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Excerpt
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1 Introduction

India had one of the fastest-growing economies in the world over the last two decades. Economic growth reached double digits, and the country has since been regarded as one of the emergent global economic powers of the twenty-first century. The OECD has projected that India's share of global GDP will more than double by 2060.[1] This economic emergence has been due, at least in part, to manufacturing. The transformation of raw materials and other inputs – from cotton to basic chemicals to iron and steel – into intermediate and finished goods, from shirts to gears to medication for hypertension, is an important part of India's growth story, one often overshadowed by the services sector in general and information technology (IT) services in particular. Growth in manufacturing value added has frequently surpassed overall per capita growth in the economy over the last two decades (fig. 1.1), with output in consumer durables tripling and capital goods more than doubling over less than a decade (fig. 1.2).

What causes and sustains this industrial growth performance? Scholars of comparative political economy have long argued that the

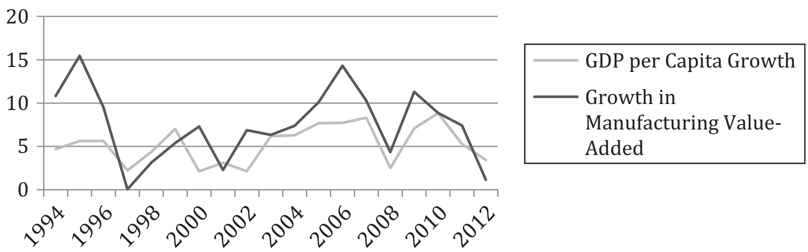

Figure 1.1 GDP and Manufacturing Growth in India, 1994–2013.
Source: World Development Indicators, databank.worldbank.org

[1] Braconier et al. 2014.

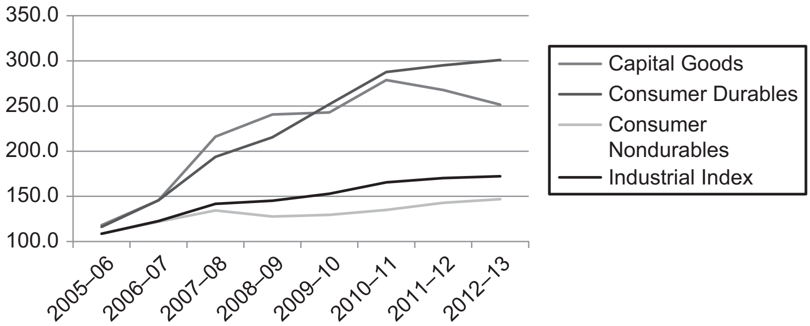

Figure 1.2 Indexed Growth in Manufacturing by Segment, 2005–2013.
Source: Index of Industrial Production, MOSPI (100 = 2004–2005)

state plays a crucial role in facilitating industrial development.[2] This is seen as particularly the case in developing countries, such as those in South Asia. Yet the persistence of growth in manufacturing in contemporary India is taking place in the context of an Indian state with little willingness and less capacity to promote industry effectively.

Most concretely, the contemporary Indian state has not proved willing to execute long-term investments in public goods. Intense electoral competition has led governments to favor short-term clientelistic spending on crucial constituencies over more diffuse, long-term public investments such as infrastructure. In a telling episode in July 2012, the national electricity grid failed twice, affecting up to 600 million people and shuttering tens of thousands of industrial units.[3] Writing on the Delhi satellite city in 2011, Jim Yardley asks, "[Gurgaon] represents a riddle at the heart of India's rapid growth: how can a new city become an international economic engine without basic public services? How can a huge country flirt with double-digit growth despite widespread corruption, inefficiency and governmental dysfunction?"[4] The answer, he argues, "is that growth usually occurs despite the government rather than because of it." These dynamics are more generally reflected in the conditions for investment; the World Bank's 2014 Ease of Doing Business index ranked India 142nd out of 189 countries, below Sierra Leone and Uzbekistan.

[2] World Bank 1997; Wade 1990; North 1990; Kohli 2004. [3] Magnier 2012.
[4] Yardley 2011.

More subtly but no less importantly, the state has substantially less influence over the provision of key factors of industrial production. As state-promoted "development finance" institutions have been dismantled or privatized, manufacturing must compete in a tight and chaotic capital market with an in-built preference for quick returns and an aversion to long-term, concentrated investments such as manufacturing enterprises. Industrial labor is increasingly fragmented and footloose, as state-mediated encompassing arrangements between organized workers and management have broken down. And government institutes for technical and vocational training have chronically undersupplied industry with skilled workers; thus manufacturing enterprises have difficulty recruiting and retaining them in order to meet the demands of production. The provision of land and energy to manufacturing enterprises has similarly fallen from the focus of the state's attentions and abilities.

