# Financial Liberalisation and Financial Fraud: Revisiting the 1990s

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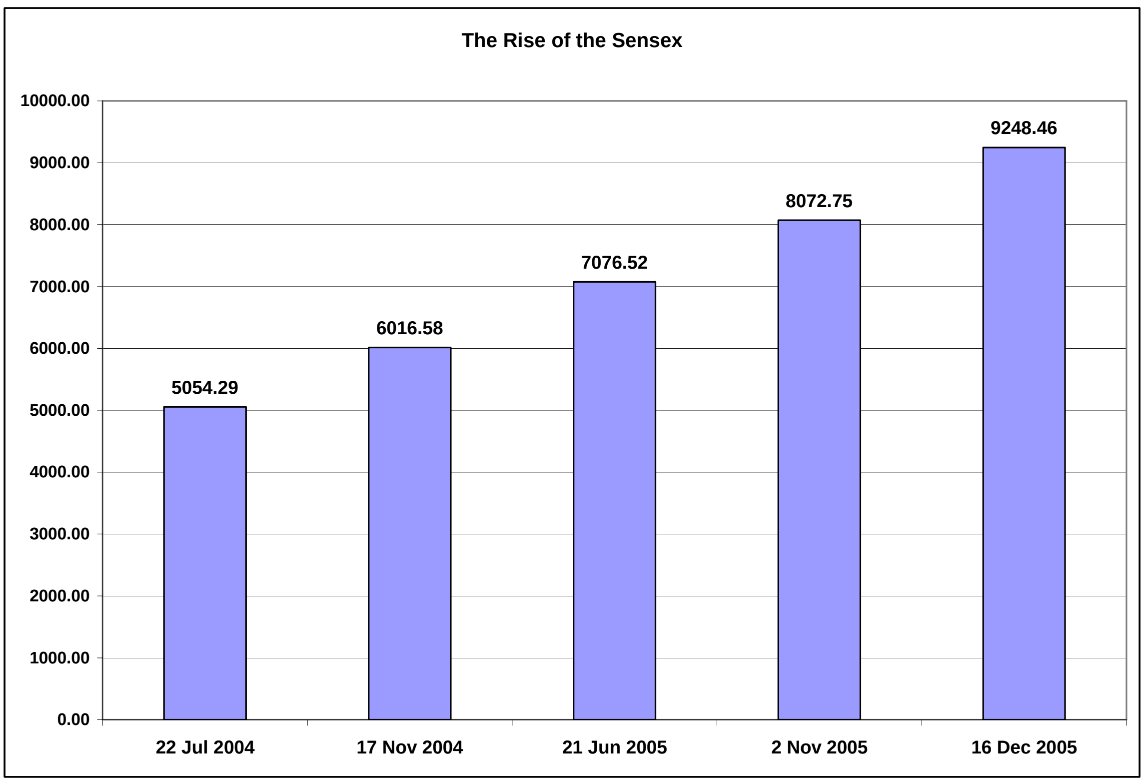
## Introduction

With the Bombay Stock Exchange sensitive index (Sensex) having temporarily settled above the 9000 mark, evidence of an unprecedented bull run on India's stockmarkets is now incontrovertible. Similar trends in the past have been followed by an unwinding process triggered by news of market manipulation or fraud of one kind or another. But this time around, both the government and the regulator, after initially expressing caution, appear sanguine.

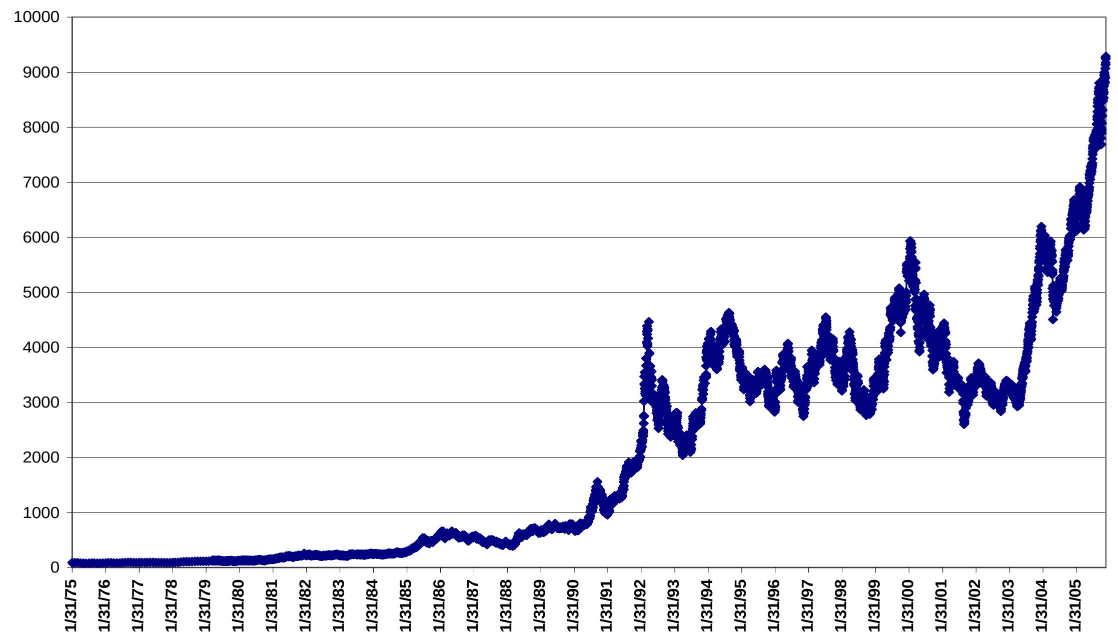
The rise of the Sensex has in fact been steep (Chart 1). Having closed above the 5000 mark in July 2004, it crossed 6000 in the middle November 2004, 7000 in June 2005, 8000 in November 2005 and stood above 9200 on 16 December 2005. This 82 per cent rise over a 17-month period and 53 per cent rise over just more than a year is indeed remarkable even by the standards of the post-reform years.

