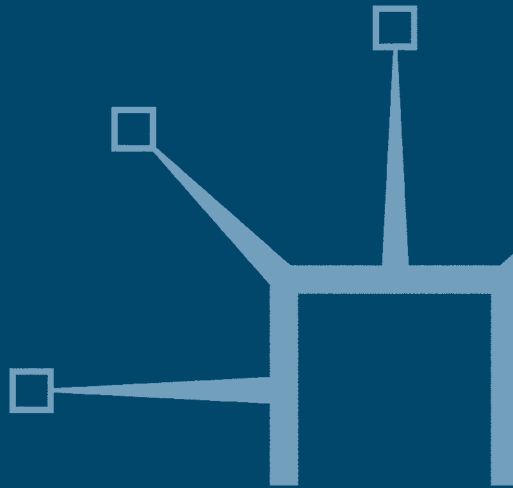
palgrave macmillan

Perspectives on the Indian Corporate Economy

Exploring the Paradox of Profits

Ananya Mukherjee Reed



International Political Economy Series

General Editor: **Timothy M. Shaw**, Professor of Political Science and International Development Studies, Dalhousie University, Halifax, Nova Scotia

Titles include:

Pradeep Agrawal, Subir V. Gokarn, Veena Mishra, Kirit S. Parikh and Kunal Sen
POLICY REGIMES AND INDUSTRIAL COMPETITIVENESS
A Comparative Study of East Asia and India

Roderic Alley
THE UNITED NATIONS IN SOUTHEAST ASIA AND THE SOUTH PACIFIC

Dick Beason and Jason James
THE POLITICAL ECONOMY OF JAPANESE FINANCIAL MARKETS
Myths versus Reality

Mark Beeson
COMPETING CAPITALISMS
Australia, Japan and Economic Competition in Asia-Pacific

Deborah Bräutigam
CHINESE AID AND AFRICAN DEVELOPMENT
Exporting Green Revolution

Steve Chan, Cal Clark and Danny Lam (*editors*)
BEYOND THE DEVELOPMENTAL STATE
East Asia's Political Economies Reconsidered

Dong-Sook Shin Gills
RURAL WOMEN AND TRIPLE EXPLOITATION IN KOREAN DEVELOPMENT

Jeffrey Henderson (*editor*)
INDUSTRIAL TRANSFORMATION IN EASTERN EUROPE IN
THE LIGHT OF THE EAST ASIAN EXPERIENCE

Takashi Inoguchi
GLOBAL CHANGE
A Japanese Perspective

Pierre P. Lizée
PEACE, POWER AND RESISTANCE IN CAMBODIA
Global Governance and the Failure of International Conflict Resolution

Ananya Mukherjee Reed
PERSPECTIVES ON THE INDIAN CORPORATE ECONOMY
Exploring the Paradox of Profits

Cecilia Ng
POSITIONING WOMEN IN MALAYSIA
Class and Gender in an Industrializing State

Ian Scott (*editor*)
INSTITUTIONAL CHANGE AND THE POLITICAL TRANSITION IN HONG KONG

Mark Turner (*editor*)
CENTRAL–LOCAL RELATIONS IN ASIA–PACIFIC
Convergence or Divergence?

Fei-Ling Wang
INSTITUTIONS AND INSTITUTIONAL CHANGE IN CHINA
Premodernity and Modernization

International Political Economy Series
Series Standing Order ISBN 0–333–71708–2 hardcover
(*outside North America only*)

You can receive future titles in this series as they are published by placing a standing order. Please contact your bookseller or, in case of difficulty, write to us at the address below with your name and address, the title of the series and the ISBN quoted above.

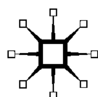
Customer Services Department, Macmillan Distribution Ltd, Houndmills, Basingstoke, Hampshire RG21 6XS, England

Perspectives on the Indian Corporate Economy

Exploring the Paradox of Profits

Ananya Mukherjee Reed
Associate Professor
Department of Political Science
York University
Toronto

palgrave



© Ananya Mukherjee Reed 2001

All rights reserved. No reproduction, copy or transmission of this publication may be made without written permission.

No paragraph of this publication may be reproduced, copied or transmitted save with written permission or in accordance with the provisions of the Copyright, Designs and Patents Act 1988, or under the terms of any licence permitting limited copying issued by the Copyright Licensing Agency, 90 Tottenham Court Road, London W1P 0LP.

Any person who does any unauthorised act in relation to this publication may be liable to criminal prosecution and civil claims for damages.

The author has asserted her right to be identified as the author of this work in accordance with the Copyright, Designs and Patents Act 1988.

First published 2001 by
PALGRAVE
Houndmills, Basingstoke, Hampshire RG21 6XS and
175 Fifth Avenue, New York, N. Y. 10010
Companies and representatives throughout the world

PALGRAVE is the new global academic imprint of St. Martin's Press LLC Scholarly and Reference Division and Palgrave Publishers Ltd (formerly Macmillan Press Ltd).

ISBN 0–333–80387–6

This book is printed on paper suitable for recycling and made from fully managed and sustained forest sources.

A catalogue record for this book is available from the British Library.

Library of Congress Cataloging-in-Publication Data
Mukherjee Reed, Ananya.
Perspectives on the Indian corporate economy : exploring the paradox of profits / Ananya Mukherjee Reed.
p. cm. — (International political economy series)
Includes bibliographical references and index.
ISBN 0–333–80387–6 (cloth)
1. Industrial policy—India. 2. Corporate profits—India. 3. Capitalism—India. 4. Corporate culture—India. I. Title. II. Series.

HD3616.I43 M85 2001
338.954—dc21

00–054527

10 9 8 7 6 5 4 3 2 1
10 09 08 07 06 05 04 03 02 01

Printed and bound in Great Britain by
Antony Rowe Ltd, Chippenham, Wiltshire

*To **my mother** and to the memory of **my late father** for giving me life, love and consciousness*

and

*to **Darryl** and **Siddharth** for travelling with me*

This page intentionally left blank

Contents

List of Tables viii

List of Figures xi

List of Boxes xii

Preface xiii

List of Abbreviations xx

Part I **1**

1 India in the Post-Interventionist Era: Towards a New Political-Economy? 3

2 Corporate Structures, Corporate Control, Corporate Power: Some Conceptual Explorations 20

Part II **51**

3 Corporate Capital in Colonial India: Genesis, Structure and Transformation 53

4 Corporate Capitalism in Independent India: the Interventionist Model and its Contradictions 93

Statistical Appendix 125

5 Corporate Capitalism in Post-Interventionist India: Paradoxes and More 129

Statistical Appendix 176

Part III **181**

6 The Paradox of Profits: Some Tentative Conclusions 183

Notes 198

Bibliography 214

Index 226

List of Tables

2.1 Corporate Control: Types and Mechanisms 26
2.2 Formalities of Subsidiary Operation 30
2.3 Evolution of Corporate Groups: A Suggested Historical Trajectory 35
2.4 Characteristics of Firms Under Divergent Models of Corporate Capitalism 49
3.1 Paid-up Capital of Companies Registered in India, 1914–15 to 1946–47 57
3.2 Racial Composition of Capital in India, 1914–47 57
3.3 Paid-up Capital of Sterling and Rupee Companies, 1914–15 to 1946–47 58
3.4 Corporate Capital in Colonial India: Political and Sociological Dimensions 65
3.5 Comparison of British and Indian Managing Agencies 69
3.6 Multiple Directorships Held by Leading Indian Industrialists (1932) 71
3.7 Structure of the Marwari Firms in Colonial India 74
3.8 Aggregate Profit Rates: 1910–44 75
3.9 A Profit Index Constructed by the Office of the Economic Adviser to the Government of India (1928=100) 76
3.10 Prices and Profits in India, 1940–44 76
3.11A Ratio of Net Profits Before Income Taxes 77
3.11B Ratio of Net Profits After Income Taxes 78
3.12 Number of Companies Managed by Selected British Managing Agencies (1950) 83
3.13 Decline in Number of Managed Companies and their Paid-up Capital (PUC) 91
4.1 Factions within the Congress Party and their Social Linkages at the Eve of Independence 96
4.2 Shareholding Structure of Selected Public Limited Companies 101
4.3 Control of Companies through Inter-Corporate Investments (1972–73) 103
4.4 Comparison of Indian and Foreign Business Houses 107

4.5 Share of Public Sector Funds in the Paid-up Capital of Indian Companies Owned by Leading Business Houses 109
4.6 Exercise of the Convertibility Clause by Public Financial Institutions 111
4.7 Percentage of Listed Companies with Nominee Directors, 1983 112
4.8 Growth of the Private Corporate Sector, Numbers and Paid-up Capital (in rupees million) 114
4.9 Assets of Top Twenty Houses, 1971–85 115
4.10 Return on Capital Employed for Large and Medium Public Companies, 1960–94 117
4.11 Rate of Return on Total Capital Employed in Manufacturing: Some International Comparisons 117
4.12 Profitability of Korean Industry: 1969–84 118
4.13 Wages and Salaries as Relative Proportions of Value-added in Manufacturing 121
4A.1 Market Share of Top Four Firms in Selected Indian Industries 125
4A.2 Relative Share of Cases Referred to the MRTP Commission by the Department of Company Affairs (DCA) 126
4A.3 Import Availability Ratios by Industry Groups 126
4A.4 Growth Rate and Employment Generation by the Private Sector 127
4A.5 Growth Rates of Assets of the Largest Indian Business Houses 1980–90 128
4A.6 Capacity Utilisation and Profitability: Some Illustrative Data from ICICI-assisted Companies 128
5.1 Changes Sought in the Post-interventionist Model 134
5.2 Private Placements in India 136
5.3 Governance Structures of Indian and Foreign Firms in the Post-interventionist Model 156
5.4 Structure of Shareholding of Selected Companies: 1996 and 1999 159
5.5 Major Foreign Beneficiaries of Preferential Share Offerings 161
5.6 Major Indian Beneficiaries of Preferential Share Offerings 162
5.7 Corporate Sector Growth: Gross Sales per cent 162
5.8 Corporate Sector – Profitability: profit after tax/Net Worth – (per cent) 163
5.9 Index Number of PBDIT: base 1985–86 163
5.10 Growth Rates of Selected Variables of Non-financial Companies 164

5.11 Economic Profits, Market Profits and Market-value Added of Selected Companies 166
5.12 Share of Wages in the Total Value of Production (per cent) 173
5A.1 Assistance Sanctioned and Disbursed by Development Banks 176
5A.2 The Top Ten Zero-Tax Profit Makers in 1994–95 176
5A.3 Major Foreign Beneficiaries of Preferential Share Offerings 177
5A.4 Major Indian Beneficiaries of Preferential Share Offerings 178
5A.5 Growth in Gross Fixed Assets of the Indian Corporate Sector 178
5A.6 Market Capitalisation of Largest Indian Companies: IFC versus the Bombay Stock Exchange (BSE) 179
6.1 Industrial Growth Rates: Use-based Classification, 1980–81 to 1998–99 185

List of Figures

2.1	Ownership of the Iron Ore Company of Canada	24
2.2	Inter-Corporate Control through an Apex Company: The House of Mitsui	29
2.3	Variations in Corporate Structure: The Straight Line	31
2.4	Variations in Corporate Structure: The Interlocking Model	32
2.5	Variations in Corporate Structure: The Satellite	33
4.1	Role of Development Banks in Gross Fixed Capital Formation, 1970–71 to 1980–81	110
4.2	Growth Rates of Assets of Indian Public Limited Companies: 1951–75	116
4A.1	Profits after Tax as Percentage of Net Worth: 1950–51 and 1977–78 Medium and Large Public Limited Companies	127
5A.1	IFC Indexes: Adjusting for Cross-Ownership	180

List of Boxes

3.1 Features of the *Companies Act*, 1956 90
5.1 Salient Features of the Companies (Amendment) Act, 1999 144
5.2 Principal Regulations Regarding Buyback Under the Companies (Amendment) Act, 1999 145
5.3 Substantial Acquisition of Shares and Takeovers: Highlights of the SEBI Takeover Code 149
5.4 Kumar Mangalam Birla Committee on Corporate Governance: Some Mandatory Recommendations 151
5.5 CII's Code for Desirable Corporate Governance: Highlights 152

Preface

In many ways, 1989 was one of the most significant years of the last century. For me, it was the year I left India – quite unable to anticipate at the time how the journey was to unravel. Upon my arrival in the US, I was immediately struck by the interest in the changes that were occurring in India. The possible 'awakening' of the Indian 'Tiger' under the charismatic leadership of Rajiv Gandhi seemed to be on many people's minds. Was the era of Indian socialism finally coming to an end? Will the bureaucratic *raj* eventually be dismantled? Will free enterprise finally be given a chance? As I travelled across the US visiting institutions and meeting people from various walks of life, I realised that there was in fact a strong perception amongst many that India had been a 'socialist state'.

The question as to whether the on-going changes were for 'real' became irrelevant soon enough – given the feverish pace at which events unfolded. Between 1989 and 1991 four major events took place: Rajiv Gandhi – Nehru's grandson and perhaps his most virulent ideological challenger – proactively brought about the demise of 'Nehruvian socialism'; in 1989, for the first time in India's history a minority government took power; on 12 May 1991, Rajiv was assassinated; later in 1991, a weak Congress government headed by Narsimha Rao and Manmohan Singh launched the formal institutionalisation of neo-liberalism in India.

As an aspiring political-economist, I naturally felt compelled to understand these changes and, most of all, to assess them against the canvas of India's 'socialist past'. As I indicated above, I did not feel particularly committed to that characterisation. Neither did I feel satisfied with the theories that claimed exactly the reverse. As I struggled with these competing and overt characterisations, I became convinced of the necessity to theorise Indian political-economy from the vantage point of formations *other than* 'socialism' or 'capitalism'. Thus, I turned to the debate on the *developmental state*, and in particular Alice Amsden's work on South Korea (which also appeared in 1989). This culminated in a dissertation that compared the nature of state intervention and state autonomy in South Korea and India, and came to the conclusion that not only was India not 'socialist' (in the sense of having eradicated 'capital') but, in comparison with the East Asian economies, Indian

intervention had failed to control capital in any substantive way. The reason behind this lay not in the inadequacies of state capacity but in the contradictory interests that shaped the interventionist strategies of the Indian state. As I argued then, Indian interventionism reflected a series of compromises and reciprocal concessions administered by the state in order to accommodate complex and contradictory interests. In offering this thesis, I do not mean to confirm the popular theory of the *neutral state* trying to 'manage' a 'demand overload' from competing factions of civil society; the reality is quite to the contrary. It was fallacious, it seemed, to view the Indian state as either neutral or residing outside the realm of competing interests; but neither were its actions reducible to one overriding class interest dominant at all points in time.

In other words, if one rejects the classical Marxist view that the state acts as a mere instrument of capital, or the neo-liberal view that it is ideologically biased *against* capital, then one is left with the need to identify a 'self-interest' that the state seeks to maximise. I believe that self-interest of the state to comprise in *legitimation*, i.e., a complex mechanism through which the state seeks to engender trust in itself.[1] In modern (and complex) societies, legitimation can be defined as a necessity of the state to appear neutral in conflicts between competing social entities *without actually being so*. In the specific context of India's development strategy, the primary conflict that the state had to 'manage' emerged from its two contradictory activities: to augment accumulation on the one hand, and to alter the distributive outcomes of such accumulation on the other.

The state's distributive activity thus has two goals. First, it compensates for those distributive outcomes of the market which systematically disadvantage certain groups. As such, it provides subsidies, tax exemptions and social goods in order to augment consumption. More importantly, the state attempts to 'punish' those classes which are disproportionately benefited by the market. Therefore, it imposes special taxes on monopolistic profits, on capital gains, on luxury consumption, etc. These 'punishing' activities of the state aid legitimation both in *real* and *ideological* terms. In real terms, it generates resources which the state can use for its various acts of intervention. In ideological terms, it serves as a *method of establishing public control over private accumulation*. The very creation of mechanisms to establish such public control serve to legitimate the state, quite irrespective of whether these institutions actually function to *implement control*.

The above might suggest the fundamental problem with intervention: that no single act of intervention can be *legitimate* with respect to all

competing classes at the same time; what the state does to legitimise itself *vis-à-vis* one class, makes for its de-legitimisation *vis-à-vis* another. As such, all interventionist policies create *legitimation deficits*, leaving the state with a constant need to offset these deficits. Following this logic one can conceive of intervention as an infinite process through which the state continuously creates legitimation deficits on the one hand, and attempts to offset these deficits on the other, being confronted by a *net deficit* at every point in time. As a result, there emerges a vicious circle of intervention rendering impossible the design or implementation of policy (especially policy that would benefit the overwhelming majority with least access to the state).

As may be apparent to the reader by now, this particular conceptualisation of state intervention draws extensively from the work of Jürgen Habermas, in particular his theses on the crisis of legitimation. Indeed, having been fortunate to spend a year at the University of Frankfurt, hear Habermas in person, and mingle with his students gave me a great opportunity to sharpen my thoughts. Also fascinating and stimulating were the three years I spent travelling, teaching and researching in post-Communist Central Europe, especially because I got to see first hand at least the last vestiges of *really-existing-socialism*. Rather fortunately for me, I had the opportunity to engage with the on-going debate on post-socialist transformation with some key thinkers from the region. These experiences not only sharpened my understanding of state intervention in India, but led me to see the ongoing reforms in a different light.

If indeed intervention comprised a series of reciprocal concessions to satisfy the state's legitimation needs, it would be reasonable to assume that the reforms would also comprise such reciprocal concessions. In other words, the *dismantling* of the interventionist regimes as professed by the champions of economic reform could be politically feasible only if it continued – or replaced – the concessions and compromises that existed before. In that case, the dismantling of old relationships that were to characterise liberalisation could well be only a temporary, reversible, and ad-hoc process. Alternatively, such dismantling may not even be possible wherever vested interests are seriously threatened, restricting the scope of the reform to mere cosmetic changes.

As I continued to observe the Indian scenario, I realised how contradictory the reform process was and how difficult it was to separate change from continuity. I was particularly intrigued by the claim that in this post-interventionist era, there was to occur a progressive decoupling of the state and the market. Indeed, it is this claim that has most directly inspired the present work. While the bulk of the literature

on liberalisation focuses on the consequences of this de-coupling, I thought it necessary to investigate its exact content. In what ways were the state and the market being 'de-coupled'? Specifically, what impact was such de-coupling to have on profit strategies of corporations?

As I have argued here, such an examination of profit strategies has critical implications for development. In particular, profit strategies determine levels of employment created by corporations; further, profit strategies determine the overall conditions of employment, i.e., what technologies are deployed, whether shopfloor innovations are encouraged or whether production processes are Taylorised, whether a learning environment is enabled, and whether, broadly speaking, employee participation in corporate decision-making is allowed. As the East Asian (especially Japanese) experience has demonstrated, these conditions are likely to exist only if labour, and gains in labour productivity, are crucial to profit strategies of firms. If, on the other hand, profit strategies are such that they depend more on market structures (and imperfections thereof), state aid, or *rentier* incomes, then it is likely that labour will be increasingly marginalised, even when political and legal regulations attempt to guard against such marginalisation. The dependence of corporate growth and profitability on a high-quality, knowledgable and innovative labour force is what I believe ensured the political and economic empowerment of East Asian labour – despite the presence of structural and historical factors preventing such empowerment. In India, by contrast, the presence of an elaborate set of labour regulations, high degrees of political awareness of labour, and a democratic polity, could do little to ensure any such cumulative improvements. The point is not to deny that the East Asian societies remain undemocratic; rather, it is to appreciate the kind of empowerment that East Asian labour has been able to wrench out of the wombs of a highly hierarchical political, economic and normative system.

It is largely these contrasts that drew me to the inquiry of profit strategies, and an assessment of the reform programme in terms of its effect on profit strategies. Viewed through this specific lens, the apparently dramatic changes associated with the reforms cease to appear so dramatic. I refer specifically to policy changes that claim to increase competitive pressures on firms by withdrawing state support. While state support as we knew it in the interventionist era has indeed been withdrawn, it has been reinstated in more subtle ways. Because of such reinstatements, the current changes in policy fail to address the critical requirements of development, for they fail to alter fundamentally the

sources of profits in a way that innovations and productivity gains (derived out of genuine learning processes rather than increasingly efficient methods of 'value extraction') become more crucial than market structures, state support, or *rentier* incomes. Unless this happens, it seems to me, a reform programme is unlikely to have much positive impact on development. For a developing country like India, the irony lies precisely here. While the people are its greatest resource, corporations seem to have little interest in developing that resource into their primary source of value; rather, value is sought in creating conditions that systematically *undervalue* labour. This is clear from the drive towards increased 'labour market flexibility' in the context of economic reforms, unaccompanied by a strategy for combating the deeply debilitating effects of such flexibility.

There are two substantive critiques of the work that I anticipate. The first, will stem from the neo-liberal claim that I underestimate the potential of the economic reforms and what it can do for the average Indian. To this I need not say much – except that I would be happy to be proved wrong. But the evidence so far does not give us much cause for hope. The second critique I expect will come from critical political-economists who, while agreeing with my basic conclusions, would nevertheless ask why I went to such great lengths to characterise the specificities of Indian corporate capitalism (over a period of almost a hundred years), to come to the conclusions that I did. After all, were these problems and contradictions not to be necessarily expected of *any* model of capitalism?

Perhaps; perhaps not. I have agonised over this question and have finally arrived at an answer which I now endorse with great conviction. If one's primary commitment is to locate possible trajectories of change, then it is necessary first to reject all forms of determinism and then to concede that the constraints and possibilities that emerge in a specific situation are a matter of active politics which cannot be predicted a priori. Second, and more specific to my problematic, is the question as to whether all forms of capitalism do in fact affect the possibilities of development in the same way. To some extent, perhaps they do. But concrete examinations of alternative realities alert us to the different possibilities as well: for instance, if we focus on the differential patterns of empowerment associated with different models of capitalism, it indeed appears legitimate that we examine the differences between different models in a nuanced manner. This analytical necessity to focus on differential models is reflected in the growing literature on *comparative capitalism* which has drawn into its foray statists, institu-

tionalists, Keynesians, Neo-Marxists, corporate strategists and a whole range of more eclectic scholars of development.

Needless to say, not all of these inquiries are prompted by the necessity to understand empowerment, although a good many of them are. Most are focused on identifying strategies of economic growth and synergies between corporate growth and development. But in exploring these strategies, many of the contributions on comparative capitalism do explore differences in empowerment. The present work is, in the most immediate sense, motivated by the question of empowerment and the related question as to how different strategies of economic growth *empower differently*. Different strategies of growth in turn are embedded most directly in the processes of capital, i.e., in the profit strategies of large, complex and modern corporations. This is true now perhaps more than ever before. I must mention however, that I have not dealt explicitly with empowerment in this work. That is the subject matter of my on-going work on human development.

In relation to this book, there are many I am indebted to, in ways I can hardly categorise. In particular I would like to thank the Shastri Indo-Canadian Institute, Calgary and York University, Toronto, for financing much of the research; all my professors in Jadavpur University, Calcutta; Prof. J. N. Sheth, for his continuing and invaluable support at times when I needed it most; my professors at the University of Southern California, especially my advisor Nora Hamilton, and Profs. Judith Grant and Eun-Mee Kim; my colleagues at York University; my friends, especially Himani Banerjee, Robert Drummond, Ishani Duttagupta, Parasara Mishra, Stephen Newman, Patricia Stamp and Sandra Whitworth, all of whom helped me with the book (and various aspects of my life) in very substantive ways. I would like to especially thank Prof. Timothy M. Shaw, whose involvement and support for this work have gone much beyond the usual obligations of a series editor.

There are two people without whom the book – or anything else in my life – would not have been possible: my mother and my husband. I do not have enough words to thank them for their love and support.

I also wish to thank the staff of Vaughan Road Day Care in Toronto who took care of my little son Siddharth and thereby gave invaluable support to this endeavour.

On this occasion I also remember with great sadness two other people: my father and my beloved grandmother, neither of whom lived to see my work in print. At an age when parents don't discuss much with their children other than homework, mine had begun their efforts to sensitise me to the problem of inequity. Although I could hardly appreciate their

efforts then, the theme lingered with me and has shaped my queries since. I fear though that I have disappointed them – for all I have produced is a mere book.

Toronto ANANYA MUKHERJEE REED

List of Abbreviations

ASSOCHAM	Associated Chamber of Commerce
BIFR	Board for Industrial and Financial Reconstruction
BJP	*Bharatiya Janata Party*
CCI	Controller of Capital Issues
CII	Confederation of Indian Industries
CMIE	Centre for Monitoring the Indian Economy Pvt Ltd
DCA	Department of Company Affairs
EVA	Economic Value Added
FEMA	Foreign Exchange Management Act
FERA	Foreign Exchange Regulation Act
FICCI	Federation of Indian Chambers of Commerce and Industry
FII	Foreign institutional investors
FIPB	Foreign Investment Promotion Board
FPI	Foreign portfolio investment
GIC	General Insurance Corporation
GOI	Government of India
ICICI	Industrial Credit and Investment Corporation of India
IDBI	Industrial Development Bank of India
IFCI	Industrial Finance Corporation of India
ILPIC	Industrial Licensing Policy Inquiry Committee
LIC	Life Insurance Corporation of India
MOU	Memorandam of Understanding
MRTPA	Monopolies and Restrictive Trade Practices Act
NPA	Non performing asset
NRI	Non Resident Indian
PAT	Profit After Tax
PUC	Paid-up Capital
RBI	Reserve Bank of India
SBI	State Bank of India
SEBI	Securities & Exchange Board of India
SFC	State financial corporation
SIDC	State Industrial Development Corporation
UTI	Unit Trust of India
VHP	*Vishwa Hindu Parishad*
VRS	Voluntary Retirement Scheme

Part I

This page intentionally left blank

1

India in the Post-Interventionist Era: Towards a New Political-Economy?

As this book goes to press, exactly ten years have passed since the economic reforms were formally launched in India. What was initiated as a response to a deep and intractable crisis exacerbated by 'external' pressures, has since evolved into a highly focused and coherent policy regime. This regime comprises three primary elements: a reduction in the role of the state, an enhancement of the market, and the development of a symbiotic relationship between domestic and global capital.

Central to this transition is the neo-liberal faith in private enterprise as the primary agent of development – and the specific assumption that India's failure to achieve the 'economic miracle' lies in its repressive approach to private enterprise. This shift in emphasis towards private enterprise marks the end of the *mixed economy* model that characterised India over the last five decades. According to this model, the state was to undertake two somewhat contradictory tasks. On the one hand, it was to actively aid, promote and subsidise the accumulation of private capital. On the other hand, the state was to *legitimise* such accumulation by ensuring that it did not jeopardise certain minimal requirements of social equity. Most importantly, it was to contain untrammelled growth of private accumulation by retaining control over the general direction of the economy through its Five-Year Plans. Second, the state was to directly own, control and operate large-scale enterprises in some key sectors of the industrial economy. Third, to whatever extent possible, the state was to provide some basic elements of welfare to its citizens.

Unfortunately, the merits of this experiment came to be seriously criticised from both sides of the political spectrum. Those on the left saw the mixed economy as having failed to deliver even the basic

necessities of life to the majority of Indians; those on the right argued that the cumbersome mechanism of controls on the private sector has been singularly responsible for the absence of economic growth.[1] This latter view became particularly dominant since the mid-eighties, especially as Rajiv Gandhi, the grandson of Jawaharlal Nehru and the son of Indira Gandhi, assumed office as Prime Minister in 1984.

In keeping with the global trends of the eighties, Rajiv Gandhi and his cohorts argued strongly against the plausibility of the mixed economy model. Particularly responsive to the view that private enterprise in India was reeling under the pressure of state control, Rajiv redefined the ideal Indian state as one characterised by free enterprise, high technology, a consumerist middle-class and minimal state intervention. In order to bolster private enterprise, Rajiv embarked on a programme of liberalisation that not only removed the Nehruvian controls on capital, but also sought profitable linkages with global capital.[2]

The material basis for the reforms lay in two primary occurrences: the internal crisis of the Indian state, and the external pressures from global capital. Where exactly was Indian capital in this equation? Contrary to popular wisdom, Indian capital was by no means in as obvious a crisis as the Indian state, and as such, hardly under the same pressures to embrace structural change.[3] It was therefore a willing but cautious player in the attempted process of reconstitution – keen to realise the potential gains in the new arrangement but cautious to avoid whatever might work against its interests. It was this relatively stronger position of Indian capital *vis-à-vis* the Indian state that had a fundamentally defining impact on the reform programme.

Added to this material reality were the various normative assumptions of neo-liberalism which further aggravated the imbalance between state and capital. Of these normative assumptions, the most important was perhaps the belief that both growth and equity could (and, in fact, *should*) be achieved through the development of private enterprise, provided of course, the degree of direct economic activity of the state was minimised.

As is well-known, Rajiv's programme of liberalisation was cut short by his assassination in 1991. His successors, Prime Minister Narsimha Rao and Finance Minister Dr. Manmohan Singh, executed and carried forward the process initiated by Rajiv, giving it its full and distinct neo-liberal content. Indeed, 1991 was the year when the 'Indian crisis' reached its climax, 'forcing' the Rao–Singh regime to resort to an IMF loan worth $1.78 billion.[4] Not surprisingly, the loan came as part of a comprehensive structural adjustment programme from the IMF, which

finally and formally put in place the era of neo-liberal economic reforms.

Several governments have come and gone since then. And despite the differences in their claims, it seems fairly clear now that whatever is the character of future Indian governments, and whatever their levels of stability, the general thrust of the liberalisation programme will prevail. It takes, of course, different specific forms under different governments, being contingent upon their specific ideologies and their coalitional strengths and weaknesses. In general, however, it is possible to identify a process of transition from a state-interventionist model to a post-interventionist model with a distinctly different ethos of state involvement in the economy.

It is this transition that I wish to explore. While there are many aspects of this transition, my focus will be on the changes occurring in the private sector, where the underlying characteristics of the transition are perhaps most apparent. The private sector in a developing country like India is, however, a large and complex entity that does not lend itself easily to analyses. As such, I will focus in this work on the organised part of the private sector comprising of modern corporations. This I will refer to as the *corporate economy*. The reason behind choosing this particular focus derives directly out of the dynamics that I described above: the emergence of an era in which corporations – and the corporate economy – have unequivocally been designated as the principal agent of development, and therefore, the new centre of political power. As such, the contours of economic development in the future are likely to be defined much more by the needs and the demands of corporate capital than ever before. It has become necessary, therefore, to address the broad theoretical question as to the role corporate capital can play in development, especially in the context of a severely limited role of the state.