These particular aspects of relative state incapacity in supporting industry are together a product of a wider phenomenon, that of *economic liberalization*. India, along with many countries in the developing world, went through a complex series of liberalizing economic reforms that drew the government out of the notion that it can, and indeed must, direct industrial development. From the beginning of the 1980s through the middle of the 1990s, the Indian state dramatically changed its role in the economy. State actors have by no means disappeared from the economy, but the state's institutional capabilities in structuring *industrial* investment have become severely circumscribed.

Yet popular and powerful state-institutionalist theories, through which we have come to understand industrial development, were formulated in the era of state-directed development from the 1950s until roughly the late 1980s, and thus in a context before this liberalizing turn. The very foundations of the political economy of later industrialization have from the beginning been predicated on the actions of the state.[5] Dependency theorists argued that the state needed to empower itself in order to execute import-substituting industrialization, through trade restriction and active industrial policy.[6] Scholars of the developmental state tradition located the remarkable economic successes of the previously backward East Asian "tiger" economies in

[5] List 1856; Gerschenkron 1962.
[6] Gunder Frank 1966; Cardoso and Faletto 1979.

powerful, autonomous state institutions that directed capital and disciplined labor; comparativists then explained the economic success and failure of developing countries through the differential capacities of their states to direct development.[7] These state-institutionalist frameworks, though powerful explanations for what drives cross-national variations in growth in the postwar decades, have not fully contended with fundamental changes in the role of the state during liberalization at the end of the twentieth century. The persistence and growth of manufacturing after economic liberalization in India thus pose a challenge to classical institutional theories of "late" industrialization that have privileged the state as the paramount driver of development.

Free market advocates, by contrast, have long argued that this withdrawal of the state may in fact be the *cause* of India's relative successes in manufacturing. In their view, the state's withdrawal has led to the unleashing of "animal spirits" and thus a surge in investment and sustained production, without the smothering impact of government interference.[8] There are some problems with this perspective, however. The first is empirical: Indian manufacturing grew at a steady pace during the Nehruvian era of high statism – averaging 6.9 percent between 1955–1956 and 1965–1966 – and then again from the early 1980s onward.[9] Liberalization cannot by itself be the cause of successful industrial development, if manufacturing grew both in the presence of statism and in its absence. Second, in India, as in most developing countries, market institutions – from developed financial mechanisms to rigorously enforced property rights – are both necessary for the functioning of "free market" capitalism and underdeveloped relative to those in industrialized countries.[10] Further, the development of such market institutions is the outcome of historical political and social struggles in which the national state plays an important role.[11]

7 See Johnson 1982, 1995; Amsden 1989; Woo-Cummings 1991; Evans 1995; Herring 1999; Chibber 2003; Kohli 2004; Doner, Ritchie and Slater 2005; Vu 2010.
8 For proponents of the free market perspective, see Bhagwati 1993; Das 2000.
9 Bardhan 1984, 18. McCartney (2009, 2010) makes this argument explicitly.
10 For more on developed market institutions, see Vogel 1996; Hall and Soskice 2001.
11 Polanyi 2001 [1944]; Zysman 1994.

Most importantly, successful industrial development requires institutional coordination among disparate actors over time. In India, straightforward market incentives would not suggest this course of action, regardless of the long-term potential, because of the presence of simpler, shorter-term alternatives for investment, from real estate to the consumer retailing of imported goods. Absent institutional structures, such as those provided by state-directed development regimes in the postwar decades, industrialization in developing countries would not – indeed, could not – flourish.

So how might we understand how manufacturing works after economic liberalization, particularly in the Indian context? The first part of formulating an answer to this question lies in the core concept of institutions: interrelated collections of formal rules, mutual understandings, and regulated practices provide the relative certainty and facilitate the coordination necessary for manufacturing. For industrial development to occur, institutions must enable private sector industrial firms – as the key frontline drivers of Indian industry – to invest capital and to recruit, train, and retain workers. Capital and labor are, after all, the most use-intensive and thus the most crucial factors of production in manufacturing.[12]

If capital and labor are the two most important factors of production for industry, everything depends on the predictable supply of these factors to manufacturing firms. I contend that industrial production is only possible if firms are able to overcome coordination challenges relating to labor and capital to enable the provision of trained workers and "patient" finance at a big enough scale and for long enough to arrange and deploy manufacturing processes. In order to do this, there has to be a coherent and durable framework of institutional relationships that link firms to their workers and sources of capital. Collectively, I call this institutional framework *industrial governance*.