Chart 1




It is well recognized that stock market buoyancy and volatility has been a phenomenon typical of the liberalization years. Till the late 1980s the BSE Sensex graph was almost flat, and significant volatility is a 1990s phenomenon as Chart 2 shows.

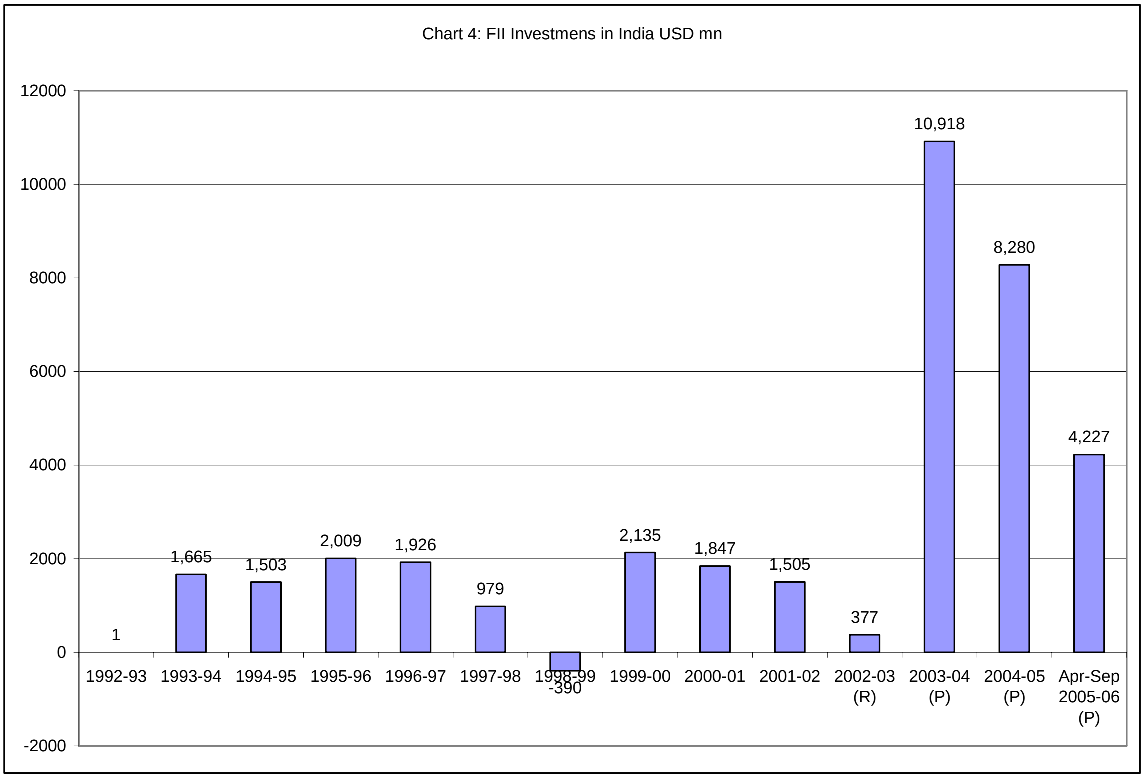
**Chart 2: Closing Value of BSE Sensex 1975-2005**




An examination of trends since 1988, when the recovery began, points to the extreme volatility in the Sensex during the liberalization years (Chart 3). And judging by trends since the early 1990s, the recent surge is remarkable not only because of its magnitude but because of its prolonged nature.

**Chart 3: BSE Sensex Since Liberalisation 1988-2005**

Those acquainted with the recent history of the market know that most peaks in the volatile 1990s scenario were the result of market manipulation of one kind or another, amplified by the role of foreign institutional investors who have discovered the Indian market since liberalization and targeted the country with large and volatile flows since the early 1990s (Chart 4).




Volatility is of course a result of the structure of India's financial markets. Markets in developing countries like India are thin or shallow in at least three senses. First, only stocks of a few companies are actively traded in the market. Second, of these stocks there is only a small proportion that is routinely available for trading, with the rest being held by promoters, the financial institutions and others interested in corporate control or influence. And, third the number of players trading these stocks are also few. According to a late 1990s Report of the SEBI's Committee on Market Making, "The number of shares listed on the BSE since 1994 has remained almost around 5800 taking into account delisting and new listing. While the number of listed shares remained constant, the aggregate trading volume on the exchange increased significantly. For example, the average daily turnover, which was around Rs.500 crore in January 1994 increased to Rs.1000 crores in August 1998. But, despite this increase in turnover, there has not been a commensurate increase in the number of actively traded shares. On the contrary, the number of shares not traded even once in a month on the BSE has increased from 2199 shares in January 1997 to 4311 shares in July 1998." The net impact is that speculation and volatility are essential features of such markets.

But any explanation of post-liberalisation trends must focus on some changes in the structure of India's stock markets during the 1990s. Till the late 1980s, India's stock markets were almost wholly dominated by the large financial institutions like the Unit

Trust of India and the Life Insurance Corporation, which made investments in corporate equity not so much with the intention of making large capital gains from wide swings in the Sensex, but of benefiting from the return offered by reasonable dividends. As a result, they tended to make their investments in select scrips of companies with strong fundamentals, and held these investments for long periods of time. The extent of trading in even the so-called "actively traded" shares was limited. This implied, on the one hand, that even though a few scrips dominated the Sensex, it was a good indicator of market activity, and on the other, that movements of the Sensex occurred within a relatively narrow range.

