
**Business systems in India**

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**Abstract**

In an ideal-type market economy, firms are hierarchies, relations between firms are competitive. This reflects a universal contrast: one morality inside the group, another outside. Since colonial times, India’s market economy has depended heavily on the state, and many firms were controlled by powerful hierarchies (‘industrial lineage firms’, managing agencies). Nehru introduced a strict planning régime (‘Licence-Permit Raj’) to achieve self-reliant development and protect vulnerable groups, with moderate success. State employees, businesses enjoying state patronage, ‘organized sector’ workers and low castes had some protection from insecurity and competition.

How was this half-planned economy co-ordinated, how were hierarchical authority relations within the private and public sectors organized, and how have they changed with liberalization? New ways of doing business emerge as firms adapt to more competitive markets: less security; more subcontracting; some networking between interdependent ‘flexibly-specialized’ firms. Lines between public and private, ‘organized’ and ‘unorganized sectors’, become blurred. But the impact of liberalization has been modest so far.

How can India meet the challenge of global markets in a way which will increase employment, incomes and welfare for the mass of its people? Can it repeat the success of the East Asian ‘Tigers’? What are the opportunities and constraints of the present ways of doing business? We need to understand the economy in order to improve it, to achieve goals like prosperity, greater social and sexual equality, and freedom. These ends are matters of moral and political choice: the study of business systems may suggest the means.

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Whitley describes business systems as

rather general patterns of economic organisation which deal with the three basic questions that arise in any market economy: how are activities to be coordinated, how are markets to be organised and how are economic activities within authority hierarchies to be structured and controlled? (Whitley 1992:271)

These problems arise not just in a market economy, but in any economy. The Soviet command economy, which was not designed on market principles at all, solved some of them by means of an unofficial market system of barter or illegal payments between directors of state enterprises, favours given and received, fixers collecting their percentage of deals, bypassing the bureaucracy: in our terms, systematic corruption, but also a market which made the unworkable command economy work after a fashion, as a system of competing bounded hierarchies instead of the single hierarchy of the command economy.

This is relevant to India, because although India never tried to abolish markets as the Soviet Union did, in the thirty-odd years after Independence, Indian governments tried to subordinate both the private sector and the large public sector to a planning régime which severely constrained market forces, the so-called Licence-Permit Raj. The state looked after its own: public sector employees, businesses which benefited in one way or another from state patronage or help, those workers who were covered by labour laws, and social groups which won special protection. So the questions as they apply to India are rather: how was such a half-planned economy co-ordinated, how were hierarchical authority relations within the private and public sectors organized, and how have they changed in the long gradual running down of Licence-Permit Raj?

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1 I use ‘state’ in the commonly understood sense, to mean the government, especially the central government. But India, like the USA, is a federation of ‘states’: when I refer specifically to these, I write ‘(regional) state’.

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Solidarity inside, competition outside: a universal contrast

In an ideal-type market economy, the corporate decision-making units are firms. Relations inside each firm are governed by hierarchy, authority, loyalty, and trust; relations between firms by competition, limited only by law and commercial morality – a system brought to perfection by Weber’s Calvinists. Reality is always more complex: there are competition and conflict within firms, and relations of trust, co-operation or collusion between firms. But the contrast between inside and outside, where different patterns of behaviour are expected, is a good starting point for the discussion of how real economies work, and the chances of making them work better to achieve our social and economic goals.

This reflects a universal contrast in all societies. One morality applies within the group, another outside. Jane Jacobs (1992) says human societies have evolved two distinct moral systems, ‘guardian’ and ‘commercial’, each appropriate to a different kind of organization. The two must be kept separate: it is dangerous to mix them. Simon Caulkin sums up her argument:

The ‘guardian’ syndrome arises from foraging and protecting territory and governs the behaviour of governments, bureaucracies, political parties, armed forces, police, religions and the justice system. Being about the effective use of power, it stresses loyalty, tradition, hierarchy, honour, vengeance, exclusivity and the distribution of largesse. It shuns trading. On the other hand the ‘commercial’ syndrome, emerging from the needs of trade, depends on honesty, voluntary agreements, easy collaboration with strangers, the panoply of enterprise and industriousness, and shuns force. (Caulkin 1994:8)

A business system, by definition, is about trade; yet relations within the firm – at least the firm organized on Weberian bureaucratic lines, or on Taylorist lines – have some features of the ‘guardian’ morality: hierarchy and loyalty within, competition outside (look at Japanese companies). The contrast between the ‘guardian’ state and the private firm is not so sharp.

Karl Polanyi (1957, 1959) distinguishes sharply between three modes of exchange: reciprocity, redistribution and market exchange.

