of 6.6 per cent and net profits of 16.6 per cent in 1980-81 against the percentage growth of 21.7 and 31.0 respectively in 1979-80.[12] The second category of limits to growth are the environmentally-imposed limits. These include the inevitable decline in population growth, scarcity of resources, the compulsion of protecting the environment, the side effects or technological advance, public attitude towards big business and government regulations.[13] Finally, as Schumacher has argued the cult of bigness and unlimited growth is self-destructive. To quote, "From the economic point of view, the central concept of permanence is wisdom. Nothing makes economic sense unless its continuance for a long time can be projected without running into absurdities. There can be "growth" towards a limited objective, but there cannot be unlimited, generalised growth ..... Permanence is incompatible with a predatory attitude which rejoices in the fact that 'what were luxaries for our fathers have become necessities for us'... Scientific and technological 'solutions' which poison the environment or degrade the social structure and man himself are of no benefit, no matter how brilliantly conceived or how great their superficial attraction. Ever bigger machines, entailing ever bigger concentration of economic power and exerting ever greater violence against the environment, do not represent progress : they are a denial of wisdom."[14]

The limits to growth notwithstanding, there are optimists who hold the view that although population will decline sooner or later there is no reason to believe that growth will be slowed down. The problems of scarcity of resources, pollution, and government regulation are temporary phenomenon. Improvements in management will soon provide a climate conducive to creative and innovative technology which will solve all the problems of humanity.[15] Will it be so? That is the question.

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