These characteristics of the market changed with the stock scam of the early 1990s, which saw speculative transactions in a wide range of shares, including new issues of relatively unknown companies. At one point in time, virtually any company could list itself and expect its primary share of offering to be oversubscribed. Further, shares that were actively traded could be purchased in relatively small lots and offered returns not so much in the form of dividends but through capital gains. This was when a number of small investors shifted out of bank deposits as their principal financial asset, to garner much higher returns from stock market investments. The entry of the small investor had two consequences. First, since such investors were driven by "market analysis" purveyed through the media and operated in herd-like fashion, wide movements in share prices, most often in the upward direction, was common. Second, the Sensex, while indicative of movements of leading shares, did not fully capture market activity. All this, however, came to an end when the scam responsible for driving the market to its frenzied heights could not be sustained. The market collapsed and a number of small investors, who bought close to the peak, suffered losses.

The consequence of that experience was two-fold. It resulted in a sharp decline in the direct participation of small investors in the market. To the extent they stayed, it was in the form of investments in mutual funds set up by the institutions. This also meant that principal buyers were the institutions who were choosy about the kind of shares they acquired. As a result, the market for initial public offerings dwindled and the secondary market once again came to dominate stock market activity.

Though similar to the scenario of the late-1980s, this situation was not a return to the past, when the domestic financial institutions dominated the market. Policy changes in the interim had altered the structure of the markets in one significant way. As part of its policy of financial liberalisation, the government decided in 1993 to permit foreign institutional investors (FIIs) to make portfolio investments in India's stock markets. In search of new opportunities to diversify their portfolios and hedge against risk, such FIIs soon discovered India as one more developing-country, emerging market. There were elements of both similarity and difference between the FIIs and the domestic financial institutions. The similarity was that they too were choosy about the shares they held, and concentrated much of their investments in leading shares despite repeated statements by observers that the FIIs are looking to diversify into equity of less well known and even unlisted companies. The difference lay in two features that influenced the investment strategy of the FIIs much more than the domestic financial institutions: at any point of time, decisions with regard to the quantum of investment in particular markets were determined by global factors, such the opportunities and risks in other "competing" markets; and, once investments were made, the objective was to maximise capital gains in the short run.

Given the huge funds at their disposal, even relatively small investments by the FIIs meant big money for stock markets in countries like India. That influence was visible even in 1994-95, when the ratio of FII investment to market capitalisation (1.1 per cent) was smaller than that for the domestic financial institutions (6.6 per cent). Hence, at the margin the impact of the FIIs on domestic markets are much greater than suggested by the share in capitalisation. With such significant operators in the market whose trading activity is driven by global considerations, medium-term swings in either direction were to be expected. Developments like the Mexican debacle, the return of Hong Kong to China, the collapse of Southeast Asian currencies or political uncertainty in India, result in a reordering of FII investment priorities in different emerging markets, with effects on the volume of gross and net FII purchases for a period of time. There is reason to believe that the medium term swings in Indian markets in recent times have been significantly affected by such global influences on FII investments.

Further, FII investments are also motivated by a desire to trade actively in pursuit of capital gains. This has forced the domestic financial institutions to take note and respond. As a result their trading activity has also increased substantially. This new revival in trading is however in relatively large lots and is confined to the shares of dominant companies. This has two implications. First, it increases the volatility of the Sensex. Second, movements in the Sensex do not capture the state of trading in the market as a whole, and conceal the fact that segments of the market like that for primary issues have virtually dried up.

Liberalisation and the entry of FIIs affect market behaviour through their implications for economic policy as well. Foreign Institutional Investors (FIIs), whose exposure in Indian markets is an extremely small share of their international portfolio, pursue international investment strategies that could involve periodically investing in or withdrawing from India. This forces government's, keen to have them constantly making net purchases and driving markets upwards, to bend over backwards in appeasing them. A corollary of this influence of the FIIs is that any market player who is able to mobilize a significant sum of capital and is willing to risk it in investments in the market can be a major influence on market performance.

For example, revelations of fraud, evidence of insider trading and a consequent collapse of investor interest led to an almost unstoppable downturn in India's stock markets after the presentation of the budget for 2001. This link with the presentation of the budget was not coincidental. The point to note is that the concern with attracting foreign capital flow has been reflected in the government's post-liberalization fiscal, monetary and financial policies. And budgets have been framed with the intent of not just satisfying financial investors from abroad but of attracting them by keeping financial markets buoyant. The spoken responses of financial agents and the activities as reflected by market indices were therefore seen even by the Finance Ministry, and not just by the media, as an indicator of success in budget formulation. This has meant that the pressure to please financial players has played a major role in shaping recent budgets, though, given the whimsical demands of finance, success is never guaranteed.

Paradoxically, for the speculator in the stock market this has provided another counter to bet on. Would the budget trigger a sharp rise in financial markets, however short-lived or would it not? Differing answers to that question would elicit different speculative responses. This was the question which Ketan Parekh, the most recent incarnation of the perennial 'big bull' in India's stock markets, had set himself and answered in the positive in February 2001. What ensued is now history.