Market exchange is the exchange of goods at prices based on supply and demand. Redistribution is the movement of goods up to an administrative center and their reallocation downward to consumers. Reciprocity is the exchange of goods that takes place neither through markets nor through administrative hierarchies. (Keesing 1985:205)
Where these writers see a sharp contrast between different moralities, Marshall Sahlins (1972) - building on social anthropological theories of exchange which go back to Mauss’ *The gift* (1954, originally 1925) - sees a continuum. Redistribution or pooling is also a kind of reciprocity. Most social relations, including those we call ‘economic’, can be placed along a ‘spectrum of reciprocities’, ranging from ‘generalized reciprocity, the solidary extreme’ (Malinowski’s ‘pure gift’), through ‘balanced reciprocity, the midpoint’ (direct exchange), to ‘negative reciprocity ... the attempt to get something for nothing with impunity’ (Sahlins 1972;193-5). Each type of society – hunter-gatherers, peasants etc. - has its own typical ways of drawing lines between spheres of social relations where different rules apply: in-groups and out-groups. There are conventionally defined situations in which convention defines the situations where ‘economic’ rules of exchange apply: here it is legitimate to trade, to maximize utility, to act as economic man.

In our capitalist society, relations within the firm are theoretically governed by pooling or redistribution, a hierarchically-organized type of generalized reciprocity. Market relations between firms range from short-term balanced reciprocity to negative reciprocity, depending on how ruthless the competition is. But in real business systems the lines are not so neatly drawn. A web of social relations of co-operation, trust, and conflict cuts across the boundaries of firms.

Reconstructing traditional business systems in India

This contrast, between hierarchy inside and competition outside, has been worked out in distinctive ways in Indian civilization. We have to look to the past to understand present reality, but we should avoid the temptation to exaggerate the continuity and unity of Indian culture, or to see everything since colonialism and modern industry as new. The past, as Indians and foreigners perceive it, is often an idealized ‘traditional’ past: the joint family to which people look back, or the self-sufficient village community beloved of gandhian and other intellectuals. It is a mistake to oppose ‘traditional’ to ‘modern’ (equated too easily with colonial or post-colonial India).

Remembering that tradition is an amalgam of real history and nostalgia, we can reconstruct traditional business systems in India, especially but not only among the Hindu majority. Most people were, and still are, peasants. Their dominant ‘business system’ was the so-called jajmani system: the exchange of goods and services between families belonging to interdependent castes, each carrying out its customary duties - high or low - in return for customary rewards of food and other perquisites from the dominant-caste peasants and landowners. In principle - and it was a principle deeply rooted in popular ideology - there was little or no competition, as long as everyone kept to
the traditional occupation of his or her caste, sanctified by religious duty. Members of each caste (barbers, washermen, carpenters...) divided up the available work according to custom. In principle, and to some extent in practice, everyone had security as long as they carried out their caste duties to a minimum required standard. Wiser (1936), who introduced the term ‘jajmāni system’, saw it as an all-embracing system which gave some protection even to the poorest. Gandhi wanted to revive this non-competitive order which, he believed, had been corrupted; but Meillassoux (1973:99) saw it only as ‘a relationship of clientship affecting a relatively weak part of the population’, a thin disguise for exploitation.

Although the system was found in its most complete form in villages, many of its features existed in the traditional Indian city. The jajmāni system is almost dead, but the ideal and nostalgia linger on.

The jajmāni system had one enormous loophole, through which market forces and technical innovation could pass. Some castes (like leather workers, barbers and priests) held genuine monopolies. Other castes were traditionally farmers or traders, but they had no monopoly: in practice agriculture and trade were more or less open to all who had the means to engage in them (Pocock 1962), though the lowest castes, being poor, had few chances to acquire the means. Each caste, subcaste or sub-subcaste might exploit a niche in the economy, a new product or service, while doing its best to keep out competitors from other castes.

In theory there was no way to translate economic success into higher caste status. In practice, successful castes or splinter subcastes staked their claim by ‘sanskritization’, copying high-caste customs like vegetarianism, and could gain tacit recognition as ‘originally’ members of a higher caste if they were rich and strong enough to persuade their neighbours. This process of sanskritization – mobility within the caste system – has been well documented, and appears to have gone on for centuries (Silverberg 1968). Only the highest and lowest castes, Brahmans and ‘Untouchables’, remained almost closed. Muslims and other non-Hindus fitted roughly into the system, and were divided into their own caste-like groups.