[12] This book does not focus on land and energy; while certainly important, they constitute fixed and variable costs, respectively, that are largely exogenous to the continuing institutional relationships that preoccupy manufacturers. Securing premises is a prerequisite for investment in manufacturing, but once land is secured and a factory is built or bought, land figures little in the ongoing daily business of production. Beyond protest, manufacturers can do little about the high cost and uneven supply of electricity in India because there are no ready substitutes to government provision. For more on the political economy of land and power in India, see Levien 2013 and Chatterjee 2015.

In most of the extant literature on the political economy of industrial development, the state is thought to provide this industrial governance and thus direct the provision of capital and labor, by creating rules and channeling resources for industrial promotion. And in fact, during the era of statist development from independence until the 1980s, the Indian government, directly and through allied agencies and organizations, expended significant amounts of resources and political capital to this end. This book explores the nature and institutional sources of contemporary industrial governance after the state withdraws from governing the industrial economy.

Industrial Governance after Statism

There are several potential candidates for new forms of industrial governance that could explain how industrial production might be structured after statism. One possibility focuses on subnational governments. This perspective is informed by the remarkable regional variation in economic development in India, as well as other countries in South Asia and beyond. Indian market reforms have, moreover, been accompanied by the devolution of resources and political authority to state governments. Certain states have assertively claimed ownership over economic success within their borders. Narendra Modi, India's current prime minister and the former chief minister for Gujarat for more than a decade, campaigned throughout the 2014 elections on spreading "the Gujarat model" of industrial promotion – what Aseema Sinha has called a "subnational developmental state"[13] – to the rest of the country. It seems plausible that state governments in the pursuit of regional development provide industrial governance around sites of industrial growth.

A second possible alternative to statist industrial governance suggests the importance of institutions at the sectoral level. Globalization, the deepening of international trade and investment, has affected different industries in distinctly different ways. It seems equally plausible that globally competitive Indian industries, famously IT services but also pharmaceuticals and automotive components, might benefit significantly from institutional signals from partners, patrons, and clients in global markets, whereas industries facing threats from international competition might instead resort to

[13] Sinha 2005.

defensive protectionism, and thus substantively different forms of organization. Further, the export-promoting agencies of the Indian state and the organizational capacities of business associations – both are organized by sector – might provide new institutional structures after the depletion of the more encompassing industrial promotion regime under statism. In this context, a variety of forces and actors might combine to provide industrial governance at the level of industry or sector.

In locating the institutions that support contemporary industrialization, I take a different explanatory approach. Rather than subnational or sectoral institutions providing industrial governance after the retreat of the central state, I argue that sources of stability for industrial production can be most clearly located at the level of the firm. As I hope to demonstrate throughout this book, in the absence of credible external cues, industrial firms *as institutional actors* structure their ambient environment themselves in order to invest successfully in manufacturing. Indian firms thus proactively make and maintain long-term relationships with financiers and with workers.

By suggesting that firm owners, directors, and managers proactively participate in creating coherent institutional frameworks for production, I depart from the conventional wisdom on the institutions behind industrial development in three ways. First, I place the focus of my analysis on the firm as an institutional actor, and thus a political agent. Firms are not often considered in this way, because of a ubiquitous framing of their motivations as straightforward profit maximization. But Susan Strange argues that the firm can be seen as a political actor if politics are defined by "the human ability not just to act but to act in concert" rather than simply by what governments or politicians do:

> From the moment when its originator conceives the enterprise, he or she needs the supporting wills of creditors, employees, managers and salesmen to achieve the dream. Bargaining, persuasion, the offer of inducements, the threat of negative sanctions, the inspiration with a common vision – all these activities are little different from what politicians do when they seek election. If business people in action simply told their financial backers or their employees that the enterprise would reduce transaction costs by internalising them, they would not get very far. The cold logic of economic theory will not get people acting enthusiastically in concert to compete energetically with rival firms.[14]

[14] Strange 1996, 36.

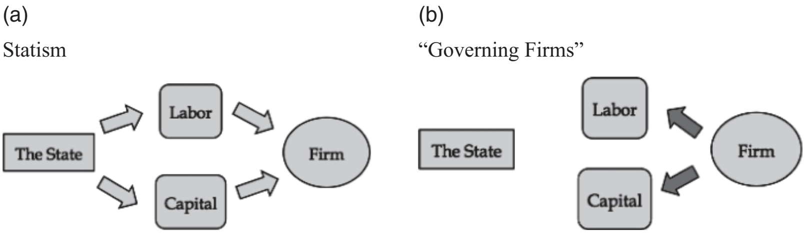

Figure 1.3 Industrial Governance during and after Statism.

Most extant political economy scholarship, by contrast, understands industrial firms and their directors as relatively short-term rational, even mechanistic actors, straightforwardly responding to the incentives and constraints provided by states, or the signals of international markets in such a way as to maximize profits. In other words, they are often understood as *institution-takers*.