Expecting to be able to offload stocks of a select set of companies at higher prices in the wake of the budget, Parekh built up large positions in these scrips. In normal circumstances, this very act of investment by a market-mover like Parekh should have provided a spur to the Sensex. It in fact did. Both just before the budget was presented and immediately thereafter prices did rise. But that very signal, gave cause for a bear cartel to turn suspicious. Allegedly consisting of stock-market insiders, including the BSE chief himself, who in violation of SEBI norms checked out from the surveillance department who was making large purchases and of which stocks, this cartel discovered that the rise in the index was the result of speculative purchases of select shares. In a world where financial gain, however garnered, is the indicator of success, the cartel chose to offload large volumes of the very same stocks acquired at prices much lower than those prevailing in the market, driving prices down. There must have been a brief period when Parekh struggled to keep prices of his favourite stocks buoyant in the wake of the bear hammering. But if he did, his effort obviously failed, paving the way for the downward descent of all stock market indices.

Not surprisingly, therefore, the recent spurt in the market has been associated with an unusual intense interest of foreign investors in Indian markets (Chart 4). The question that arises is whether this trend has been accompanied by any other tendencies which could make the current boom different from previous surges.

A notable feature of previous surges was the presence of individual manipulators, such that any post-1990 history of the stock market would be replete with names of "rogue" players such as Harshad Mehta, Chain Roop Bhansali and Ketan Parekh, besides domestic and foreign banks and institutions, including Credit Suisse First Boston. The nature of the scam in each case involved, therefore, two sets of issues: first, the source of the large funds needed to indulge in the scam; and second, the specific way in which the market had been manipulated.

The first of the major scams relating to 1991-92 involved the siphoning of funds from banks and public sector units through transactions in securities, arranged through brokers, that were in violation of rules relating to permitted activities and investments. In hindsight, the extent of the surge in the market created by this scam, estimated to have involved transactions to the tune of Rs. 12.9 crore, was much less than the volatility experienced in subsequent instances of manipulation. This was probably because FIIs were still to enter the market then and amplify fluctuations with their own speculative investments.

But the influence of financial liberalization was visible. The parallels between two episodes in India's recent financial history- one identified with Harshad Mehta and the other with Chain Roop Bhansali - are obvious. Both began as one among the small and ambitious men who people Dalal Street. Some unidentifiable combination of intelligence, nerve and fate allowed them to get ahead of the pack. Soon they were 'picked up' by the financial system, the government and the media, and portrayed as the stuff which India's "maturing" financial sector should be made up of - intrepid, market-savvy but trustworthy managers of other people's money. Being chosen had its merits. Their business empires grew rapidly with new companies being created even faster than the pace at which the funds they managed grew. Those empires were complex networks of companies, investments and people (spread across the financial sector, industry and the government) whose very inscrutability enhanced the aura that surrounded them. But at the centre of it all was the one individual whose publicised financial genius and integrity generated investor confidence.

The growth of these empires was however driven not just by the sagacity of these individuals. Four other "fundamentals" had to be in place. First, financial liberalisation, which on the one hand allowed the banks and the financial institutions greater flexibility in determining their portfolios, and on the other forced them to seek greater profits on investments in order to meet the situation created by a regime in which new and old players sought to attract domestic savers with the promise of higher returns. Second, the inability of the formal financial sector to make the kind of speculative and risky investments needed to earn high returns, necessitating a "bridge" in the form of a "fund manager" outside the pale of the formal sector. Third, a desire by corporations to use the financial sector to both mobilise capital as well as balance the low profits from real investments with "other income" derived from investments in financial assets. And, finally, the desire of the government, especially the finance ministry, for financial buoyancy of a kind that would keep the confidence of NRI and foreign institutional investors, whose investments beef up reserves even when India's balance of trade is under strain.

Without this combination of supportive factors, there was no way in which these "money managers" could in a short period of time raise the volume of funds they controlled to the astronomical figures they did reach. The CRB group did raise money from the public through fixed deposits and equity issues, but success on that front itself depended on the size of its transactions with the formal financial system. There were many sources of formal finance such as: borrowing from banks and housing finance companies often against non-existent assets; investments by agencies like the UTI and the Gujarat government often through private placements; investments in CRB Mutual by corporations who allegedly expected the funds to be utilised to prop up their own share values as a quid pro quo; and accommodation by the State Bank of India in the form of encashment of interest and deposit warrants even when there were no balances in the CRB accounts concerned. The credibility which such transactions managed to generate, and policy decisions such as the high credit rating given by CARE, the permission to set up a full-fledged bank provided by the RBI and grant of tax exemption for its Power Bonds by the Central Board of Direct Taxes, allowed the group to mobilise huge amounts from the public. Having been picked as a winner, Bhansali got the support needed to win small investor confidence in his extremely attractive deposits, and that confidence seemed to justify official efforts to bolster the growth of his empire, even if there was reason to believe that Bhansali was meeting past obligations with new loans or investments.

This deep involvement of virtually the whole system with the CRB group implied that neither the government nor the autonomous agencies like the RBI and SEBI could afford to curb its growth. There were two reasons: first, Bhansali, like Harshad Mehta earlier, was a creation of and represented the success of the new financial regime instituted by the government; second, once he had got going, there was so much at stake that every effort had to be made to sustain his empire. This was also important because a collapse of the group could set off a run on the deposits with other Non-bank Financial Companies making nonsense of the government's claim about financial buoyancy. For all concerned, there was no going back. The net result was that even a host of violations of the law by the group were suppressed when discovered. According to reports, evidence of tax evasion to the tune of Rs.5 crore unearthed in a raid in 1993 has not led to any penalty or settlement. As far back as June 1996, the SEBI, after inspection of the finances of the group held back clearances for any new mutual fund schemes and ordered an audit enquiry. However, a month later, the RBI granted "in principle" clearance for a CRB bank. Two months later the RBI discovered a number of irregularities in the functioning of the group and put the clearance on hold, but the CBDT under the finance ministry subsequently provided tax rebates for the power bonds which were to mobilise more money from the market for the group. The mirror image of Mr.Bhansali mobilising more money in the market to meet past commitments was a set of government agencies providing new clearances in the hope that the performance of the group would justify their past errors. Even if it could be argued that these agencies functioned in a non-coordinated manner, each ignorant of the actions of the other, there is little doubt that an "apex agency" like the Finance Ministry would have been privy to all the information.