The jajmāni system was not a command economy and did not abolish the market; but it was an attempt to subordinate the market to overarching principles of hierarchy and interdependence. The pursuit of profit was a legitimate aim for castes of traders and cultivators, just as the pursuit of power and wealth (artha in Sanskrit) was the proper aim of the Kshatriya or warrior castes. The eternal dharma had to be reconciled with the reality of markets, competition, technical and population change, and political accidents.
The merchants and artisans of the cities had, and have, their own work ethic, justifying ruthless competition in the market, and sometimes sharp practice, while setting limits to it in the name of commercial morality and the solidarity of families, castes and guilds.

Peasants, merchants, artisans, priests and nobles all had some idea - partly based in reality - of a sphere of social life fenced off from competition and the market, an area where hierarchical relations of authority, loyalty and trust were considered proper; and areas where naked competition, the unbridled pursuit of wealth and power, was legitimate and approved. Above all, the joint or extended family was seen as an area of ideal co-operation, a haven against conflict. In practice, families were split by personal tensions, struggles over property, and conflict between brothers and in-laws: a traditional excuse for the break-up of joint families was that women's quarrels turned brothers against each other. At the village level, endemic factionalism everywhere set subcaste against subcaste, family against family.

The colonial and post-colonial state, and business systems.

Security and hierarchy within the group, competition outside: this is how the lines were drawn in colonial and earlier times. Contemporary India draws the lines in different places, but we need to go back to these institutions in the ‘traditional’ society - as it was, and as people now believe it was - to find the roots of business systems which now exist. These lie in what Whitley (1992:269) calls background social institutions, deep-rooted cultural patterns ‘covering trust relations, collective loyalties to non-kin, individualism and authority relations’. The other kind of institutions which shape business systems are ‘proximate social institutions’, which ‘concern the availability of, and conditions governing access to, financial and labour resources, together within the overall system of property rights and political control... The political, financial and labour systems’ (ibid.).

This distinction between ‘cultural’ background institutions and proximate ones is difficult to maintain in India, because of the pervasive influence of the state on relations between and within firms: the colonial state, and the post-colonial state, the reforms which got seriously under way in the 1990s, and are still incomplete. It is hard to distinguish traditional ideas about authority, trust and hierarchy from those which grew up under the shadow of colonial law and administration, and then the democratic-bureaucratic government of independent India.

Nineteenth-century British rulers like James Mill and Macaulay set out to do in India what they could not do in Britain itself: to design a new system of law and administration on utilitarian
principles, ‘with power devolved downwards to assignable individuals through a disciplined chain of command’ (Stokes 1959:148), for the common benefit – they believed – of Indians and British alike.\footnote{Sir Charles Trevelyan (1838, quoted in Stokes 1959:47) wrote ‘The natives will not rise against us, we shall stoop to raise them... The educated classes, knowing that the elevation of their country on these [European] principles can only be worked out under our protection, will naturally cling to us... The natives will have independence, after first learning how to make good use of it, and we shall exchange profitable subjects for still more profitable allies.’}

The élite Indian Civil Service, nicknamed the ‘twice-born’ after the highest castes, was staffed almost entirely by the British until well into the twentieth century. Under its protective wing, a new Indian middle class grew up, filling the lower ranks of the bureaucracy and the learned professions, especially law (Misra 1961). Most came from the highest castes, and their careers depended largely on the goodwill of British officials; except for some independent-minded, sometimes heroic mavericks in the Indian ranks. The British-led army, of course, was equally hierarchical and its influence almost as pervasive. These hierarchical structures fitted in very well with the ideological model of a hierarchical, non-competitive society which ideally gave security to everyone who conscientiously performed the duties of his or her station.

The British did not invent this whole mixture of bureaucracy, despotism and petty legalism which marks most working relationships in formal settings, but they embodied them in precise and lasting structures and gave them a powerful impetus, after which these systems of relations seemed to become self-sustaining, feeding on their own practice and ideology. (Heuzé 1992:13. My translation.)

The new system of commercial law was largely designed to favour British companies, which needed an intermediate class of Indian managers and foremen to mediate between them and the labourers they employed; but a vigorous Indian capitalism also grew up in the late nineteenth century, especially in the textile centres of western India (Bagchi 1972:56, 174; Holmström 1984:57).