Interestingly, however, much of the analysis of the impact of liberalisation remains preoccupied with the Indian state rather than the corporate sector.[5] As with the era of intervention, relatively little analytical attention is focused on firms, especially on the large complex conglomerates that have come to dominate India's industrial economy today. How do these firms operate? How do they generate profits? How does their profitability compare with other countries in the developing world? What drives their primary profit strategies – innovations or market power? How does liberalisation and globalisation affect these profit strategies? The present work seeks to address some of these questions by developing a detailed characterisation of the Indian corporate

sector in terms of its history and evolution, its modes of corporate governance, its 'political-economy', and the impact of changes induced by liberalisation. Broadly speaking, I have attempted three things here:

First, I have attempted to trace the historical evolution of Indian corporate capitalism, with the specific purpose of identifying the continuities and discontinuities in its evolution since the colonial era. In particular, this involves a characterisation of the typical Indian conglomerate, its origins and developmental trajectory, the specific ways in which creates value (i.e. through which combinations of market and non-market forces), its relationship with the state, and a discussion of the question as to whether these characteristics make it particularly vulnerable (or resilient) to the pressures of globalisation.

Second, I have sought to address what constitutes perhaps the most popular myth about corporate capitalisms in the developing world, namely, that *state intervention has managed to produce a chronic crisis of corporate profitability*. There are two analytically separate elements of this claim: first, that corporate profitability in developing countries like India has been universally low, and second, that state intervention has been the single most definitive cause behind low profitability (Ahluwalia, 1985; Cassen and Joshi, 1994).

I examine both these claims with respect to India. Without taking recourse to exceedingly technical analyses of economic variables, I have examined exactly how the Indian corporate sector has performed during the interventionist era in terms of profits, growth, and asset formation. Three primary insights seem to emerge from the analysis. First, that there is no obvious evidence of a chronic crisis in profitability. Second, that the effect of intervention on profitability is highly ambiguous; in fact, when I explore the specific profit strategies employed by Indian firms, it becomes clear that they have relied heavily on state policy. Third, these profit strategies have, in and of themselves, hardly been conducive to increased levels of macro-economic growth, employment or welfare.

Next, in light of the above, I go on to examine the changes sought by the post-1991 programme of economic reforms. In particular, my aim is to assess whether the reforms have the potential to alter the profit strategies Indian firms have hitherto employed. Do the reforms have the potential to force more 'market-dependent' profit strategies on firms? Are the reforms really capable of *structurally decoupling* state and capital? Why or why not? Finally, are the reforms fundamentally more conducive to economic growth, particularly of incomes and employment? This last question requires us to examine yet another claim of the

reform programme: that once the state 'withdraws' and the levels of corporate profitability begin to rise, the levels of growth and investment will also begin to rise in a sustained way.

My analysis seems to suggest a rather limited and tenuous success of the reforms in translating these claims into reality. The results so far are at best ambiguous, and highly contingent on a host of complex factors that go beyond the purview of the reforms. Most importantly, perhaps, it seems that some of the specific elements of the reform programme reinforce the relationship between profit strategies and state support that prevailed in the interventionist era. In the context of a severely de-limited regulatory role of the state, such a reinforced relationship between corporate growth and state policy may not only run counter to the claims of neo-liberal economics but also generate results counter-productive to India's developmental priorities.

I begin the discussion by explicating some theoretical ideas necessary for our exploration of the corporate economy (see Chapter 2). Presented also in Chapter 2 is a brief sketch of the notion of *development* that I employ in order to assess the overall impact of the corporate economy. The notion used here is most definitely a restrictive one, and clearly does not do justice to the complexity and divergence of the views that constitute the literature on development today. That said, I believe that there are some aspects of development that a modern corporate economy should clearly be able to address. It is useful, therefore, despite its restrictiveness, to construct a definition of development drawing upon those aspects to serve as criteria for assessment.

Using the ideas developed in Chapter 2, Chapters 3, 4 and 5 present a detailed characterisation of the Indian corporate economy in terms of three historical models: the colonial model (1900–47); the interventionist model (1947–85); and the post-interventionist model (1985 to the present). The discussion of the three models evolves along a fairly uniform structure. In each case, I begin with an analysis of the circumstances of emergence of the particular model; this is followed by a discussion of the governance structures and profit strategies associated with the model; next, there is an examination of the levels of corporate growth and profitability that resulted from those structures; and finally, I discuss the overall impact of the model on 'development' as I have defined it in Chapter 2.

Chapter 3 will provide an historical account of the origins of the corporate economy in India during the colonial period. As is well-known, there exists already a very substantial scholarship on the relationship between indigenous Indian capital and imperial capital during

this period.[6] What is relatively understated in this literature, and will constitute my point of departure, is an explicit examination of the profit strategies associated with this phase of capitalism in India.

Chapter 4 will present a discussion of the corporate economy under the interventionist model. It begins by tracing the colonial antecedents of these structures, and goes on to discuss the form it took under state intervention. Next, it discusses how Indian firms have performed in terms of profits and competitiveness during the interventionist period, and attempts to establish a linkage between the patterns of performance with structures of governance. In particular, it explores the myth of low profitability that I alluded to above. It argues that firm-level profitability in India is (and has historically been) actually quite *high*; however, in contrast to its East Asian counterparts, patterns of profit appropriation or policies regarding reinvestment were not those most conducive to increasing levels of macro-economic growth. This disjuncture between high firm-level (private) profitability and low macro-level economic growth is the key to understanding the 'Indian crisis'. I argue that such an exposition of the Indian 'crisis' points to the fundamental inadequacies of neo-classical economic theory that are currently hegemonic and policies derived therefrom.

This chapter also takes up the controversial question as to whether intervention actually helped or hindered profitability. What, for example, has been the impact the Indian state's pattern of financing the private sector? Or of the infamous and much-maligned policy of industrial licensing? Finally, and somewhat briefly, the chapter will dwell on the rather contentious issue as to the nature of political power enjoyed by the corporate sector. Here, I will not dwell so much on the issue of political power wielded by business through illegal means, but rather on the political power that emanates from the historical relationship between state and business.

There are two quite divergent (and extreme) views regarding this issue: one which believes Indian business to possess unconstrained political power and yet another which believes the Indian state to have completely dominated business (Chaudhuri, 1975; Lal, 1988). As we shall see, the truth lies somewhere in between: the relationship between state and capital in India is complex; while neither has been able to establish complete dominance over the other, both have enjoyed moments of dominance that are quite significant. As such, existing simultaneously with an apparently conflictual relationship between state and business, one can also discern a collaborative aspect to the relationship. This complex dialectic between conflict and collaboration

emanates primarily out of the early maturation of Indian capital into a powerful political entity with a distinct role in the formation of the post-colonial state.

It is this dialectic, I argue, that provides the primary explanation as to why the outcome of intervention was in fact a 'crisis' rather than a 'miracle', even when the major instruments of intervention were very similar to that of the miracle economies. It is this dialectic that informs my analysis of the economic reforms in Chapter 5. Not surprisingly, what I arrive at are some striking continuities with the pre-reform era that lead me to question both the viability and the ultimate utility of the reforms. In Chapter 6, I present the conclusions of the analysis.

In developing these arguments, I have tried, so far as possible, to employ terms and concepts that have emerged as fairly standard in the relevant literature on economic reforms. Nonetheless, semantic controversies often seem to shroud the most innocuous of terms. It may be useful therefore to devote the rest of this introduction to the clarification of some of the notions and theories that inform the work.

Anatomy of the reforms: marketisation and deregulation

There are two analytically separable aspects of the reforms process. The first major component is *deregulation*, i.e., the relinquishing of the existing state controls on the private sector. In theory, this does not imply complete freedom from all regulations altogether. What it does mean is that the responsibility of regulating the corporate sector now shifts to *autonomous* institutions rather than government bodies. The new regulatory institutions are to be *autonomous* in the specific (liberal) sense that they are not subject to interference by the government. Instead, they are governed by a board of directors comprised of representatives of the government, the corporate sector and other public bodies which may be concerned with the activities of the corporate sector. Such regulatory bodies are central actors in liberal capitalist economies. In India, the first such attempt to set up an autonomous regulatory body was the establishment of the Securities & Exchange Board of India (SEBI). I will discuss at a later point the contradictions that have surrounded the evolution of SEBI.

The second major component of liberalisation constitutes the withdrawal of direct state assistance to the corporate sector in a manner that increases the corporate sector's exposure to market forces. This I will refer to as *marketisation*. In the Indian context, *marketisation* constitutes the withdrawal of the state from the four major ways in which it aided

the corporate sector during the interventionist era. First, through a regime of nationalised banking, the state made capital available to industry at highly subsidised rates and under highly flexible repayment conditions. Second, through an expansive system of government spending, it provided a captive market for the output of the private sector. Third, through its system of administered pricing and subsidies, it made all infrastructural inputs available to the private sector at subsidised rates. And finally, through its aggressively autarkic trade regime, the Indian state protected Indian capital, especially its largest faction, from external competition. As we shall see there exist serious political limits on the ability of the state to withdraw from these activities. These limits are imposed not only by the immediate electoral interests of the ruling parties, but evolve out of the state-capital relationship that has historically characterised India. As such, the process of marketisation proceeds not in a straightforward cumulative manner, but through a series of continuous negotiations between state, society, the domestic corporate sector, and in a less direct fashion, global capital.[7]

Global capital has historically operated in India through multinational corporations (MNCs), which have been subjected to controls more stringent than those on domestic capital. The current reforms have attempted a significant dilution of these controls. One of the most important effects of this dilution has been the introduction of foreign portfolio investment, undertaken mostly by foreign institutional investors (FIIs). In contrast to MNCs, FIIs do not need to set up operations in India, but invest in stocks of Indian companies. The operation of FIIs have, for the first time, introduced the threat of take-over of Indian companies by foreign institutions and corporations; this threat is aggravated by, and is imposing serious challenges to, the way in which Indians have traditionally financed and managed their companies.

In assessing these changes, it is important to note that the two components of liberalisation – i.e. deregulation and marketisation – represent two contradictory aspects of the reforms process. The first, deregulation, represents a positive gain for the corporate sector in that it dismantles cumbersome state regulations and directly increases corporate autonomy. By contrast, marketisation represents a somewhat negative step in that it takes away from the corporate sector some very important advantages it enjoyed during the interventionist era. The exact balance of these gains and losses should be difficult to predict a priori, even though there seems to be a general consensus, especially amongst neo-classical economists, that the gains in corporate autonomy

far exceed the losses from the withdrawal of state assistance (Ahluwalia, 1995; Cable, 1995).

The post-interventionist model

In principle, there are many different models of corporate capitalism that India could have chosen from. The literature on comparative capitalisms and systems of corporate governance distinguishes between at least three models of corporate capitalism: *market-led* systems (the Anglo-American model), *state-led systems* (the Japanese/East Asian model) and *corporatist* systems (the Continental model). The distinction between these three models can be conceptualised along a variety of axes (Boyer, 1996; Boyer and Hollingsworth, 1998; Coates, 1999). For our purposes, the most important distinction is located in the differential relationship that capital bears to the state – and implicitly, to other classes in society.

The central premise of the Anglo-American model is its belief in the efficacy of the private corporate sector in generating economic growth provided, of course, that (1) state intervention is minimised, and (2) corporations maximise shareholder value. When satisfied, these two conditions can be expected to ensure a feasible macro-economic growth rate. As is well-known, the model constitutes the most important element of neo-classical (or marginalist) economic theory, which has, since the late seventies, dominated the policy discussions of the developing world. Interestingly, it is also precisely since the late seventies that this model of corporate governance has been challenged in the Anglo-American world (Nader, Green and Seligman, 1976; Reich, 1983).

Broadly speaking, the Anglo-American model does not concern itself with the macro-level growth or national economic development *per se*. It sees macro-economic growth as a simple derivative of micro-level activity. Also, in the classical form of the Anglo-American model, business owes no special responsibility to society or to workers, as long as it abides by the existing set of regulations and creates wealth for its shareholders (Friedman, 1962).[8]

The European models of corporate governance reflect an effort to balance better the interests of business, labour and society. Having developed in the historical context of states that sought to balance the contradictory tasks of legitimation and accumulation, the European model allows for extensive state regulation over the behaviour of capital (Habermas, 1975). The mode of regulation differs of course, quite fundamentally from the kind of regulation in the Anglo-American model,

and is in essence a much more extensive and complex model of regulation (Boyer, 1996; Offe, 1984). As has been extensively theorised by continental writers, the complexity of the European model lies precisely in the fact that it sought to manage the contradiction between accumulation and legitimation in a way that gave explicit recognition to the rights of workers (a) to increasing standards of living; (b) to universal welfare; and (c) to organise themselves politically (Boyer, 1999). While different European countries accommodated these rights differently into their respective structures of corporate governance, almost all of them have traditionally allowed for serious legal constraints on corporations to protect these rights (Hopt *et al.*, 1998).

The Japanese model is essentially different from both the Anglo-American model and the European model. On the one hand, it is premised on the belief that business should be the conduit to economic growth and, more importantly, to national prowess. In sharp contrast to the Anglo-American model, the Japanese model 'reflects' little faith in the ability of the competitive mechanism to generate macro-economic growth. It ascribes much less value to short-term corporate profitability, its focus being on the development of technology and long-term growth (Johnson, 1988). As is well-known, the Japanese model involves a very high degree of state intervention, with a state-determined and state-executed central plan, state-controlled patterns of domestic consumption and high degrees of social control.[9]

Of these three different models, countries like India seem to have shown a distinct preference for the Anglo-American rather than the European or Japanese models. The primary features of this post-interventionist model are:

- primacy of the private sector as the agent of development
- very limited role of the state, especially in redistribution and direct economic activity
- a transfer of regulatory power from the state to autonomous regulatory bodies.

However, with respect to the last premise, which in some sense is central to the Anglo-American model, the Indian reform process reflects some fundamental ambiguities. How exactly are autonomous bodies to be constituted? How agreeable are particular governments to withdrawing from their regulatory roles? Most importantly, how are corporations likely to respond to these new regulatory institutions when historically they have been accustomed to negotiating only with the state and

specific components thereof? Notwithstanding these ambiguities, a transition to the model specified by these three postulates is being attempted through the twin processes of *deregulation* and *marketisation*. The underlying premise of this policy decision is that there is an urgent need to augment corporate profitability by removing state intervention, since it is state intervention that has been primarily responsible for India's dismal economic performance.[10]

Existing theories

One can identify three broad classes of theories which address the relationship between the state and business, and the impact of that relationship on development. The first, represented typically by versions of Marxist political-economy, sees a collaborative, and sometimes symbiotic relationship between state and capital. In this schema, the state's function is largely to augment the profitability of capital. The second type of theory, represented by neo-utilitarian political-economy, envisages a conflictual relationship between state and capital, where the state's function is essentially to extract 'rents' from capital (Krueger, 1974:291–303; Bhagwati, 1982:988–1002; Colander, 1984). In this neo-utilitarian view, the state intervenes solely for the purpose of enriching itself at the cost of capital. A third approach which concerns itself with the relationship between state and business is that of the *institutionalists*. Of late, the institutionalist viewpoint has been adopted by both economists and political scientists, with perhaps equal influence on development thinking. In what follows, I briefly discuss these theories to examine where their strengths and weaknesses lie. I begin with a discussion of the Marxist tradition, followed by a discussion of the neo-utilitarian view; finally, I take up the institutionalist view.

Classical Marxist political-economy theorises capitalist development as the outcome of conflict between the two classes – capital and labour. As long as capitalism prevails, all political and economic power is vested in capital; in this schema, the state is simply an extension of capital – an institutional framework that exists purely as an instrument of the capitalist class. It makes little sense therefore for an orthodox Marxist to speak of the state as an autonomous entity, with an objective that it wishes to fulfil.[11] Informed by this instrumentalist position, Marxist writing has often conceived Third World states as an instrument of imperial capital: this is the classic argument of the Dependency School that gained currency in the seventies (Frank, 1969; Amin, 1974). This particular version of dependency theory has often been criticised for its

inability to allow for any role played by the domestic bourgeoisie, or the state: both these entities are reduced to mere agents or *compradors* of imperial capital.[12] As the experiences of many Third World countries have illustrated, while imperial or foreign capital has very often dominted economic policy, the role of domestic elites has also been quite substantial in giving 'peripheral capitalism' its particular content (Alavi, 1982). In countries like Brazil, India, Mexico, and South Korea, for example, domestic capitalist classes have entered into relationships with foreign capital that often constituted contradictory strategies of collaboration and conflict. This somewhat stronger and more autonomous role played by Third World states and businesses has been theorised by another genre of Dependency writers (Cardoso and Faletto, 1979; Evans, 1979). These writers have suggested a tripartite alliance between state, local capital and global capital and have argued that a pattern of *dependent development* has evolved out of this alliance. In contrast to the instrumentalist position, these writers explicitly reject an analysis of the periphery that derives 'mechanistically significant phases of dependent societies only from the "logic of capitalist accumulation"' (Cardoso and Faletto, 1979:xv; Carnoy, 1984:193).

Yet another genre of Neo-Marxists writing in the context of development have theorised that the state as an entity that does indeed possess a certain degree of autonomy. However, as characteristic of Marxist scholarship, these writers ultimately contend that in all capitalist social formations, state autonomy is *relative* as well as *constrained*, the constraints being imposed both by domestic and international capital (Alavi, 1973; Bardhan, 1984; Hamilton, 1982). In this schema, the relationship between state and capital is an outcome of several different factors: the level of development of the internal capitalist structure, the degree of organisation of the subordinate classes (especially labour), and the degree of dependence on the global capitalist structure (Hamilton, 1982:23–5).

The relationship between capital and the state in this theoretical scheme are determined, in reality, by the nature of the class conflict which, in turn, must depend on the nature of capitalist development. While this view does capture the essential dynamics of states in the Third World, it is less capable of explaining the recent phase of neoliberal transformations where even factions of labour and civil society also seem to 'favour' a deepening of capitalist structures (Biersteker, 1990). It may be helpful in my view to consider some specific aspects of contemporary capitalism in order to understand its apparent 'broad-based' legitimacy in the developing world.

It is possible to identify at least three legitimating factors that are suggested by the evolution of corporate capitalism in the post-war era. In general, the development of capitalism since the Great Depression, and in particular the emergence of the Fordist form of corporate capitalism, have delivered a material standard of living to workers in the West that allegedly socialist economies have failed to deliver. Further, the possibility of *regulating* corporate capitalism through a combination of market and non-market devices, has also helped to ameliorate some of the excesses associated with laissez-faire capitalism. Finally, in contrast to socialism, the expansion of capitalism has been possible within a framework of liberal democracy.

It is not clear however that these legitimating factors have actually redressed the fundamental concerns raised by critics of capitalism. In particular, two issues remain important. First, it remains necessary to identify the exact nature of corporate power, and the ways in which it creates or destroys the potential for substantive democracy. Second, it remains necessary to ascertain whether regulated corporate capitalism is able to offer a significantly better mode of genesis and distribution of surplus than alternative, non-corporate forms. It is precisely in order to arrive at such an assessment of contemporary capitalist form and its apparent legitimacy that a micro-analysis of that corporate form becomes necessary. This is exactly where traditional Marxist analysis may be found wanting.

There is, of course, a highly respectable body of work on corporate capitalism within the Marxist tradition (Hamilton, 1982; Scott, 1986; 1996; 1997; Zeitlin, 1970; 1989). The general problematic in some of these works is, however, somewhat different from mine. As characteristic of Marxist sociologists, these authors are interested in the final instance in class formation and, in some cases, on the nature of state autonomy in a capitalist system. In terms of class formation, the central issue addressed by them concerns the rise of the managerial class (and the attendant rise of *managerialism* as a theory). Managerialists argue that control of the modern corporation in twentieth century America had passed into the hands of managers – a group of autonomous, salaried personnel who were separate from the owners. Moreover, with the expansion of the stock market, the ownership of the corporation could not be identified with a certain class of people as in earlier periods. Hence, argued the managerialists, the development of corporate capitalism has given rise to a new class separate from capitalists, and who in effect have wrested control from the capitalist class (Berle and Means, 1932).

This basic managerialist thesis dominated thinking about class formation till almost the seventies, at which time a counter was mounted by the group of Marxist sociologists mentioned above. As Maurice Zeitlin argued in his seminal work in 1974:

> Our review of discrepant findings on the alleged separation of ownership and control of the large corporation in the United States.... should make it clear that the absence of control by proprietary interests in the largest corporations is by no means an 'unquestionable', 'incontrovertible', 'singular' or 'critical' social 'fact'.... On the contrary I believe that the 'separation of ownership and control' may well be one of those rather critical widely accepted pseudofacts with which all sciences occasionally have found themselves burdened and bedevilled.[13]

Scott, addressing the same problematic in 1997 asserts:

> A capitalist class of propertied families owning their superior life-chances to the income and wealth that is generated by their possession and use of property can still be found at the head of the stratification systems of contemporary capitalism. Far from having their privileges usurped by upwardly mobile career managers, they remain a potent economic and political force. The emergence of impersonal possession has resulted merely in a managerial reorganisation of the propertied class.[14]

This kind of research – i.e., one that explored the linkages between corporate structures and class formation – remained rare for most of the developing world. Notable exceptions were Zeitlin's own work on Chile, Hamilton's work on Mexico, Hazari and Bagchi's work on India, etc.[15] The present work attempts to follow a similar analysis of corporate structures, but the ultimate focus, as I explained above, is not on class formation. Rather, it is on discerning/assessing the impact of liberalisation on the corporate sector, and on development in general.

Let us turn now turn to a fundamentally different normative and theoretical approach that has gained great currency in recent years, namely, neo-utilitarian political-economy. In particular, the neo-utilitarian school's *rent-seeking hypothesis* has had a profound impact on the thinking about states in the Third World (Evans, 1992). The hypothesis proceeds from the premise that the state becomes an instrument through which rulers, especially bureaucrats, extract rents from

capital. This renders the state a predator, which typically encroaches so far into the economy that economic activity becomes impossible unless agents are able to fulfil the predator's demands. The necessity to provide the state with these rents inflates production and transaction costs, and generates a series of *directly unproductive (DUP) activities*.[16] Once these conditions for DUP are created, the bulk of the society's resources, especially private sector resources, are allocated towards them. Needless to say, this misallocation of resources results in decreased growth and profitability, and lack of international competitiveness. State intervention therefore, is valid only in the earlier stages of modernisation and only in order to create conditions for the development of the private sector. Once these initial conditions are created, the state should minimise its intervention in the economy, and at best operate only in those areas which the private sector does not consider profitable, and for which there may be some social need.

There are several serious critiques of this argument and the policy implications that come with it. First, it needs to be recognised that the rents generated through state intervention did not (and do not) accrue to the state only. Rather they were distributed amongst the state, the bureaucracy, local capital, foreign capital and other dominant classes according to the distribution of power amongst them. Even in the global context, there is enough evidence that rent-seeking need not be practised only by the state, but characterises the behaviour of any entity that operates within a context of unequal bargaining positions. The major example of this are large corporations enjoying monopoly power (or monopsony in the labour market), transnational corporations, and landlords operating in 'inter-locked' markets of semi-feudal contexts like India (Bhaduri, 1984). Thus, if rents are to be eliminated from the system, very significant institutional changes need to be attempted. Removing state controls on business in and of itself would hardly suffice.

The logical inconsistencies of neo-utilitarian theory were further revealed by its failure to explain the most important development saga of the twentieth century: the emergence of the East Asian states. These states showed, at the same time, the highest rates of economic growth and the highest degree of state intervention. Provoked primarily by the case of East Asia, and in some sense as a counter to the rent-seeking school, yet another paradigm of development has become dominant since the eighties. This is the paradigm of the *developmental state* (Amsden, 1989; Evans, 1992; Johnson, 1982; Wade, 1990). In contrast to the rent-seeking school, the adherents of this paradigm argue that a

collaborative relationship between state and business can actually be beneficial for development (conceived primarily as economic growth). In making this argument, developmental state theorists reject both the Marxist and the neo-utilitarian claim that a collaboration between state and capital is necessarily problematic. However, developmental state theory shares one fundamental premise with the rent-seeking school: that the primary goal of state intervention should be the development of the private sector, for it is the development of private sector that will foster national economic growth.

Epistemologically, the developmental state paradigm is situated in the institutionalist school that takes as its central focus the analysis of institutions.[17] The developmental state theorists, of course, focus exclusively on one institution: the state. However, some versions of contemporary institutionalist analysis, especially those developed by Amsden, Chandler and Williamson, also examine the corporation as a specific organisational form.[18] Williamson and Chandler have both argued, in dissent with traditional economic theory, that the internal organisation of the corporation has a stronger influence on its activities than the market (Chandler, 1977; Williamson, 1985). However, Chandler and Williamson differ quite fundamentally in their premises. Chandler focuses on the hierarchical nature of the modern firm, and argues that it is this element of hierarchy that makes the corporation efficient.[19] Williamson on the other hand emphasises the market-like and *non*-hierarchical aspects of the firm. He argues that, of all the alternative organisational forms available to modern society, the corporate form is the most efficient in that it minimises *transaction costs* (i.e. the costs of designing, negotiating and enforcing contracts, etc.).

By far the greatest problem with Williamson's approach is its overt functionalism: he abstracts away from the political-economic context in which the firm functions. As characteristic of most functionalist approaches, it also tends to be a static, behavioural analysis of the firm *as it exists at a point in time*.[20] Most importantly, Williamson's approach takes transaction costs as given, i.e., ignores the broader contextual reasons as to why certain types of transaction costs may emerge at particular points in time, or what role states and non-state actors might have in biasing transaction costs in specific ways.

Summary and conclusions

Let me summarise the theoretical approaches presented above. I reviewed three strands of theory: Marxist political-economy, neo-

utilitarian political-economy and institutionalist political-economy. While each of these approaches provide some important insights into the complexity of contemporary forms of capitalism in the Third World, they leave unexplained some substantive issues. Except for authors writing in the context of East Asia, neither of the three approaches focus much analytical attention on the Third World firm, its specific structures and modes of governance, accumulation strategies, etc. Why? For many Marxists, such analysis makes little sense since they assume a certain uniformity in the logic of capitalism across space and time. For neo-utilitarians the analysis of Third World firms seems futile, since it is their thesis that the functioning of those firms are distorted by the actions of the state. For institutionalists, the emphasis has largely been on the state; for firm-theorists such as Chandler or Williamson, the context is exclusively that of advanced capitalism.

What emerges from the above is the need to analyse the specific ways in which corporate capitalism operates in specific contexts. While it is true that corporations across the world share some important characteristics, the differences between national contexts remain important as analytical/exploratory categories.[21] A proper assessment of divergent national contexts requires that we take an historical view, since it is through distinct historical processes that national contexts come to be.

When studying the Indian case, or evaluating the various theories, my broader objective will be to examine the neo-classical assumption that corporate profits are necessarily conducive to economic growth, especially the kind of economic growth that can substantially augment levels of employment and income, skill formation of the industrial workforce, etc. It is, of course, beyond the scope of this work to study these aspects of growth in detail. There is however enough evidence that in many Third World countries like India, high rates of corporate profitability have not brought about the kind of industrial transformation that East Asia has experienced. This relationship between corporate growth and overall growth and development of an economy has now become a focal issue of research in the US and the UK, the two economies which have been the strongest adherents of the Anglo-American model and the salience of private enterprise. Paradoxically, while such soul-searching continues in the Anglo-American world, the liberal capitalist model seems to be embraced by economies in the Third World, quite irrespective of the differences in political regimes which prevail. It is in the context that I wish to examine the emergence of the model in India.

2

Corporate Structures, Corporate Control, Corporate Power: Some Conceptual Explorations

In this chapter, I will explicate certain theoretical notions with respect to the corporate economy. Obviously, much of corporate theory as we know it today has evolved in the West, alongside the development of corporate capitalism. While the developmental dynamics in the developing world have been quite different, some of the basic institutional mechanisms of Western corporate capitalism have been imported to the developing world through the relationships of colonialism. As DiMaggio and Powell (1983) have argued, a colonial history produces a certain degree of institutional 'mimicry', whereby organisational forms adopted by post-colonial states come to reflect colonial structures. In any case, it is possible to argue that certain similarities characterise capitalisms of both worlds, at least to the extent that they both concern the accumulation of capital through the institution of the modern corporation. In both worlds, the corporation seems to have provided an enduring framework for the ownership and control of assets, the investment and accumulation of capital and the organisation of production.

A theoretical understanding of the corporation – its internal framework as well as its relation to society – is therefore the legitimate starting point of this work. I will begin by explicating the relevant notions of what the corporation is, how it is structured and how it functions. More specifically, I will examine the phenomena of the *conglomerate* – or the complex corporate group – since it is this specific institutional form that has come to define corporate capitalism as we know it today. Here I will be concerned with three aspects of the phenomena: first, the particular organisational features through which conglomerates create wealth; second, the historical trajectory through which the form evolved, and

third, the relationship of business to politics in a corporate economy. In the final section I will present a conceptual framework to explore the relationship between the specific nature of a corporate economy and its impact on development.

Before I proceed, let me emphasise what I think is my point of departure – from two important sets of literature that concern similar themes. The first is the literature on corporations and corporate governance that takes epistemologically from neo-institutionalist economics. This literature emphasises primarily the *internal* structures of corporations and conceives of corporate governance as comprised of issues purely internal to the firm. The second comprises the literature in political-economy: this literature, with some exceptions, does not take as a primary analytical category the internal structures of governance of firms. Rather, it focuses on the political relationships of capital as a whole with entities such as the state, labour, or more generally, civil society.

I wish to propose an approach that mediates between these two extremes: the dichotomy that currently exists between the internal dynamics of the firm and its external, *political* behaviour, may serve us better when substituted by a framework where the two are seen as mutually constitutive of each other. Structures of corporate governance evolve historically and reflect responses to the particular balance of social forces that obtain at different points in time, as do institutional/political structures, which regulate corporate capital. In that sense, drawing a rigid line between what is internal to the firm and what is external may be somewhat misleading. Similarly, conceiving of only some corporate acts as *political* (e.g. lobbying, campaign financing etc.) and others simply as 'business' can also be misleading. With these two caveats in mind, I present an approach that gives equal weight to the internal structures/principles of governance of the firm and its external behaviour, with an effort to delineate the linkages between the two.