Unfortunately for all of them, with performance belying hopes, the group soon began defaulting on its payments. Since those affected were not just the big players in the financial system and the government, but small time investors, there was no way in which the matter could be dealt with within the confines of the financial system. As soon as the government and the regulatory agencies began to act, even if belatedly, the groups activities virtually collapsed, necessitating an official freeze on its activity and assets. Discounting details on the precise nature of the activities indulged in by the two groups, the similarity of the CRB fiasco with the Harshad Mehta episode is striking.

But the similarity does not end with the growth experience and performance record of the two groups. It shows through in the salvage operation as well. The thrust of that operation is to deflect attention from a holistic picture which suggests that the drive towards financial liberalisation in India and the emphasis on financial buoyancy explains much of what happened. Rather, criticism is focused on individual members in the banking system, such as the managers who accommodated interest and deposit warrants, and on specific failures, perhaps even of individuals in the regulatory apparatus consisting of virtually the entire sphere of government responsible for financial transactions. Some have dismissed even such criticism. The then Finance Secretary Montek Singh Ahluwalia has gone on record to state that the CRB scam cannot be attributed to the failure of the regulatory system, since "no regulatory framework ensures that fraud can be prevented" (Interview in the Pioneer dated June 5, 1997). Hence, in his view it is not the government's responsibility to protect investors when NBFCs collapse, since "investors know they are taking a risk". The scam according to him only shows that "grey area companies are risky".

There is an element of candidness in this response, since it implicitly admits that it is not the weakness of the regulatory mechanism that the CRB scam exposes, but the inability of the financial regime to preempt fraud and failure and protect investor interests. A policy which promotes greater inscrutability in the financial system cannot ensure its regulation as well. After all it was not just the public, but the RBI, the SEBI and the Finance Ministry that were fooled by this "grey area company".

More recently, however, the role of individual players in determining surges and slump seems to have receded, even while speculation plays a role. Consider for example Black Tuesday, April 4, 2000. On that day players on the Bombay Stock Exchange displayed nerves of cotton wool. The BSE Sensex, which closed at 5,052.94 points the previous day, collapsed to an intra-day low of 4666.95, and recovered only marginally to 4691.46. This single day loss of 361 points was reportedly the "seventh largest single day loss in India's capital markets", and the highest decline since the stock market scam of the early 1990s. It was when the latter scam was revealed and leading player Harshad Mehta arrested, that the Sensex fell by 570 points in a single day on April 28, 1992. That was a Black Tuesday too, but one which came in the wake of an engineered, speculative boom in the stock markets. This time around there was no obvious scam to nail, though the volatility in the markets on, prior to and after that day suggests that speculation ruled India's financial markets. We must recall that the Sensex which stood at 5375.11 at the end of the first trading day of 2000, fluctuated around that level till early February, then rose dramatically from 5313.59 at the end of February 4 to 5933.56 by the end of February 13, and then slipped gradually to reach its April 4 closing of 4691.46.

The evidence pointing to speculation is in fact abundant. In February, price-earnings ratios in the case of many stocks, especially those from the much-celebrated new economy, had touched levels that were not warranted by even the most optimistic estimates of future earnings of the firms concerned. Few believed that such prices were "real" or could be sustained. But yet prices remained high because those bereft of such stocks wanted in, and those holding them dared not dump them for fear of losing out on further highs. The collapse, euphemistically termed "correction", of that speculative rise in stock price, had to wait for the weakest nerves to give. And Tuesday the 4th they did.

In normal circumstances, speculative losses are considered just recompense for those taking more from the till than their palms can hold. But not so in post-liberalisation India. Virtually ignoring the obvious role of speculation, the government set about searching for reasons to explain market nerves, so as to respond to them. Two came in handy. First, notices served by India's income tax department, on a set of foreign institutional investors, demanding payment of close to Rs. 9 crores, in view of their avoidance of capital gains tax. The IT department's notices were based on a presumption that companies that were not eligible to avoid paying tax in India under the terms of the double taxation agreement between India and Mauritius, had claimed such benefits. And, second, signs of a collapse of a similar boom in the Nasdaq, the New York index of high tech stocks.

The response to the first was indeed appalling. It is now well known, that using the benefits of India's double taxation treaty with a quasi-tax haven like Mauritius, companies were routing all their investments through that country. According to reports there were around 150 companies "based" in Mauritius that had investments in Indian markets. According to one estimate, these firms accounted for close to two thirds of the cumulative $11.4 billion portfolio inflow into India till April 4. However, given the income tax department’s reading of the terms of the treaty, it had made clear that it did not consider all these companies as meeting the criteria rendering them eligible for the benefits of the treaty. In fact, in assessments conducted till then, there are 24 companies that have been allowed the benefits, and a similar number of companies who have been certified as ineligible. It was to some of the latter that the notices had been served.