The large Indian-owned companies modelled their management systems on those of the British, including the peculiarly British-Indian system of ‘managing agencies’. A managing agency was not usually a holding company, but one which raised capital for operating companies and appointed their managers, under an ‘agency agreement’. The agency often maximized profits, not by building up companies under its control, but by milking them of cash and by speculative transactions between the companies. Middle managers were appointed by the managing agency, often as a result of nepotism, and sometimes spied on the senior managers for the agency. Labour recruitment and supervision were left to promoted workers, the jobbers. For employees at any level, job security and

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promotion depended on relations with sometimes capricious and corrupt patrons, tempered in places by violent clashes with trade unions. By the 1930s the system's cost and inefficiency were obvious: it was gradually replaced by more stable management systems, with a strong paternalist ethic, and abolished after Independence.¹

Indian-owned management agencies were private limited companies, usually controlled by a single family. The big conglomerates which replaced them have dominated much of Indian large-scale industry since before Independence, sheltering behind tariff walls and restrictions on foreign companies, while chafing at other restrictions intended to check monopolies and encourage 'small-scale industries'. Their management practices became steadily more professional, as they tried to adapt western or Japanese management styles in their core business, while subcontracting more and more work to medium and small firms.

The managing agency system has gone, but has left its legacy in these hierarchically-organized firms with diverse interests in manufacturing and commerce. Often each hierarchy is controlled by a tightly-knit group, usually from the same family, caste or religion. These are the biggest and most successful examples of what Pierre Lachaier (1992) calls the 'industrial lineage firm', a system of patron-client relations typical of much Indian industry. The original company is divided and subdivided among the founder's kin, who are bound to each other and to small-scale worker-entrepreneurs by complex subcontracting relations. Planning, marketing and assembly are carried on in the central unit under the direct supervision of the Karta, the effective head of the family. Loyal employees are helped to set up ancillary firms; sometimes the distinction between employer and employee almost disappears.

Larger firms subcontract work to smaller ones not only for the usual reasons - flexibility, risk-spreading and so on - but to take advantage of government incentives to smaller firms, and to evade labour laws and social security by putting out work to nominally independent firms too small to be covered by the legislation.

The industrial lineage firm is bound together by a strong paternalist ideology, which the founding family and top management promote and which other employees may or may not share. Managers sometimes point to the fabled loyalty of Japanese employees, as an ideal rather than a reality in their own firms. For employees who share this ideology, employment in the modern

¹ For an account of the managing agencies, and their system of labour recruitment and supervision, see Holmström 1984:45-55.
company is akin to work as a religious duty in the jajmāni system (Holmström 1976:88-95, 126-7). Gérard Heuzé shows how nineteenth-century reformers gave a new meaning to the traditional value of sevā, which originally meant the ‘service’ or duty owed to one’s superiors within the family:

These ideas are still very much alive in many Hindu families, especially families of high status. They provide much of the ideological environment, and the context of social relations, in which young Indians first learn about work as a duty. Serving and being served means (among other things) relating to others and reinforcing the hierarchy through one’s acts. It means belonging to chains of relationships which make you a human being. (Heuzé 1992:12-13. My translation.)

The new economic and administrative tasks, salaried and waged work, were justified and dignified as sevā, service to the organic unit which was the family, caste or village, and is now the firm.

The industrial lineage firm’s weaknesses have become more obvious in recent years. It is vulnerable to family quarrels over property and control of subsidiaries, and to personal tensions. Sons from the dominant lineage are sent abroad to study engineering and management, but can only supply a small part of the professional management and technical expertise required. Some of the biggest industrial houses, notably Tata, have always distinguished clearly between top positions filled by the family, and all other posts filled by professional managers appointed strictly on merit and competence. Other firms have a reputation for nepotism, clientelism and favouritism, like the former managing agencies. Both kinds of firms offer a high level of job security to permanent employees at every level, but not to a large flexible work force of temporary, casual or contract workers.

In the period of Licence-Permit Raj, foreign companies investing in India were subject to tight restrictions on majority ownership of Indian subsidiaries and repatriation of profits. The large Indian conglomerates, mostly organized as ‘industrial lineage firms’, had an obvious interest in maintaining these restrictions, which allowed them to make agreements for technical and financial collaboration if they could find foreign partners willing to invest on these terms.
Not all new or growing firms are ‘industrial lineage firms’. Entrepreneurs with a background in engineering or professional management find backing from other sources: government schemes to encourage ‘technocrats’, or financiers looking for a spread of profitable investments. For contracts, ideas and advice, these entrepreneurs have useful contacts in the private or public sector enterprises where they worked before setting up their own business. Long friendships between men who worked or studied together, who belong to the same clubs and aspire to the same managerial lifestyle, can replace family ties as a basis for trust and joint action.1 Innovative small and medium firms can achieve a certain independence of the large firms; especially if they can co-operate, formally or informally, in marketing, product development, and subcontracting among themselves. This is a world of relatively self-contained management hierarchies, sometimes competing fiercely with each other, sometimes co-operating to a limited extent in the face of external competition, while jealously guarding their independence.

