Overview

In 1999 an English teacher in Hangzhou, China, started a company in his apartment connecting small Chinese exporters to potential customers abroad. The teacher was Jack Ma. His company, Alibaba, has made him the richest man in China today. Starting with 18 friends and students, Ma has built his company into one that employs 24,000 people and moves more goods than Amazon and eBay combined. In September 2014, Alibaba issued the largest global initial public offering in history, when its market value surpassed that of Facebook. Alibaba's market capitalization overtook that of Walmart and GE a few months later. Jack Ma is worth an estimated $21 billion.

After working in the pharmaceutical distribution business, Dilip Shanghvi borrowed 10,000 rupees (about $1,000 in the 1980s) from his father to start a drug company. His company, established in 1983, produced lithium, a medication to treat bipolar disorder. The company made its first sales in 1987 and started exporting in 1989 and carrying out research in 1991. Sun Pharma went public in 1994. In 2014 it was worth $27 billion, making Shanghvi (worth $12.8 billion) the second-richest man in India. Sun Pharma is the largest drug company in India, employing 16,000 people.

In 1959 Ahmet Nazif Zorlu dropped out of high school at age 15 to work in his family's small textile business in Babadag, Turkey, a mountain village the size of Luray, Virginia. By the mid-1970s, Zorlu was the boss. He embraced technology, logistics, and global markets, transforming the company into a mega-factory producing curtains and polyester yarn. By the 1990s the company dominated world markets in these products. It expanded into other industries, applying the same modern production and distribution techniques Zorlu had brought to textiles. One of the most notable acquisitions was Vestel, a bankrupt television manufacturer. By 2000 the revamped company had captured one-quarter of the European television market and was a major exporter of washing machines and refrigerators. The Zorlu Group employs 30,000 people and accounts for more than 3 percent of Turkey's total manufacturing exports. Ahmet Nazif Zorlu is worth $2 billion.

These three success stories tell a story that is strikingly at odds with conventional wisdom about the rise of wealth in recent years in developing countries. The examples demonstrate that prosperity is not necessarily a result of crony capitalism, unfair business advantages or control of natural resources, monopolies, and favoritism. In fact, a new billionaire class has emerged that is testimony to innovation, creativity, ingenuity, and other capitalist skills traditionally associated with advanced economies. Far from disadvantaging poor and middle-class workers, these billionaires have compiled an impressive record of providing employment opportunities that have raised living standards and increased economic stability in countries that have not always enjoyed success in these areas.

The examples of Ma, Shanghvi, and Zorlu tell only the beginning of the story. In China the leaders of globally ranked companies like Huawei, Lenovo, Alibaba, Xiaomi, ZTE, Hisense, and Tencent are all worth hundreds of millions of dollars or more. Knowledge- and technology-intensive industries now account for 20 percent of China's GDP, four-fifths of which comes from private firms. Shanghvi is one of a number of pharmaceutical leaders in India: Dr. Reddy's Laboratories Ltd., Cipla, Lupin, Aurobindo, Cadila, Jubilant, Ipca, Torrent, and Wockhardt are among India's largest companies. All have annual sales of more than $1 billion, and most have manufacturing plants outside of India; many of their founders are billionaires. India is now the third-largest pharmaceutical producer in the world.

Thanks to Zorlu and other appliance producers, Turkey has become known throughout Europe for high-quality, low-price durable goods. Along with Vestel, the Turkish giant Arcelik is home to the Beko brand and part of Koç Holding, which accounts for 8 percent of Turkey's GDP and 10 percent of the country's exports. It is the only Turkish company in the Fortune 500. The Koç family is among the wealthiest in Turkey.

Entrepreneurs who build large companies are becoming increasingly common in emerging markets.[1] Before the growth spurt of the 2000s, the

1. For expositional purposes, the terms *developing country*, *emerging market*, and *South* are used interchangeably to refer to countries outside the high-income OECD. The terms *advanced* or *developed countries* and *North* refer to high-income OECD countries.

vast majority of the superrich outside advanced countries inherited their wealth, made it from resources, or reaped unearned benefits accrued not from productive investment but from government connections, government-sanctioned monopolies, or privatizations that benefited people with connections. This group of so-called rent seekers or rentiers got rich not from supreme talent or innovation but because of commodity price movements and/or government connections.