However, when the Income Tax Department chose to launch limited action against those it felt were wrongly using the terms of the agreement, an expected "correction" of a speculative boom in the market was attributed to FII disappointment with the action. The fact of the matter is that, FII investments hardly turned negative in the wake of that action. It is true that net FII investments fell from $99.3 million on 2 April 2000, to $24.3 million on April 4, the fateful Tuesday. But a positive net investment can hardly be a cause for a collapse in the Sensex. Moreover, such volatility is typical of FII net investment flows, which, for example, fell from $363.2 million over December 1999 as a whole to $34.8 million in January 2000, only to rise sharply to $639.4 million in February and fall again to $244.1 million in March. In any case, the rather moderate rates of capital gains taxation in India can hardly dampen investor sentiments. Despite all this, the government responded with unusual alacrity to (engineered?) market rumours that the tax notices had set off the April 4 slide and issued a clarification that very day that the action would be put on hold. By ensuring large FII flows through financial liberalisation, the government has rendered India vulnerable to a sudden withdrawal of such capital. This vulnerability is now being provided as the reason for subordinating domestic policy to the requirements set by *perceived* FII sentiment.

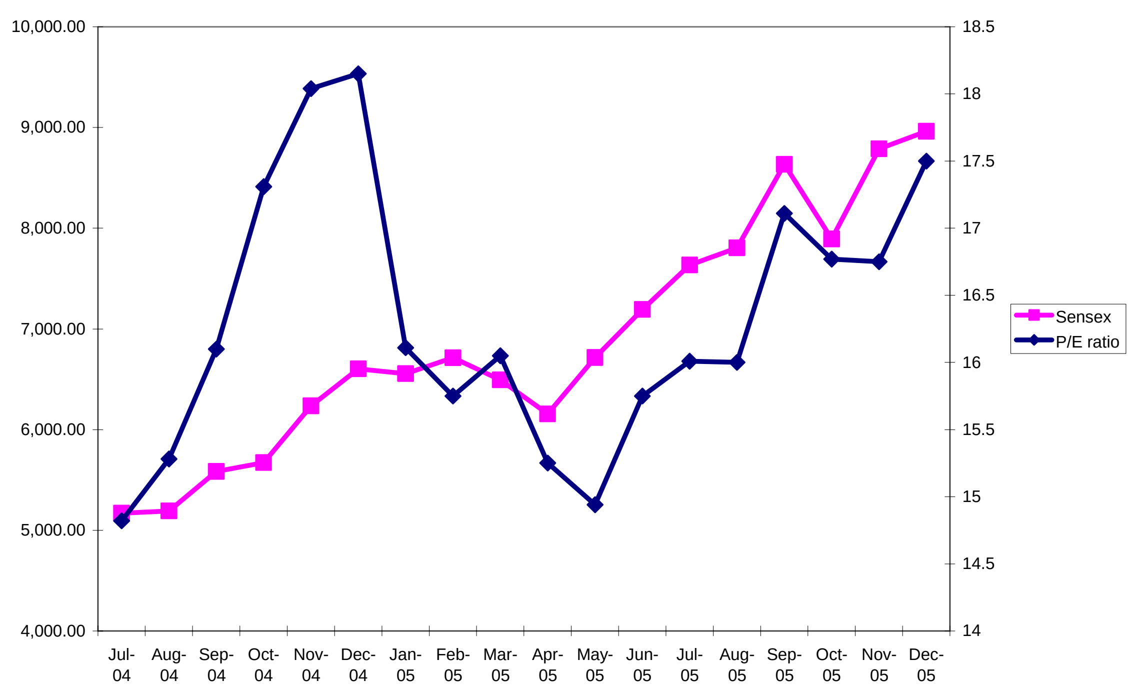
"Perceived" because in hindsight, it appears that the second of the factors quoted above, namely "Nasdaq sentiment," appears to have been the likely cause for the April 4 slide. Through March, new economy stocks in the US have been under stress, as investors who were betting on companies that had been toting up losses for months on end, had begun to loose nerve. This was aggravated by two other developments. A spate of auditor's reports pointing to questionable accounting practices as well as clear signs of lack of viability in the case of a number of "new economy" firms. After a number of days of almost repeated losses, on Tuesday the 4th, the Nasdaq plunged 13 per cent by mid-day. Though the index recovered subsequently, it was clear that the high-tech stock boom in the US had lost its vigour, even if it had not fully collapsed.

This experience should have had only a marginal impact on India. The growing number of internet-based, dotcom companies were yet to dominate the market here, being predominantly financed by venture capital firms, whose funds were being poured into advertising in order to attract clients and consumers to new sites and portals. However, there were other factors that could have resulted in the Nasdaq developments influencing market sentiment in India. To start with, much of the boom in the market had been focused on "new economy" firms from the IT and entertainment sectors. As a result, price earnings ratios in the case of these firms had reached astronomical levels, making it clear that there was little likelihood of the actual performance of these companies matching the expectations implicit in those ratios. The losses of dotcom firms that appeared to be spiking the internet bubble in New York, had a parallel here in the form of the inadequacy of actual relative to implicitly expected profits of a few new economy firms that dominated the market. At the peak of the February boom, one such firm (Wipro) accounted for 15 per cent of market capitalisation in the BSE and the combined market value of around 150 software companies accounted for 32 per cent. This compares with the fact at the beginning of the 1990s, these companies hardly featured in the BSE. Every major fund manager had created a special fund for investment in what were seen as hitech stocks. The realisation that such stocks were not the best buys would, therefore, have affected market sentiment at the margin.