Nehruvian socialism and Licence-Permit Raj

All this has happened within limits set by the state, in an economy where the state was a major player as regulator, customer and source of funds for investment. It is fashionable now to damn the whole nehruvian project as an aberration from the market path, a lost opportunity to achieve outward-looking growth like the ‘Asian Tigers’; yet it had many positive achievements. The state did things the private sector probably could not have done in a desperately poor country with a largely illiterate population, and laid the foundations for a more open competitive economy.

Licence-Permit Raj could be regarded as a malignant growth on a reasonable project, Nehru’s ideal of self-reliant development towards a ‘socialistic pattern of society’: not a command economy on the model of the Soviet-dominated ‘socialist bloc’, but a democratic pluralistic socialism designed to achieve rapid economic growth by building the infrastructure and heavy industry to support private sector development; to protect domestic industry, while preventing the excessive growth in size and power of the big Indian-owned conglomerates, by licensing and quotas where there was a lack of effective competition; to create employment in small-scale and cottage industries; to extend the protection of the social democratic state to as many groups as possible; and to achieve more immediate ends, like raising the status of the Scheduled (ex-‘Untouchable’) Castes and Tribes though reservations in education and employment.

1 For an extended treatment of these networks in Bangalore’s engineering and electronics industries, and the foundations and limits of useful trust between entrepreneurs, see Holmström 1997, 1998a.
An unintended consequence was to establish the state as an area fenced off from competition and insecurity, containing powerful fiefdoms: big firms sheltered by tariff protection, import quotas and licensing, which prevented fierce domestic competition; peasants and small-scale industries protected by subsidies, which sometimes ended up in the pockets of the rich; ‘organized sector’ workers protected by labour laws and party patronage of politicized trade unions; employees in the overmanned public sector, including a fortunate minority from the Scheduled Castes and Tribes. The closer you were to the centre of state power, the more protection and security you enjoyed.

The notion of the state sector as a moral area fenced off from competition and insecurity was not new, but it took new forms under the nehruvian settlement. The job as *sevā*, service to a hierarchically-organized group, and particularly as a piece of property to which some people are morally entitled, is a legacy of a society stratified by caste and wealth, modified to some extent by the requirements of an incomplete capitalism and a vague socialism, and by the equalitarian ideas which inspired the Independence movement and Gandhi.

The attempt to right wrongs and satisfy political demands by job reservations reinforced the idea that a job is property, especially a job in the public sector. The reservation of scholarships and public sector jobs for the Scheduled Castes and Tribes – about one eighth of the population – was written into the Constitution as a special exception to meritocracy, a form of protective discrimination originally meant to be temporary. It has led to persistent and partly successful demands for similar concessions to much larger groups, the so-called OBCs (‘Other Backward Classes’, meaning castes). In the jajmani system, the lowest castes – or at least those who were lucky enough to be clients of local landowners – had a recognized claim to subsistence. Leach (1960:6) even argues that this put the lowest castes in a privileged position (‘In a class system, social status and economic security go together – the higher the greater; in contrast, in a caste society, status and security are polarized’). This is a questionable view of the traditional caste system, but paradoxically it may have a certain truth now. The claim to a moral right to jobs is now made by those who were lower in the hierarchy – not just the Scheduled Castes who had first claim after Independence, but the OBCs each claiming to be more backward than the others. In the old days, of course, castes claimed high status if they could make the claim stick.

The notion of the job as property sits uneasily with a meritocratic ideology, the idea that hard work and integrity bring their own just reward: an idea which is not merely an import of ‘western’ values. The British Empire was profoundly hierarchical; so were the attitudes of many British businessmen in India. Meritocracy has its own roots in traditional India, as in the work ethic of trading and artisan castes, and of religious sects like the Lingāyats whom the British called ‘puritans of
the East'.

Licence-Permit Raj had its roots in a mixture of Nehru’s fabian socialism and gandhian idealism, an attempt to build a harmonious rather than competitive society; for some enthusiasts, almost an attempt to restructure the jajmāni system on a national scale and to reconcile it with equalitarian and meritocratic ideals – a reply to Gandhi’s emphasis on the village, and his attempt to restore and purify an imagined lost village republic, but now on a national scale. As Licence-Permit Raj is gradually dismantled, the public sector is perhaps the last, rapidly crumbling redoubt of a moral order which began as an expression of worthy ideals before it was corrupted.

**A range of business systems now**

In India now, there seems to be no one dominant business system but a range of identifiable systems, each with its own rules and practices.