Today an expanding group of successful emerging-market entrepreneurs building large companies is getting extraordinarily wealthy. Many are transforming global markets as their companies compete for customers and investment opportunities around the world. In 2004 just 20 percent of the 587 billionaires identified by Forbes in its World's Billionaires List were from emerging markets. A decade later 43 percent of the world's 1,645 billionaires were from emerging markets. More than 500 emerging-market fortunes were added over this period, and founders of non-resource-based, nonfinance companies contributed more to that growth than any other group.

These gains are reflected in the lists of the largest companies, which show a similar trend. Emerging-market firms made up 30 percent of the 2014 Fortune 500 list, more than twice their share a decade earlier. Forbes Global 2000, a list of the world's 2,000 largest companies, shows the same expansion. Given current trends, by 2025, 45 percent of Fortune 500 companies and 50 percent of the world's billionaires are expected to come from emerging markets.

These business leaders are helping drive emerging-market growth. Because an increasing share of the new money is earned from innovative companies, as opposed to rents and inheritance, it is associated with job creation and growth. The effects are extending beyond local markets. Many entrepreneurs are gearing their products to foreign markets, building subsidiaries around the world, and enhancing global competition. Although a sizable share of wealth still accrues to owners of property and resources (inducing distributional rather than productive consequences), large-scale entrepreneurship is growing rapidly in the developing world.

Tycoonomics: Big Firms, Big Money, and Development

This book argues that the creation of large corporations and the accompanying rise in extreme wealth are inevitably part of the development process. The record suggests in case after case that as countries develop, a handful of exceptionally productive firms grow rapidly and become giants, making the founders spectacularly wealthy. Even when foreign investment catalyzes the process, the economic transformation happens when large-scale domestic entrepreneurship follows. The new company leaders are not satisfied with dominating local markets. Their mega firms are increasingly targeting global markets. Many operate production facilities around the world, and some are buying and restructuring well-established firms in advanced countries.

Successful companies are not just a product of the development process. They add to that process. One way that company founders in emerging markets contribute to development is to provide more and better jobs through the firms that they create. They accelerate the normal development process in agrarian-based poor economies by pulling resources out of subsistence agriculture and into industry and services, expanding the middle class. It is not a coincidence that all countries that have developed rapidly over the past 200 years have experienced some version of this process of "tycoonomics."

In principle, extreme wealth is not a necessary ingredient for development to occur. The majority of firms in an economy could grow relatively rapidly, yielding modest wealth for many, without extreme wealth. But this does not happen in practice. Alternatively, state-owned firms could drive industrialization, but such firms have been incapable of producing sustainable growth. Achieving more than a decade of strong growth requires vibrant private sector, where new firms drive out weak firms and the strongest firms grow very large. In fact, a growing body of evidence shows that a relatively small number of privately owned superstar firms with stellar growth supports rapid economic growth better than either broad-based growth across most firms in an economy or the rise of state-owned firms. The smartest, pushiest, and luckiest of the founders of this group of firms become the superrich.

The importance of a few large firms in driving growth is an illustration of the first principle of economics: that when resources are scarce, the allocation of capital and labor is critical to a country's potential output. Until recently, economists thought that only the allocation of capital and labor across industries was important. If capital and labor flowed to the sectors where they were used most productively, a country would grow rapidly. Recent research, using newly available firm-level data, shows that some firms are many times more productive than others, even within the same sector. As a result, not only is growth stronger when capital and labor flow to the sectors where they are most productive but also the resources must move to the most productive firms in those sectors. For example, if capital is more productive in the cloth sector than the food sector, raising incomes is not just about pulling capital out of food and into cloth but also about pulling resources to the most productive firms in the cloth sector. Accordingly, growth in a small number of superstar firms that use capital and labor most efficiently is an important factor in economic development.

Structure of the Book

This book is divided into four parts. Part I develops a system of classification, or taxonomy, of the superrich and their sources of wealth, splitting them into five categories:

1. people who inherit wealth,
2. company founders,
3. company executives,
4. government-connected billionaires whose wealth derives from natural resources, privatizations, or other connections to the government, i.e., rent-related billionaires, and
5. finance and real estate billionaires.