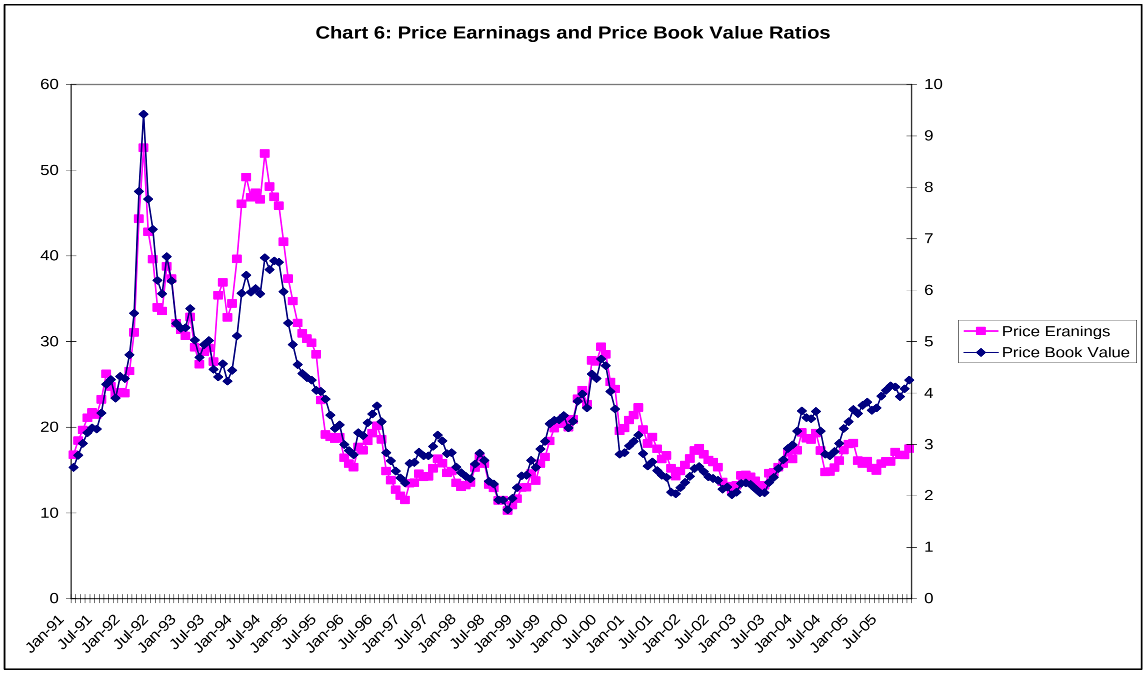
This transition away from a situation where individual “rogue investors” were responsible for episodes of speculative booms in the market is now being used to explain away the recent surge in the market. Government spokesmen who were earlier making a case for caution are now treating the surge as normal, on the grounds that it is being driven by improved corporate performance. Two kinds of numbers are being quoted to defend such an argument. First, it is being argued that the performance of manufacturing and service companies has recorded remarkable improvements. And, second, the effects of this are reflected in “comfortable” price-earnings ratios, even as stock prices are registering remarkable increases.

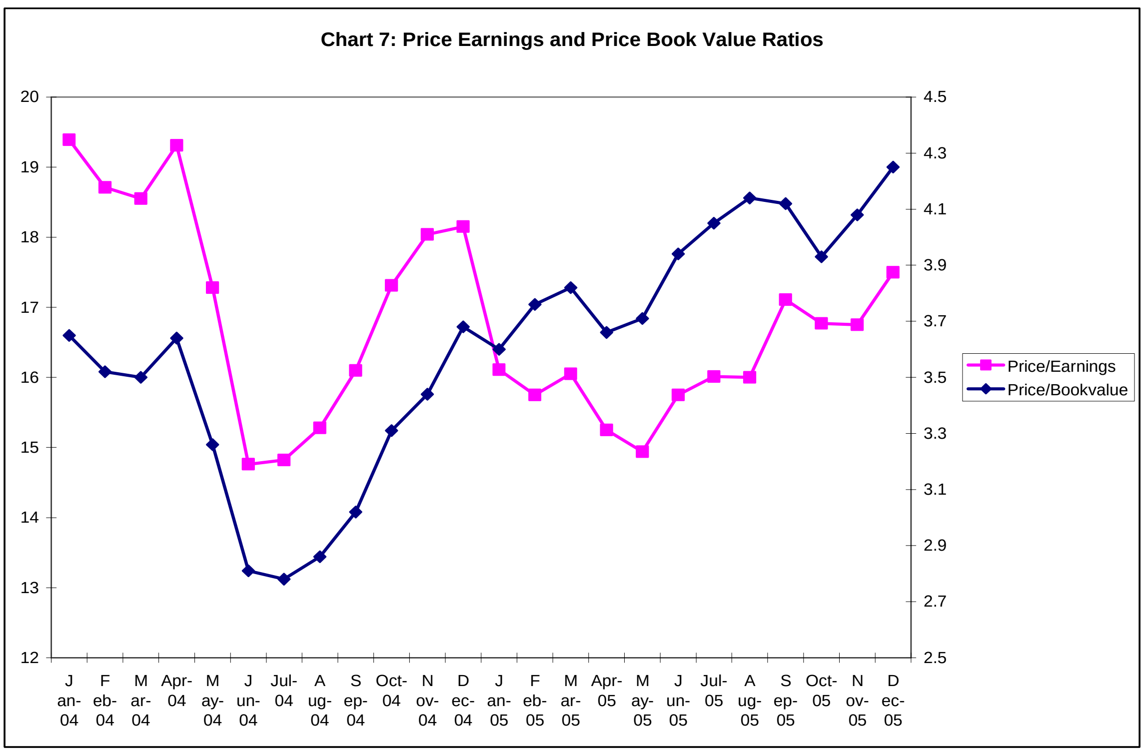
This view is to an extent exaggerated. As Chart 5 indicates, the surge in the Sensex in recent months has been accompanied by a rise in the Price-Earnings Ratio. In fact, the two graphs show very similar movements. However, a P/E ratio of 17.5 is relatively low, and it is even lower than levels it had touched in December 2004 when the Sensex was much lower.