Discussions of Indian economic life often begin with a neat classification of the various types of organization into pigeonholes. A set of dualistic distinctions roughly describe reality and bring some sort of intelligible order into it. These are entrenched in law, public policy, and attitudes. They can be misleading, yet they make as good a starting point as any for a summary account of business systems. These distinctions are between

1. **Rural-agricultural and urban-industrial**: a broad value-laden view of two stereotyped ways of life. Rural ‘firms’ are farms, with unpaid family labour and some paid labourers, often seasonally employed and low-caste. Vestiges of paternalist obligation are left over from the defunct jajmāni system, but the relation between landowners and labourers becomes steadily more mercenary and short-term. Farmers are involved in the market economy but seldom compete directly with neighbouring farmers, except for status. There is more competition between rural traders.

   The urban-industrial economy is commonly thought of as harshly competitive. The contrast between rural and urban ways of life was always oversimplified and is now more misleading than ever, with the spread of capitalist farming. Agriculture becomes an investment for rural or urban capitalists, to be balanced against competing returns on other investments.

2. **Public and private** The public sector is still enormous and its influence pervasive: the central and (regional) state bureaucracies, services like education, nationalized banks, and much of manufacturing industry.

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For many years Indian governments have tried to make public sector enterprises more competitive, market-friendly and even profitable, with varying success. This is still an area of secure employment for those regarded as deserving, but it is less insulated from market forces than before. The pace of change has speeded up since the economic reforms of the 1990s, with plans to cut waste, reduce overmanning by voluntary or compulsory redundancies, and to find new products and markets, with some planned privatizations. At its worst, the public sector remains a dumping ground for people with influence, political connexions, or recognized victim status. Other parts of the public sector show signs of revival and adaptation.

3. ‘Organized and ‘unorganized sectors’, corresponding roughly to the ‘formal’ and ‘informal’ sectors (though the notion of an informal sector is confusing, hard to define, and of limited use: see Breman 1985, Joshi 1980). The organized sector consists of all public sector units, and private companies employing over ten permanent workers, who have been covered for many years by laws on unfair dismissal, union recognition, Provident Fund for retirement, and Employees’ State Insurance against sickness and unemployment. To avoid these laws, employers sometimes break up a firm into smaller units, each employing (on paper) not more than ten workers, but all operating in the same building as an integrated factory.

In practice, especially in the smaller ‘organized sector’ firms, these workers’ rights can only be secured where unions are strong. They do not apply at all to the large and growing number of temporary, casual or contract workers in firms of all sizes, who may work alongside permanent workers earning twice as much, and who may have little chance of acquiring permanent status (Holmström 1984:311-2).

If the public sector was a protected area for enterprises and employees, the organized sector - defined and regulated by the state - was almost an extension of it. Big firms enjoyed protection against imports. Some industries were dominated by oligopolies, with little incentive to innovate and little chance to expand, because their licensed capacity was limited to allow ‘small-scale industries’ to come up. For workers, the organized sector was a citadel of security: the important thing was to scale the walls, usually with the help of someone already inside. Once in, a worker could look around for a better job, but security almost always came first because life outside was so grim. This partial and relative security is now threatened in the private sector, and to a lesser extent in public sector enterprises.

Within the organized sector, there is a further important division into foreign and Indian firms.
Foreign firms were allowed to operate only in certain sectors, usually through subsidiaries with a majority Indian shareholding. Repatriation of profits was restricted. These controls are now being swept away, but suspicion of multinationals is still widespread across the political spectrum.

4. Large firms and 'small-scale industries' in the private sector. Government policy since Independence has been to protect the small against the large, through an array of subsidies, cheap loans, advisory and support services, and product lines reserved for small firms. Within the 'small-scale sector', ‘tiny’ or ‘cottage industries’ are singled out for special treatment.

While the organized and organized sectors are defined by the number employed, ‘small-scale industries’ are defined for official purposes by the amount of capital invested. This allows rich investors or big companies to buy up many small companies, or divide medium-sized companies into notional small ones, and to pocket the extra profit and subsidies. Many really small entrepreneurs, on the other hand, have not asked for help because they prefer to remain unregistered, invisible to tax inspectors and other officials. Some of these subsidies and privileges, notably reserved product lines, are now being dismantled or have gone.

Blurring the boundaries: the present restructuring of Indian business

This habit of dividing the economic and social landscape into ‘sectors’ made some kind of sense. From the point of view of workers, managers and entrepreneurs, the sector boundaries could be pictured as a series of concentric circles: the closer you were to the safe centre – public centre employment – the more security you had. Outside the public sector, but still inside the organized sector citadel, employment in a large firm was almost as safe as in the public sector, and better paid. Employees had less security and income in smaller ‘organized sector’ firms; and even less in ‘unorganized sector’ firms, including those which took advantage of the status of a ‘small-scale industry’, and which could be very profitable for employers. Temporary, casual and contract employees found work when and wherever they could. The outer circle of genuinely ‘informal’ enterprises offered the least security of all to workers and petty employers, but not always the lowest incomes. Peasants are outside my scope, though they are the large majority.