Ways of thinking about the corporation

Two somewhat inconsistent conceptions have dominated our thinking about corporations since the late nineteenth century. In the first conception, the corporation is seen as the private property of its owners (stockholders), the exclusive purpose of which is to create wealth for these owners. The second conception sees the corporation not as the private property of stockholders, but as an institution, a form of social compact among various constituencies. In this view, the corporation is

not strictly private. It also has a public purpose of advancing general welfare, and may legitimately be expected to eschew, or at least restrict, profit-maximising behaviour should it come into conflict with the needs of public welfare.[1]

The property perspective has historically been the most prevalent in the US. Reflected, for example, in the famous Michigan Supreme Court Case between the Dodge Brothers and the Ford Motor Company in 1919, the property perspective argues that the right to govern the corporation should be vested strictly in those who *own* it. Interestingly, however, those who espouse this view do not necessarily suggest that every aspect of governance – or day to day management of the corporation should be determined by the 'owners'; it is in the appropriation and reinvestment of profits that they suggest the owners should have their say.[2]

Underlying this corporate concept are two philosophies, first, that power derives from ownership; and second, that owners should be able to exercise their power in line with their investment. In this conception, the rights of the creditors, employees and all others who are stockholders are strictly limited to statutory rights. This property view equates the duties of directors with the duty to maximise profits of the firm for the benefit of shareholders. In this framework, the legitimacy of the corporation is determined by its ability to do exactly that, i.e., operate the firm to maximise shareholder returns.[3]

Rooted in the mid-19th century Western, principally English ideology, and institutionalised in the Joint Stock Companies Act passed by the British Parliament in 1844, this conception of the corporation ascribes central importance to the notion of the individual, emphasising personal freedom and self-regulation under the common law.[4] It was essentially along these lines that company law developed in the U.S., reflecting the primacy of property rights. Developments in Continental Europe, however, followed a different path, and came to reflect, by and large, the social entity conception of the corporation which conceives the purpose of the corporation to be much more than the maximisation of shareholder returns.[5] Surely contributors must be assured a rate of return sufficient to induce them to contribute their capital to private enterprise. But the corporation has other purposes perhaps of equal dignity, i.e., the satisfaction of consumer wants, the provision of meaningful employment opportunities and the making of a healthy public life of communities (Charkham, 1994:10).

Since the eighties, there has begun, in both worlds, a movement toward convergence: the continental modes have begun to look for more flexibility in decision-making whereas in the US, a concern for

'good corporate governance' and 'ethical business' has assumed importance. In general there seems now to be less disagreement on the view that the corporation is a complex, multi-faceted entity embedded in webs of societal relationships, and that it can be legitimately expected of the corporation to attempt to strike a balance between the different social groups with which it interacts. Further, there is increasing recognition of the fact that how exactly this balance is struck is circumscribed by the specificities of the context within which corporations operate, i.e., the different systems of political, legal and economic institutions, as well as differences in cultures and value systems. Within a given macro-institutional framework, however, how an individual corporation strategises to obtain this balance depends on the people and the structures that govern the corporation. Hence, the question as to *who controls the corporation* remains central to all inquiries like ours, i.e., those which seek to analyse the relationship between corporate actions and the broader political-economy.

Corporate control

The problem of control of corporations (or *public limited companies* as they are technically called) is rooted in the fact that they are owned by a large number of owners, each of whom owns small pieces (i.e. stocks) of the company. A public company may be 'owned' in any one of the following ways:

- its shares may be held by a large number of financial institutions (FIs) and individual investors, with no dominant holding
- a majority of its shares may be held by FIs and other institutional investors, with one or more institutional investors dominant
- a majority of shares may be held by FIs and institutional investors, but with another corporation dominant with respect to the remaining equity.
- a majority of shares may be held by the public,
- a minority of shares may be held by the public, with the dominant interest in the hands of another company

A public corporation comes, therefore, to be 'owned' by a large number of several different entities at the same time, all of whom cannot take part in its management and direction simultaneously. Figure 2.1 below represents a particularly complex model of corporate ownership. Note in particular how the Iron Ore Co. of Canada is 'owned' by a series of

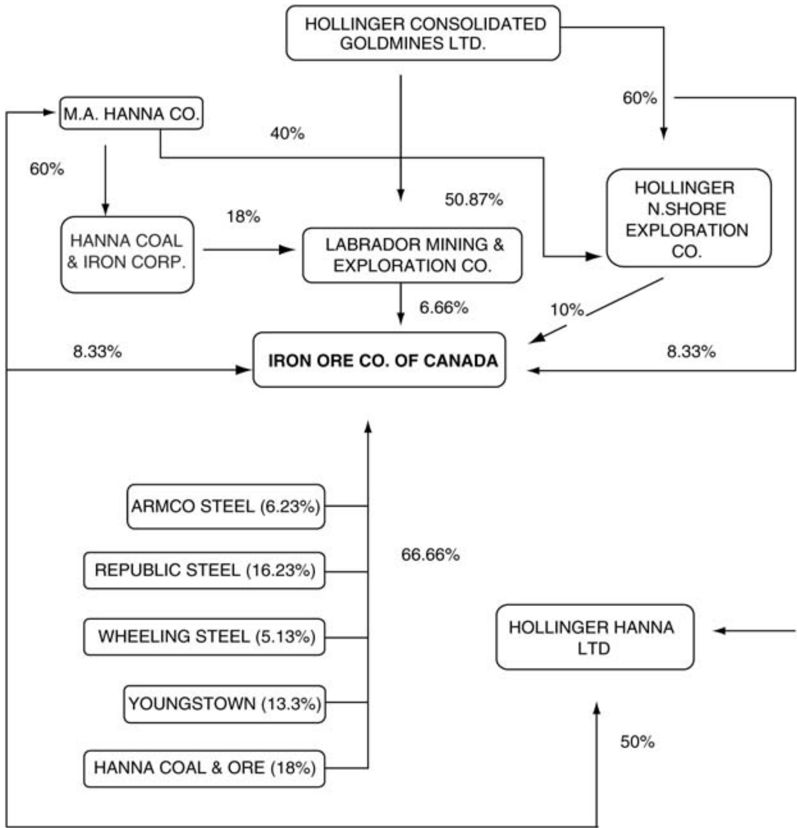


Figure 2.1 Ownership of the Iron Ore Company of Canada
Source: Based on Daniel R. Fusfeld, 'Joint Subsidiaries in the Iron and Steel Industry', *American Economic Review*, Vol. 48, No. 2, p. 584.

direct and indirect shareholders, each of which are separate corporations owned by their respective group of shareholders. Owing to such complexities, decision-making in public corporations usually rests with a group of professional managers who, along with the board of directors, come to exert considerable (if not exclusive) control over its evolution. Such a separation of ownership and management, or more importantly, the separation of *ownership and control*, comprises one of the central problems of modern corporate economies.

This 'problem' was first documented by Berle and Means (1932) in their famous treatise *The Modern Corporation and Private Property*. They

argued that between the Civil War and the Great Depression, a separation of ownership and management had taken place. This separation had resulted in the emergence of (1) a professional managerial class whose power was bolstered by the advent of *scientific* management in the early twentieth century and (2) the maturation of stock exchanges which led to the emergence of *financial capitalism*. Berle and Means observed and documented that, by 1932, the entrepreneurial capitalism of the nineteenth century, where owners and managers were the same people, had given way to financial capitalism where owners and managers were no longer the same. Berle and Means offered the more controversial proposition that this separation of ownership and management also meant the separation of ownership and *control*. Specifically, they argued that in 1932, '44 per cent by number and 58 per cent by wealth (assets) of the largest 200 non-financial corporations... were under the control of management' (Herman, 1981:5). In their view, this transformation to management control amounted to a revolutionary change in property relations in the US – as fundamental in scale and importance as the shift from feudalism to capitalism.

The idea of management control since then has given rise to a number of hypotheses regarding managerial objectives and the use of managerial power. In traditional notions of the corporation, the latter is looked upon as a relationship of trust, associated with which is a normative belief that managers and directors would necessarily act in the interest of the owners, since it is in them that the owners of the company have delegated authority and responsibility. In other words, the managers would operate on behalf of the shareholders maximising their returns and consider themselves to be accountable to the shareholders. The disjuncture between this normative model of *responsible stewardship* and actual corporate behaviour has prompted analysts to offer alternative accounts of the corporation and corporate control (Fama and Jensen (1983). More contemporary theories of the corporation conceptualise the corporation as *a nexus of contracts* between principals (shareholders) and agents (the directors). Contract theories then go on to explore how these 'contracts' can be designed so as to minimise conflict between principals and agents.

Whatever the theoretical approach, the point of departure of managerialism was the fact that ownership had ceased to be the basis of control fairly early on in the life of corporate capitalism and as the diffusion of ownership continued, it became almost irrelevant to corporate control. In other words, control of the corporation became possible *without*

ownership, i.e., *without any substantial financial stake in it*. This is one of the most significant developments in the history of the corporation, and I will return to it below. For now, let us look at some alternative sources from which corporate control can arise. The following table presents some possible bases and mechanisms of corporate control.

Management (or managerial) control designates cases where the power over key decisions is held by an insider group (the managers) who have a relatively small ownership stake. Management control can be acquired through various processes. For one, managers who have been hired by the company may come to acquire strategic positions in the board. For another, senior management positions and board seats may be acquired by virtue of one's relationship to the founder of the corporation. More often than not, these positions are acquired through inheritance (of company stocks), and in that case, control is exercised jointly through strategic position and direct ownership (although the ownership may be quite small). This is the route through which *family control* over a corporation is maintained and exercised.

In the West, however, the rise in management control signified a decline of individual/family control over the large corporation (Herman, 1981). While this is certainly true of the US and the UK, it is much less true for other advanced countries like Canada, Belgium, Spain, and Italy (Clement, 1975; La Porta *et al*., 1998). As in this latter set of countries, familial control in large enterprises remains strong all

Table 2.1 Corporate Control: Types and Mechanisms

Types of control	*Mechanisms through which control is exercised*
Control through strategic position (or management control)	Senior management position; seat on the board of directors
Control through ownership of shares	Ownership of a majority of shares or, ownership of a minority of shares
Financial control	Representation on the board from creditor institutions
Control through political institutions	Government control as in India; control by workers as in Germany
Control through inter-corporate networks	By having control over an 'apex' company which acts as the centre of a large corporate network

Source: Adapted from Herman (1981).

over the Third World. In India, for example, many of the largest companies are still controlled by industrial families. Members of these industrial families obtain corporate control through their nomination to a senior executive position by senior family members. This is often bolstered by minority ownership, although their control exists more by virtue of the position (and their nomination to it) rather than ownership.

Control through majority/minority ownership: Majority ownership includes all cases of ownership in excess of 50 per cent of voting shares. The idea that one necessarily needs to own in excess of 50 per cent to become a majority owner has changed over time, with the increasing diffusion of ownership of corporate equity. Recent writers suggest that a holding of about 5 per cent is enough to exert control. In other words, with the evolution of the corporation overtime, minority control has emerged as the norm of the day. As Maurice Zeitlin writes in his classic work:

> Minority Control is one of the most important consequences of the development of the corporation as the decisive unit of productive property: the great majority of shareowners are stripped of control by a small segment of the capitalist class made up of the principal shareowners of the large corporations, who are thus able to extend their control of capital (and of the political economy) far beyond their ownership.
>
> (Zeitlin *et al.*, 1974:92)

What Zeitlin suggests here is of utmost and enduring importance: the emergence of minority control made possible *the co-existence of widely diffuse ownership with concentrated control* (Zeitlin, 1974). However, minority ownership does not give one control unless it is combined with a strategic position (Herman, 1981). Indeed, minority ownership combined with a strategic position in the company (e.g., a seat on the board) has emerged as the most common mechanism of corporate control in recent times.

Financial control implies control by commercial or investment bankers, other creditors, or financial speculators. The evolution of financial control, and the dominance of financial institutions (FIs) has emerged as an issue of great significance in recent years. The classic model of financial control is, of course, provided by Germany; Japanese corporate structures also show high degrees of interlocking between banks and corporations but the relationship between the two constitutes something quite substantively different from *financial control*. In Japan,

banks and companies are elements of the same entity, whereas in Germany they are more distinct from one another. In India, the participation of FIs is particularly critical. As I will show in Chapters 4 and 5, in some of the largest Indian corporations they hold close to 50 per cent of the total equity, whereas the directors and their relatives hold less than 1 per cent. Does this imply that Indian corporations are controlled by FIs and directors have no control? The reality is in fact quite the contrary. Although there is a system of appointing nominee directors from the institutions which invest in large corporations, it is largely the case in India that nominee directors have been passive in their involvement in management.

Government control, taken to imply control of private sector firms by the government, is mostly absent in capitalist economies. However, in most economies the state imposes constraints on corporate activity rather than actually controlling the (day-to-day management) of the corporation. Though companies wholly owned and controlled by the state (known as public sector corporations in India) comprise a significant sector of India's industrial economy, the are not our immediate concern in this work.

Inter-corporate control is, in the present context, probably the most pervasive form of corporate control. Inter-corporate control implies a situation where a number of companies are governed by an apex company. The apex company exerts both direct and indirect control on the member companies through an elaborate network of *inter-corporate investments*. Out of this elaborate network of investments emerges the large corporate groups or 'network': the 'group' comprises typically a large number of subsidiaries and associate companies producing a wide variety of products catering to a large number of markets. By and large, the production decisions of each of these member companies come to be controlled by the group.

A number of instruments are used to retain group control, the foremost of which is, of course, inter-corporate investments. The other is *interlocking directorships*; as the name suggests, *interlocking directorships* imply a situation whereby a limited number of individuals occupy directorships in a large number of companies in the group. Of course, it is also very commonly the case that the same set of people occupy directorships *across different groups*, which implies that control of several groups and a large amount of productive assets get exercised by a fairly limited number of people. As Louis Brandeis wrote in his famous treatise *Other People's Money and How the Bankers Use It*, interlocking directorships between financial and non-financial companies had already

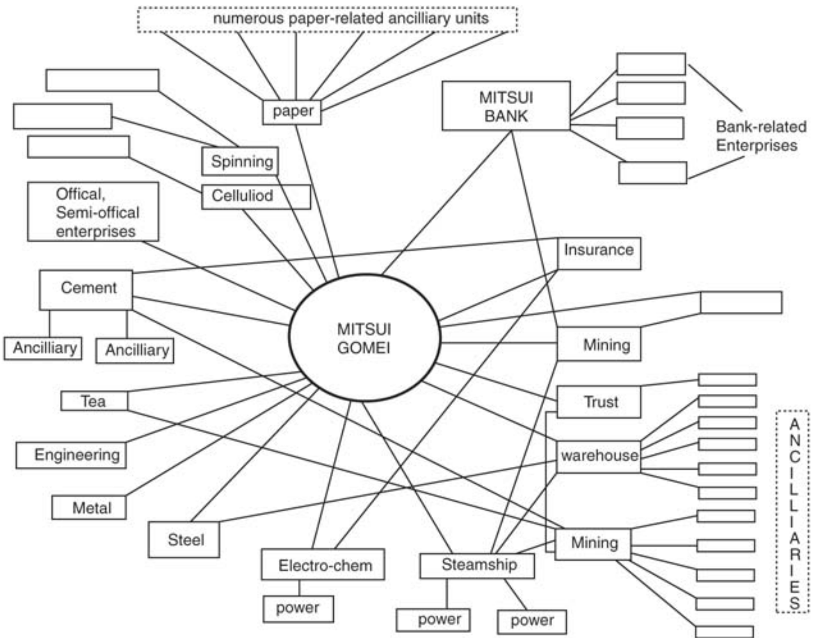


Figure 2.2 Inter-Corporate Control Through an Apex Company: The House of Mitsui
Source: Adapted from Allen, G. C. 'The Concentration of Economic Control in Japan', *Economic Journal*, Vol. 47, Issue 186, pp. 271–86.

emerged as the most potent instrument of corporate control in America in the early twentieth century (Brandeis, 1967).

More generally, the problems associated with the emergence of 'corporate groups' (i.e., a series of companies linked via directorships and investments), had become a subject of intense debate since the beginning of the century. In the US, there had emerged fairly early on a social consensus *against* increasing centralisation (Chandler, 1977). What is interesting, however, is that despite this apparent consensus and a fairly early development of anti-trust laws, the corporate group remains the predominant organisational form in the U.S., and in most parts of the world. Indeed, corporate groups have taken on particular relevance in the context of East Asia, both in explaining the phenomenal growth of those countries as well their recent crises.[6]

This phenomenon of corporate groups or conglomerates (as I would refer to them more often) that is examined below.

Understanding corporate groups

As noted above, corporate groups or conglomerates are probably the most predominant form in which the modern corporation exists. Referred to as 'group companies' in the Anglo-American literature, as *zaibatsu* in Japan, as *chaebol* in Korea, 'business houses' in India, the term conglomerate implies a number of quasi-independent but associated firms which are controlled by an apex controlling authority, embodied usually in a firm or an investment trust. The control exerted by the apex body may be direct or indirect and may combine varying degrees of financial control. The critical point to note in this context is that the control of the apex body on the other firms is not determined by the extent of ownership or financial control. For instance, the apex company may have bought up one of the group companies through debt or equity capital raised from outside investors (leveraged buy-outs). In that case, the apex company has no financial control on the group company, but it obtains full managerial control on the newly bought firm.

There may be several different kinds of association between the apex firm and the other firms in the conglomerate. The simplest types of

Table 2.2 Formalities of Subsidiary Operation

A. Integration of Activities of the Parent Company and the Subsidiary

The following activities are co-ordinated by the parent company for all its subsidiaries and affiliates:

- Sales and marketing efforts
- Purchases of inputs
- Coverage of warranties
- Loans, guarantees, or other financial assistance
- Inclusion of the subsidiary in the insurance coverage of the parent company
- Consolidated tax returns
- Use of common corporate names, logo, trademarks, advertising campaigns;
- Representations to the public that the constituent companies are integral parts of one group

B. Separation of Activities of the Parent Company and the Subsidiary

- Separate books of account
- Separate bank accounts
- Separate meeting of Board of Directors
- Separate meeting of shareholders
- Separate directors/officers/employees/offices

Source: Adapted from Teubner (1990:90–1).[7]

relationship between an apex firm and other firms are described as that between a *holding company* and a *subsidiary*. In most countries, subsidiaries are technically defined as follows: Company B becomes a subsidiary of Company A, (and A becomes the *holding company*), only if (1) A owns 50 per cent or more of the nominal value of B's equity capital or (2) A exercises or controls more than half of the voting power of B or (3) A controls the composition of the board of directors of B. Needless to say, increasing complexity of corporate structures has rendered such direct relationships between apex companies and affiliate companies quite rare. Most contemporary corporate structures are characterised by a series of complex inter-relationships between companies that blur the distinction between holding companies and subsidiaries. The following illustrates the formal aspects of the relationship between subsidiaries and the core firm.

Depending on the nature and complexity of the parent-subsidiary-affiliate relationship, one can identify a variety of structures of corporate groups. I will discuss here the three most common types of group structures: the straight line subsidiary structure, the inter-locking structure, and the satellite structure.

The Conglomerate as a series of *Straight Line* Subsidiaries:

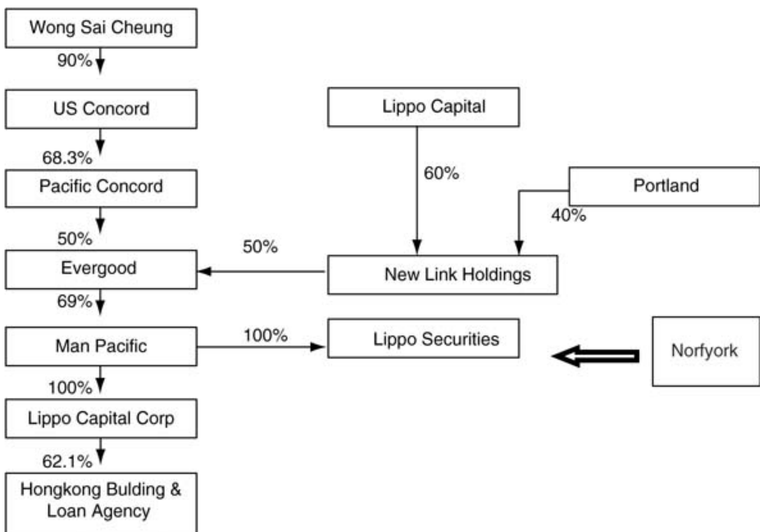


Figure 2.3 Variations of Corporate Structure: The Straight Line
Source: Adapted from Tricker, Robert I., *International Corporate Governance*, 1991, p. 382.

This straight-line structure is one of the simpler corporate structures. Here the apex company owns a series of subsidiaries which are unrelated to each other by criteria (1)–(3) above.

By contrast, the other structures allow for a more complex relationship between the affiliates and the apex company (Figures 2.4 and 2.5 below). Allegedly, such structures perform three particular functions: help protect better against take-over threats, help protect against regulations preventing inter-corporate investments and finally, help reduce

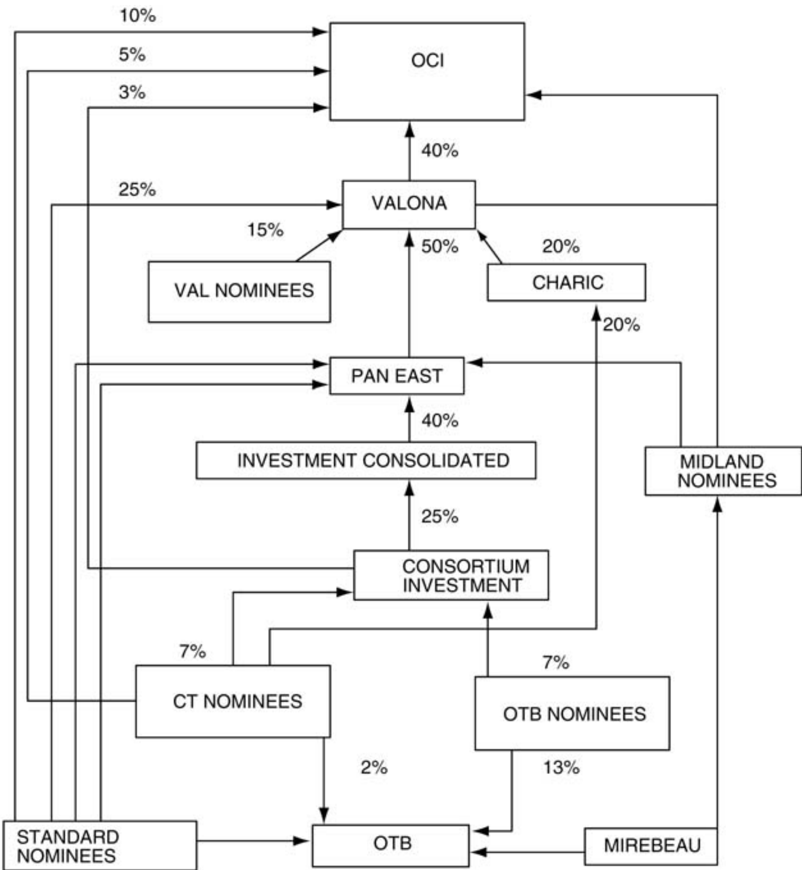


Figure 2.4 Variations in Corporate Structures: The Conglomerate as a set of Interlocking Subsidiaries
Source: Adapted from Tricker, Robert I, *International Corporate Governance*, 1991, p. 327.

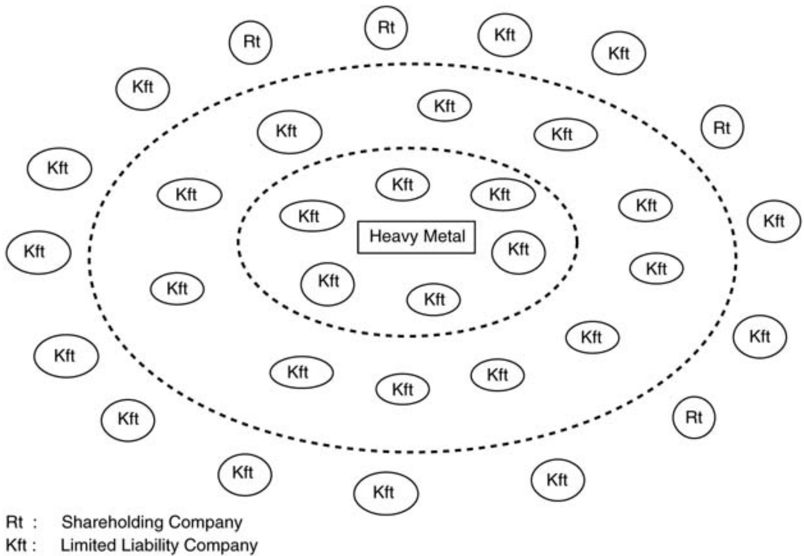


Figure 2.5 Variations in Corporate Structure: the Satellite
For all companies immediately surrounding Heavy Metal, it owns 100 per cent; for companies in the next ring, it owns between 51 and 99 per cent; for companies in the outermost ring, it owns between 12 and 50 per cent.
Source: Stark, D, *Recombinant Property in East European Capitalism*, 1994.

tax obligations of the group as well as individual affiliate members by blurring the boundaries of ownership.

The satellite, while not uncommon in other countries, has emerged as particularly common in the transitional economies of Eastern Europe. Consider, as an illustration the case of one of Hungary's largest metallurgy firms. The apex company *Heavy Metal* is the majority shareholder of 26 out of 40 corporate satellites. As Stark explains,

> Like Saturn's rings, Heavy Metal's satellites revolve around the giant corporate planet in concentric orbits. Near the centre are core metallurgy units, and strategic planning units held in a kind of geosynchronous orbit by no less than 100 per cent ownership. In the next ring, where corporate headquarters hold roughly 50–59 per cent of the shares . . . these satellites are linked to each other and to the core units by ties of technological dependence. Like the inner ring, they are kept in geo-synchronous orbits by the headquarter's majority ownership as well as by their technological dependence. Relations

> between the satellites at this middle ring and the company centre are marked, on the one hand, by the centre's recurrent efforts to introduce stricter accounting procedures and tighter financial controls, countered, on the other hand, by the unit's efforts to increase their autonomy – co-ordinated through personal ties and formalised bi-weekly meetings of the 'Club of KFT Managing Directors'. . . . The satellites of the outer ring are even more heterogeneous in their production profiles and are usually of lower levels of capitalisation. Units of this outer ring are less fixed in Heavy Metal's gravitational field: some have recently entered and some are about to leave. Among the new entrants are some of Heavy Metal's domestic customers. Unable to collect receivables HM exchanged inter-enterprise debt-for-equity for its clients, preferring that these meteors be swept into an orbit rather than disintegrate in liquidation.
>
> (Stark, 1994:18)

Most groups manifest a combination of elements of the three structures I noted above, depending upon the institutional structures within which they are embedded. With the intensification of global competition, relations between group companies have become more complex; at the same time that they have become somewhat less structured, they have also become highly centralised. I will explore this below.[8]

For now let us proceed to answer three critical questions that need to be considered in order to assess the impact of corporate groups: First, how exactly can one account for the emergence of corporate groups? Are they the outgrowth of conscious design (and corporate strategies) or do they reflect an inevitable natural dynamic? Second, are corporate groups 'efficient' as forms of economic organisation? What accounts for their efficiency? And third, what are the political effects of the emergence of corporate groups?

Emergence of corporate groups

In order to analyse these questions, it is necessary to go beyond an examination of the morphology of corporate groups and trace their evolution historically. For our purposes, it is important to see the emergence of specific group structures at particular points in time as the outcome of particular strategies of accumulation chosen by corporations. I will refer here primarily to two broad strategies, *agglomeration* and *enucleation* (Sapelli, 1990). *Agglomeration* implies the expansion of the group through mergers and acquisitions, where

such acquisitions are made, allegedly, in order to rationalise interdependencies and enhance technological and managerial performance; historically, agglomeration was used as a strategy to delimit market competition and set output rates, market shares and price levels.

Enucleation represents a subsequent development in corporate history and implies the passing from a multidivisional corporate structure to a structure where the divisions were vested with greater autonomy: it evolved out of the strategic search for a reduction of internal costs and for expansion through the continuing selection of technical, market, service and financial opportunities.

In the following table, I have attempted to map the historical pattern of formation of corporate groups through these two corporate strategies.

As indicated in the table, the patrimonial group emerged during the earliest phase of capitalism in Britain and the US. According to Sapelli, 'the "central economic agent" in the patrimonial group is characterised

Table 2.3 Evolution of Corporate Groups: A Suggested Historical Trajectory

Period	*Group Structure*	*Nature of accumulation and value addition*	*Strategy for corporate growth*
Pre-industrial	Patrimonial	Value addition through 'primitive accumulation' – usury, trade or other forms of rentier incomes	agglomeration
Laissez-faire Industrialisation	Financial	Value addition through financial participation in potentially high-yield projects; corporate income comprises of both rentier earnings and profits	agglomeration
Fordism	Managerial	Value addition through (1) increasing quantity of output, (2) technology and process innovation and (3) diversification	enucleation
Post-Fordism	Network	Value addition through optimising degrees of flexibility in quantity of output, choice of technology and choice of process	agglomeration

Source: Adapted from Sapelli (1990).

solely on the basis of its activity of maximising return to capitals by operating on controlling shareholdings' (Sapelli, 1990:195). In other words, corporate control in this model derived solely out of ownership, where ownership was at the same time the ownership of both risk and rewards.

The patrimonial group was followed by the emergence of the financial group. In sharp contrast to the patrimonial group, the apex body in a financial group did not necessarily *own* each member company, but was inevitably their principal financier. Also, in contrast to the patrimonial group, control in a financial group was exerted through *debt*, rather than equity financing. It is critical to note that the financier (of debt capital) was essentially different from the owner (of equity capital) in that the former did not share the risk, but was contractually guaranteed a payment irrespective of the success of the investment. Expansion of a financial empire came about specifically as a result of this fact: financiers were quick to capitalise on the inability of borrowers to pay back borrowed capital, and sought compensation by buying out defaulting firms at prices significantly lower than their market value.

The expansion and consolidation of financial groups became particularly fervent during the nineteenth century, and set the preconditions for the emergence of the *industrial* group. The industrial group became particularly consolidated in the US for its ability to control the enterprise system with not only financial instruments but also other specific types of managerial instruments, i.e., product policy, logistics, choice of technology, systems of internal communication, etc. Obviously, the industrial group represented the archetypal organisational form associated with Fordist production, and while it could realise significant efficiency gains in that era, the intensification of global competition made visible some of its obvious inadequacies (Brenner, 1998). Without going into a detailed discussion of these inadequacies, let us note the following. First, the expansion of the typical Fordist group depended critically on the continued expansion of the market that allowed for increasing degrees of integration, both vertical and horizontal. Second, such a continued expansion of the market depended in turn on the absence of global competition as well as on the buying power of overseas markets.

With the increase in global competition it became necessary to ensure decision-making at an enormous speed, not possible in an organisational form composed of a series of *autonomous* divisions. Obviously, such divisional autonomy presented the 'group' from responding to market developments and caused them to miss out on opportunities.