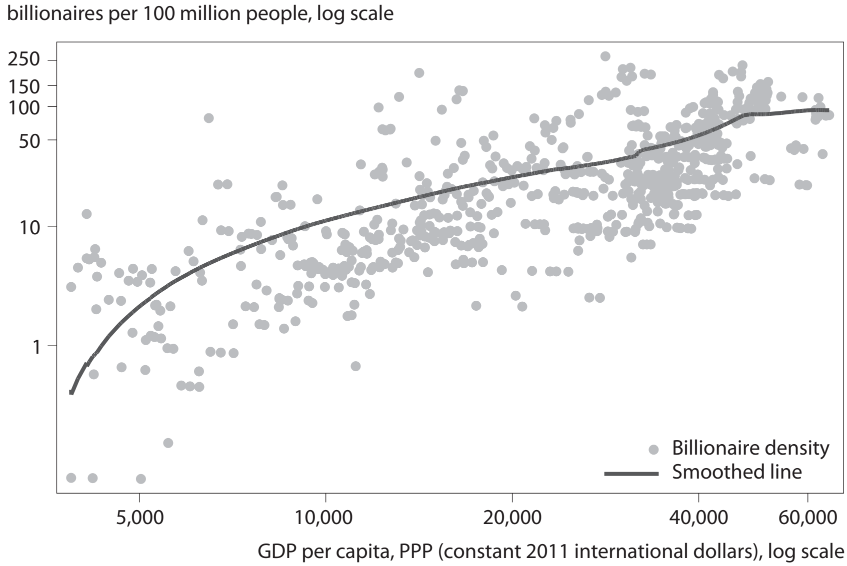
The most surprising conclusion resulting from this taxonomy is the significant shift between 2001 and 2014 to company founders and executives in emerging markets (and the slight decline in this group's share in advanced countries). Among the superrich in emerging markets, company leaders are twice as prevalent as they were in 2001. This shift took place despite soaring commodity prices, which pulled capital and labor into those rent-related sectors in many emerging-market countries. The shift, moreover, is absent in advanced countries, despite the rise of new technology giants. This part of the book examines the sectors and countries that are a main force behind the change. It highlights East Asia, the most dynamic region, and the Middle East and North Africa, the only emerging-market region in which the share of inherited wealth expanded and the share of company founders declined.

Part II attributes the expansion of wealth to the role of large firms, and even individual firms, in economic growth. Three important trends are occurring in many emerging markets: the rise of mega firms, the emergence of extreme wealth, and rapid income growth. The evidence suggests that the three trends are closely related. Recent research shows that when economies perform well, the most productive firms grow rapidly. Development requires reallocating resources to highly productive firms and allowing them to mature into mega firms. The development of the mega firms helps to transform a country's economic structure as these firms pull workers out of agriculture and into industry. The firms tend to be in internationally competitive industries and thrive because they are among the best in the world at what they do and are competitive on global markets. As these firms attract more resources, the wealth of their founders grows.

The emergence of mega firms in the fastest-growing emerging markets is similar to the growth of big business during the rapid modernizations of the United States and Europe in the late 19th and early 20th centuries, Japan after World War II, and Korea in the 1960s and 1970s. The economic historian Alfred Chandler (1992) has demonstrated the crucial role of big business in creating economic growth during these episodes. Much of what he has written applies to the more recent modernizers. For example, mechanization of food packaging allowed family-owned companies like Heinz and Campbell Soup to thrive in the United States, just as innovation has allowed Tee Yih Jia Foods (the world leader in spring roll pastry) to thrive in Asia and M. Dias Branco (a leading manufacturer and distributor of pasta, cookies, and other goods) in Latin America. The chemicals industry in Germany developed because BASF, Bayer, and Hoechst exploited returns to scale. The Indian chemicals industry is now charting a similar path. The role Chandler envisions for big business in economic development is as visible in the emerging markets now as it was in advanced countries, with the fastest-growing countries recording an increasing share of the world's largest companies.

The relationship proposed here between extreme wealth and development follows from the association between big business and development, such that they all move together. The evidence indicates, moreover, that extreme wealth not only is associated with development but also in fact contributes to it. Figure O.1 shows a scatter plot of the number of billionaires per million and GDP per capita. The two are tightly linked, especially during the period of structural transformation, when economies move out of agriculture and into industry. Over the past 15 years, for example, China's per capita income rose from less than $3,000 to more than $10,000 (in 2011 purchasing power parity international dollars); the steep slope indicates that the wealthy population grows especially rapidly during this stage. When countries are very rich, the relationship is flatter. Part II of the book presents evidence that a higher density of extremely wealthy people is associated with structural transformation in emerging markets but not in advanced countries. Controlling for the level of development, more billionaires per capita is associated with more employment in industry and less in agriculture. The section also shows that trade is more important for emerging-market companies and their owners than it is for advanced-country firms and their owners.