Since the reforms of the 1990s got under way, this neat arrangement began to break down. Boundaries between ‘sectors’ became blurred, with the gradual deregulation of business and opening up to the world economy. Fears that Indian industry would be swamped by aggressive foreign investors proved largely unfounded, but the now welcome multinationals injected enough competition to raise the quality of Indian products. Management remained hierarchical and taylorist
in most companies. The organized sector citadel became less secure: people who had believed they had a job for life, often one which could be passed on to a son or relative, were rudely disappointed. The government moved cautiously towards an 'exit policy', making it easier for bankrupt firms to close down and lay off workers. Though parts of the public sector were reorganized or prepared for privatization, it remained a relatively safe haven, more and more exposed to political pressures to employ members of the 'Other Backward Classes', in addition to the Scheduled Castes and Tribes who have enjoyed positive discrimination since Independence (Holmström 1999).

As the boundaries between 'sectors' - large- and small-scale, organized and unorganized, even public and private - became blurred, the real boundaries of the firm shifted too. For many years the government has helped 'technocrats' to set up high-technology, often capital-intensive firms in the 'small-scale sector'. With the easing of restrictions on large firms, the advantages of 'small-scale' status are less and less worth having: it makes more sense to let the firm grow. Many small firms are spin-offs from larger units, either 'industrial lineage firms' or entrepreneurs who set up trusted employees in business as their suppliers. These small firms are effectively part of the decision-making hierarchy of the parent firm. However some large firms now try to curtail old relationships with ancillaries, and shop around for alternative suppliers who can meet their requirements for price and quality. Small and medium enterprises increasingly have to fend for themselves.

In this situation, smaller firms can aim for independence, dependence, or interdependence. They can design, make and market their own products: easiest if the technology is simple and the market local. They can do 'job work' - one-off, possibly repeatable, contracts to supply parts or services to other firms, large or small: an insecure source of income, but sometimes lucrative. Or they can seek to become regular suppliers to the largest firms, including multinationals, sometimes displacing long-established ancillaries. The subcontracting small firm must work exactly to the designs and tolerances laid down by the buyer, which sometimes makes it necessary to buy expensive new equipment. It helps to have personal contacts with managers in the purchasing firm, who can pass on information about new plans; but this is generally a hard-nosed competitive relationship, rather than the old-style bond between patron and client. Since big firms try to avoid over-dependence on a single supplier, subcontractors also look for alternative markets.

The third option is interdependence. Networks of smaller firms (usually but not necessarily in the same industrial district) can complement each other to achieve economies of scale and scope. They co-operate on marketing, improving quality, developing new products, and stages of production for which some firms have specialized machinery or workers. This allows them to do things they could not do if they were isolated in a jungle of competing firms. They are interdependent, and

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independent of the large firms when this is to their advantage.

This is the small-firm variant of Piore and Sabel's 'flexible specialization' (1984, Sabel 1982). Where this strategy is successful, as in north-central Italy, smaller firms can achieve economies of scale and scope which large firms achieve through centralization, while remaining more flexible, cheaper, and more responsive to demand from even a few customers.

The chief obstacle is lack of trust. Flexible specialization requires some degree of trust between entrepreneurs, and between them and their workers. It could develop spontaneously, as local entrepreneurs see the advantages of acting together and develop effective sanctions against cheats and free-riders. Yet much of Indian business has always been a jungle, where trust was limited to a few kin and close friends, or to close-knit moral communities bound together by religion or caste, like the shoemakers of Agra (Knorringa 1991, 1994, 1998).

Effective networks of co-operation, capable of making India's smaller firms competitive on national and world markets, seem unlikely to take root without a push, a deliberate policy to encourage this kind of development. This happened in Italy, Germany, Denmark and Spain, where local or national governments worked with business associations, and sometimes with trade unions and universities, to provide what Italians call 'real services', like training, consultancy and design, which single firms cannot afford to provide for themselves; and to encourage and support consortia or other local arrangements which gave clusters of interdependent small and medium enterprises access to wider markets.