It is this sense of missed opportunities that gave rise, finally, to the *network group*. Associated primarily with the Japanese-style flexible accumulation, the term *network* refers to a chain of supply and distribution firms tightly controlled by a core firm at the centre where the core firm usually has little or no equity ownership in those firms (Imai and Itami, 1984; Gerlach, 1989). As is well-known, analysis of Japanese organisational forms such as this has preoccupied Western theorists quite significantly. More often than not, theorists in the U.S. have emphasised their fluidity and the lack of centralised control; other theorists, especially those on the continent have emphasised exactly the opposite, i.e., the high degrees of centralised control.[9] In this continental view, the 'network' is actually a highly hierarchical structure. Such a hierarchy is required, paradoxically, in order to be fully flexible in responding to the uncertainties of global competition. For ensuring full flexibility, every unit of the network has to completely surrender its autonomy to the 'centre'. The centre alone plans and controls corporate strategy according to market demands it perceives, and sends commands to the subordinate units which simply pick and execute these commands.

In other words, while some theorists see the strength of the network to lie in its ability to imitate markets, some others see its strength to lie in its ability to imitate 'hierarchies'. The market-view visualises the network (and more generally, any firm) as a series of contracts, while the hierarchy-view visualises it as an 'organisation' embodying essentially different co-ordination principles. In what follows, I will explore this debate between markets and hierarchies and contracts and organisations. This exploration should help us not only to a better understanding of the network as a category, but also give us a better insight into the variety of organisational forms through which contemporary corporate capitalism operates. More broadly, this debate can provide us with an entry to the central question for developing countries today: what kind of development is possible when complex corporate groups become the central economic actors? Are the specific organisational forms through which they operate likely to make a difference? What kind of strategies are they likely to employ? What impact are those strategies likely to have on society?

Networks: contract, organisation or beyond?

Let us begin with the distinction between contracts and organisations. Contracts represent a simple and voluntary exchange relationship

between two (or more) interested parties. For our purposes, the most important aspect of a contract is that it is established and executed by the parties themselves, *without the need for any external entity to intervene*. Using contracts as a unit, organisations, especially firms, can be visualised as *a series of contracts* between different parties: the shareholders, directors, employees, creditors, suppliers, etc. (Grossman and Hart, 1986; Alchian and Demsetz, 1972:777).

A problem arises, however, if one takes into account four factors: (1) that there is uncertainty and prospective parties cannot adequately assess the future value of contracts under such uncertainty; (2) that the contracting parties resort to opportunistic behaviour and do not respect the terms of the contract; (3) that people are rational but their rationality is 'limited'; and (4) that there may exist asset specificity, i.e., a situation where one of the contracting parties is not willing to give up the asset currently owned in exchange for the asset that is offered (Williamson, 1985).

If one or more of these factors prevail, either establishing or executing contracts can become a problem. It is under situations like this that organisations develop, but even within organisations, rational individuals seek to preserve the basic elements of contract. This is because all rational actors (and rational societies, which are simply an aggregate of rational actors) choose arrangements which minimise *transaction costs* and contracts clearly have a greater ability than organisations to do so.[10] Since even within organisations individuals seek to preserve the basic elements of a contract, Williamson suggests that there is essentially no difference between the two as institutional forms. In this view, Japanese-style organisations like the *keiretsu* are 'hybrid' arrangements that are chosen at a point where on the one hand market controls are weak, and on the other, the transactions cost of a fully integrated organisation are too high (Williamson, 1985:83).

A number of theorists have argued that such an attempt to level the distinction between contracts and organisations reveals a serious conceptual flaw in Williamson's theory. Teubner, for example, finds the limits of mainstream economic thinking reflected here, especially in the claim that the organisation 'has no power of fiat, no authority, no disciplinary action any different from contracting' (Alchian and Demsetz, 1972:777). The result is 'an impossible reductionism: the attempts of the new institutional economics to explain organisational behaviour solely in terms agency, asymmetric information, transaction costs, opportunism and other concepts drawn from neo-classical economics. Such a conceptualisation ignores key organisational

mechanisms such as authority, identification and co-ordination, and hence are seriously incomplete' (Simon, 1991:43).

The alternative argument is that contracts and organisations are fundamentally different social systems: they differ from each other in principle. In sum, organisations are built on *co-operation* and not *exchange* as contracts are. In this sense, contracts are self-referential whereas organisations are not – organisations must behave according to some principle, which exists irrespective of the wishes of its members. Purely market-based contractual relations are on the one hand extremely flexible, changeable and innovative; on the other, they do not develop long-term attitudes, forcefulness, coherence and accumulated experience. Organisations on the other hand *do* develop such long-term orientations but are susceptible to rigidity, bureaucratic problems, problems of motivation, lack of innovations etc., which cause economic agents to miss out on opportunities. Teubner argues that it is this sense of missed opportunities – rather than calculated responses of individual actors – that provided the most important stimulus to new institutional forms like the network (Teubner, 1993).

Embedded in these contingencies, the network necessarily reflects these dual concerns: on the one hand, the need for flexibility as characteristic of the market, and on the other, the need for stability as characteristic of the hierarchy. It is thus an enhanced form that goes beyond both markets and hierarchies and is capable of encompassing the characteristics of both without ever dissolving their differences.

The nature of political power of corporate groups

I can now proceed to answer our third question; viz., what is the political and social impact of the emergence of networks as corporate actors? The answer to such a question is obviously context-dependent. However, some generalisations may be useful.

Analysts dealing with the question of political power seem to suggest, fairly unequivocally, that corporate groups are highly powerful entities with the power to permeate all other decision-making centres in society. While the Marxist theories about the structural power of capital most powerfully make this point, they do not, however, analyse the ability of particular organisational forms – such as corporate groups and networks – to exercise their power in particular ways. For example, as both Sapelli and Teubner argue, by devising ways to incorporate the contrary principles of markets and hierarchies within the same organisational form – large corporations/groups develop tremendous resilience to external

regulation and societal control (Teubner, 1993). In Teubner's view, any simple understanding of the corporation and/or a limited view of the tasks of legal regulation will not go far in curbing the political power of these corporations. What is required is an understanding of the precise ways in which corporate networks combine elements of markets and hierarchies so as to *internalise* efficiency gains as well as *externalise* risks. This *dual ability* to realise efficiency gains and externalise risks brings to corporations (illegitimate) advantages which regulation must seek to eliminate.

Further, the success of networks may depend on a host of other factors, such as 'internal power relations, exploitation of the internal members, opportunistic behaviour of the core firm itself, shifts of risks to third parties, artificial contractual restrictions of responsibility, and synergies of risks for other people' (Teubner, 1993:58). Arguably, these require extensive regulation to an extent and in areas where theorists of corporate regulation have not yet ventured. As Sugarman and Teubner (1990) summarise:

> investors in complex groups have little knowledge or even less control over the way in which their capital is being employed. The directors of such enterprises can embark on virtually any form of business activity or speculation without the need to secure the approval of their shareholders or in many cases even to inform them of the nature of the operations. The position of minority shareholders in partly owned subsidiaries is notoriously weak.... There is no effective protection for the creditors of subsidiaries which are permitted or even encouraged to go into liquidation with insufficient funds to meet their obligations.... Nor is there any protection for the employees of supposedly independent subsidiaries which are run down or closed in the interests of greater profitability for the group as a whole, despite the obligation of the directors of those subsidiaries to act in the best interest of the subsidiary, including its employees, regardless of the interest of the group as a whole.[11]

Authors like Sapelli, Streeck *et al.* raise a question that is more familiar to analysts of social power: has the rise of large complex corporate organisations systematically decreased state power? Reviewing US history, Sapelli argues that such a possibility has always been foremost in the minds of state elites, who have looked upon regulation as the solution. The institutionalisation of regulation, however, required a systematic process of interaction between state and capital; paradoxically,

it is this very process that legitimised the demands of the corporation, and its power to make such demands, by inscribing it into the public realm. This has led to a situation where 'economic decisions increasingly derive not so much from free competition as from a system of agreements amongst representatives of big firms, organised interest groups and the State' (Sapelli, 1990:191) In such a situation the liberal conception of society – as the confrontation of a political class and an economic class where each imposes a check on the power of the other – breaks down. It remains true though, that the two classes pursue two different objectives: the former seeks *consensus* and the latter seeks *economic and organisational rationality*. However, what happens with the deepening of capitalism (which is reflected in the development of complex organisational forms), is that there emerges increasing interdependence between the two classes. In order to secure consensus, the political class (acting through the state) becomes dependent on certain distributive measures, the resources for which are provided by corporations in the form of taxes, donations, employment, investment etc. On the other hand, to secure economic and organisational rationality that augments profitability, corporations become dependent on the state. It is this interdependence that increases the political power of capital under organised capitalism in a manner that is essentially different from earlier forms of capitalism.

As mentioned at the outset, the specific ways in which corporations exercise their power depend on the specific ways in which the relationship between state and capital has been historically shaped. For many countries, both states and businesses have developed through highly collaborative relationships where they were united by the need to oppose colonialism. India is a quintessential case where an early collaboration between political and economic elites made available to businesses certain avenues for the exercise of power that might have been unavailable otherwise.

Profit strategies and political power

The question of political power of large corporations is linked explicitly to the ways in which profits are generated. There exist a widely divergent set of profit theories which conceive of profits fundamentally differently: needless to say, these differences in conceptualisation are so fundamental that they generate quite different notions about the normative justifiability of profits. In what follows, let us briefly review different notions of profits and profitability.

For our purposes here, the most important distinction is perhaps between *pure profits* and *market profits*. The idea of pure profits, associated primarily with Joseph Schumpeter and Frank Knight, asserts that profits should arise either as a reward for innovation or for superior decision-making abilities under situations of risk. These profits are *pure* in the sense that they do not arise out of short-term market disequilibria, but arguably out of more fundamental factors. Market profits on the other hand may be defined as those that arise not out of structural factors but out of market conditions. Schumpeter identifies innovations as the only source for pure profits, where innovation comprises the following:

> (1) The introduction of a new good – that is one with which consumers are not yet familiar – or of a new quality of a good. (2) The introduction of a new method of production, that is one not yet tested by experience in the branch of manufacture concerned, which need by no means be founded upon a discovery scientifically new, and can also exist in a new way of handling a commodity commercially. (3) The particular branch of manufacture of the country in question has not previously entered, whether or not this market has existed before. (4) The conquest of a new source of supply of raw materials or half-manufactured goods, again irrespective of whether this source already exists or whether this has first to be created. (5) The carrying out of a new organisation of any industry.
>
> (Schumpeter, 1961:66)

Schumpeter's argument is well-known: the innovative ability of an entrepreneur is what constitutes capitalism's underlying dynamic; profits are simply a reward for this unique ability and hence, fully justifiable. Frank Knight follows a similar line of reasoning; he attributes profits to the ability of the entrepreneur to take risks under uncertainty:

> Profit arises out of the inherent, absolute unpredictability of things, out of the sheer brute fact that the results of human activity cannot be anticipated and then only in so far as even a probability calculation in regard to them is impossible or meaningless. The receipt of profit in a particular case may be argued to be the result of superior judgement.
>
> (Knight, 1921:46)

In both these instances, however, pure profits must necessarily be temporary, for, once possibilities of pure profits are recognised by

other agents, the innovations would be imitated and pure profits would disappear. It is in this sense that in the realm of neo-classical economics, profits can be conceived only in *disequilibrium* i.e., *these profits become available only during the period in which the system has not fully adjusted to changes*. In any event, it is not clear whether pure profits either in the sense of Schumpeter or Knight can be realised without the aid of market power, and in that case, it is suspect to what extent those profits arising out of uncertainties or innovations are not eventually reducible to market profits.

As to market profits, there is little disagreement that they are earned through *market power*, which in the narrow neo-classical sense implies the power to manipulate prices and outputs. In neo-classical economics, such monopolistic power is often naturally associated with the growth in corporate size and as such is an indication of the inherent dynamics of the market system. Economists, however, are aware of the problematic effects of monopoly power and suggest regulation to check such power. What neo-classical economics does not theorise adequately is how such market power gets ineluctably linked to *political* power, and can be wielded eventually through various institutions associated with the state. In most modern corporate economies, such political power is not unmitigated and has to be negotiated continuously between business and the state (and by implication, between business and society). Liberals place an enormous emphasis on this contingent nature of the political power of business in democratic societies and use it to confront the Marxist theses that profits are linked, above all, to the structural characteristics of capitalism.

The theory of profits advanced by Marxists and Marx-inspired political economists is well-known. In this view, profits originate because of the exploitation of labour by capital, where exploitation is defined as the appropriation of surplus value by the owners of capital from the owners of labour-power. Needless to say, profits here are not conceptualised as a reward for the capitalist's unique abilities, but arise out of the structural power vested in capital in a capitalist mode of production. Profits are therefore most explicitly linked to political power, albeit in a fundamentally different sense than in liberal approaches such as rent-seeking.

While all Marxists raise certain critical issues with respect to the genesis of profits, some Marxists have seen in capitalism the potential for increasing industrialisation, employment and proleterianisation, and eventually, the potential for transformation to socialism. As is well-known, there is a body of Marxist theory that advocates the spread

of capitalism in the Third World, specifically with these assumptions (Brewer, 1990; Warren, 1980). In so doing, these Marxists choose to ignore the specificity of capitalisms; in particular, they ignore the 'retarded' or 'distorted' nature of peripheral capitalism that distinguishes it from capitalism at the centre. This insistence of some Marxists on the irrelevance of *form* also assumes importance in the current context of economic reforms in that it makes for a much impoverished policy debate. From the very inception of the reforms, there has hardly been any discussion – or even an explicit recognition – of the fact that there was an unquestioned acceptance of the Anglo-American model as the only way forward. This implied, for instance, an unquestioned faith in the potential of capital markets, in the speedy deregulation of labour laws (especially job security), in increasing concentration through mergers and in ascribing primacy to near-term profitability. As is increasingly becoming clear, these strategies are resulting in a trajectory of growth that does not conform to India's developmental needs.

Of course, India's acceptance of the Anglo-American model was not an isolated event, but a part of the general 'triumph' of neo-liberal economics that emerged in the eighties. Since then, events like the Asian financial crisis, the more general crises in Europe – contrasted with the 'boom' in the US – have only managed to reinforce this triumph. However, there is a growing body of literature that suggests a careful assessment of the Anglo-American model, especially in the aftermath of the Asian crisis (Stiglitz, 1999; Mathews, 1998). As Mathews explicitly argues, it is because of the movement towards the Anglo-American model – with the emphasis on near-term profitability – that the East Asian systems became increasingly incapable of fostering economic development, even in the narrow sense of economic growth.

Profit strategies, political power and the question of development

Development is a complex concept involving economic, political and social dimensions. Here I emphasise the interplay between the first two, acknowledging implicitly the relationship with the latter. I am interested in particular in economic growth and an associated pattern of industrial transformation that has the potential to accomplish at least three things:

- bring about a sustained increase in assets, incomes and skills of workers;

- unleash a process where the semi-feudal conditions and relationships under which labour is initially employed are replaced by (enforceable) contractual arrangements regulated either by the state or the market or a combination of the two;
- gradually democratise the realm of production (this includes not only increased participation of labour in decision-making, but also a gradual de-politicisation of the relationship between state and business in a way that accumulation and wealth creation are progressively less dependent on such a relationship).

At least two conditions need to be satisfied if the above is to occur. First, it needs to be ensured that profits cannot be generated without genuine value addition *as well as* the continuous expansion of productive capacity. Second, in order that such continuous expansion becomes viable, there will have to occur a corresponding expansion of aggregate demand. This, in turn, will have to occur through redistributive processes emanating from both the market and the state (from the market through increases in wages and corporate asset ownership, and from the state, through taxation).

The first point to note is that there is nothing endemic in the corporate form itself that satisfies these conditions, despite the claims of neoclassical economics. In fact, both in the US and the UK, where the corporate economy exists in its classical (liberal) form, achieving and sustaining macro-economic growth has long emerged as a problem.[12] As Porter (1997) argues:

> The US system of allocating investment capital both within and across companies appears to be failing. Although the system has many strengths, including efficiency, flexibility, responsiveness and high rates of corporate profit, it does not seem to be effective in directing capital to companies that can deploy it most productively and, within companies, to the most productive investment projects. As a consequence many American companies invest too little in assets and capabilities critical for competitiveness (such as employee training), while others waste capital on investments with limited financial or social rewards (such as unrelated acquisitions). This distortion of corporate investment priorities puts American companies in a range of industries at a serious disadvantage in global competition and ultimately, *threatens the long-term growth of the US economy.*
>
> (Porter, 1997:5; my emphasis)

A very similar concern has been raised in the UK In a *Sunday Times* survey of April 1990, it was revealed that British firms performed way above other European firms in terms of profitability. Yet, in the same period, the UK's economic growth was *negative* – and lower than that of France, Germany and the Netherlands, all of which recorded positive growth rates (Hampden-Turner and Tompernas, 1993).

The critical point with respect to both the US and the UK is the relatively high levels/rates of corporate profits *coexisting* with low rates of macro-economic growth. To understand this paradox, it may be useful to examine profit strategies of leading firms in the US and UK Consider, for instance, the famous Yorkshire businessmen James Hanson and George White who, during Margaret Thatcher's regime, were held as paragons of British business and awarded peerages for their performance as wealth-creators. Hanson became particularly noted for his 'commitment to his shareholders' and his ability to acquire companies that continuously maximised shareholder value. The strategy to accomplish this did not, however, come from the growth and expansion of the businesses acquired. Rather it came "from closing factories, from shedding labour, from pension holidays and appropriating surpluses in pension funds, from avoiding stamp duty on purchases by shuffling assets internationally, by tax evasion through the use of 26 Panamanian companies, etc." (Hampden-Turner and Trompenaars, 1993:314).

As a contrast to these Anglo-American approaches to wealth creation, consider the Japanese/East Asian strategy:

> One key factor in Japanese growth was the willingness to invest heavily in both product development and process development for more than two decades while cash returns were low and growing too slowly.... Over the same period many American firms were actually ceding products and functions to foreign competitors and diversifying into less risky and more profitable are as such as car rentals and financial services, unrelated to their original lines of work.[13]

These two fundamentally different profit strategies obviously impact very differently on development. However, little systematic analysis of profit strategies and their macro-economic impact exist, especially in the literature on development. In fact, analyses of profits and profitability of firms in developing countries are few and far between. A notable exception is Haber (1989), who examines the impact of profitability and industrial structure on development in Mexico. While Haber acknowledges the essential contradictions of the Mexican economy, he

remains confined within the neo-classical framework to conclude that the problem of low and uncertain profitability was one of the primary reasons why industrial investment remained diffident. He does not raise perhaps the more fundamental question as to why, despite a fairly high level of industrialisation quite early on, profitability remained uncertain and low.

The primary reason, it may be argued, is that industrialisation could not generate sufficient levels of aggregate demand, by failing to bring about significant and sustained increases in workers' incomes, skills or assets. This inability derives directly from the specific profit strategies of Mexican firms, which were associated primarily with market power and rent-seeking. Unless profits are dissociated from such rent-seeking, high corporate profitability will not be conducive to growth; in fact, the relationship may even be the reverse of what is commonly hypothesised.

Of course, the thesis that rentier or speculative (rather than entrepreneurial) incomes undermine the dynamic properties of capitalism is not new (Veblen, 1904; Veblen, 1923; Schumpeter, 1961; Keynes, 1936; Leibenstein, 1978). Albeit in a slightly altered form, it has also been at the centre of the corporate governance debate in the Anglo-American world since the eighties, especially in the context of the 'American decline' as well as the merger wave of the eighties (Porter, 1990; 1997). In this debate, the critical issue that divides the two sides is the extent to which the capital market – and values created in that market – should determine the overall direction of corporate activity. As Porter suggests, this dominance of the capital market characterises the US and produces the following characteristics:

- The US system is less supportive of investment in general, because of its sensitivity to current returns combined with corporate goals that stress current stock price over long-term corporate value.
- The US system favours those forms of investment for which returns are most readily measurable. This is why the US routinely under-invests in intangible assets, where returns are more difficult to measure.
- The US system favours investment in discrete projects rather than ongoing programs of investment that yield sustained capability improvement. This helps explain why the US under-invests in areas such as employee training and supplier relationships.

By contrast, the Japanese and German systems

> appear to come closer to optimising long-term private and social returns. Their greater focus on long-term corporate position – encouraged by an ownership structure and governance process that incorporate the interests of employees, suppliers, customers, and the local community – allow the Japanese and German economies to better capture the *social benefits of private investment*.
>
> (Porter, 1997:13; my emphasis)

What Porter emphasises most is the differential commitment of investors to projects in the US *vis-à-vis* Japan or Germany; thus in the US what evolves is a regime of *fluid capital* whereas in Japan/Germany we see a regime of *dedicated capital*. Stiglitz (1999) presents a broader characterisation of the differences between the two systems in terms of each of the three markets for labour, product and capital. As Table 2.4 shows, these differences result in significantly different types of enterprises, which in turn are likely to result in different profit strategies.

Clearly then, it is acknowledged in these discussions that different goals of investors and corporations can produce different profit strategies which in turn can differentially impact the content of development. However, conspicuously absent from some of these discussions are (1) explanations as to why in certain societies and at certain points in time corporations adopt certain goals/behavioural patterns and (2) reflections on strategies through which these goals be influenced so that they conform to broader societal priorities. These questions are, of course, not central to Porter's project, and hence he does not provide a systematic treatment of these questions. Amsden (1989) on the other hand, has addressed precisely these questions in her analyses of the phenomenon of 'late-development'. However, as we know, Amsden's faith finally rests on the state and on the fact that for some reason East Asia produced a series of regimes which believed in harnessing capitalism for broader developmental goals.

The critical issue for development today is to respond to a situation where states, bureaucracies and corporations do not share a developmental objective. How are corporate goals and objectives to be influenced in those situations? Two broad sets of answers are currently available. One represents the liberal view that asserts that the prevalence of a particular set of goals/objectives reflects a societal preference for the same, and hence seeking to influence those are essentially undemocratic. The other represents the more critical perspectives, coming most often from Marxists or Marx-inspired theorists who argue that once capitalism is in place, the developmental impact of specific forms

Table 2.4 Characteristics of Firms Under Divergent Models of Corporate Capitalism

Firm characteristic	*Liberal/Anglo-American model*	*Statist/corporatist models*
Labour market		
Inducement to high effort	High unemployment and efficiency wage	High involvement induces effort even with low unemployment
Compensation	Contractual wages	Wages plus profit sharing
Wage differentials	High differential as incentive for individual advancement	Low differential for increased group solidarity and cohesiveness
Employment security	Low: dismissal is credible threat for discipline	High security to promote identification with enterprise
Training costs	Paid by individual to increase marketability	Paid by firm as long-term human capital investment
Macro-environment	Can adjust to and contribute to larger recessions with layoffs	Works better with and contributes to fewer and smaller recessions by avoiding layoffs
Product and Factor Markets		
Relationship	Arm's-length, market-oriented, and competitive	Long-term relation based on commitment, trust and loyalty
Product	Standardised (to foster competition)	Customised to buyer or seller
Curb to opportunism	Exit and competition	Voice, commitment and trust
Capital Market		
Relationship	Arm's-length and market-oriented finance	Long-term relational finance
Time perspective	Short-term since hard-to-monitor human capital investments downplayed	Long-term and patient to reap return to human capital investments
Debt/equity ratios	Need low D/E ratio to provide flexibility in face of unforgiving market	Can have higher D/E ratios with patient relationship financial sources and with involved, more flexible workers
Low costs of equity	Low costs since no sharing of income or control rights with workers	Lower costs for internal equity since workers already share some income and control rights

Source: Adapted from Stiglitz (1999).

of capitalism has only limited relevance. They are, in essence, based on the unjust appropriation of surplus value.

I will return to these questions in the last chapter, when I have reviewed the Indian case. For now, I proceed with the working assumption that specificities of capitalism do matter. Taking these specificities seriously allows us to challenge the apparent triumph of the Anglo-American model and its widespread acceptance in the developing world *both from the vantage point of other forms capitalism as well as from the vantage point of non-capitalist forms of development*. In particular, viable alternatives to the capitalist form cannot be developed unless its strengths and weaknesses are adequately theorised.

Conclusions

Let me briefly summarise the ideas developed in this chapter. First, I examined the structure of modern corporations, noting in particular the complexity of the issue of corporate control. Next, I examined in detail the phenomenon of the *corporate group*, the historical trajectory through which it emerged, the intricacies of its functioning, and finally, its relationship to the state. To be noted here is that the histories and theories discussed here pertain primarily to the development of corporate capitalism in the West, and they will provide us with a point of entry to the discussion of the Indian case. In the next three chapters, I proceed historically, examining in turn the colonial period, the interventionist period and the post-interventionist period beginning in 1985. In these three chapters I will be concerned with the issues discussed above: histories, structures of control and governance, patterns of accumulation, and the nature of political power enjoyed by corporations.

Part II

This page intentionally left blank

3
Corporate Capital in Colonial India: Genesis, Structure and Transformation

As I pointed out in Chapter 1, my aim in this work is to develop an historical analysis of the Indian corporate economy. In particular, I wish to assess to what extent the specificity of Indian corporate capitalism can be used to explain the lack of sustained industrial growth, a phenomena that seems to plague India even today. Broadly speaking, two sets of reasons have been considered in the mainstream literature on development, particularly in the context of liberalisation and structural adjustment: the problems of labour productivity and of firm-level or corporate profitability. My focus here will be the latter, i.e., the problem of corporate profitability. Specifically, I will try to assess whether and to what extent low corporate profitability may have hindered industrial development in India. In this chapter I will examine these questions in the context of the colonial period, spanning roughly the years between 1914–1947.

Several arguments have been advanced in order to explain the absence of an industrial breakthrough during this period, despite the presence of a fairly well-developed industrial bourgeoisie quite early on. These arguments can be broadly categorised as follows:

- dualistic division of the economic space based on a racial barrier imposed by colonial rule (Bagchi, 1970; Ray, 1994)[1]
- factionalisation amongst the capitalist class (Markovitz, 1985; Kochanek, 1974)[2]
- absence of the entrepreneurial spirit pre-determined by primordial factors such as religion and community (Lal, 1988)[3]

- 'innate mercantilism', manifest in the reluctance to undertake industrial ventures since trading activities yielded greater profits (Morris, 1987)[4]
- essentially comprador nature of the bourgeoisie (Desai, 1967).[5]

I wish to suggest here that an alternative theory can be proposed, that draws upon and attempts to extend the arguments advanced by Bagchi (1970) and Ray (1994). The primary thrust of this line of reasoning can be summarised as follows:

> Thus foreign control of industry in India brought neither technical knowledge to the Indians ... nor did it bring any extraordinary ability to adjust to changing conditions. It can be argued that by increasing the reverse flow of dividends from India to the West and by obstructing the emergence of Indians into positions of leadership in industry, it may even have increased the degree of economic backwardness of India and aggravated her problems of adjustment to a world of aggressive capitalism.
>
> (Bagchi, 1992:196)

In his disaggregated regional analysis of the development of indigenous Indian entrepreneurship, Bagchi goes on to show that Indian businesses did emerge successfully in areas where the penetration of British capital was less direct or slower to evolve. In fact, there is a significant body of scholarly work that documents the rise of Indian entrepreneurs despite the obvious racial and colonial barriers that confronted them (Chandra, 1982; Mukherjee and Mukherjee, 1988). Especially since 1914, Indian businessmen systematically entered the economic space dominated by Europeans, and the general record of growth and expansion of corporations during that period was quite remarkable. However, the nature of corporate expansion was not based on a sustained cycle of corporate savings and re-investment of the type that could satisfy any of the conditions I outlined in Chapter 2. To recapitulate briefly, these were:

- a sustained increase in assets, incomes and skills of workers
- a gradual restructuring of the semi-feudal conditions and relationships under which labour is initially employed and
- a progressive democratisation of the process of production.

Rather, in this structure of accumulation, corporate wealth was distributed very unevenly amongst three societal groups: (1) the investing

public at large; (2) the workers; and, (3) the managers. Central to this pattern of wealth creation was the managing agency system. As I will discuss below in detail, the managing agency model was premised on an essential contradiction: on the one hand it enabled the mobilisation of financial and managerial resources in a diverse, fragmented and colonial economy; on the other hand, it allowed for high degrees of concentration of decision-making powers. Most importantly, it enabled firms to generate and sustain high profits without expanding output (as much as they would have to in a competitive economy), enhancing levels of technology or increasing the skill levels and/or incomes of labour. Accumulation in this model became a direct outcome of concentration, non-competitive pricing policies, and political patronage, circumscribed by an extreme skewness of assets and incomes that is characteristic of an underdeveloped economy.

Now, in some sense, these traits may become endemic to any corporate form and emerge as inevitable in any model of growth that relies on the corporate form; arguably, the costs associated with this can be controlled either by a strong state or an elaborately regulated market, or a combination of the two. As is well-known, a combination of state intervention and market regulation was tried in India after Independence with much the same result: remarkable levels of corporate profitability and corporate growth *unaccompanied* by comparable levels of macro-level industrial growth. One explanation of this paradox lies in the fact that industrial policy never actually attempted to purge the predominant corporate form of the antecedents of the managing agency system. Attempts to reform the system – even its abolition – have not resulted in the development of alternative models that seriously remedy the problematic governance structures of its colonial past. The explanation seems even more convincing if I take into account the fact that this model derives directly from the Anglo-American model, and that several recent criticisms of the model in the US and the UK address exactly this paradoxical *inability* of corporate growth to sustain national economic growth (see my discussion in Chapter 2 above).

It is within the framework of this general argument that I examine the nature of the corporate economy in colonial India. The plan of the chapter is as follows. In the first section, I will discuss the nature of corporate growth in the colonial period, beginning from the late nineteenth century. While technically the colonial period ends in 1947, our discussion here covers the early post-Independence period as well. In the second section, I will examine the structures of corporate governance associated with the colonial economy. In the third section, I will attempt to integrate

the discussions of corporate growth and governance to explain the nature of industrial development of the period. The fourth and final section will present our conclusions and some tentative hypotheses.

The genesis of corporate capital in India: economics, politics and sociology

At the time of Independence, a domestic business class had already emerged in India. British administrative opinion of the time, however, pointed consistently toward the inability-of this business class to behave as an industrial class and tried to explain the (alleged) shyness of Indian capital to venture into 'modern' industries by referring to its preference for the high and safe profit margins available in pre-modern economic activities (Morris, 1987). While there may be some truth to this view, it cannot be denied that Indian capital did make significant achievements in industrialisation during the period 1914–47. It is true, however, that these achievements were limited in that they produced a very few pockets of industrialisation in the country.[6] Bombay for instance emerged as the leading centre of Indian industrialisation led by businessmen belonging to the Parsi community, while similar levels of industrialisation were hardly witnessed in the rest of the country. In the east, where business became dominated by the Marwaris an immigrant community from north India mercantile rather than industrial activities did continue to dominate for a somewhat longer time. There is an interesting debate as to the degree and nature of the transition achieved by Indian capital during this time. While I refrain from recapitulating this debate at length, it will certainly be useful to dwell on two of its dimensions: one, the relationship between foreign capital and domestic capital that evolved through this process of transition and two, the relationship of domestic capital to the political elite that was also shaped through this process. Both these aspects bring to light the one fact that is distinctive about Indian capital, especially as compared to its counterparts in other colonies, viz., the degree of political and economic organisation it had attained by the time India achieved Independence.