Figure O.1 Correlation between density of billionaires and stage of economic development



PPP = purchasing power parity

Sources: Data from Forbes, The World's Billionaires; and World Bank, *World Development Indicators*.

The evidence on wealth, big business, and structural transformation is consistent with the emergence of extreme wealth as part of the development process. To the extent that the best entrepreneurs in emerging markets create globally competitive firms and attract labor and capital, they are steering resources to more productive uses. The resulting increase in productivity helps countries to grow and develop. The development is broad-based because the mega firms create jobs, improving the lives of the poor and middle classes, and these jobs pay relatively high wages. In this way, the route to extreme wealth is an integral part of the modernization process because wealth and modernization both rely on the creation of big business. The existence of extreme wealth owing to innovation can be especially beneficial in emerging markets, because entrepreneurs are likely to be better intermediaries of capital than governments, and the lack of deep financial markets means that the concentration of wealth may make the large investments needed for industrialization feasible.

If the new emerging-market superrich are creating the big businesses for development, exploring their characteristics will provide insight into how business may grow and change over time. Part III explores the age and gender of billionaires, the age of their firms, and the extent of turnover.

Emerging-market billionaires tend to be younger than advanced-country billionaires, looking more like the new technology billionaires. Their companies are also relatively young: The median firm of a self-made billionaire in the South was just 28 years old in 2014, compared with 47 years old in the North. There is a strong up-or-out phenomenon, where individuals who cross the billion-dollar threshold either continue to get richer over time or fall off the list all together—it is extremely rare to stagnate. As in advanced countries, very few billionaires are women, and female company founders are especially scarce. To the extent that this reflects bigger hurdles for female entrepreneurs in accessing finance to grow large companies, it implies that a wealth of great ideas are not being fully exploited.

Part IV explores potential concerns about the rise in inequality that results from extreme wealth, even when extreme wealth enhances development overall. Policy options to promote innovation and efficiency while limiting wealth concentration are explored. Even if the creation of big business and the resulting extreme wealth benefit those who are less well off, the current debate about inequality—with a focus on the top of the distribution—demonstrates that many people find the existence of wide disparities in wealth and income to be morally unacceptable and dangerous to political stability. As an Oxfam report (Seery and Arendar 2014) notes, it is hard for many people to stomach the fact that a single double-decker bus of people has more wealth than the bottom half of the global population. As the billionaire bus fills with people speaking Chinese, Hindi, and other non-European languages, these concerns may be magnified, because the compatriots of the newly arrived billionaires are relatively poor: The gap in living standards between Jack Ma and the average Chinese worker is greater than the gap between Bill Gates and the average American worker.

But the disparity of incomes is not the only measure that matters when thinking about equity. Improvements in living standards of rich and poor alike may be an equally or even more important metric for evaluating the impact of the rise of the very rich. By this metric, inequality in poor countries appears to be a very different phenomenon from inequality in advanced countries. In the advanced countries of the so-called North, billionaire-level wealth grew three times as fast as aggregate incomes between 2006 and 2014. By contrast, aggregate incomes grew faster than the incomes of those in the extreme wealthy class in the poor countries of the South. To put it another way, Jack Ma's compatriots have seen their incomes grow alongside his own; Bill Gates' have not. This phenomenon may explain why it is in the rich countries that people are calling for more equitable distribution while populations in the South remain more concerned about economic growth and jobs.

Reducing poverty and increasing opportunity—not the rise of the top 1 percent and the stagnation of the rest—remain the most important considerations in emerging markets. The concern about inequality has been raised politically in the wake of the global financial and economic crisis that began in 2007–08, which hit low-income families the hardest and spurred protests over economic fairness on both the left and the right. But the focus on extreme wealth and income inequality among many policymakers and pundits appears to reflect an Anglo bias, as it is largely in the English-speaking world that these trends are especially pronounced. Despite data showing that the rise of the top 1 (or .0001) percent relative to the rest is mainly an Anglo country problem, concerns about extreme incomes and wealth expressed by international institutions tend to treat the problem as a global one.