Cut-throat competition, as well as older communal divisions, make Indian entrepreneurs too suspicious to share information or to develop stable forms of co-operation. Yet there are recently documented cases of local networks of firms, including innovative and successful ones in fast-developing industries, which have developed effective networks of informal co-operation, based on economic interest and personal friendship, sometimes cutting across communities of birth; business associations of firms in the same industrial sector or simply in same place, like an industrial estate;

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1 Like those flooring tile manufacturers in Morbi (Gujarat) who use inferior materials for a quick profit, tarnish Morbi's image as a centre of tile manufacture, and could force the other manufacturers to lower their standards unless they can act together (Das 1996).


and, much more rarely, formal arrangements like consortia for marketing or to develop new products. There is some evidence not only that such forms of co-operation have developed spontaneously in some places, but that some – not all – of the ‘real services’ provided by national and state governments, or by business associations, have been effective in helping smaller firms to do things they could not do by themselves. It seems likely that public provision of ‘real services’ in India can not only make up for lack of trust between entrepreneurs, but can sometimes build trust by demonstrating the advantages of consortia and co-operation, and by building up solid friendships and social networks, cemented in social clubs like Rotary and Lions, professional associations of engineers or specialists, and the new culture of seminars and conferences which attract ambitious entrepreneurs and managers.

1 See Holmström (1994:53-63 and 1998a:00-00) on consortia in Bangalore and Coimbatore.

2 I have described the array of publicly provided ‘real services’ available to Bangalore’s engineering and electronic industries (Mark Holmström 1998a:00-00). Some, like the nationally-funded Central Machine Tools Institute (now renamed the Central Manufacturing Technology Institute) and the Nettur Technical Training Foundation (a voluntary organization) provide valued services to smaller firms. Other services are provided – with varying success – by business associations and the state government, and nationally-funded research institutes located in Bangalore because of its concentration of scientific talent and technologically advanced industries, especially since the Second World War. Cities like Pune (Poona) and Hyderabad appear to have similar advantages.
‘Real services’, then, can be useful both in doing what they are set up to do (training, help with marketing, testing &c.) and indirectly, in building solidarity and trust, laying the foundations for useful co-operation and the networks of social and moral relations which make ‘collective efficiency’ possible: not only in the relatively high-tech industries which face the stiffest international competition, but also in more traditional industries.¹

**Concluding remarks**

The Indian economy is becoming more genuinely competitive, but the real competing units are not always individual firms, each with its own decision-making hierarchy. Nor are they giant conglomerates in long-term relationships of trust with dependent firms, as in Japan, in spite of the continuing strength of ‘industrial lineage firms’. Long-established relationships between private or public sector enterprises and dedicated ancillaries give way to more competitive sourcing, as customers seek better value and consistent quality. Management in large firms is often hierarchical, centralized and fordist, with some gestures in the direction of Japan – participation, quality circles and so forth.

Among small and medium enterprises, forms of co-operative networking or ‘flexible specialization’ are emerging in places.² Where this happens, the boundaries between firms are blurred: an industrial district, or a geographically dispersed sector of industry, behaves in some ways like a large firm, with a presence in the market and common institutions to promote market-led innovation, yet decision making is decentralized. The chief obstacle to this kind of development is lack of trust between entrepreneurs. However some institutions to promote innovative small firms, run by government bodies or business associations, partly make up for this lack of trust and may help to build trust.

For workers, the ‘organized sector’ citadel of security disappears, or is redefined. The labour market is polarized, and is likely to remain so for a long time. A large part of the work force, well educated and with access to training or experience with new technologies, have bright prospects and rising incomes: their security is the knowledge that they can easily find another job at least as good as

¹ P.M. Mathew & J. Joseph (1994a, 1994b, Mathew 1995) have shown how the right kind of ‘real services’ could improve competitiveness, wages and conditions in traditional cottage industries like Kerala’s cane and bamboo industry.

the one they have. Many more workers - some well educated, most with little education - continue to find what temporary or casual work they can, in large firms or small. These workers can hope, at best, to learn a skill with some market value in small firms, paying perhaps half or one third of the wages paid to regular employees in large factories. Surplus labour and the weakness of unions keep wages low, and encourage employers to go for cheap labour rather than building up workers’ skills (Holmström 1999).

The impact of liberalization on Indian business has been modest. Licence-Permit Raj has been largely but not fully dismantled. The economy is more open to imports: this raises the quality of Indian goods and helps to make them more competitive on world markets. Multinationals are welcome at last, but are feeling their way cautiously in the new environment: much of public opinion is still suspicious of them. These changes have not transformed ways of doing business, but there are hopeful signs: big firms are more competitive and innovative, small ones show some capacity for networking and ‘flexible specialization’.

Some of these developments seem startling, even traumatic, by contrast with the immobility of decades. At least the logjam has broken: parts of Indian industry can move into the rapids of international competition. When this will lead to better work, incomes and welfare for the mass of Indian people is another question.

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