Economics of the transition

A number of economic historians have suggested that a fundamental transition in the structure of Indian political-economy began to occur after the First World War (Dutt, 1942; Pavlov, 1975; Chandra, 1982).

Central to this was the transition from a pre-capitalist system (based on primitive accumulation) to a more advanced form of industrial capitalism. As Table 3.1 indicates, the development of capitalism took an increasingly corporate form during this period, reflected in the visible expansion in the index of paid-up capital of joint stock enterprises.

What is more important to ascertain however is how much of this expansion constituted the expansion of Indian capital. Table 3.2, which I have reproduced here from Rajat Ray's seminal work on the Indian corporate sector, gives some indication of this. However, as Ray warns us, these figures should be taken merely as a basis for further study and not as strong evidence of the increasing dominance of Indian capital.[7] It is more instructive therefore to look for qualitative data in this regard.

Table 3.1 Paid-Up Capital of Companies Registered in India, 1914–15 to 1946–47

Years	*Index of Paid-up Capital*	*Index of Wholesale Prices*	*Paid-up Capital at 1915 prices*
1914–15	100	100	100
1919–20	155.0	184.86	152.24
1924–25	342.3	149.34	333.25
1929–30	348.1	112.50	413.23
1934–35	373.5	83.55	349.94
1939–40	404.8	88.14	404.85
1944–45	518.5	182.40	511.96
1946–47	639.2	221.90	573.52

Source: Investors' India Year Book, cited in Rajat K. Ray, *Industrialization in India: Growth and Conflict in the Private Corporate Sector, 1914–47*, OUP, Delhi, 1982, p. 39.

Table 3.2 Racial Composition of Capital in India, 1914–47

Years	*European*	*Mixed*	*Indian*
1914	65.35	13.73	20.91
1920	59.18	15.95	24.86
1930	44.11	21.12	34.76
1935	44.93	21.06	33.99
1940	41.05	28.12	30.81
1947	26.31	22.06	51.61

Source: as Table 3.1 above, p. 52.

Table 3.3 Paid-Up Capital of Sterling and Rupee Companies, 1914–15 to 1946–47 (1914–15 =100)

Years	*Rupee companies*	*Sterling companies*
1914–15	100	100
1919–20	155.0	144.7
1924–25	342.3	172.5
1929–30	348.1	253.4
1934–35	373.5	198.7
1939–40	404.8	267.6
1944–45	518.5	250.1
1946–47	639.2	257.4

Source: *Joint Stock Companies in India and the Indian States*, cited in Ray, 1982, p. 42.

In qualitative terms, the changing equation between Indian and foreign capital was reflected in three processes: (1) the entry of Indian capital into areas such as heavy chemicals, iron and steel which were, until then, the exclusive domains of British capital. The major breakthrough by the House of Tatas in entering the production of steel and hydel power and its consistent refusal to sell stocks to interested foreign buyers succeeded in keeping British capital from entering any of the high growth areas (Bagchi, 1972:83ff, Ray, 1982:Chapter 3); (2) its entry into the financial sector (such as banking and insurance), which was also dominated by the British until this time; and (3) expansion of the general size of operations controlled by Indians. By 1944, Indian private capital controlled about 62 per cent of the manufacturing units employing 1,000 or more workers, and about 58 per cent of the labour force in such factories While British capital still controlled a significant share of the largest units, these constituted only 4.7 per cent of the total factory sector (Mukherjee and Mukherjee 1988: 532–3).

Further, Indian control over the domestic market also increased during the period in review. One study estimates the share of foreign enterprises in the total gross output of Indian industry on the eve of Independence at only 25 per cent. Even after adding to this the share of the domestic market through imports, the total share is estimated to a maximum of 28 per cent (Shirokov, 1973:48–9; Mukherjee and Mukherjee, 1988:532). The same is held to be true for the Indian share of finance capital. While in 1914 foreign banks owned 70 per cent of the total deposits, by 1937 this share had decreased to 17 per cent (Kidron, 1965:42).

Sociology of the transition

The transition was dominated by two business communities, the Parsis and the Marwaris. Parsis, a migrant community from Persia, were amongst the first communities to enter into collaboration with the British (Masani, 1961; Bagchi, 1972:202). Operating primarily out of the western Indian city of Bombay, the Parsis soon established dominance in basic industries like steel, coal and cotton before the First World War. Foremost amongst the Parsi business houses was the House of Tatas; founded by J. N. Tata is 1912, it came to enjoy a monopoly position in India's steel and heavy engineering industries, both of which were leading sectors in Indian industrialisation (Buchanan, 1934:Chapter XIII). To date, the House of Tatas continues to be one of the two largest conglomerates in India.

The second important business community comprised of the Marwaris, a migrant merchant community from the desert areas of north-western India. They migrated to the eastern city of Calcutta, and entered into industrial investment long after the Parsis (Tomlinson 1981:p. 460). By the end of the Second World War eminent Marwari business houses like that of Birla Brothers had begun to dominate the industrial scene in the eastern city of Calcutta through their investments in cotton, jute, sugar, paper and a variety of other consumer goods (Tomlinson, 1981:460).

In his seminal work Timberg identifies three types of Marwari firms: (1) the 'great' firms or the conglomerates which engaged in a variety of businesses; (2) the brokerage firms attached to the European houses; and (3) the speculative firms or venture capitalists (I discuss the organisational properties of these firms below). The brokerage relationship and the subordinate distributing network, along with that of the great firms, emerged as the main source of accumulation of the Marwari diaspora. The capital accumulated from these ventures went into the development of speculative markets in India, which the Marwaris pioneered. The Marwaris were singularly responsible for the development of the futures markets in India, especially in commodities. The major focus of this activity constituted opium trade with China. A second focus was the stock market, which originated in Calcutta as far back as in 1850, although it was not formally organised until about 1908.[8] Initially, the main players in the stock market were Bengalis but, as with respect to all other commercial activities, Marwaris soon took the lead here too.

The Marwaris also played a central role in the takeover of expatriate interests by Indian businessmen that took place in the eastern region

after 1945. The Birlas, the Dalmias, the house of Surajmall Nagarmalls, all constituted eminent conglomerates which challenged the dominance of imperial capital during colonial rule (Tomlinson 1981:462–3). The challenge manifested itself in two ways. First, they established new jute mills and collieries, which implied a progressive movement away from trading activities into manufacturing ventures. Second, they undertook 'steady purchases of shares of European managing agencies, to a point where the Marwaris could first force their way into the boardrooms and then take over the firms':[9]

> the extent to which the Marwaris entered the industry through stock market trading is best appreciated by a detailed examination of the records of jute mill and colliery companies from 1920–1955. In 1918 only 3 out of 114 directorships of jute companies were held by Marwaris. Six years later, 16 out of 46 jute mill companies controlled by expatriates had at least one Marwari director on its board, and 5 had two Marwari directors.
>
> (Goswami, 1994:237)

Goswami identifies two factors behind this 'sudden influx of dhoti-clad, turbaned, "unsophisticated" Marwaris into the rarefied atmosphere of European boardrooms'. First, Marwaris rapidly purchased enough equity through the stock market to demand seats on the boards of the companies. Second, they organised a form of debt-equity swap in which they lent money to cash-strapped European firms; when the debtors proved unable to repay, they acquired shares of companies which they held as collateral.

> the other method of boardroom entry is even more revealing, for it shows how strong the Marwaris were vis-à-vis colonial firms in spite of the seemingly subservient postures of the former in the presence of the latter...during the inflationary years of the early 1920s many European-managed companies found themselves undercapitalised, strapped for funds, and needing cash to expand capacity in their jute mills. Marwari banias offered them loans at interest rates a point or two lower than the going rate of return on company debentures. As collateral they took blocks of jute mill shares. Through the 1920s most managing agencies had cash shortages, and the Marwaris continued to refinance these companies, held onto the shares, and got themselves onto boards.
>
> (Goswami, 1994:238)

With a style quite different from the Marwaris, a third important community contributed significantly to the industrial transformation in India. This comprised the Bengali businessmen from the eastern regions of India. Bengalis were in fact the first entrepreneurial community who entered into commercial relationships with the British. Initially, Bengali businessmen took up the work of *banians* with European agency houses:

> A *banian* is a person by whom all purchases and all sales of goods, merchandise and produce are made and through whom all shipments are made on account and on behalf of the merchants or mercantile firm in whose establishment he is a *banian*. Such a banian is therefore responsible for the quality and quantity of goods, merchandise, produce and shipment made through him . . . or servants whom he employs. He has to make good any deficiency in weight or quality, to make compensation for any fraud in shipments of such goods or produce. The *banian* receives . . . a percentage of sale and produce of goods and merchandise.
>
> (Sinha, 1994:71–2)

This profession brought tremendous wealth to Bengalis, much of which was invested in export trade, primarily in opium. During the middle of the nineteenth century, several members of the Bengali elite who had acquired some sort of professional training (law, accounting, etc.) as well as knowledge of English, began to enter into such trading partnerships with the British. A number of banks and banking-related financial businesses were established between 1845 and 1870 with majority Indian ownership and with the specific purpose of reducing dependence on foreign capital and indigenous usury capital (Bagchi, 1972:204). Such a creation of financial capital aided the development of entrepreneurship in Bengal. Dwarkanath Tagore, for instance, became a dominant partner in the biggest Indo-British banking venture, the Union Bank, which developed a capital base of more than £1 million. Dwarkanath also promoted and directed a number of other ventures in sectors like insurance, mining, and transportation, sectors which were hitherto exclusive domains of the British.

Unfortunately, this nineteenth century spurt in the growth of Bengali business could not be sustained. The collapse of the Union Bank in 1847 proved to be the turning point, particularly since it destroyed the trust Bengali businessmen had in their British partners. Between 1847 and 1860 many of the leading Bengali businessmen died, leaving their wealth in the hands of successors who had little interest in productive

reinvestment of their capital. A highly retrograde pattern of divestment emerged, combining elements of conspicuous consumption and investment options that sought safety in European ventures. In a complete reversal of the anti-imperialist trend started by people like Dwarkanath, these new 'vents for surplus' resulted in channelling the bulk of indigenous capital into European hands.

Another, second phase of radical anti-imperialist entrepreneurship emerged in Bengal in the early twentieth century. These Bengali nationalist-entrepreneurs were primarily owners of small firms and could not compete with the other communities in terms of actual expansion (Sinha, 1962:Vol II, Chapters 7–9). Some scholars, such as Levkovsky, also point out the significance of the fact that by the twentieth century the entire small sector was Indian-owned (Levkovsky, 1966:287). It was not only a national-bourgeois ethos, but also the anti-monopoly ethos that permeated this fast evolving small sector. Amongst these radicals, there was a strong consensus for expanding the industrial base consisting of associations of small independent producers (Ghosh, 1988:2446–8).

This group of small entrepreneurs were distinct from other business groups in terms their sociological origin, as well as the source of their primitive accumulation. They did not have linkages to British capital as managing agents or financial intermediaries; neither were they speculators or traders. Most of them came from the educated petty bourgeoisie and were mostly scientists, technicians, and skilled workers. The source of their initial capital was therefore from their own earnings or borrowings from relatives and friends. They were also distinctively more Schumpeterian, in that they usually possessed an in-depth knowledge of the production process, and most often were innovators of products and processes (Ghosh, 1988:2446).[10]

To sum up, the Indian private sector at the moment of state formation was a highly polarised entity. On the one hand, it comprised a strongly integrated and economically fortified oligopolistic faction; on the other hand, it comprised a loose federation of small and financially weak nationalist entrepreneurs. The latter group was allied with the radical faction of the political elite. In fact, many of these small entrepreneurs were former party workers. The members of the conservative faction of the political elite, on the other hand, were elected to office with the aid of the big bourgeoisie through a complex of linkages – both direct & indirect. The fundamentally unequal positions of the two factions of the private sector were obviously a product of the difference in financial resources that they could mobilise, but no less, the organisational cohesiveness of the larger group, as will be seen below.

Political organisation, corporate capital and the transition

There is some disagreement amongst authors as to whether Indian business was able to constitute itself as a 'class' before Independence. Some authors, most notably Bipan Chandra, have argued that this in fact has been the case. In this view, the formation of the Indian capitalist class comprised of three processes: the transformation of merchant capital to industrial capital, the consolidation of Indian capital vis-à-vis foreign capital, and the increase in political and organisational cohesion between different groups of Indian capitalists. Most notably, Indian capital showed the necessary ideological cohesion to subvert intra-class conflicts and short-term interests in order to safeguard their long-term interests (Mukherjee and Mukherjee, 1988:533).

As noted above, some other authors are of the view that factionalisation amongst the Indian business classes were one of the primary reasons behind the absence of India's industrial development. One obvious and somewhat superficial basis for this assumption lies in the regional differences amongst Indian businesses. As noted in my discussion of the sociology of the transition, there did exist quite strong regional differences amongst business groups in terms of ideologies, sources of primitive accumulation, patterns of accumulation, etc. (see Table 3.4).

Despite these differences, most leading industrialists were convinced of the need for a national organisation for the representation of business. Efforts were being made by the leading industrialists like G. D. Birla and Purshottamdas Thakurdas to set up such a national organisation representing commercial, financial and industrial interests. This culminated in the formation of the Federation of Indian Chambers of Commerce and Industry (hereafter FICCI). Because of its ability to attract participation from numerous groups of capital in the far-flung regions of India, the FICCI was soon given official recognition by the British government (Kochanek, 1974; Levkovsky, 1966:323). Initially, the FICCI was considered necessary in order to combat the Associated Chambers of Commerce (ASSOCHAM), a stronghold of European business interests:

> The creation of FICCI in 1927, as a permanent body to represent the interests of Indian capital, was in many ways a remarkable achievement. The federation came into being despite innumerable family, community and regional rivalries and was able to survive despite the development of strong conflicting interests and differences over political strategy and tactics.... Furthermore, it marked the

> beginning of sustained associational activity at the all-India level. The FICCI became an important forum for the expression of Indian views on all economic issues affecting the subcontinent . . . although the leadership of FICCI worked hard to give the new federation an all-India character . . . it was clear from the very beginning that for all the sprinkling of Parsi, Muslim, Bengali and Chettiar names, the federation was actually dominated by the Calcutta Marwaris and the Bombay Gujratis.
>
> (Kochanek, 1974:160)

The dominance of these two business communities was greatly facilitated by their allegiance to the nationalist movement, and most notably to Mahatma Gandhi.[11] However, while their loyalty to the Mahatma was strong, their allegiance to the nationalist movement often wavered, as if unable to ascertain whether it was beneficial to sever all linkages with the British or to simply re-negotiate the terms of colonial rule. By and large, however, big business allied itself closely to the nationalist movement.

As G. D. Birla wrote in the first annual report of the FICCI, 'Indian commerce and industry are intimately associated with, and are indeed, a part of the nationalist movement – growing with its growth and strengthening with its strength' (FICCI, Annual Report, 1928:4). In his introduction to the report he wrote, 'It is impossible in the present . . . political condition in our country to convert the [British] government to our views . . . the only solution . . . lies in every Indian businessman strengthening the hands of those who are fighting for the freedom of our country' (FICCI: 264). Similarly, Thakurdas wrote: 'Indian commerce and industry are only an integral phase of Indian nationalism, and deprived of its inspiration in Indian nationalism, Indian industry and Indian commerce stood reduced to mere exploitation of labour' (cited in Ray, 1982:316).

By the end of the thirties, the FICCI was represented in various government bodies including the Planning Commission Advisory Board, the Export Advisory Council, the Import Advisory Council, the Indian Council of Agricultural Research, the Indian Institute of Science and the Indian Statistical Institute (Mukherji, 1988:167–78). Most of these governmental authorities also had members nominated by the Associated Chamber of Commerce (ASSOCHAM), a confederation of expatriate capital groups situated in different centres throughout India. By representing itself in the same bodies as Assocham which was dominated by British capital, FICCI became an institutional forum for direct confrontation between Indian and foreign capital (Chatterji,

Table 3.4 Corporate Capital in Colonial India: Political and Sociological Dimensions

	Region of origin	*Sources of primitive accumulation*	*Primary areas of investment*	*Leading industrialists*	*Chambers of commerce*
Parsis	Bombay Presidency (West)	agrarian trade, particularly opium	cotton, iron and steel	J. R. D. Tata	not strongly affiliated to any chamber of commerce
Gujaratis	Ahmedabad (West)	land and agrarian trade, but mainly inland	cotton	P. T. Thakurdas A. Sarabhai	FICCI, Indian Merchants Chamber
Bengalees (First Generation)	Calcutta	land and agrarian trade, mostly offshore in collaboration with the British	coal, jute, banking, insurance, transportation	Dwarkanath Tagore	Bengal Chamber of Commerce
Bengalees (Second Generation)		none	small manufacturing	P. C. Ray	not strongly affiliated to any chamber of commerce
Marwaris	Rajasthan (North)	agrarian trade, particularly opium	cotton, jute, coal	G. D. Birla, R. K. Dalmia	FICCI, Indian Chamber of Commerce
Chettiars	Madras Presidency (South)	agrarian trade, commodities, particularly precious minerals	banking and money-lending; some degree of commodity trading especially in gold and diamonds; overseas investments	Muthia and Chidambaram	Madras Chamber of Commerce

Source: Compiled from various texts.

1981:340). FICCI also initiated a process whereby the individual local chambers of commerce (which comprised FICCI) sent their members to the provincial and state legislatures and other local government bodies (Mukherji, 1988:182–3). Through these measures, FICCI become vocal not only on issues concerning business, but on all political and economic issues of the day (FICCI Annual Report, 1941:22–24; 1946:71–6).

In 1937, the British government agreed for the first time to grant political autonomy to the provinces; this offered the prospect that the Congress could contest elections in each of these provinces and, on winning, could establish its autonomous provincial government (Markovitz, 1985:120). G.D. Birla along with the other businessmen welcomed this decision and agreed to finance the Congress campaign. In some provinces, business involvement in financing came only in exchange for nominating business leaders as Congress candidates. On average, however, there was no perceptible increase in the direct participation of businessmen in electoral politics. Businessmen tended to work behind the scenes and continued to use successfully and in a systematic manner the financial weapon to navigate political action (Markovitz, 1985:120). The most important of these influences was the ability of the business leaders to pressure the Congress to weed out trade unionists and leaders who they thought were ‘too radical’. In this period between 1937 and 1947 the need to control the radical element in the nationalist movement became one of the strongest reasons behind business's commitment to the nationalist movement.[12]

I have sketched the main contours of the colonial corporate economy and the transitions it underwent in the early part of the twentieth century. Using this as a canvas, I examine below the question of corporate structure and governance that emerged out of this transition.

Structure and governance in the colonial corporate economy: the managing agency model

A major contributor to the rise of the corporate oligarchy in colonial India was the institution of the managing agency. An institution rather unique to India, the managing agency not only spurred the growth of modern corporations in India but, with the control it exercised over the companies that it ‘managed’ also served as the basic mechanism of corporate governance. In examining the managing agency as a form of corporate governance, I shall first offer a brief historical account of the emergence of the managing agency model. This will be followed by the delineation of the defining characteristics of the model.

Managing agents are individuals or business firms (partnerships or private joint stock companies) which entered into a legal contract with joint stock companies to manage the affairs of the latter. The managing agency, if not an institution entirely unique to India, is certainly most closely identified with India and took its most elaborately developed form there. As Kling (1994) argues:

> The managing agency system came into existence when an agency house first promoted and then acquired the management of a joint stock company. This combination of events occurred initially in 1836 when Carr, Tagore and Company promoted and assumed the management of the Calcutta Steam Tug Association. In this arrangement, Carr, Tagore and Company followed certain precedents – organizational forms developed by defunct agency houses in the period before 1834. Originating in the late eighteenth century, the old agency houses were private partnerships capitalised by the savings of civil and military employees of the East India Company.... *Carr, Tagore's chief innovation was to harness the commercial experience of the agency house to the greater financial resources of the joint stock company. Thus they led the transition from international trade to the development of domestic industry in India.* ... *It is ironical that a system whose innovation is always attributed to British mercantile houses should have started with an Indian-owned firm.*
> (Kling, 1994:94–8; my emphasis)

However, for about fifteen years following the formation of Carr, Tagore and Company, the agency houses remained as unlicensed, unincorporated bodies not protected by the limited liability clause. Provisions for limited liability were legally granted to Indian companies much later, with the passing of the Indian Companies Act of 1850 and the subsequent emendations in 1857. By paving a firm foundation for the establishment of joint stock companies, these developments also allowed for a greater diffusion of the model introduced by Carr, Tagore and Company in 1836 (see below).

Not long after the establishment of managing agencies in and around Bengal, Indian managing agencies began to emerge on the west coast of India, especially in and around Bombay, and Ahmedabad. These initial agencies, which were predominately established by merchant families, focused on the cotton and textile industries. These merchant families were attracted to the managing agency system primarily because of two reasons: (1) the quick turnover of capital it allowed, since the marginal productivity of capital in their hands was high; and (2) this quick

turnover in turn allowed them to spread thin a relatively small quantity of capital into a large number of ventures. These two features permeated the rubric of the Indian corporate system in a very fundamental way. Also critical features of governance systems in the Anglo-American models, they provide a crucial key to understanding of relationship between macro-level growth and firm-level profitability.

Underlying the spread of managing agencies were the particular political-economic conditions of the day. When British merchants first started acting as managing agents, what confronted them in India in the middle of the nineteenth century was a potentially rich resource base, a large labour supply and a consuming public (Lokanathan, 1935:15–16). The development and exploitation of this resource base had not been undertaken due to, among other reasons, a lack financial and managerial resources. This meant that for the initial entrepreneurs who could bring the necessary financial and managerial resources together there was tremendous potential for profitability. British merchants with experience in the region proved up to the task and realised this potential through the institution of the managing agency. As business enterprises, such managing agencies served three basic functions. First, they started or 'promoted' new companies. Typically, a businessman or a group of businessmen would float a company with their own capital. After it became successful, they would then sell off most or all of its shareholdings, but still retain control of the company on the basis of a managing agency contract. Second, managing agencies were often asked to manage *existing* companies. In such instances, managing agencies were sought because of their managerial expertise, as demonstrated by their track records. Thirdly, managing agencies provided important financial functions. Here, their ability to attract new investors, to secure bank loans, etc., made managing agencies attractive to investors in joint stock companies especially at a time when the credit system was not yet fully developed and capital markets were still in their infancy. The initial area of operation for British managing agents was in and around Bengal, the seat of Imperial power in India. Also, in line with British colonial policy, British managing agencies developed the rich resource base (e.g., jute, coal, tea) for export rather than for industrial production in India (Sharma and Chauhan, 1965:149ff.; Rungta, 1970).

Let us now examine the model more critically by delineating its principle features. For this, I wish to draw upon the discussion of corporate control in Chapter 2. Table 3.5 below identifies the formal characteristics of the model, and the differences between British and Indian agency houses.

Table 3.5 Comparison of British and Indian Managing Agencies

Characteristics		*British managing agents*	*Indian managing agents*
Defining features of the Model	Formal Mechanism of Governance	managing agency contracts with **private partnerships** as the predominant corporate form	managing agency contracts with **joint stock companies** as the predominant corporate form
	Macro-economic Context of Governance	• undeveloped capital markets • weak credit system linked to the credit markets in London • weak regulatory system • *laissez-faire* trade policy until 1930; protection after 1930	• undeveloped capital markets in the modern sense, but an elaborate network of indigenously developed capital market instruments and trading arrangements (viz., *hundi, fatka, badla*, etc.) • expansive credit system linked to the *bazaar* • weak regulatory system • subjected to discriminatory colonial policy, both in its laissez-faire and protectionist forms
	Locus of Control	• strategic position (as managing agent) • majority ownership financial control	
	Other Mechanisms of Control	• intercorporate investments and loans • interlocking directorates • discouraging shareholder activity	• intercorporate investments and loans • interlocking directorates • discouraging shareholder activity
Profit Strategies		• price manoeuvres, colonial extraction and monopoly control	• price manoeuveurs

Source: Adapted from Reed, D. *Three Historical Models of Corporate Governance: An Evaluation of Corporate Economic Responsibilty in India*.

The formal mechanism of governance in both cases is the same: the managing agency contract. The particular provisions of the contract were articulated by the agents themselves and hence weighed heavily in favour of the agents and against those of the shareholders. Most notable amongst these provisions was the irrevocable and permanent nature of the contract which resulted in an almost total lack of accountability of the agents.

One important difference between European and Indian agency houses lay in the organisation of the companies they managed. As Morris (1994) argues, once the Companies Act was passed, Indian companies showed a strong preference for the joint stock form, since it allowed for the mobilisation of finances from a large number of small investors. European companies on the other hand were primarily closely-held or private partnerships. By and large, however, both Indian and European managing agency houses were governed in the same way.

Locus of power in the managing agency model

In many senses, the managing agency model was a true precursor of the industrial conglomerates as we know it today, in particular in that it shifted the locus of corporate power and corporate control from the level of the individual joint stock company to the parent or apex company. Managing agencies, or some of them at least, constituted such apex companies and it was the managing agency contract which enabled a managing agency to control several firms at the same time. This was true both for Indian and British managing agencies. As Reed argues:

> The ultimate locus of control, however, was located elsewhere, viz., in ownership of the managing agency. It was ultimately ownership of the managing agency that enabled managing agents to maintain control over managed firms insofar as it was on the basis of ownership that they controlled the managing agency. Again, this was generally true for both Indian and British managing agencies. There was some difference, however, between the pattern of ownership between Indian and British managing agencies. While most of the British managing agencies were initially established as partnerships, a number were founded as (private) joint stock companies. More significantly, the relationships between partners (or shareholders) were predominantly commercial in nature. In the case of Indian managing agencies, they were only almost exclusively founded as partnerships, though in later years many became (private) joint stock companies.

> More characteristic, however was the fact that such partnerships were predominantly restricted to family relations. Moreover, when they did go beyond the family, the limits rarely extended beyond the family's ethnic community. In such family business houses, the exercise of power here tended to assume a patriarchal form.... It was not unusual for a family business house dominated by a 'karta' to be in control of several managing agencies, each of which might manage several joint-stock companies.
>
> (Reed, 1998:23)

In order to maintain and exercise control, managing agencies extensively employed the device of *inter-corporate networks*. The two most important mechanisms through which inter-corporate networks were sustained were *interlocking directorates* and *intercorporate investments*.[13] Both foreign and Indian managing agencies engaged in the practice of interlocking directorships (see Table 3.6). At least until 1914, the interlocking occurred mostly between a number of industrial concerns. But later into the century, Indians (especially Marwaris) were increasingly successful in obtaining positions on the boards of banks. This resulted in a high degree of interlocking between banks and companies financed by those banks, and between industrial and finance capital in general (Mehta, 1952).

Interlocking directorships not only helped managing agents to ensure that they were retained as managing agents, but also the conditions under which they were retained. Thus, by having membership on the various boards of the firms associated with the business house, managing agents could consolidate their business empires (while investing little of their own capital). Moreover, by having directorships in other

Table 3.6 Multiple Directorships Held by Leading Indian Industrialists (1932)

Name	*Number of companies in which directorships held*
F.E. Dinshaw	65
Sir Purshottamdas Thakurdas	42
Sir Pheroze C. Sethna	34
H. P. Mody	14
Sir Fazulbhoy Currimbhoy Ebrahimbhoy	26
Sir Lalubhai Samaldas	26
N.B. Saklatwala	29

Source: Bagchi (1972:208).

firms not associated with the managing agency (or larger business house), the managing agent could strengthen business ties with key partners (financiers, suppliers, etc.).

Such widespread interlocking of directorships co-existed with intercorporate investments. Intercorporate investments involved the managing agent using funds from one managed firm (e.g., from retained profits, loans, etc.) to invest in another firm. The firm receiving investment latter could be an existing firm managed by the managing agent (which might be in financial difficulty), a firm newly floated by the managing agent or an existing firm not managed by the managing agent. Intercorporate investment allowed the managing agents to retain control over their empires and to expand them (by taking over existing firms or floating new firms) with only a minimal injection of their own capital.

Let us now turn to the macro-economic context within which the managing agency system was located. As Table 3.5 (above) shows, there were several macro-economic policy variables which contributed to the growth of the system. The first was undeveloped capital markets. The undeveloped nature of the capital markets (indeed, the very absence of stock markets when the first managing agencies were founded) had a two-fold significance. On the one hand, it meant that there was an important financial role to be fulfilled and opportunities for whoever could fulfil it. It was managing agents who proved to have the ability to step in to fill this void, an ability that meant they were attractive to firms not only (or even primarily) for their management skills. On the other hand, the undeveloped capital market meant that there was virtually no market discipline to be imposed upon managing agents. A second important macro-economic element was a weak, and more importantly fragmented credit system (see below). Third, the system was characterised by lax government regulation. In the absence of legislation against the abuses of power by managing agents, including the methods used to attain and maintain control over firms, the contracts they established were legally binding and their legality was upheld by the courts over the objections of shareholders (Rungta, 1970:234). Moreover, the British government was hardly keen on developing effective regulate on the as it 'considered it more important to keep Indian law in line with British law so that British investors would know where they stood' (Rungta, 1970:259). Finally, it needs to be noted that in keeping with the colonial spirit, government policy systematically favoured European over Indian entrepreneurs (Bagchi, 1972; Ray, 1982).

The impact of these discriminatory practices of the colonial government were somewhat ameliorated by the resources of the *bazaar economy*. As noted in Table 3.5 (above), an important difference between the British and the Indian agency houses lay in the latter's connections with the indigenous or *bazaar economy*. On the face of it, the colonial economy comprised two distinct sections – the *bazaar* inhabited by the indigenous bankers, petty traders, speculators, etc., – and the modern business and industry dominated by the Europeans. However, as Ray (1994) explains:

> this is not to say that the economic organisation of colonial Indian society fitted neatly into the well-known model of the dual economy – an 'organised' sector of foreign trade, factory industry, banks, corporations and managing agencies, and an 'unorganised' sector of indigenous bankers, traders, moneylenders, peasants and artisans. To single out the Western-styled concerns alone as the organised sector and to put the rest of the economy in an undifferentiated, unorganised and static mass of traditional concerns would be to miss the complexity and sophistication of the indigenous part of the economy. It had its own institutions and forms of organisation, and though these forms did not correspond to Western models, they were capable of adapting to changing conditions. Indeed, that part of the world of commerce and credit which the official reports of monetary conditions referred to as the *bazaar* had a certain dynamism. It was from the *bazaar* that the Indian industrial capitalism emerged in the late-nineteenth and twentieth centuries.
>
> (Ray, 1994:11)

The prime actors in the *bazaar* had worked out a mutually beneficial arrangement with the European businessmen where the latter relied on the former for obtaining produce from inland and for the distribution of their goods in the inland. 'The shroffs and arhatiyas submitted to the regime of worldwide economic and political empire, but they did so, in a certain measure, on their own terms' (Ray, 1994:13).