Economic policymakers in many emerging markets, on the other hand, are less concerned with inequality than with innovation and growth. This requires establishing strong property rights, ease of business entry and exit, and openness to trade and foreign investment. This combination of policies steers resources to their most productive uses while offering the high returns that are necessary to promote large-scale entrepreneurship. Ease of entry and openness to trade ensure that extreme wealth is accruing largely to people competing in contestable industries, not to domestic monopolies.

Even with such policies, however, distortions can prevent large-scale enterprise from developing. To spur large-scale entrepreneurship, concessional financing has proven useful in a number of contexts. It is more successful when it targets the most productive and externally oriented firms than when it supports all firms in a given sector through a broader industrial policy.

As countries develop, the challenge is to avoid creating excessive amounts of unproductive wealth. Estate tax can prevent wealth from accruing on the basis of inheritance as opposed to talent. Part IV discusses policies to limit wealth in sectors that may offer high returns but are relatively unproductive from a social perspective (the clearest example in this category is much of the recent hedge fund wealth).

The rise of an innovative wealthy class in emerging markets is a positive contributor to economic growth and higher living standards. It is not clear, however, how the power associated with wealth will affect political systems. Two issues are particularly important. First, once a new business becomes well established and highly profitable, owners have incentives to erect barriers to entry to protect their market and maintain profits. Strong government ties increase the threat that the wealthy distort government regulation and taxation (what is sometimes called crony capitalism). Second, the power associated with wealth may give the rich disproportionate power over the political system, which can move it away from the interests of the majority. In more authoritarian regimes, where the government does not serve the majority, private wealth may be used to support a regime in exchange for friendly treatment of the associated business. But wealth can also be a force for change, by promoting democracy (as Mikhail Khodorkovsky of Russia and Wang Gongquan of China have tried to do) or demanding institutions that protect property rights (as Daron Acemoglu, Simon Johnson, and James Robinson [2005] show is possible). These issues are not the focus of this book (much has already been written about them) but are discussed briefly in chapters 2 and 5.[2]

A Note on the Approach

The contribution of this book is twofold: It provides a taxonomy of the superrich using the World's Billionaires List from Forbes, and it connects the appearance of large firms and the ensuing wealth to development. Where data permit, the book examines large firms broadly and various levels of wealth, but the focus is on billionaires and their firms, especially the most innovative, whose multinational corporations are transforming economies. The focus is on billionaires not because they are more important for the economy than other big businesspeople but because their main sources of wealth can be traced and the firms they create are highly visible.

The disadvantage of this approach is that it focuses on a very exclusive group; as a result, it does not yield a complete picture of a country's businesses, especially in countries with only one or two billionaires. Even so, a discussion of the characteristics of billionaires can shed light on important issues, such as the role of large businesses and how wealth is created and acquired more generally. The sectoral composition, age, and method of wealth accumulation provide an image, however incomplete, of business and entrepreneurship in that country.

The book examines the appearance of the superrich in emerging markets from a purely economic standpoint. The broad message is that the rise of extreme wealth in emerging markets reflects a new breed of entre-

2. A discussion of campaign finance, lobbying, and the rich in office is beyond the scope of this analysis. Darrell West (2014) provides a comprehensive account of the role of wealth in politics in the 21st century, with a focus on the United States. John Kampfner (2014) discusses the controversial relationship between wealth and politics over the past 2,000 years.

preneurs who think beyond local markets and embrace technology and innovation.

The linkage between the creation of large companies and large fortunes is not surprising. Private firms that grow rapidly generate huge fortunes for their founders. Bill Gates is superrich because Microsoft is enormous; Jack Ma is superrich because Alibaba is huge.

What is perhaps more surprising is the tight link between growth in the share of the world's billionaires and growth in the share of the world's Fortune 500 companies from emerging markets. This positive correlation is a sign that the new emerging-market billionaires are not purely agents of political rent seeking, as is commonly thought, but are building mega firms that produce globally recognized brands. These capitalists and their mega firms are related to the extraordinary growth occurring outside advanced countries. They are harnessing the resources of their countries and taking advantage of global markets. That said, there is substantial variation across countries in the importance of innovation and entrepreneurship. And although rent-seeking activities are declining, they still account for about one-fifth of emerging-market fortunes.