**Chart 5: Closing Sensex and P/E Ratio**



In fact, a puzzling feature of recent trends in the market is the relative movement of prices and earnings. Chart 6 provides a comparison of Price to Earnings and Price to Book Value Ratios since the early 1990s. It shows that, while in the past these ratios tracked each other quite well, more recently the ratio of price to book value has risen ahead of the price earning ratio, resulting in an unusual divergence. In fact, the Price-Book Value Ratio which was below the Price Earnings Ratio has now risen well above the latter (chart 7).

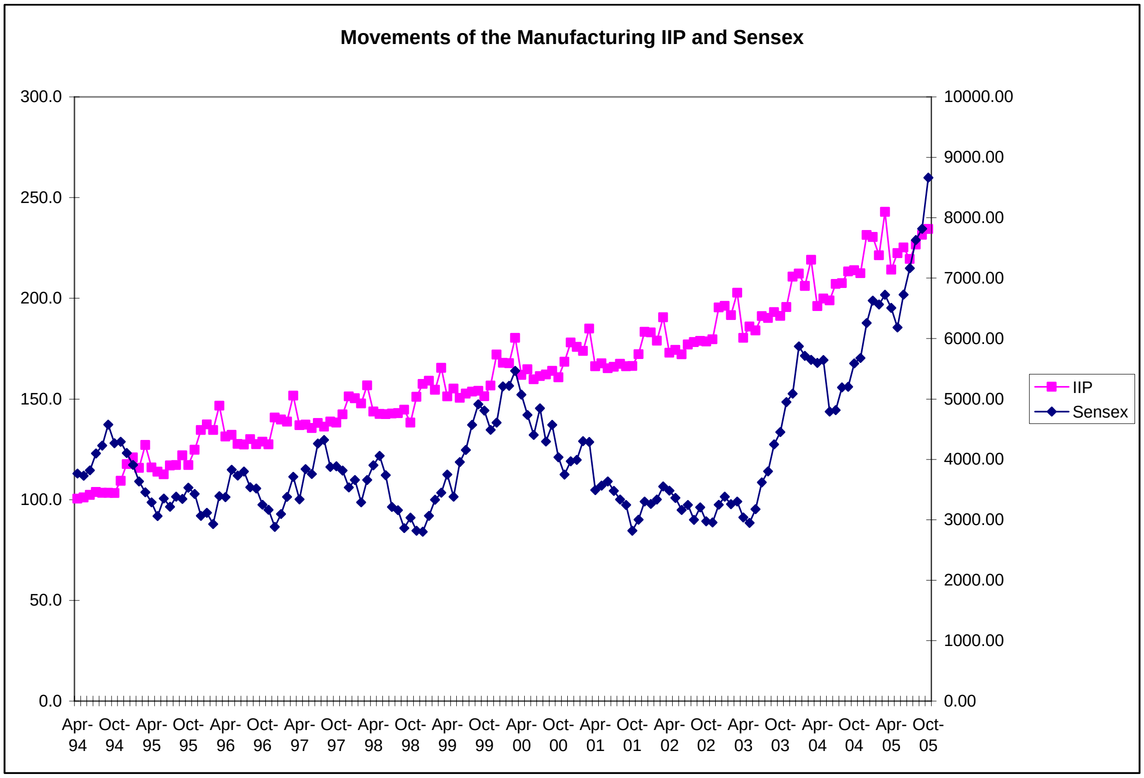


The implication of this should be obvious. Corporate performance has improved so remarkably in recent months that despite the price surge, the price-earnings ratio has remained at comfortably low levels.

The puzzle then is the remarkable rise in corporate earnings. It is indeed true that the Index of Industrial Production does point to an improvement in manufacturing performance in recent months. But that in itself cannot explain such a sharp improvement in earnings. In fact, there appears to be no relation between the movement in the manufacturing IIP and the Sensex (Chart 8).

Chart 8




There could have been other factors. What is crucial is this should not include the manipulation of accounts aimed at driving up stock prices, with the aim of using high stock market values to issue new capital at a premium and substantially bring down the cost of capital. If it is, then the recent spurt of FII investment driven by attractive P/E ratios could turn into an exodus.

We must recall that the late 1990s boom in US stock markets was sustained through accounting fraud that afflicted even leading companies and the subsequent crash was spurred by revelations of such fraud. Charges of accounting fraud have been levied against Enron, Adelphia Communications, Tyco, Peregrine Systems, Global Crossing, Worldcom and Parmalat among others.

The following quotation from a New York Times Report is instructive: “The fraud went on and on for more than a decade. The auditors never noticed. That was the image that emerged .. as Italian investigators said they had learned that Parmalat's fraud began more than a decade ago, around the time the company went public in 1989 and long before it became Italy's largest food company. The collapse of Parmalat has produced inevitable comparisons to Enron, which, like Parmalat, used related companies in the Cayman Islands and elsewhere to hide some of its odd transactions. But the closer comparison may be to CUC International, which held the title of largest American accounting fraud until it was eclipsed by the wave of frauds that have come to light in the last two years.

CUC International, formerly known as Comp-U-Card, grew rapidly through the 1980's. Extensive fraud there, which involved inventing most of the profits the company ever reported, began about the time the company went public in 1983, according to former officials who have since pleaded guilty to fraud charges. It led to what was called the largest accounting fraud ever when it was finally exposed in 1998."

India has successfully, even if prematurely, absorbed much from the West: rapid services growth, an IT spurt, and a dot com boom and bust to name a few. Hopefully, accounting fraud to trigger stock price inflation is not among them.