The Marwaris were one of the prime actors of the *bazaar* economy and it may be useful to briefly discuss the nature of the organizational forms developed by Marwaris. As noted above, Timberg identifies three types of Marwari firms (1) the 'great' firms; (2) the brokerage firm attached to the European houses; and (3) the speculative firms or the venture capitalists. The defining characteristics of these firms are outlined in Table 3.7.

Table 3.7 Structure of the Marwari Firms in Colonial India

Defining characteristics of the model	*The 'great' firms*	*Brokerage firms*	*Speculative firms*
Formal Mechanism of Governance	• the 'network' or the conglomerate with an apex company	• the brokerage contract and guarantee	• none
Circumstances of Governance	• undeveloped capital markets • fractured monetary and credit system • weak regulatory framework	• the colonial division of space between the *bazaar* and the 'modern' economy	• colonial trade policy • weak regulatory framework • absence of price control
Locus of Control	• control of the apex company • intercorporate investments and loans • interlocking directorates	• majority ownership	• financial control
Profit Strategies	• quick turnover of capital, exports	• conscious attempts to increase levels of intermediation and brokerage	• speculation and price manoeuvres

Source: Adapted from Timberg (1994).[14]

Profitability

Let us now consider the impact of these governance structures on the nature of profitability. The following table presents an index of aggregate profitability during the period.

As Goswami (1994:234) illustrates, very high profits were available from the two leading industries of the day, namely jute and coal.

> In the decade 1910–20, the average annual value of raw jute arrivals in Calcutta and Chittagong was Rs.5.86 billion. Conservatively assuming that the Marwaris accounted for half this trade and that

Table 3.8 Aggregate Profit Rates: 1910–44

	Years	*Mean profit rate*
Period of relative prosperity	1910–20	15
Period of prosperity	1918–22	25
Period of normalcy	1923–29	12.6
Period of depression	1930–39	8.6
Period of relative prosperity (Munshi)	1939–44	15.44

Source: Goswami (1994); M. H. Gopal, *The Theory of Excess Profits Taxation* (Mysore: Bureau of Economic Research 1947); M. C. Munshi, *Industrial Profits in India* (New Delhi: FICCI, 1948).

> the trading profits were 15 per cent, profits accruing to Marwaris were around Rs.440 million per year. The estimate excludes profits from *fatka* and from trade in jute bags and cloth.
>
> (Goswami, 1994:234)

Goswami goes on to say that

> as far as the Marwaris are concerned there were no barriers to entry in two major colonial industries, jute and coal. . . . In the coal industry, purchases rose by 30 per cent between 1910–13 and 1914–8 leading to a 30 per cent hike in prices. High colliery profits were made all-around: the average net-profit rate, as a share of paid-up capital was around 65 per cent; for many firms it surpassed 100 per cent. For jute mills the situation was spectacular. In 1918, for instance, thirty out of thirty-five joint stock public limited companies declared net profits that were greater than 100 per cent of paid-up capital. Of these ten earned upward of 200 per cent; the modal dividend rose to 150 per cent on the face value of ordinary shares, and shares were quoted at 10 times their face values.
>
> (Goswami, 1994:235)

However, with the onset of the Depression, profit in these traditional industries began to fall, whereas profits in non-traditional industries, particularly manufacturing, began to rise (Table 3.9 below). Initially the profit rates in manufacturing were not as high as in trade, but were nonetheless substantial. In reaping these profits, Indian business houses exploited to the full the declining profitability of the colonial industries.[15] The growth of the new industries was also, quite directly, the outcome of protection.[16]

Table 3.9 A Profit Index Constructed by the Office of the Economic Adviser to the Government of India (1928=100)

	1930	*1931*	*1933*	*1935*	*1937*	*1939*
Cotton	37.9	52.5	82.8	89.0	138.2	154.6
Jute	37.9	8.7	12.6	39.8	11.1	13.6
Tea	14.9	−19.8	−1.1	63.5	108.4	96.2
Coal	122.1	91.2	75.0	63.8	71.8	139.1
Sugar	93.6	144.5	253.9	157.7	122.3	179.4
Iron and steel	70.6	78.0	66.2	192.9	211.6	289.3
Paper	91.3	86.6	92.4	136.4	182.8	151.8

Source: Ray (1994:57).

Table 3.10 Prices and Profits in India, 1940–44

Year	*Index of industrial production (1936=100)*	*Index of profitability (1936=100)*
1939–40	114	590
1940–41	117	617
1941–42	123	896
1942–43	109	926
1943–44	108	1044

Source: Bengal Industrial Chamber, Survey Commission Report, Chapter 9, pp. 212–13, cited in Mukherji, 1988.

The existence and acceleration of high profit rates continued in to the forties. Most branches of industry, including the traditional ones, were increasing their profits to such an extent that it induced the British government to introduce an Excess Profits Tax in 1942–43.

Let us now explore the possible factors that might have contributed to the high profits of this period. As I discussed in Chapter 2, profits can derive out of two types of sources: competitive, drawing primarily upon innovations of products and processes, or non-competitive, occurring primarily out of ‘scarcity’, price changes, intermediation and brokerage etc.

As several studies indicate, inflation, caused sometimes by external conditions and sometimes because of the failure of price control, was one of the major factors behind high profitability in India. I referred to the phenomenal price hikes in coal and jute between 1910–20. Except for the Depression, the same relationship between price and profitability

existed right through the thirties and forties. Munshi provides an industry-wide breakdown of the relation between price and net profits and notes that:

> there is one more notable factor in all these industries that has a bearing on net profits, namely, that after the failure of the six Price Control conferences, by October 1941, despite the statutory controls, year after year, even the controlled prices had to be put up from time to time; and I have later on emphasised how the Government itself started the hare and hound race of prices and wages (and costs in general) in the country as a result of their policy of financing the War largely by inflationary methods.
>
> (Munshi, 1948:46)

The inflationary impetus to profits is further reflected in the comparison between net profits in India and the US.

The tables show that profitability in India compared quite favourably to that in the US in the same period. The war years show an increasing divergence in the two rates, a divergence which is largely explained by the strong inflationary conditions in India *vis-à-vis* the controlled prices in the American War Economy. These tables also validate the general argument that in and of themselves, rates (or levels) of corporate profitability in India were not low enough to have inhibited macro-level growth. Several other factors, viz., the allocation of profits, rate of reinvestment, level of investment in skill formation, etc. also need to be examined. In this context it is also critical to note that the pace of

Table 3.11A Ratio of Net Profits Before Income Taxes

	American corporations 200 largest	*American corporations 800 others*	*Our general ratios (average of 7 industries)*
1936	10.9	9.7	10.3
1937	10.8	8.8	10.0
1938	6.8	4.7	11.9
1939	9.7	8.6	10.7
1940	12.3	11.3	13.9
1941	14.7	15.2	17.9
1942	12.4	13.4	21.4
1943	11.5	12.0	22.1
1944	10.3	10.1	21.7

Source: (Munshi, 1948:58). The United States figures are taken from the *Survey of Current Business* for August 1946 and September 1947.

Table 3.11B Ratio of Net Profits After Income Taxes

	American corporations 200 largest	*American corporations 800 others*	*Our general ratios (average of 7 industries)*
1936	9.1	8.0	8.9
1937	8.9	7.1	8.2
1938	5.5	3.5	8.8
1939	7.9	6.9	8.0
1940	8.5	7.5	9.1
1941	7.2	6.8	9.8
1942	4.7	4.1	9.8
1943	4.1	3.3	7.7
1944	4.1	3.0	7.4

Source: Munshi (1948:59).

increase in profitability is quite unmatched by the pace of increase of output, a characteristic that usually reflects monopolistic pattern of accumulation (see Table 3.6 above). By severing (and, in fact, reversing) the link between output expansion and profitability, what monopolistic control also necessitates is a channeling away of dividend earnings from reinvestment. However, if such dividend earnings are widely dispersed amongst a large number of shareholders then the resultant spurt in aggregate demand may still have a stimulating effect on investment. Such a demand-investment nexus is in fact the basis of the Keynesian justification for corporate capitalism. However, dividend earnings in colonial India were highly erratic and skewed in terms of distribution, and succeeded little in animating the demand-investment nexus.

A logical corollary of this colonial model was also the absence of product/process development. As Bagchi argues:

> Jamsetji Tata is reported to have helped in the development of ring spindles and their adaptation under Indian conditions . . . this spirit of innovation seems to have atrophied later, as witnessed by the difficulties of the Bombay cotton-mills industry in the inter-war years. On the other side of India, the jute mill industry had become technically stagnant: *no major changes in production methods had taken place after the 1880s*.
>
> (Bagchi, 1994:186; my emphasis)

There is no real historical evidence that contact with an economy that was in fact going through the Industrial Revolution itself resulted in

significant transfers of technology. Bagchi's famous 'deindustrialisation' hypothesis argues the reverse: that under colonial rule, India underwent a process whereby lower levels of technology were substituted for higher ones which existed before colonization. While this is certainly true of many industries, it is also true that quite significant levels of industrial research and product innovation did occur in colonial India under the aegis of a group of radical nationalist small entrepreneurs in Bengal. These entrepreneurs however were somewhat unsuccessful in exploiting these innovations for commercial success, and much less in impacting upon the industrial development of the country in any sustained way.

Let us now summarise the discussion so far. In the period between 1850 and 1950, a rather fundamental transition took place. Despite the systematic policies of racial discrimination administered by the colonial government, Indian businessmen were highly successful in establishing their presence as an organised entrepreneurial class. This entrepreneurial success was reflected in the relatively high profit rates in the leading industries of the day. Further, as characteristic of colonial rule, the source of these profits did not lie in innovations or gains in productivity but rather in inflation, intermediation and trade, arising in general from elements of imperfection and incompleteness of the market. Such imperfection was largely manifest in the functioning of the managing agency model. Despite these successes, the corporate economy in the colonial period remained characterised by a dualistic division between the 'modern' European-dominated economy and the 'pre-modern' *bazaar* economy dominated by the Indians. However, contrary to conventional wisdom, the *bazaar* economy was a highly dynamic entity, perhaps even more so than its European counterpart, and provided the basis for the transition of the Indian economy.

The developmental impact of the colonial model

We are now in a position to assess the impact of the models and strategies discussed above. In particular, we need to assess the impact of the managing agency model in terms of its ability to foster economic growth. Generally speaking, the impact of the model can be assessed at two levels: at one we can examine the abuses of the system and the impact of those abuses; at another, we can examine the more systematic properties of the model, particularly in order to trace the continuities between the colonial and post-colonial structures of governance. Our emphasis here will be on the latter, focusing more on the model itself, and the kind of growth it could have generated even if the abuses were regulated.

The strength of the system supposedly lay in two major elements: (1) that it could mobilise large amounts of capital in a capital-scarce economy in the absence of a stock exchange and (2) that it could optimise the use of scarce managerial talent. Both these aspects of the managing agency model were bolstered by the prevalence of the joint stock form. As I noted above, the joint stock form was adopted in India quite early on, and more importantly, it was adopted more extensively by Indian businessmen than by the British. For such a joint stock model to be conducive to growth, the one major condition (especially in a context of underdevelopment) that would need to be satisfied is that shareholders forego dividends and agree to reinvest in sustained fashion. This would require in turn that the shareholders have the right to participate in decision-making processes of the firm and determine the trajectories of growth chosen by the firm.

This was, of course, not the case. Managing agents quite blatantly violated this basic right of shareholders, and sought consciously to exclude them from having any effective voice in the manner in which the firm was run. As Rungta (1970) explains, in order to minimise shareholder participation, managing agents first had to attain control of firms. This often involved first establishing a firm themselves and then selling out their stake (or diluting their stake by offering new shares) to new shareholders. In some cases this involved the actual establishment of a successful firm, while is some cases the activity was primarily speculative in nature. As noted above, such cases also routinely involved the use of intercorporate transfers, and control over a whole network of firms could be obtained simultaneously through the use of interlocking directorships and intercorporate investments. Through such intercorporate investments the shareholders of a profitable company could be forced to finance losses of other companies or put up risk capital for new ventures. It also became a practice of Indian managing agents to acquire the stakes of those foreign investors who were looking to withdraw from Indian companies. These interests, which were usually acquired at a high premium, were often financed by the resources of companies on which the agents had control, and more often than not, without adequate disclosure to the shareholders.

Once they had attained control of the firm, managing agents used two basic devices to limit shareholder participation (especially with an eye to inhibiting shareholders from removing them as managing agents). On the one hand, they would include stipulations in the managing agency contract which would make it legally impossible (e.g., long-term and even perpetual contracts) or prohibitively expensive (e.g., separation

agreements) to remove the managing agent. On the other hand, they would also control the issuing of shares, e.g., offering deferred shares, limiting the public distribution of shares, etc. They would also draw up special stipulations to retain control, for example, debentures issued by one company could be subscribed mainly or entirely by companies in the same group or in companies in which the managing agents have financial or other interests.

Next, let us examine the critical issue that concerns the patterns of value creation within the managing agency system. First, being an integral part of the colonial system, the primary source of value creation was not the augmentation of productive capacity, but trade and intermediation. In keeping with this colonial pattern of accumulation, corporate income accrued primarily as fees and commissions, based upon some aspect of the firm's performance, viz., sales, production, gross profit or net profit. However, the levels of any of these variables were not dependent on a serious expansion of productive capacity, which in this case would involve increasing degrees of integration between the agrarian economy and the nascent industrial sector. As is well-known, such a deepening of linkages between the two sectors have been critical to the growth of most Western economies in the initial years, and its non-occurrence in India has had enduring effects on economic growth.[17]

One obvious problem which arose in this regard was that basing the level of remuneration on any criterion other than net profit inevitably led to a conflict of interests between the managing agents and shareholders. Any number of such conflicts and abuses of shareholder rights can be cited (Sharma and Chauhan, 1965). In any event, managing agents were able to procure overly generous payments for themselves by ensuring that their compensation was set at an exorbitantly high percentage of the profits. As Munshi argues:

> Paper is the only industry in which the dividends paid have throughout been kept within the limits of net profits. In all other industries they were required to draw on past reserves at least once and in the case of jute and coal thrice each. . . . Our table shows that a majority of these industries have followed a pattern of distributing their profits by way of dividends rather than building up reserves.
>
> (Munshi, 1948:53)

There were, of course, exceptions to unjustifiably high rates of remuneration. As early as 1877, for example, an Englishman, James Greaves

of Greaves Cotton & Co., established a rate of remuneration of 10 per cent of net profits, the same standard that would be adopted three quarters of a century later in the 1956 Companies Act as a 'fair' rate of remuneration. While Greaves was followed in this practice by a few others, including J. N. Tata, such examples remained the exception to prove the rule (Rungta, 1970:237–8). That this is so is indicated by a Reserve Bank of India study that found the average rate of compensation for managing agents in the years 1950–52 to be 27.7 per cent of net profits (Sharma and Chauhan, 1965:174).

A third key feature of this pattern of wealth creation was its non-competitive nature. I already referred to one aspect of this, namely the relationship between profits and prices. What perhaps is more important is the absence/requirement of a commitment to earning profits on the basis of innovation rather than other strategies which go against fair market competition (e.g., imposing barriers to entry, collusive behaviour, restricting information, etc.). In this context, it may be useful to examine levels of economic concentration in this period. Of course, levels of concentration are not perfect indicators of non-competitive practices. High economic concentration may result from a range of factors other than non-competitive practices by individual firms, most notably, perhaps, the level of economic development and national economic policy decisions, e.g., to restrict foreign entry into markets (Chaudhuri, 1975).

The question of whether there existed significant levels of economic concentration in India during the period prior to the decline of the managing agency system is not open to any serious doubt. Scholars and government commissions have only disagreed on the extent of concentration and what the best indicators of concentration are. One potential indicator of concentration is the share of output in different product markets and economic sectors by the largest industrial concerns. Although there was very strong product-wise concentration in India during the period in question, there are two basic limitations with using this as an indicator. On the one hand, it does not necessarily imply anti-competitive practices as, at this stage, much of this concentration can be attributed to underdeveloped markets and the British colonial policy of discouraging industrial development. On the other hand, it tends to underestimate the nature of concentration as it does not provide any information about concentration in the larger economy, notably the extent of the operations of these firms in other market sectors.

A second potential indicator of concentration is the ownership of share capital. In India ownership of share capital was not very diffuse

at the time. A Central Bank report, for example, estimated that in 1953–54 there were only 101,033 shareholders in the country, a number representing an infinitesimally small part of the total population. Moreover, of this number 1.4 per cent received some 31.5 per cent of the dividend income (Chaudhuri, 1975: 20).

Another possible indicator of economic concentration involves management and directorships of firms. As noted above, there were numerous individuals holding multiple directorships and extensive interlocking directorships among both Indian and British firms. A study conducted by Mehta (1952) in 1950–51 indicated that nine leading Indian industrial families held nearly 600 directorships or partnerships in Indian industry, with the Dalmias and the Singhanias alone holding 200 of these. Moreover, 100 individuals were found to hold 1700 directorships in the corporate sector, 30 of them holding as many as 860 directorships and the top ten holding about 400 directorships. It was also the case that there was significant concentration in the management of firms. The same study of Mehta estimated that during the period in question 600 industrial concerns were controlled and managed by 36 managing agency houses. Of these only 250 were managed or controlled by nine leading British managing agencies, of which Andrew Yule and McLeod alone controlled 90 of them (see Table 3.12). A similar pattern was also evident among Indian managing agents.

In the pre-Independence period increasing concentration among Indian business firms occurred in the context of gradual constitutional and economic reforms which were occurring as the Indian struggle for independence progressed. As the strength of the nationalist forces grew,

Table 3.12 Number of Companies Managed by Selected British Managing Agencies (1950)

Managing agency	*Number of companies managed*
Andrew Yule	50
McLeod	40
Martin Burn	26
Duncans	26
Octavius Steel	24
Martin Bird	21
Jardine Henderson	20
Gillanders Arbuthnot	20
British Indian Corporation	20

Source: Adapted from Mehta (1952).

the British gradually had to relax their *laissez-faire* economic policy and other restrictions that inhibited the development of Indian industry, a process that was greatly accelerated by the two World Wars. As a result, large Indian capital (overwhelmingly in the form of business houses) grew rapidly. Whereas, for example, in the period from 1900 to 1905, the share of small enterprises in industrial production was three times that of larger ones, by the period 1942 to 1947 the production of larger enterprises was 1.6 times that of small ones (Sharma, 1989:32). At the same time large Indian capital slowly began to catch up to and overtake British capital. In 1946, for example, the total assets of the three business houses of Tata, Dalmia-Jain and Birla were Rs.6 billion while the combined assets of the three largest European companies (Andrew Yule, Bird–Heilgers and Martin Burn) were only Rs.740 million. Further, between 1939 and 1945, the paid-up capitals of four Indian companies had crossed the 100 million mark, while only one British company in India, Bird–Heilgers, had managed to do so (Shirokov, 1973:49; Tomlinson 1979).

It is not difficult to link the increases in concentration, both in the pre-and post-Independence periods, directly to the managing agency model (Chaudhuri, 1975). The institution of the managing agency, along with interlocking directorates, enabled business houses to make use of intercorporate loans (and other forms of financing) to establish new firms and to take over existing firms. The significance of incorporate investments (and the small proportion of investments by the business family) seems to be confirmed by the *Vivian Bose Commission Report* which indicated that only 3.7 per cent of the new share capital raised by 'inner circles' in this period (1951–58) came from the controlling interests, while 83 per cent came from companies, with 12 per cent coming from trusts and 5 per cent from individuals (GOI, 1963: 42). As noted above, the use of intercorporate loans and other forms of financing to induce the 'breeding process' of new firms was not only generally conducted without the consent of shareholders, but frequently also in opposition to their interests.

Let us summarise the discussion so far. What I examined above are the systemic properties of the colonial corporate economy as manifested through the managing agency model. Let us now examine the abuses of the system. Of course, as should have become evident in the preceding discussion, the systemic properties and the abuses are closely connected; there is however, a need to conceptually separate the two.

The first and perhaps most rampant occurrence of abuse was with respect to perquisites. Managing agents were not only able to command

such perquisites due to their control over the firm, but were able to greatly inflate the size of such allowances beyond any justifiable need. Thus, while the nominal purpose of this allowance was to cover the administrative expenses of the managing agent, in practice its real function was to provide an extra source of income for the managing agent (Baig, 1971:86; Sharma and Chauhan, 1965).

A second area of abuse involved financial irregularities in the running of the company. The Vivian Bose Commission (GOI, 1963) investigating the activities of Dalmia-Jain during the 1950s found nearly the complete range of possible financial irregularities in one managing agency. These included: (1) improper intercorporate transfers which benefited the management at the expense of shareholders; (2) the practice of advancing funds of companies as unsecured loans; (3) the practice of investing funds of publicly held companies, including banks and insurance companies for acquiring controlling interests in others firms, especially in those with high liquid assets; (4) the practice of transfer of assets of public companies to closely held private companies, then converting the public companies into private companies and thereafter taking the private companies into liquidation with liquidators who would be sympathetic to the management; (5) non-declaration of dividends even when companies were making profits. This latter practice often led to a fall in the price of shares which then instigated the shareholders to sell. These shares were then picked up by the management and, after the shares have been so cornered, huge dividends were declared. Other types of financial abuses involved operating in the black economy (with the result that profits did not appear on the books and dividends did not have to be paid), the appointment of sole purchasing agents, speculative activities, etc. (Baig, 1971:83–85).

While the Dalmia-Jain case may have been among the worst examples of financial mismanagement, the type of abuses of which it was accused were common among many if not most managing agencies to some extent. To a not insignificant degree, it was on such a basis that the major business houses were able to build their business empires. As Sharma notes, even houses like the Tatas could not escape this logic of the managing agency system, 'in spite of their claims to be the legitimate heirs of professional management in India. They were also using their financial power to bring more and more firms under the umbrella of Tata Sons. Similar was the case of Birla Brothers' (Sharma, 1989:32).

A final area of abuse involves what is often referred to as a lack of professional management. What such abuse entails, however, is not clear without some definition of 'professional management'. This term

has at least three distinct connotations. Reed (1998) identifies three possible notions of professional management. First, the notion is frequently used (at least in India) to indicate non-proprietary management; second, professional management may indicate the use of managers with professional training in management; and third, it may indicate that managers operate according to certain codes of professional ethics.

Let us briefly examine these three. In managing agencies, at least in the early years, it was frequently the case that managing agents founded firms with their own capital and were initially proprietor-managers. Eventually, however, they would sell off all or a substantial amount of their shares and just retain management control through the managing agency contract. In other cases, they were never true proprietary managers at all, holding but a small percentage of the companies shares. In both cases, the shareholdings of managing agents in the firms they managed tended to drop over time. Still, however, through the managing agency contract they were able to operate like proprietary managers and exercise their 'divine right' of management, including the naming of their heirs (Sengupta, 1983:282). This was, as noted above, a violation of the basic notion of shareholder democracy. However, it was not necessarily a violation of the shareholders' right to have the firm run in their interests. Managing agents could, in principle, be good managers and corporate governors. The problem, however, is that they tended to have different interests from (other) shareholders which lead them to act in ways which did not maximise shareholder value (e.g., not paying dividends, making intercorporate loans, etc.). Moreover, hereditary transfers of powers also often meant that previous abuses of power were hidden (Baig, 1971:84).

A second notion of professional management connotes some form of professional education or technical training. Among managing agencies such education was frequently lacking. One reason for the dearth of professional qualifications was that many firms initially took on managing agents not for their managerial ability, but because of their ability to raise equity capital or bank loans. Not infrequently, these former abilities were not tied to any particular competence in management and corporate governance. Another reason relates to the problem of the 'divine right' of management noted above. In many managing agencies, especially those controlled by family business houses, it was almost invariably family ties, not professional competence, that determined who managed the firm. One study cites only 30 per cent of family members having the appropriate qualifications to run a business

(Verma, 1987). It could be argued, however, that a lack of professional training did not necessarily go against shareholder interests, if there were other characteristics or advantages to offset this situation. Verma, for example, argues that the lack of professional qualifications was often compensated for by the ability of families to manage turbulence, the compactness of their management structure, etc. (Verma, 1987:208). Others, however, would deny that it was the off-setting advantages in the managerial realm which compensated for the lack of professional and technical qualifications. Lokanathan, for example, cites a list of poor management techniques and ends by arguing that 'such success that they have achieved is due to their financial resources and an early start' (Lokanathan, 1935:16). This is not to say that there was no movement in the direction of professional management among managing agents. J. R. D. Tata, for example, was among the first both to recruit professional directors from outside of the firm as well as to appoint employees with outstanding records in the firm to the board. He, however, was more the exception to prove the rule.

A third understanding of professional management refers to the notion that management can be understood to have certain 'professional standards' or norms. While the exact nature of the norms of the management profession are a subject of dispute, it is clearly the case that many practices of managing agents would have been a violation of any set of professional norms. In some early instances, for example, managing agents showed no interest at all in managing the firms under their control and rarely even visited them. There was an even more widespread tendency for managing agencies to take on more firms than they could reasonably be expected to manage (Rungta, 1970).

Reforms of the managing agency model

The nature of corporate control that managing agents exercised over the companies that they managed made confrontations with shareholders and the public inevitable. As Rungta (1970:225ff.) documents, clashes between shareholders and managing agencies date back to the emergence of the managing agency system in the mid-nineteenth century. Major abuses of the system first began to emerge with the entry into industry by people of questionable reputation during the economic upswing of the early 1870s. In Bombay, such abuses not only lead to outcries by shareholders, but also resulted in shareholders taking direct action to remove managing agencies as well as taking recourse to the courts (which proved only too willing to uphold managing agency contracts). In Calcutta, if the

public outcry was more muted it was only slightly so and this can be attributed more to the fact that the shareholding pattern was different (viz., it included primarily British subjects many of whom had returned to Britain) rather than better management practices (Rungta, 1970). In Ahmedabad, as well, newspaper editorials were vocal against the abuses of shareholder rights (Tripathi and Mehta, 1990).

The first real occasion for reform came with the passage of the English Companies (Consolidated) Act of 1908. In 1909 for the first time the Government of India solicited suggestions from provincial and local governments for amendments to the Companies Act. The near unanimous response was for strong controls over the activities of managing agencies. Anticipating some opposition from the business community, the government decided to first introduce a new Companies Bill in 1913 with the intention of addressing the issue of managing agents the following year. The initial compromise plan would have required all firms to have boards (which were not required even in British law until 1908) in which the managing agents were to be in a minority. It also proposed tighter controls and greater restrictions on the activities of managing agents and greater information for (potential) shareholders. When an even further watered down version was introduced, the government was forced to remove the clause restricting managing agency representation on the board. As a result, the managing agency system continued virtually intact as the managing agents found it very easy to circumvent the spirit of the law by establishing boards consisting of the managing agents themselves as well as their friends and relations (Sengupta, 1983:22ff.; Baig, 1971:15–16).

It was only with the Companies (Amendment) Act of 1936 that the managing agency system was actually acknowledged to fall within the purview of company law and some of the problems relating to it were addressed.[18]

Despite its apparent advances in protecting the interests of shareholders and the public the 1936 Companies Act suffered from a variety of shortcomings. First, it overlooked many of the problems of the managing agency system and left a variety of loopholes open. Of particular importance were its failure: 1) to set a limit on the number of firms which managing agencies could have under its control; 2) to establish (rather than merely recommend) a formula for remuneration of managing agents based upon net profit; 3) to provide for the removal of managing agents in the event of fraud, breach of trust, gross negligence, etc.; and 4) to address the problem of secret profits. Second, some of its provisions (e.g., the formalisation of the 'office allowance') only made the situation worse than it previously was by providing legal sanction to

practices which could be readily abused. Third, the Act did not provide for any administrative machinery to enforce its provisions (Sharma and Chauhan, 1965:186–187; Baig, 1971: 88; Reed, 1998).

As Reed (1998) points out, the net effect of these shortcomings was that the abuses of the system not only continued unabated, but even tended to increase. The increase in abuses was spurred by two historical events. On the one hand, the Second World War provided industrial houses not only with an increased ability to control and manipulate the production and marketing of consumer goods, but also to abuse the interests of shareholders. On the other hand, as I noted above, the impending Independence of India induced many foreign, especially British, interests to withdraw from India and encouraged further expansion by Indian business houses. In many instances such expansion was undertaken in ways which did not necessarily serve the interests of the shareholders of the firms involved. Such practices eventually evoked a sharp response from shareholder groups, most notably the Bombay Shareholders Association. In a Memorandum issued in 1949, this group listed a wide range of abuses by managing agents and suggestions for reform (Sharma and Chauhan, 1965:188). Such pressure by shareholder groups, combined with the general post-Independence political climate, meant that radical changes to, if not the complete abolition of, the institution of the managing agency were inevitable.

The new Indian government was well aware of the need for change and had already begun to address the problem. In 1946 an investigation was commissioned to propose the lines along which the Companies Act should be revised. A few years later, in 1950, the *Company Law Committee* (popularly known as the Bhabha Committee) was established to develop recommendations for a new draft act. Following the submission of the Bhabha Committee report in February 1952, the government introduced the Companies Bill in the Lok Sabha in September 1953. It was passed at the end of 1955 and came into effect on 1 April 1956.

The regulations of the new Companies Act concerning the managing agency system reflect a number of different concerns and opinions. As noted above, the abuses of the system could not be denied. The crucial question at this point was whether the managing agency system still had anything to offer the Indian economy. As several committees noted, its primary contribution in the past had been its role in providing the financing for (and the promotion of) new and established industrial companies. The importance of managing agents in these roles, however, had been decreasing over time and was likely to decrease even further with the establishment of new government financial institutions. Still,

even among those who thought that the system had no long-term future, including the Finance Minister and several government committees, there was some concern about whether abolishing the system might have some major adverse effects on the economic development of the country (Sharma and Chauhan, 1965:199).

