India: Gigantic corporate fraud at Satyam Computers deals body-blow to Indian elite’s global ambitions

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India's fourth-largest information technology (IT) company, Satyam Computers, is on the verge of collapse following its chairman's admission that for "several years" he fraudulently misstated the company's financial position, including cash on hand, revenues, profits and debt load.

In a January 7 letter to the company's board of directors, Satyam Chairman Ramalinga Raju said the company had US$1 billion less than claimed in its most recent quarterly report.

Satyam's share price has since fallen almost 90 percent and, in a desperate attempt to avert Satyam's outright collapse and reassure investors, the Indian government has replaced the company's boards of directors and promised a thorough and far-reaching investigation. The now-defrocked Satyam chairman, his brother and Satyam managing director, Rama Raju, and the company's chief financial officer, Srinivas Vadlamani, have been arrested, as have two PwC (PricewaterhouseCooper) auditors.

The fate of tens of thousands of Satyam employees hangs in the balance as its IT outsourcing rivals are busy poaching the stricken firm's contracts. Exactly how many employees Satyam has is unknown. It had claimed to have 53,000 employees, but Raju has said that his fraud included inflating the number of company employees by 10 to 12 thousand.

The unraveling of Satyam has delivered a staggering blow to the Indian political and corporate elite's global ambitions. The IT and IT-enabled (business-processing sector) of which Satyam was a "crown jewel" has been pivotal to India's recent economic expansion or "rise." Not only does the IT sector account for some 5 percent of India's GNP; it is the one technologically advanced sector in which India can claim to be a world leader.

The Satyam fraud threatens to undermine investor confidence in India at a time when the country's economy is already reeling from the world financial crisis and recession. In October and November, exports fell by more than 10 percent on a year-to-year basis. This fall represents a disaster in the making for the Indian elite since its plans to achieve 8 percent annual economic growth are predicated on boosting exports by more than 20 percent per year.

At the same time, foreign investment is drying up. The withdrawal of billions of dollars of foreign institutional investment has spearheaded a precipitous decline in Indian share values. Over the course of the past year, India's principal stock index, the Sensex, has fallen by almost 60 percent, from a record 21,206 points in early January 2008 to 8674 yesterday.

Satyam was no fly-by-night company. Sitting on its board of directors were some of the most renowned names in corporate India. Raju, Satyam's founder and principal shareholder, had been repeatedly hailed by the corporate elite and Indian business as a shining corporate role model. At a ceremony in London last September, he received the "Golden Peacock Global Award for Excellence in Corporate Governance for 2008" from Dr. Ola Ullsten, the former prime minister of Sweden.

An editorial in the London-based *Financial Times* said the Satyam fraud would not only damage India's software and outsourcing industry; it had raised "disturbing questions about the risks of doing business in India—and even the sustainability of the country's much-vaunted growth miracle."

After a relatively long period of silence, Indian Prime Minister Manmohan Singh described the fraud at Satyam as a "shocking development." Speaking at the annual "*Economic Times*' Awards for Corporate Excellence," Singh described Satyam (which ironically means "truth" in Sanskrit) as "a blot on our corporate image."

The Satyam episode "indicates," continued Singh, "how fraud and malfeasance in one company can inflict suffering on many and can also tarnish India's image more broadly."

In an attempt to prevent being tainted by the Satyam fraud, N.R. Narayana Murthy, the chairman and co-founder of Infosys, India's second-largest software-services company, urged investors and clients not to "overreact" to the scandal. Saying much more than he meant to, Murthy declared, "I believe that India's corporate governance standards are pretty much on par with the best in the world.... We have seen the debacles of Enron, WorldCom, Tyco and many Wall Street companies. That does not mean the standard of corporate governance in the United States is bad."

Satyam and India's political elite

Satyam was founded by the Raju brothers in 1987. It has offices in a number of countries including the US, Britain, Brazil, Singapore and Australia. Among its clients are Nestlé, the world's largest food company; Telstra, Australia's largest telephone company; Arcelor-Mittal, the world's largest steelmaker; and General Electric Co. Nestlé has said it is considering turning to other outsourcing companies to avoid any disruption to its IT operations.

While Satyam Chairman Raju has incriminated himself with his January 7 letter, there is much reason to believe that the letter was itself a lie, aimed at covering up that he had been systematically siphoning off funds to his other companies.

In mid-December, Satyam proposed to purchase the Raju family-owned Maytas Properties. But Satyam shareholders revolted against what they considered to be the wildly inflated price Satyam was offering. It has been suggested that in addition to being a means of further enriching the Raju family, the Satyam takeover of Maytas Properties was aimed at covering up years of looting of the IT firm.

What is incontrovertible is that the Indian political elite, especially in Andhra Pradesh (AP)—Satyam is based in the Hyderabad, the AP state capital—have lavished government contracts and other forms of patronage on the Raju family.

The former Telugu Desam Party (TDP) chief minister of AP, Chandrababu Naidu, routinely exalted the Satyam CEO, portraying him as almost a demigod. The current Congress state government awarded Maytas Infra—another Raju-owned business—a Rs. 120 billion (US$2.4 billion) contract to build a 71-km metro (rapid transit) system in Hyderabad, although Maytas Infra has no experience in metro construction.

Last month, the Congress state government of Y.S. Rajasekhara Reddy allowed Satyam to purchase 50 acres of land in a Special Economic Zone in Visakhapatnam, a port city in AP, at a cost of Rs. 1 million per acre, although the market price is Rs. 50 million per acre.

In the wake of the scandal at Satyam, Reddy has said the land deal will not be revisited: "It was for an institution and not an individual."

Raju has reportedly not been shy in speaking, while under police custody, about his close political connections. According to press reports, he has said: "I had the full backing of the powers-that-be. Otherwise, I could not have accumulated so much land in such a short period. I should say those in government departments openly supported our activities since they knew who were behind us. The land registration offices worked overtime and sometimes even on Sundays for our benefit. Of course we took care of the peripherals (transport, food and also entertainment) for those who were working for us."

Although he has not given details—let alone said how he and his companies "thanked" their political allies— Raju has boasted that his needs were attended to by both the current Congress Party state government and the TDP government that preceded it. "Naming people or parties will not help," said Raju. "I am also not naming which period either. I was given full access since they had confidence in whatever we were doing both before 2004 [when the Congress Party led coalition came to power, ousting the previous TDP government] and also now."

Raju has claimed that he sought to acquire large tracts of land as a buffer to fall back on if the US turned protectionist and sought to limit business-process outsourcing to India.

The Satyam boss reputedly told police, "It was my strategy—a buffer plan to hold on in the market in the event the US turned totally against outsourcing, an eventuality we all feared."

Meanwhile, the World Bank has revealed that Satyam and two other Indian IT companies—Wipro technologies, India's third-largest software services company with 95,000 employees worldwide, and Megasoft—have for some time been denied the right to do work for the World Bank because they engaged in corrupt or questionable practices. While the World Bank has provided few details, the companies are said to have devised means of benefiting World Bank staff, presumably for steering work in their direction.

The fraud at Satyam delivers a further blow to an Indian economy reeling from the world economic crisis. It also threatens to shed what for India's political elite will be most unwelcome light on the web of corruption and patronage that links India's corporate titans—dubbed India Inc. by their cheerleaders in the media—to governments and parties across India.