This book takes a more ecumenical and empirical approach. The state might indeed influence or even direct a firm's strategies and practices, either with sticks such as regulatory enforcement or with carrots such as incentives. But this is the case only when the state deploys enough resources and political capital to provide such sticks and carrots coherently and credibly. When these signals from the state are weak, confused or absent, however, manufacturers must pro-actively form relationships with capital and labor and thus structure the institutions necessary for production absent direction from the state. In these instances, manufacturers are *institution-makers*.

Second, the interests and capacity of the state to promote industry through directing factor markets can change significantly over time; thus, the model of firms as institution-takers might have been appropriate during the statist era, but it may be less so after its conclusion. I outline histories of national development and of the international economy that inform the broader politics behind the rise and fall of statism in industrial governance, linking macro-historical processes to the dynamics at the firm level. The early postwar period saw the Indian government, among those in many developing countries, build up an autonomous state apparatus to direct the factor markets crucial to industrial development. Manufacturing firms operating in this context saw their activities both supported and disciplined by the powerful institutions of industrial governance emanating from the state. The results of this project were mixed both within and across country cases: South Korea was more successful than Nigeria, and within India, pharmaceuticals were more successful than heavy engineering. Yet starting from the late 1970s and then building in the 1980s, international forces and changes in domestic political economies combined to induce a fundamental shift in the broad relationship between the state and the industrial economy, from statism to liberalizing economic reform.

I contend that the level of institutional agency and autonomy on the part of firms is an outcome of economic liberalization: state actors – at national, regional or sectoral levels – are less interested in and capable of expending resources and political capital to define a single set of rules for industrial production through the control of factor markets. The signals from these agencies are weak and cannot be relied upon to structure industrial production. This is in stark contrast to the statist era, in which the state provided the rules of engagement for capital and labor, and used its disciplinary authority and abilities to concentrate and allocate resources to enforce a coherent regime of industrial governance. In other words, I contend that there has been fundamental change in the structures of industrial production over time, which has been neglected in favor of variation in the state's institutional capacity to promote industry across different countries.

Third, through my research, I uncovered significant variation in the ways that firms overcome these institutional challenges. This variation is in part a consequence of the retreat of the state from industrial governance; the lack of clear external signals leave firms to their own devices in terms of creating and maintaining institutional structures. But firm-level variation is a distinctive feature of Indian industrial economy, one that has been largely unnoticed due to our emphasis on national (or regional) models of capitalism in political economy. A focus on variation in structures and practices at the firm level can provide us with insights into the nature and social consequences of industrial capitalism in contemporary India that might otherwise have been overlooked. But how might we characterize and account for such variation?

Industrial Variation after Statism

Over interviews with more than 160 firms across several sectors and states, I found that firms in India broadly tend to structure their key institutional relationships in one of two ways. Some firms build their relationships through formal, explicit, contractual rules – in a way, replicating, at the level of the firm, frameworks of industrial production that exist in more highly institutionalized institutional macro-environments, such as in Aichi prefecture or in Baden-Wurttemberg. Other firms govern themselves through dense networks of personal ties and more informal understandings, submerged in social norms and maintained through larger kinship and community structures.

The character of firm-level institutional practices can diverge quite markedly, even for notionally quite similar enterprises. Consider two examples. In the Delhi National Capital Region (NCR), a textile trader turned industrialist, with a yarn empire of $500 million in annual sales accumulated over less than a decade, operates out of a small and rundown office in the Okhla Industrial Estate. He buys "sick" spinning mills and transforms them into productive units through the renegotiation of longstanding labor contracts. Labor relations for this firm, even given its size, are closely tied to personal relationships. Recruitment occurs mostly from rural areas, and relationships with *mukadams* or labor brokers, are important in this process: "to get labor, you need to talk to people." (2007-del2).

By contrast, just across the Yamuna River in the North Okhla Industrial Development Area, a glass office tower houses the textile operations of a venerable Marwari family, also worth $500 million in annual turnover, which has diversified and technologically upgraded their traditional spinning operations, as well as moved production downstream to fabric production and apparel manufacturing. Labor relations here are focused on formal, institutionalized training, or the development of human capital: "We have formal training systems – we give formal classroom and on-the-job training to all workers. We pick up youngsters with primary schooling and we train them for four months or six months." My respondent, the managing director, also placed a premium on human relations policies that institutionalize incentives for performance: "A worker is a human being and you need to treat him as such: [provide] a good environment, treat him well, and pay enough to cover cost of living. Why can't he be a partner? He should be as responsible as you are, he just needs to be motivated enough" (2007-del20).

These two institutional responses resonate in every state and region, in every sector and industry, with exporters as well as domestic firms, and with small firms and large ones. Presence of this variation in all