Box 3.1 Features of the *Companies Act*, 1956

- a variety of limitations relating to the term of office of managing agents (e.g., a ten year term, subjecting re-appointment to government approval, further grounds for removal from office, government and shareholder approval of amendments to the managing agency contract, in the case of resignation liability for acts committed during the period of management, etc.);
- the elimination of compensation for termination of office in cases involving resignation, suspension or removal from office;
- a prohibition on the transfer of office;
- a ceiling on remuneration of 10 per cent of net profits;
- a prohibition on commissions to managing agents on sales and purchases;
- restrictions on the ability of managing agents to enter into contracts with the managed company;
- prohibitions on loans to the managing agent and on intercompany loans (unless approved by the lending company by special resolution);
- restrictions on inter-company investments;
- limiting the number of companies for which any-one person could be the managing agent to ten;
- greater control over the managing agent by the board (including limitations on the number of directors that the managing agent can nominate to the board);
- a prohibition on managing agents engaging in any business of the same nature of the managed company;

Source: Adapted from GOI, 1956; Sharma and Chauhan, 1965.

While the new Act did not abolish the institution of the managing agent, the number and degree of the new restrictions did leave much doubt as to its future. This was reflected in the sharp decline in the

Table 3.13 Decline in Number of Managed Companies and their Paid-up Capital (PUC)

Year	*Total No. of Public Companies*	*No. of Companies Managed by Managing Agencies*	*Percentage of Companies (and PUC) Managed by Managing Agencies*
1954–55	9178	4091	44.6 (71.2)
1960–61	5688	1049	18.4 (47.4)
1962–63	5477	1149	21.0 (38.1)
1963–64	5607	1121	20.0 (44.1)
1964–65	5639	1090	19.3 (41.2)
1965–66	5606	800	14.3 (38.8)
1966–67	5543	683	12.3 (37.7)
1967–68	5452	642	11.7 (42.5)
1968–69	5432	568	10.4 (4.1)

Source: Based on Sengupta (1983:112).

number of firms managed by managing agents in the years following the new Companies Act (see Table 2.5). Between 1956 and 1965, for example, there was a drop of approximately 80 per cent in both the number of managing agents (from 3,944 to 1,960) and the number of firms they managed (from 15,055 to 1,236) (Baig, 1971:90). Ultimately, on the recommendation of the Managing Agency Enquiry Committee (more popularly known as the I. G. Patel Committee), the 1969 Companies Act (Amended) would abolish the institution of the managing agency effective in 3 April 1970.

Summary and conclusions

As indicated above, the reforms of the managing agency system, and even its abolition, did not manage to alter the growth-inhibiting properties of the model. One problem was that the system arose and operated in the context of certain historical structures which inhibited the introduction and effective enforcement of such reforms. One of these historical structures was, of course, the British colonial state. The policies of this state discouraged Indian industrial development by integrating it into the core-periphery dynamics of the imperial economy and by discriminating in favour of British capital (especially in Bengal where the native entrepreneurial class was effectively disenfranchised) (Bagchi, 1972). In favouring British capital, the government not only initially permitted the potential for abuse in the institution of the managing

agency, but subsequently failed to pass effective reforms to address the problem. This was evident, as noted above, both in the Companies Act of 1913 and the Companies (Amendment) Act of 1936.

A second growth-inhibiting factor lay in the basic inegalitarian nature of the system. As we saw above, disproportionate shares of resources inexorably accrued to the managing agents. These agents could use these resources not only directly in the economic realm to avoid the discipline of the market and operate in ways contrary to the interests of shareholders, but they could also use them to influence the policies of the state. This is exactly what the business elites did through their various regional and national organisations. At first, it was the British managing agents (especially through the Bengal Chamber of Commerce) who were most successful in using such tactics to favour their own interests (*vis-à-vis* Indian capital and/or the public at large). Their strategies were both proactive (designed to ensure further privileges for themselves) and reactive (designed to retain their existing privileges, including the institution of the managing agency) in nature. Gradually, however, as the nationalist struggle progressed and Indian capital became more organised (through FICCI), it too proved effective in using the state machinery (through the Congress Party) to favour its interests. The basic result, as we have seen above, was that the managing agency system was not effectively reformed and economic concentration continued, with Indian managing agencies displacing the British from their leading position.

The other side of this concentration of wealth and power was the stagnation of aggregate demand, reflecting once again the specific pattern of value creation in the colonial model. The stagnation, or at least the less than adequate growth in aggregate demand, was a direct result of a process of industrialisation that did not encompass systematic backward and forward linkages but developed out of the *ad hoc* profit-seeking tendencies of different forms of capital. In other words, the logic of *laissez-faire* capitalism, while succeeding somewhat in producing industrial development in the West, failed to produce the same in India's colonial context.

I started this chapter by looking at some of the reasons behind this, an exploration I will continue through the rest of the work. As I seek to emphasise, the colonial context was not only important in that it discouraged the possibility of indigenous industrial development. It was also, and perhaps more, important, that it established a particular model of capitalism – one that enabled the generation of profits through institutional arrangements rather than product/process improvement. In the next two chapters, I will examine how this colonial model shaped and defined itself through India's post-colonial history.

4
Corporate Capitalism in Independent India: the Interventionist Model and its Contradictions

In Chapter 3 I sketched the genesis and transformation of corporate capital in colonial India. In this chapter, I will attempt to develop a similar characterisation of capital in Independent India, spanning roughly the period 1950 to 1985. First, I will sketch the general context in which the interventionist model was adopted. Next, I shall discuss the principal structures of corporate governance associated with this model, looking at both the micro-level structures internal to the firm as well as the broader political-economic structures within which the firm was embedded. In the third section I will outline the nature of growth and corporate profitability that occurred as a result of the various governance structures specific to the period, and in the final section I will attempt to relate the discussion in the three sections to examine the relationship between the growth of the corporate sector and the overall growth and transformation of the Indian economy during this period.

The emergence of the interventionist model

I define the interventionist model as one in which the state participates very actively in the affairs of the private sector. By choosing this broad definition, I wish to break with the liberal/interventionist dichotomy that has been so central to the understanding of the state in traditional social science. As I hope this discussion will reveal, this dichotomy does not take us very far in comprehending the complexity of the state's role in developing capitalism in countries like India. On the one hand,

the state remained quintessentially committed to a model of liberal capitalism. This was reflected, amongst other things, in the body of corporate law fashioned after the British model. On the other hand, the state sought to regulate capital in a somewhat substantive way, often exceeding the requirements of liberal regulation. Some elements of this regulation, however, often pertained to fairly routine or trivial aspects of corporate management; while these might have imposed certain restrictions on the powers of management, they were unlikely to have radically altered the nature of Indian capitalism. Moreover, sometimes the mere act of establishing regulatory mechanisms fulfilled a symbolic function that aided legitimation. Thus, it is necessary to take as our starting point, a nuanced view of state intervention in India. The particular contradictions of capitalism in independent India have to be located, first, in the contradictions of the political-economic context in which it emerged. It is to this that I turn now.

As is well known, the central political actor in independent India was the Congress Party which, from its very inception, was a fractured and conflicted entity. At least three factions were dominant within it at the time of independence. One was a *conservative* nationalist faction which saw private enterprise as the basic instrument of development but which also saw the necessity for state involvement, primarily for protection and the development of industrial infrastructure. The second was a *moderate* faction which regarded economic planning as an essential instrument of economic transformation in India. This group conceived of state involvement as critical for improving distribution rather than a change in the organisation of production. The third group consisted of those *radical* planners and social scientists that saw planning as an instrument of gradual political evolution toward a socialist state. For this group, the development of planning and the expansion of the public sector were steps integral to this transformation (Bagchi, 1991:611).

Each of these factions, in turn, was linked in different degrees to different classes and groups in society. The *conservative* faction was most closely linked to the largest faction of business, and shared the common project of appropriating the resources of the state for capitalist development. The linkage of this conservative faction to the agricultural population, both its rich and the poor factions, was rather weak (Kochanek, 1974:274–6). The *moderate* faction was most strongly linked to the urban and educated upper middle-classes, and the self-employed professionals (Mukherjee and Mukherjee, 1988:532–4). The *radicals* consisted mostly of intellectuals and idealists from the upper and middle classes, who claimed to represent the urban and agrarian poor. Not surprisingly,

this group suffered from the usual contradictions of a 'vanguard' intellectual entity working on behalf of a weaker class. The second group comprised very small, first-generation entrepreneurs who saw indigenous enterprise as an intrinsic element of both *nationalist* as well as *socialist* development (Ghosh, 1988).

These factions within the Congress Party, with their respective patterns of social linkages, suggested different trajectories of action once the post-colonial state was formed. Accordingly, they envisioned different roles for the state. The *conservative* trajectory was to transform the extant feudal system dominated by the agrarian rich into a modern capitalist industrial economy with high rates of growth. These goals were articulated in the famous *Bombay Plan of 1944*, a memorandum authored by the leading industrialists of the day (Thakurdas P., Tata J. R. D., Birla G. D. *et al.*, 1944). The Plan accepted – and in fact strongly advocated – state participation in the economy by transferring resources from farm to industry and by allocating the lion's share of public resources to the development of large scale capital-intensive industry. In that sense, the conservative trajectory was somewhat similar to what became identified later as the statist model in East Asia.

The *moderates* placed emphasis on the state's role in distribution, and in that sense, their vision was one of 'development' rather than 'growth'.[1] While they also saw industrial expansion as the primary strategy, the moderates envisaged the state's role to be more than merely a supplier of infrastructure for private enterprise and of minimal social services. They saw state participation in the economy as essential for capital formation – both human and physical – as well as technological development, which they held to be the cornerstones of development (Deshmukh, 1957). The *radicals* at this time were looking far beyond both growth and development. This group, consisting of members of the Congress Socialist Party who worked in close association with the Communist Party of India, had gained considerably in strength due to the extensive mobilization of industrial workers and the agrarian poor (Frankel, 1978:64–70).[2]

The configuration of the various factions within the Congress Party and their social linkages as they existed at the eve of Independence can be summarised shown in Table 4.1.

Given the differences in the linkages, objectives and visions of the role of the state, it is not surprising that the actual economic strategies adopted in India reflected a compromise between the various factions. The primary features of the interventionist model that emerged from this compromise were as follows.

Table 4.1 Factions within the Congress Party and their Social Linkages at the Eve of Independence

Social linkages[3]	*Factions*	*Objectives*
Industrial elite, especially the monopolistic faction	Conservatives	Accelerated economic growth through the expansion of capitalism
Educated urban upper middle-classes, self-employed professionals, middle-rung first or second generation entrepreneurs	Moderates	'Development' consisting of growth and capital formation plus strong distributive measures undertaken by the state
The urban and agrarian poor; small indigenous first generation entrepreneurs	Radicals	Socialist transformation

Source: Compiled from various sources as indicated in text.

First and foremost, central planning was undertaken, the principal objectives of which were poverty alleviation and self-reliance through a programme of industrial development. In general, a balance between agriculture and industry was sought, although in reality the emphasis was on industry. The state and the private sector were to participate jointly in this industrialisation programme. The state was to assist the private sector, through direct participation in production, the provision of incentives and the creation of a cautious relationship with foreign capital. However, at the same time that the state was to further industrialisation, it also had the responsibility to ensure that it helped accomplish specified national objectives. As such, the state was to define certain limitations on the freedom of private capital.

The exact contours of the model that was adopted took much more from the conservative and moderate visions than the radical one, because of the gradual atrophy of the importance of the radical faction in the period that followed the formation of the post-colonial state.[4] On the face of it, however, the radicals won a victory. Their victory was symbolised by two things: (1) Jawaharlal Nehru's appointment as Prime Minister (since he was perhaps the most visible face of the radical faction); and (2) the adoption of an apparently elaborate mechanism of controlling accumulation.[5]

Nehru's assumption of office served two purposes. First, it projected an apparent victory for the radical faction, whose association with the nationalist/anti-imperialist struggle was an important element of the

legitimacy of the nascent post-colonial state. Second, it helped to diffuse radical political demands – especially land reforms and the nationalisation of private enterprise, which Nehru and the radical faction had espoused since the very initiation of discussions about the nature of the independent state (Chandra, 1975:1311). In other words, Nehru's election to the office of the Prime Minister encouraged the radical groups (at least temporarily) to work within the system rather than opposing it. This came as a relief to the conservative and the moderate factions who were unified in their joint disagreement with the radical project of socialist transformation. However, this unified stand began to weaken very soon, as their own disagreements over development policy began to unfold (Bagchi, 1993:613).

These complexities of the immediate post-Independence situation in India were directly responsible for the contradictions of the resultant system. It is important, however, not to emphasise too much the 'inherent' contradictions of the system that emerged – and to keep in mind that it was not entirely beyond the realm of possibilities that a model of regulated capitalism, if seriously implemented, may well have helped India realise some minimal goals of economic development. With this caveat in mind, let us now turn to the specific features of the interventionist model.

Structure and governance in the interventionist model

Macro-economic context

The basic framework of the interventionist model was delineated in the *Industries (Development and Regulation) Act* of 1951, arguably one of the most significant pieces of legislation in India's corporate and industrial history.[6] The basic measures of the Act consisted of the following:

- the requirement that all scheduled industries register with the government;
- the requirement that a licence be procured for the start-up of new undertakings, the expansion of productive capacity and the manufacture of new products;
- the requirement that permission be received for the change of location of an industrial unit;
- the right of the government to revoke the licence in cases of misrepresentation or misuse;
- the right of the government to investigate undertakings, require changes (in cases of mismanagement or management not in the

national interest) and, in the event of non-compliance, to take over management control;
- the right of the government to regulate the price, supply and distribution of products produced by certain designated industries;
- the establishment of a Central Advisory Council for Industry (CAC) which the government had to consult before making any subsequent changes to the Act; and,
- the establishment of Development Councils in scheduled industries (to recommend production targets and quotas, establish efficiency norms, promote research, etc.).[7]

The above set of regulations came to constitute the infamous *licence-permit-quota* regime, which came to be regarded over time as the ultimate symptom of the inefficiencies of the model. The regime comprised bureaucratic mechanisms through which the government could establish direct control over the establishment and expansion of new enterprises as well as over the development of new products. The objectives of this direct control mechanism were, avowedly, *social* and went far beyond the cost/profit considerations that guide the new ventures in liberal economies. In reality, it created a set of institutional barriers to entry for smaller firms, resulting in a systematic weakening of competition.

Subsequent to the Policy Resolution of 1951, several other regulations were put in place between 1947 and 1960:

- The *Industrial Policy Resolution of 1956* sought to set up a basic division of labour between the private and the public sectors. It divided all economic activity into three categories. Industries in *Schedule A* were to be the exclusive responsibility of the state.[8] Industries in *Schedule B* were to be progressively taken over by the state, with the private sector limited to a supplementary role.[9] The third category consisted of all the remaining industries and was open to the private sector. The *Resolution* stressed that these categories were not 'watertight' and the government could venture into other sectors when it was in the nationalist interests as well as invite private participation in Schedule A activities. The industrial licensing scheme was closely tied with a number of other government policies such as import licensing and the allocation of other scarce resources.
- As a companion to the Industrial Policy Resolution, the Indian parliament also passed The *Companies Act of 1956*. Its professed long-term objective was to lay the basis for a 'socialist pattern of

society' in accordance with the declaration of Parliament (Baig, 1971:89). Its immediate and more pragmatic objective was to stem the abuse of shareholders' rights and public money that had become rampant in the managing agency system. The Act sought to gradually phase out the managing agency system.

- Of particular importance also was the institution of the Controller of Capital Issues (CCI). Established in 1947, the *Capital Issues (Control) Act* required that official permission be obtained for the issue of all types of securities, and more importantly, the prices of all corporate securities were to be determined by the Controller of Capital Issues.
- Finally, the *Foreign Exchange Regulation Act* and the *Import and Export Control Act of 1947* sought to regulate all international transactions by private firms.

It is critical to note that, despite these cumbersome controls, the Indian Government did not actually take up the task of *allocating investment to specific sectors*, as did the governments in East Asia. Instead, through the various Industrial Policy Resolutions, it sought to assign to the state the responsibility of developing two types of industries: first, those which were of strategic importance, and second, those which were necessary for private sector development, but in the near-term did not promise sufficient material incentives for the private sector. Further, the Resolution of 1948 ensured that the state had the discretionary power to allow the participation of the private sector in *both* Schedule A and Schedule B industries. It also asserted that private units which were *already in existence* in industries now designated for the public sector would not be nationalised.

A few other defining characteristics of the macro-economic context of the time need to be noted. The first of these was the nature of the capital market. Up until the 1950s the contribution of capital markets in India remained small in comparison with direct investment. The number of shareholders remained but a very small fraction of the population. As well, commercial banks tended to shy away from financing industry. This changed somewhat in the 1950s as commercial banks, especially the State Bank of India (SBI) and its subsidiaries began to play a greater role in the field of industrial finance. However, until about 1969, this involvement did not aid the general development of industries in any sustained way since most of these banks were closely associated with large Indian business houses, and divested their funds according to those particular alliances (Mehta, 1952). It is only since the

nationalisation of fourteen major commercial banks in 1969 that bank finance became somewhat more widely available to industry.

In order to counter the lack of development of capital market, the state fostered a number of financial institutions for facilitating the allocation of industrial credit. These included both public financial institutions (PFIs) sponsored by the central and state governments, viz., state financial corporations (SFCs) and State Industrial Development Corporations (SIDCs).[10] The former included the Industrial Finance Corporation of India (IFCI) founded in 1948, the Industrial Credit and Investment Corporation of India (ICICI) established in 1951 and the Industrial Development Bank of India (IDBI) which came into being in 1964. In addition to banking and term-lending institutions, the government also sponsored investment institutions such as the Life Insurance Corporation of India (LIC), the Unit Trust of India (UTI) and the General Insurance Corporation (GIC). These various institutions came to dominate industrial financing during the interventionist period. It is also important to note that the state initiatives in this regard have played a central role in channelling household savings into industrial investment, at a time when the credibility/maturity of the corporate sector proved highly inadequate to be able to do that.

It may be argued that this policy of providing easy access to credit under soft conditions inhibited the growth of capital markets, and thereby inhibited the development of competitive credit allocation mechanisms. Other government policies also contributed to the continued infancy of capital markets. Of particular importance in this regard was the institution of the Controller of Capital Issues (CCI). As mentioned before, the government granted the CCI, as part of its efforts to channel investment funds to priority areas, the power to determine the prices of corporate securities. The resulting combination of soft credit and a bureaucratised equity market juxtaposed on an already very weak capital market was a system with little disciplinary power or allocative efficiency.

These macro-economic conditions, in conjunction with the legacy of the colonial model, somewhat pre-determined the nature of corporate governance in the interventionist model. It is to this that I turn now.

Ownership and control: the Indian conglomerate

Historically, the conglomerate or the *business house* has constituted the predominant form of corporate governance in India. Such a

conglomerate typically consists of a network of companies, each of which is promoted by the members of a particular business family. Each of these networks are centred around an apex company, and the overall directions in investment of the conglomerate, allocation of group profits etc. are decided and co-ordinated through this apex company.[11]

The Indian conglomerate arose out of the managing agency system in which a single agent managed a large number of unrelated businesses. The agent, or the *managing agent* as he was more popularly known, held very little stake in each of these companies. After Independence, the leading Indian managing agents began actively 'promoting' new businesses. The *promoter* thus became the central actor in India's post-colonial corporate economy. The promoter's primary function – much like the managing agent's – was to float new ventures by contributing a minimal amount of equity capital, and then raising the rest through public offerings or from public financial institutions. This method of promoting companies resulted in fairly widely held corporate structures, which could potentially lead to some democratisation in decision-making. The following table shows the typical shareholding structure of some of the largest public limited companies in India.[12]

First, note that no single entity holds a controlling interest, i.e. 51 per cent of the total equity. As the report of the *Industrial Licensing Policy Inquiry Committee* (ILPIC) observed far back in 1973:

Table 4.2 Shareholding Structure of Selected Public Limited Companies

Name	*Foreign (%)*	*Govt FIs (%)*	*Corporate bodies (%)*	*Directors & relatives (%)*	*Top 50 share-holders (%)*	*Others including the public (%)*
ACC	7.7	32.03	18.70	0.02	10.26	31.24
Bajaj Auto	0.43	9.53	36.82	11.19	10.02	32.01
GRASIM	22.84	32.75	23.44	0.23	0.55	20.16
Gujarat Ambuja	9.43	13.93	36.47	3.48	2.78	33.91
ITC	34.17	39.25	1.12	0.02	0.64	24.80
JK Synthetics	5.29	25.90	25.92	9.37	2.03	31.40
Kirloskar Brothers	0.21	29.25	2.44	0.72	10.13	57.22
Mafatlal	0.38	4.05	45.96	5.34	1.70	42.57
Nagarjuna	4.87	30.09	11.06	0.04	1.18	52.71
Reliance Industries	6.33	18.38	27.61	0.79	1.81	45.08
Tata Chemicals	0.71	35.73	33.32	0.46	12.01	17.77
TELCO	12.41	41.6	18.85	0.25	1.03	25.86
TISCO	1.59	47.58	10.84	0.04	1.30	38.65

Source: Compiled from the Bombay Stock Exchange Directory, various years.

> the assumption that control over a concern requires the controlling interest should have more than 50 per cent of the equity is based upon the belief that all the shareholders have the same degree of interest in the management and other internal affairs relating to the company. Experience, however, shows that this is rarely correct. Public limited companies, having a large number of shareholders, are normally controlled by groups with a much smaller share of equity holding. Two factors contribute to this. First, with the large amount of capital required for the more important companies, the number of shareholders is large and with the expansion of the capital market, and participation in investment of small investors, the share ownership is widely dispersed. The smaller shareholder normally looks upon his equity holding as an investment and is neither interested in the general meeting of companies nor is able to attend them because of the time and expenses involved. Thus, these meetings are attended only by a small fraction of shareholders. Secondly, the company law does not require any minimum percentage of shareholders to be present at general meetings of companies, the presence of five shareholders is sufficient to form a quorum in the case of public limited coys. There is also no limit to the proxies that an individual can hold. Controlling interest can, therefore be obtained and maintained merely by having a majority of votes represented at a general meeting, and normally it is possible with control over much less than 50 per cent of the equity. As a result, much less than one-third of the effective equity has been adequate for an existing management to continue its control over the company.
> (*Report of the Industrial Licensing Policy Inquiry Committee* 1969:15–16)

Direct majority stake is therefore hardly a condition necessary for obtaining or maintaining control. Minority stake, exercised through inter-corporate investments provides a much more important instrument of control. There is no easy way of obtaining data on inter-corporate investments in India; however, some indication of its importance can be obtained from the data on holdings of corporate bodies (Table 4.1). Inter-corporate investments, when combined with interlocking directorships and devised in a manner that promotes integration between financial and industrial activities are particularly successful in maintaining control with little equity stake.[13] Table 4.3 provides an illustration as to the extent to which this mechanism serves as a controlling device.

Table 4.3 Control of Companies through Inter-Corporate Investments (1972–73)

Business group	*Percentage controlled through inter-corporate investments (in descending order)*		
	of paid-up capital	*of net worth*	*of gross capital employed*
Thapar	87.43	95.93	85.68
TVS Iyengar	72.41	75.32	62.49
Walchand	57.53	60.32	60.85
Andrew Yule	54.99	62.81	48.49
JK Singhania	53.62	40.40	45.79
Bangur	53.00	57.96	58.27
Shaw Wallace	45.58	25.95	20.18
Birla	44.39	54.43	47.37
Jardine Henderson	44.28	46.91	37.55
Rallis	40.24	30.39	23.28
Mafatlal	38.17	45.53	44.83
Tata	25.18	18.88	23.9
Mahindra	20.82	9.77	15.36
Shriram	18.59	10.75	19.0
Kirloskar	16.86	12.03	18.72
Martin Burn	13.60	1.63	8.25
Parry	12.54	19.30	23.41
Modi	1.32	0.42	1.44

Source: Based on V. K.Singhania, *Economic Concentration through Inter-Corporate Investments*, Himalaya Publishing House, Bombay, 1980, p.117.

The nature of inter-corporate investments determines in turn the structure of the conglomerate. As I discussed in Chapter 2, one may distinguish between an *umbrella structure* and an *inter-locking structure*. An umbrella structure consists of a holding company at the centre and a number of subsidiaries surrounding it. Subsidiaries may be either investment companies or operating companies, and may in turn own stakes in other operating companies (see Figure 2.1).

An *interlocking* structure is more complex. As schematised by Hazari the typical inter-locking structure in India came to comprise of the *Inner Circle*, the *Outer Circle* and the *Complex*. The *Inner Circle* consisted of those companies over which the conglomerate in question had direct and effective control; the *Outer Circle* consisted of firms in which the conglomerate had 'a voice and a material influence but not the authority of ultimate control'. The union of the *Inner Circle* and the *Outer Circle* defined the *Complex* (Hazari, 1966:7). In Hazari's estimate 'the four top

Inner Circles increased their ownership of share-capital of the non-governmental public companies from 17.91 per cent in 1951 to 22.34 per cent in 1958. The comparable ratio for the Complexes went up from 21.85 per cent to 26.60 per cent. In 1958, the two largest Complexes, Tata and Birla, had nearly one-fifth of the gross capital stock of all non-government public companies'. Further, the Report showed that between 1951 and 1958, the gross capital stocks of companies controlled by the top four *Complexes*, Tata, Birla, Martin Burn and Jains, had increased by 100 per cent (Hazari, 1966:p48).

The critical point to note is that in some of these firms, control was obtained with very little financial stake. Further, As has been documented several times in India's corporate history, interlocking structures have proved particularly useful in that they provide a defence against takeover threats.

Let us now discuss each of the other categories of shareholders and the various ways in which they exert control over management of the companies.

Institutional Investors: As Table 4.1 above indicates, the largest stake in major Indian companies is usually held by public financial institutions (e.g. IDBI, ICICI, IFCI, etc.). In most cases, whenever a public financial institution holds a substantial amount of equity in a company, it also appoints its own nominee on the board of directors of the company, in order allegedly to protect the interests of the Indian public. However, the role of the nominee director has been rather controversial and to date no consensus exists as to the role the nominee directors are supposed to play. It is acknowledged by and large that the nominee directors have been, at best, passive in their involvement, except in the case of takeover threats. In most of these cases, nominee directors are believed to have supported existing management; whether this had been conducive to the protection of the public interest is an open question.

Foreign Investors and Overseas Corporate Bodies: Till the onset of reforms in 1991, foreign holding of Indian companies was somewhat limited except for subsidiaries of MNCs. In the interventionist era, MNCs were allowed to hold up to a maximum of 49 per cent in equity in their Indian subsidiaries. Between 1994 and 1997 these limits were raised to 51 per cent and for some industries, even up to 74 per cent foreign equity holding has been allowed, subject, of course, to clearance by the Foreign Investment Promotion Board (FIPB). However, the question as to whether an MNC is granted permission to increase its stake in its subsidiary is almost always a political one, implicated in the larger

question of national versus foreign control. For now, let us note that the question of national control is not simply a concern of obscurantist politics, but very much a concern of corporate capital which finds itself caught in the contradictory currents of globalisation.

The Public: The importance of the public as shareholders is determined by the extent to which the capital market is developed and individual investors feel confident about investing in private corporations. As is evident from Table 4.1, the extent of public shareholding in large Indian corporations is fairly significant, although there are large variations. Further, the proportion of total equity held by the top fifty shareholders is often quite small. This can have two somewhat contradictory ramifications. On the one hand, because no one individual/group holds a large proportion of the total stake, such a structure could potentially allow for active intervention by the small investor. On the other hand, because shares are so widely dispersed and individual shareholders hold so little of the total stake, they are hardly in the position to develop a unified stance against decisions taken by the company. This, in a context where investor education and activism has been consciously discouraged, has resulted in systematically distancing the small investor from companies.

The critical question here is to determine who, amongst all these categories of shareholders, exercises effective control over the corporation. As I noted at the outset, the typical Indian firm is a member of a conglomerate that has been founded by a business family. As the discussion above indicates, effective control by and large continues to be vested in the hands of the members of the founding family. Let us consider briefly what implications this might have. First, if this control is held and exercised through fairly democratic (and, of course, legally endorsed) structures, they are compatible with standards of fairness within a liberal–capitalist framework. Second, even when exercised through formally democratic channels, continued control by a business family – especially without a corresponding stake in equity – may still raise the question as to whether this control is *legitimate*. Unfortunately, the current trends in theorising or policy-making in the developing world hardly allow us to raise or answer such questions.

With respect to other mechanisms of control, a strong continuity with the colonial model is evident. The two predominant mechanisms of the earlier era – viz., interlocking directorates and intercorporate investments – continued to be the two most significant methods used by controlling groups to maintain their power over firms. While the *Companies Act of 1956* limited the number of directorships that an individual

could hold, this restriction is generally acknowledged to have been much too weak to serve as an effective control on interlocking directorates. A few years after the passing of the Companies Act, for example, a study showed that the top ten industrialists held 183 directorships, while 100 individuals held between them 966 directorships of leading business concerns (Mehta, 1961:292–9). The implications of this are even more serious in terms of familial control: seven leading industrial families held 303 directorships or partnerships; two of these families, the Bangurs and Goenkas, alone held 136 directorships in industrial concerns. Similarly, a study by the Company Law Board undertaken at the same time indicated than more than 20 per cent of directors held more than 10 directorships each, a figure substantially higher than in the US or UK at the time (Baig, 1971:112).

Table 4.3 below summarises the defining characteristics of the interventionist model that emerge from our discussion above. It also shows a comparison between foreign and Indian business houses, and it is interesting to note that there are some striking similarities between the governance structures of the two groups. This is not surprising since both operated on the same logical and ethical principles.

The marked difference, of course, lay in the macro-economic context of governance. Indian business houses, for example, were required to obtain governmental approval for such matters as the appointment of whole-time directors and managing directors, their salary levels, tenure, etc. Such intervention, which involved wide powers of discretion, was ostensibly intended to help contain income inequalities and prevent economic concentration. This level of intervention was unparalleled in any Anglo-American system, although not incompatible with the Japanese or German model.

Also substantively different from the Anglo-American model was the level of state subsidisation towards industry. Again, in comparison with the East Asian or German models, these levels/modes of subsidisation were not unprecedented. There is an important distinction, however, between the East Asian developmental state models and the Indian interventionist model. Following Alice Amsden, I will call this the distinction between *reciprocity* and *unidirectionalism*.

Reciprocity implies that element of intervention where every effort of the state to augment accumulation is reciprocated by capital by fulfilling performance standards set by the state (Amsden, 1989:146–150). By contrast, *unidirectional* intervention occurs where the state chooses to augment accumulation without requiring or specifying a priori, any performance standards in return. Reciprocity was built into East Asian

Table 4.4 Comparison of Indian and Foreign Business Houses

	Subsidiaries of multinationals	*Indian firms*
Formal structure of governance	• single-tiered board of directors	• single-tiered board of directors • role for nominee directors
Structural/ institutional context	• undeveloped capital markets • licence-permit-quota regime	• undeveloped capital markets • soft credit system • protected, non-competitive product markets • regulation of foreign exchange expenditure • *licence-permit-quota* regime • controlled pricing of shares • subsidised infrastructural and intermediate inputs from the state sector
Locus of control *proximate*	• minority ownership (by parent company)	• minority ownership (by apex company)
ultimate	• strategic position (management control of the parent company)	• majority ownership (of apex company by controlling family)
Other mechanisms of control	• private (or regulated) placement of stocks • debt, rather than equity financing • discouraging shareholder participation	• interlocking boards • intercorporate investments • private (or regulated) placement of stocks • debt financing through financial institutions • discouraging shareholder participation

Source: Reed (1998) and as in text.

state policies in two ways: in an *ex-ante* sense, whereby every effort was made to ensure a priori that projects financed by the state would succeed. Reciprocity was also to be ensured in an *ex-post* sense, by implementing specific disciplining/punishment mechanisms, or more generally, by establishing *credible threats*. In South Korea, for example, ex-post measures included the revoking of licences and all privileges associated with it, and reorganisation of entire industries through state-led mergers. The ex-post measures of reciprocity were particularly important in eliminating unanticipated results of accumulation that might have been impossible to foresee in the ex-ante review. Also, as

in most interventionist regimes, the ex-ante measures of reciprocity were sometimes compromised, most often for short-term gains in political legitimacy. In those cases, the ex-post review helped to ensure that the anticipated gains from legitimacy were actually realised.

As I have argued in detail elsewhere, *reciprocity was not the guiding norm for the interventionist model in India* (Mukherjee Reed, 1994). Several examples of the absence of reciprocity can be cited: the functioning of the industrial licensing system, the export promotion programmes or the development banking initiative. Without going into much detail, it may be useful here to briefly discuss the problems that came to characterise these three mechanisms, keeping in mind that they worked exceptionally well in the East Asian context, i.e., when they were implemented under conditions of reciprocity.

The system of *industrial licensing* was intended to ensure a planned development of industrial capacity by preventing the concentration of resources in certain sectors as against the paucity of resources in others. It was also intended to prevent the concentration of capacity in particular industrial sectors. However, in reality, the licensing system managed to do exactly that. The widespread abuse of licences – both in the form of overutilization and underutilization of licensed capacity – resulted in a large-scale cornering of capacity by a few firms. Not only was reciprocity not built into the mechanism in an ex-ante sense, the ex-post anti-trust measures also failed (see Appendix to this chapter, Tables 4.A1 and 4.A2).

Export promotion programmes met with the same fate. While significant promotion packages (including grants, loans and tax incentives with up to 100 per cent tax write-offs) were made available to firms, they remained unable to promote exports in any significant way. While the foreign exchange earnings of exporting firms were consistently negative, the export-intensity of their operations (i.e., the export-to-sales ratio) also remained stagnant. This was particularly true of large firms, and continued over a long period of time.[14]

Let us now briefly examine the institution of *development banking* which provides perhaps the best example of the absence of reciprocity in India. What development banking essentially entailed is the following : (1) centralised control of the credit system; (2) non-market systems of allocation of credit, where credit decisions are embedded in bureaucratic/ administrative processes rather than market processes; and (3) allocation of credit to designated *priority sectors*, consisting of several economically weaker sections of the populace. In India, a rudimentary model of development banking was adopted almost immediately after

Independence, with the state taking up the major responsibility for mobilising household savings for major investment projects, both in the public and the private sectors. The initial model was expanded significantly in 1969, with the complete nationalisation of the commercial banking system. The nationalised banking system, along with the network of public financial institutions became the two main conduits for the financing of private sector projects in India.

Table 4.4 shows the distribution of the 204 largest companies according to the extent of shareholding by the public sector financial institutions. Such availability of state financing helped in systematically reducing the necessity of the large firms to go the capital market for

Table 4.5 Share of Public Sector Funds in the Paid-up Capital of Indian Companies Owned by Leading Business Houses

	Percentage share of public sector funds (%)					
	0–5	*5–10*	*10–25*	*25–50*	*50+*	*Total*
(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*	*(7)*
1. Birla	1	1	7	6	1	16
2. Tata	3	–	2	10	–	15
3. J K Sin	1	–	1	1	–	3
4. Mafatlal	–	–	4	2	–	7
5. Thapar	–	–	2	–	–	2
6. Modi	–	1	1	3	–	5
7. A C C	–	–	–	1	–	1
8. Bangur	–	–	–	7	2	9
9. L & T	–	–	–	1	–	1
10. Sarabhai	–	–	–	1	–	1
11. Bajaj	1	–	2	–	–	3
12. I C I	1	–	1	2	–	4
13. Mahindra	1	–	1	2	–	4
14. Shriram	–	–	–	–	1	1
15. Walchand	–	–	–	1	–	1
16. Kirlsokar	1	–	1	3	–	5
17. I T C	–	–	–	3	–	3
18. T V S	–	–	1	–	–	1
19. H.Lever	–	1	1	–	–	2
20. Others	7	4	25	24	6	66
21. FCCs*	4	4	18	11	–	37
22. Other Companies	1	1	5	7	3	17
Total	22	12	72	86	12	204

* Foreign-controlled companies

Source: Institute for Studies in Industrial Development (ISID), New Delhi.[15]

obtaining investible capital; rather the state-owned commercial banks and financial institutions became a source of cheap capital at regulated rates of interest and continuously negotiable repayment schedules (World Bank, 1992:85–9).

Among the 204 companies funded by public money, in 86 companies the stake of the public sector financial institutions in risk capital was more than 25 per cent. Amongst the units financed, the number of companies of the Birlas and the Tatas (the top two conglomerates in the country) was the highest. A more aggregative view of the contribution of development banks to capital formation of the large private sector can be obtained from the following figure.

By way of its attempts to exert some management control in lieu of its financial contribution, the government put in place a system of nominating directors to the board of those companies where it contributed a significant amount of capital.[16] Not only has the institution failed to influence corporate decision-making in any substantive way, it failed even to impose the minimum requirements of reciprocity: up until today, the public financial institutions remain systematically unable to punish defaulters. As part of the development banking initiative, a mechanism to deal with default was designed, but not successfully implemented. The mechanism comprised a convertibility clause, which stipulated that if the dues came to exceed a certain specified

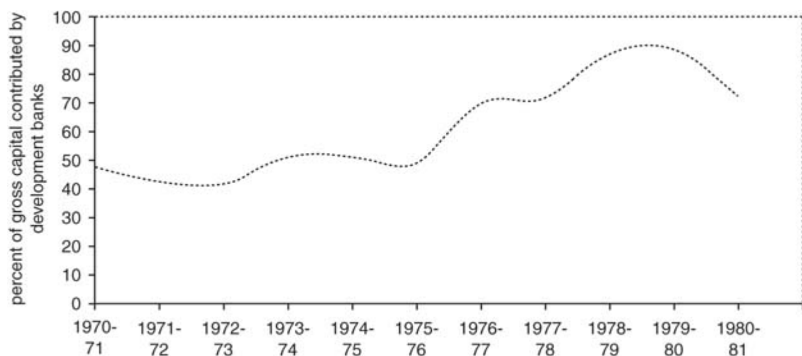


Figure 4.1 The Role of Development Banks in Gross Fixed Capital Formation of Medium and Large Public Limited Companies, 1970–71 to 1980–81

Note: Institutions covered here are IDBI, IFCI, ICICI, LIC, UTI etc. The data is based upon corporate finance statistics published by Reserve Bank of India for companies with a paid-up capital of at least Rs.50 million or more.

Source: Based on Rao, V. L. *Progress of Development Banking in India*, Chugh Publications, Allahabad, 1986.

level, the amount of capital contributed by the public financial institution would be converted into equity. As Table 4.5 below indicates, the convertibility clause was rarely put to use. IDBI for instance exercised the conversion option only in 102 cases over the 22 years of its existence; similarly, between 1948 and 1975, the IFCI exercised the convertibility option only for *one* firm.

This is particularly remarkable in light of the fact that a majority of companies actually had nominee directors on their boards. One estimate shows that by the early 1980s there were roughly 700 nominee directors representing public financial institutions (Sengupta, 1983:221). With respect to the distribution of nominee directors, a survey conducted between 1981 and 1983 by Gupta (1989) indicated that companies of all different sizes had nominee directors on their boards; almost 87 per cent of the largest firms had nominee directors (see Table 4.7).

To sum up, the failure to implement even the minimal conditions of reciprocity has emerged as one of the most dominant features of development banking under the interventionist model. In my view, a more important fact, however, is that reciprocity was often not even built into government policy in a systematic fashion. Most analyses of the interventionist model do not focus on this lacuna of the model; rather, the analytic attention is either on the *failure of implementation* or on rent-seeking and corruption. As I have argued elsewhere, both these

Table 4.6 Exercise of the Convertibility Clause by Public Financial Institutions

Financial institution	*Exercise of convertibility clause*
IDBI	Cumulatively, at the end of June 1987 • IDBI had considered the CC for 1064 companies (involving an aggregate assistance of Rs.35 billion) • Had exercised the CC in 102 cases (and acquired equity shares of Rs.236 million through conversion of loans aggregating Rs.645 million. • The CC was waived for 295 companies involving an aggregate amount of Rs.4.28 billion.
IFCI	Cumulatively, at the end of 1987–88 financial year • The CC had been stipulated in 1283 cases, exercised in 121 cases, and waived in 484 cases • Until June 30, 1975, the CC was stipulated for 180 firms and executed for 1 firm

Source: IDBI and IFCI *Annual Reports*, various years.

Table 4.7 Percentage of Listed Companies with Nominee Directors, 1983

Size-class of companies by paid-up capital (Rs lakhs)	*Number of companies covered*	*Percentage of companies having nominee director(s)*
below 25	73	32.9
25 – below 50	87	52.9
50 – below 100	69	44.9
100 – below 300	115	61.7
300 – below 1000	76	67.1
1000 and over	24	87.5
All size-classes	444	55.0

Source: Gupta (1989:28).

problems – of corruption and failure of implementation – must be evaluated in light of the structural properties of the model. Implementation for instance has been remarkable in certain areas where state and business have acted in concert. As Table 4.A3 in the Appendix to this chapter indicates, import substitution policies have been highly successful in bringing down the availability of certain items in order to protect market shares of Indian firms. Similarly, the phenomenon of rent-seeking needs to be assessed in more nuanced a fashion than is currently possible within the framework of neo-utilitarian political-economy.

Political power of capital

As my argument above should indicate, political power rather than economic efficiency has been one of primary sources of corporate profits in India, as in most parts of the developing world. In general, capital's political power derives primarily from its active participation in the process of state formation, and as I discussed above, this was manifest in some of the major policy measures adopted by the Indian state after Independence. The collaborative relationship between state and capital that evolved through the process of state formation was further consolidated through three processes in the post-independence period.

The first of these concerned corporate financing of election campaigns. In 1967, the Congress is reported to have collected 74.72 per cent of its funds from the top four conglomerates belonging to the Tatas, the Birlas, the Khataus and Martin Burn Ltd. In 1968, it was reported that the top 126 companies contributed a total sum of Rs.10 million ($1 million at the 1966 exchange rate) to political parties, including the Congress and the opposition parties. The two largest conglomerates, the

Tatas and the Birlas, contributed 34 per cent of this total sum which went to the Congress' exchequer. The Government of India's own study in 1968 showed that between 1962 and 1968 companies officially contributed Rs.250 million ($25 million at the 1960 exchange rate) to forty seven political parties (including independent candidates). The most significant recipient was the Congress Party, which received Rs.200 million (approximately 80 per cent); the other forty-six parties received the remaining 20 per cent of the total contribution (Bambhri, 1982: 149–51). By and large, however, company contributions accounted for only 20 per cent of the total contributions of business to political parties. The bulk of the contributions came in the form of individual donations.

Second, since Independence, industrialists or their appointed executives had regularly begun to contest elections to the Lower House of the Parliament (Bambhri, 1982:151). Those who won were important representatives of the 'business view' in the parliament (Kochanek, 1974:356). Kochanek gives a fascinating account of how a strong consensus began to emerge from within the business community as to the necessity for businessmen to enter into politics. He mentions a proposal that each of the top fifty business families to designate one of their younger members to devote his full time to a political career; the FICCI allegedly developed a proposal to get at least one hundred businessmen elected to the parliament by 1967 (Kochanek, 1974:229). None of these proposals, however, were eventually successful.

Third, a number of informal linkages, between the top industrialists, and Cabinet members had strengthened over the years of planning (Kochanek, 1974:274–5). These translated into at least two kinds of palpable gains for particular businessmen: the channelling of investment funds from government financial institutions, and the granting of industrial licences in a manner that contradicted the goals of licensing to favour large industrial houses.[17] In recent times, the rise of Reliance Industries into a $3 billion empire under the leadership of Dhirubhai Ambani provides one of the greatest examples of the way in which political relationships have been exploited for financial gains. The private placement of Reliance's stocks with one of India's premier public financial institutions at an estimated loss of Rs.30 million to the public is only one of the elements in the saga of Reliance's meteoric rise.

Analytically, an important question is to determine whether liberalisation can sever these linkages between state and business. Neo-liberals have argued that this would indeed be the case: once the state is rolled

back, *rent-seeking opportunities* would be drastically curtailed, so that bureaucrats would be automatically deterred from granting special privileges to businessmen. It is not clear, however, whether a simple reduction in the size of the state will actually reduce or even contain capital's structural power. In fact, the reverse could very well reflect India's reality. In any case, a simplistic view of state–business relationships is unlikely to prove conceptually adequate for capturing the complexities of the issue. As I will argue below, the central suggestion of the rent-seeking approach, that the growth and profitability of business must necessarily suffer under an interventionist regime, does not stand up to close scrutiny.

Growth and profitability in the interventionist model

As indicated above, the Indian corporate sector has experienced remarkable growth under the interventionist regime. At the present time, there are about 500,000 companies registered with the Government of India. Table 4.8 indicates the growth in the number of companies and their paid-up capital.

Approximately 15 per cent of these companies are public limited companies, and they account for about 76 per cent of the total paid-up capital of the private corporate sector. As of 30 November 1998, the Department of Company Affairs estimated the total paid-up capital of the Indian private sector to be Rs.1.4 trillion. There are approximately 9,000 companies listed in the various stock exchanges in India with

Table 4.8 Growth of the Private Corporate Sector, Numbers and Paid-up Capital (in rupees million)

Year	*Public Limited Companies*		*Private Limited Companies*	
	Number	*Paid-Up Capital*	*Number*	*Paid-Up Capital*
1956–7	8771	6.96	20512	3.09
1960–1	6663	9.15	19344	3.56
1965–6	6410	13.46	20386	3.55
1969–70	6436	17.41	22242	4.47
1975–6	7593	26.75	35162	8.22
1980–1	9388	35.50	52475	11.52
1985–6	19837	71.39	103522	23.68
1990–1	26813	145.69	196472	41.17

Source: Government of India Department of Company Affairs, Ministry of Law, Justice and Company Affairs, *Annual Reports* of relevant years.

close to $150 billion in terms of market capitalisation. At the present time, the private corporate sector contributes about 20 per cent of the net value added in the economy, up from 8 per cent in 1962–63.[18]

I will consider three aspects of the expansion of the corporate economy under the interventionist model: aggregate growth rates (in terms of the number of companies and their paid-up capital, as shown in Table 4.9); the growth rate of assets; and the growth rate of profits. Figure 4.2 presents the aggregate growth rate of assets in the corporate sector at constant prices. Not surprisingly, the rates vary quite substantially across sectors and across years and do not show the kind of steady pattern that is seen in the case of East Asia. In general, it can be said that the capital and basic goods sectors have shown the highest rates of asset formation, while consumer goods have grown at a relatively slower rate until the eighties.

Table 4.9 reveals the nature of concentration, especially since 1970. As it indicates, the top twenty business houses have recorded asset growth rates that far exceed the averages for the corporate economy. For the largest business houses, the growth rate of assets also continued at an alarming rate between 1980 and 1990 (see Table 4A.6).

Table 4.9 Assets of Top Twenty Houses, 1971–85

Year	*Assets of 20 monopoly houses (in Rs.billion)*	*Index no (1971=100)*
1971	27.00	100
1972	29.16	108
1973	33.18	123
1974	39.28	146
1975	36.30	172
1976	52.90	196
1977	58.46	217
1978	62.48	231
1979	66.18	245
1980	76.41	283
1981	83.00	307
1982	89.87	333
1983	133.76	495
1984	158.11	585
1985	202.36	749
1996[a]	950.00	3518

Source: M.K. Sharma, *Business Environment in India*, Commonwealth Publishers, New Delhi, 1989, p.202.
a From CMIE, *The Indian Corporate Sector*, April 1996, p117.

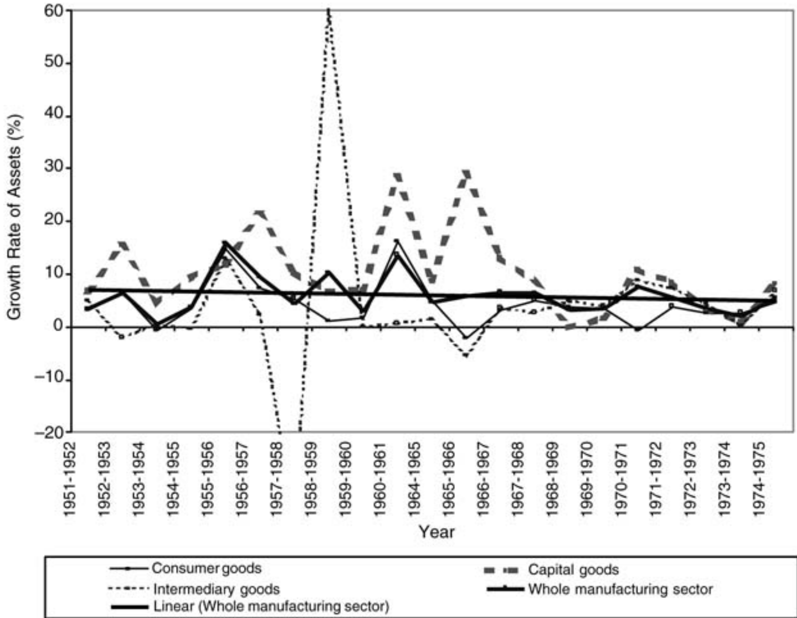


Figure 4.2 Growth Rates of Assets of Indian Public Limited Companies: 1951–75
Source: *Reserve Bank of India Bulletin*, various years.

The second and perhaps more critical aspect of the growth of corporate capital under the interventionist model concerns the growth in profitability. As is well known, a very common idea in this regard is that levels of profitability in India have been low. Profitability is considered low in two senses: first, in comparison with international standards, and second, in comparison to the levels that could have been achieved in the absence of state intervention.

In the following table I present aggregate data on profitability, and a more disaggregated sector-wise data is presented in the Appendix to this chapter (Figure 4A.4).

As the tables show, there is certainly no *prima facie* evidence of a chronic crisis of profitability. However, the important analytical issue is to assess the counterfactual claim that *profits would have been higher in the absence of state intervention*. Even though it is impossible to provide conclusive proof of such a counterfactual, some insights are possible. First, the one obvious benchmark would be to compare it with countries where the state has been less interventionist, i.e. in the classical

Table 4.10 Return on Capital Employed for Large and Medium Public Companies, 1960–94

Year	*Return on capital employed (gross profits after depreciation as % of capital employed)*
1960–61	10.0
1965–66	13.5
1969–70	13.0
1979–80	19.6
1984–85	14.5
1988–89	15.1
1989–90	16.4

Source: (a) For years 1960–70, *Profitability Ratios, Selected Medium and Large Public Companies, 1960–61 to 1970–71*, Reserve Bank of India, Financial Statistics of Joint-Stock Cos. in India, 1975, statements no. S137 and S321, (b) 1979–90, ICICI, *Performance of Assisted Companies*, relevant years.

Table 4.11 Rate of Return on Total Capital Employed in Manufacturing: Some International Comparisons

Year	*Finland*		*Germany*		*Sweden*	*U.K.*	*Japan*		*Canada*		*U.S.*	
	BT[a]	AT[b]	BT	AT	BT	BT	BT	AT	BT	AT	BT	AT
1961	13.1	10.6	9.8	3.9		10.1			6.6	3.2	8.4	4.5
1962	10.4	8.0	9.4	3.7		8.3			7.3	3.7	9.6	5.6
1963	10.6	8.5	9.7	4.2		8.7			8.3	4.7	10.3	6.2
1964	10.0	8.1	10.2	4.0		11.6			8.5	4.9	11.2	6.9
1965	8.6	6.8	8.8	3.9		10.8			10.8	6.2	11.4	7.8
1970	12.2	11.1	6.1	3.2	3.1	6.6	6.2	4.5	6.8	3.4	7.7	4.7
1975	6.4	5.6	4.1	1.1	3.8	–0.3	2.2	1.0	8.3	4.0	7.4	4.8
1980	8.8	8.0	3.5	0.3			3.3	1.1			6.5	4.1
Avg 1961–81	9.1	7.8	6.8	2.5	4.3	6.8	4.2	2.5	9.0	4.9	9.0	5.6

Notes: [a] before tax; [b] after tax
Source: Adapted from Daniel M. Holland (ed.), *Measuring Profitability and Capital Costs: An International Study*, 11–12.

Anglo-American economies like the US, the UK and Canada. As Table 4.11 shows, Indian profit rates compare quite favourably with rates in these economies.

A second meaningful comparison would be with states which have been relatively more interventionist; here again, it may be useful to distinguish between interventionist models of developed countries in

the West, and between those of the less developed nations, the classic case being that of East Asia. I have already presented data on Japan in Table 4.11 above. Table 4.12 gives an indication of the profitability of Korean industry for the period 1969–84. Again, Indian profit rates seem to compare favourably with the Korean ones, even though overall industrial or general macro-economic growth rates in India were significantly lower. What is also extremely critical to note is that the relatively lower rates of profitability in East Asia do not derive out of lack of productive efficiency, but out of a deliberate strategy (see discussion in Chapter 2).[19] As analysts have pointed out repeatedly in the case of Japan and South Korea, output maximisation rather than profitability has been the predominant corporate objective in these economies.

While the above does indicate that Indian corporates may not have experienced a chronic crisis of profitability, it is certainly necessary to note certain contradictory aspects of state intervention that may have indeed inhibited the growth of profitability. On the one hand, high profits were taxed away through tax and surcharges. On the other hand, lapses in management's ability to ensure and augment profitability went systematically unpunished. Rather, the rehabilitation of loss-making or 'sick' industries emerged as one of the crucial elements of intervention.[21] In view of the fact that the closure of firms may increase unemployment, the state adopted a policy which gave loss-making firms a grace period of seven years within which they were to become viable. During this period, 'sick' firms were given generous financial assistance, tax concessions and debt write-offs in order to facilitate the process. This policy of *rehabilitating* inefficient managements – in a regime where there were no market-based mechanisms for seizing corporate control – led inevitably to mounting losses. This occurred not only because inefficiency went unpunished, but also

Table 4.12 Profitability of Korean Industry: 1969–84

	1969–75	*1976–79*	*1981–84*
Total Manufacturing Avg	4.07	4.38	1.94
Large Manufacturing Avg	3.99	4.24	1.67
Small Manufacturing Avg	6.18	5.17	3.49
Export Industries Avg	4.99	2.00	2.43
Domestic Industries Avg	5.46	5.58	1.62

Source: World Bank, *South Korea: Managing the Industrial Transition*, Vol. II, p. 120, Table 5.11.[20]

because the policy of rehabilitation became a much-abused tool through which public funds were continuously appropriated by corrupt managements of privately owned companies.

The question as to whether the absence of state intervention had impeded profitability therefore must be examined in the light of *both* these aspects of intervention: the punishment of efficient managers in the form of taxation as well as condoning inefficient managements through specific policies. Such a view should reveal the problems with the standard arguments connecting profitability and state intervention. While it is undoubtedly true that many different types of inefficiencies exist in the Indian corporate economy, and that their removal could raise profit rates, there is no clear evidence that profitability of Indian firms have been low. A far more serious problem, both at the analytical and practical level, is to explain why aggregate growth rates continue to be low despite relatively high profit rates.

The corporate economy and the question of development

To take up this thorny question, let us briefly recall the criteria for economic growth and industrial transformation set out in Chapter 2. This involved at least three things:

- a sustained increase in assets, incomes and skills of workers;
- the emergence of a process where the semi-feudal conditions and relationships under which labour is initially employed are replaced by contractual arrangements regulated either by the state or the market or a combination of the two;
- the gradual democratisation of the realm of production

At least three conditions need to be satisfied if the above is to occur. First, it needs to be ensured that profits cannot be generated without innovation and/or the continuous expansion of productive capacity. Second, the expansion of productive capacity will have to be based upon a judicious balance between capital and labour intensity. Third, in order that the expansion of productive capacity becomes viable, there will have to be a corresponding expansion of aggregate demand. This will have to occur through redistributive processes emanating from both the market and the state (by the market through increases in wages and corporate asset ownership, and by the state through taxation).

While it is beyond the scope of this work to provide a full-fledged discussion of the issues, we can certainly examine some basic indicators

that are pertinent to our general framework. The most difficult issue is to evaluate the progress of democratisation of the realm of production. While labour in India had consolidated certain early gains in terms of their political rights, the exercise of those rights have not led to sustained increases in democratisation of the workplace. In fact, the exercise of those political rights (in terms of growing unionisation, strikes, labour disputes etc.) have often resulted in a backlash on workers by initiating lock-outs and closures which in effect have directly violated the norms of worker protection as stipulated by the constitution.[22] Several serious contradictions in labour policy and labour law in India need to be highlighted when assessing the issue of industrial democracy.

First, public policy and labour law in independent India has functioned in a way that legal adjudication under a strongly interventionist state has taken precedence over collective bargaining by trade unions. While this strategy of mediation may have – at least arguably – protected labour in an adverse condition of huge unemployment and low skills, it has undermined the potency of organised political activity. As we shall see below, these legal-institutional measures have been successful in displacing legitimate economic demands to the political realm, leading in turn to a vicious circle:

> this is a circular process: the government provides certain laws but when they are not implemented by the employers, the unions are left only with the option of demanding more laws to aid the implementation of previous ones. This makes the unions forget who they are fighting for and what they are fighting against.
>
> (Chatterjee, 1980:194)

Second, none of the governments of the interventionist era have involved workers in the process of decision-making in any serious way (Chatterjee, 1980:195–6). Third, Indian labour law, by granting equal rights to all unions irrespective of size and representation, has made possible intense proliferation of trade unions; this in turn, has encouraged factionalisation amongst workers and intense inter-union rivalry:

> the growth in the number of trade unions in India has mostly been a story of divisions and subdivisions of the same group of workers among competing unions and union centres. The government has responded typically. Labour departments in the states as well as the

centre have increased in size. Promises have been made . . . to accept the trade unions as an essential part of the apparatus of industrial and economic administration. . . . But patently the government has refused to listen to the demands of an interest-sector which is so hydra-headed . . . instead of being in a suspended animation until the unions come to some agreement about necessary policy, the government has decided to define what the real interests of the workers are and should be in a developing 'socialist' society. In a society dominated by elites, and in which the proportion of industrial workers to the total population in insignificant, the government did not have any problem in convincing the general public of the 'sectional' and 'parochial' nature of the demands made by a multiple number of mutually conflicting unions in the name of labour.

(Chatterjee, 1980:216)

In light of the arguments above, it is hardly surprising that labour politics in India has had no sustained impact on labour incomes. As Table 4.12 shows, the share of wages in value-added in manufacturing has declined quite significantly since the fifties. As I shall argue in the next chapter, this is a trend that continues and intensifies well into

Table 4.13 Wages and Salaries as Relative Proportions of Value-added in Manufacturing

Year	*Wages as per cent of value-added in manufacturing*	*Salaries as per cent of value-added in manufacturing*
1949	53.3	10.6
1952	51.6	10.7
1955	41.8	10.6
1958	39.8	11.6
1960	39.6	11.4
1961	39.2	10.6
1962	39.6	11.9
1963	37.6	11.9
1964	36.5	13.7
1965	36.6	15.0
1966	36.5	15.9
1970	35.0	n.a
1975	33.0	n.a
1980	34.0	n.a

Source: Chatterjee, R. *Union, Politics and the State: A Study of Indian Labour Politics* (New Delhi, South Asian Publishers, 1980), p.104; *Indian Labour Statistics*, various years.

the nineties.[23] Accompanying this is a steady increase in the casualisation of the workforce, and a declining role of the private corporate sector in employment generation (see also Appendix to this chapter, Table 4A.5). [24]

This apparent contradiction, (i.e., the co-existence of a relatively elaborate set of labour rights and the continued marginalisation of the majority of the working class) has emerged as the enduring characteristic of the Indian reality. Analysts have attempted to explain this in one of two ways. Most from the right have explained this as a direct effect of over-protective labour laws which have inhibited gains in labour productivity, increased costs of production and thereby stymied the growth of employment (Agrawal, 1997). From the left, the explanation has focused on the inadequacy of legal/institutional measures in the face of increasing structural power of capital.

Perhaps an alternative argument in line with the framework developed here can be offered. The reason that labour continues to be marginalised must be sought in the profit strategies employed by corporations. As we saw above, these strategies were primarily capital-intensive, monopolistic, heavily contingent upon a whole complex of institutional arrangements and – most importantly – not dependent upon the necessity to maximise output and exploit productive capacity to the full. This is especially true of large corporations (which control the lion's share of productive capital), and is reflected in the non-positive relationship between capacity utilisation and profitability (see Table 4.A7).[25] Such a non-positive relationship, in turn, implied that there was neither the necessity to create employment nor to invest in training and skill-enhancement, thus pre-empting any structural forces that might contribute to a systematic tightening of the labour market. In other words, relative to the effective demand for labour, there always remained an excess supply; and relative to level/type of skills that were in demand, labour always remained 'unemployable', justifying thereby the adoption of capital-intensive strategies.

The above, in my view, constitutes a critical contrast between East Asia and most developing countries – and explains to a large extent why, despite their authoritarian and repressive politics, the East Asian states did not entirely succeed in their efforts to prevent the empowerment of workers.[26] Unfortunately, the focus on flexible employment as the primary strategy for East Asian firms has managed to divert attention from the critical importance of labour (and 'learning') in the overall productive strategy of these economies.

Summary and conclusions

In the last two chapters, I have attempted to sketch the complexities and contradictions of India's corporate economy during the interventionist period. As explained earlier, I have focused primarily on the largest faction of corporate capital. The major conclusions that emerge from the discussion are as follows.

The development of Indian capital and its participation in the nationalist struggle vested Indian capital with a high degree of structural power. Its structural power has been manifest in its ability to shape, to a large extent, the fundamentals of the development strategy that was adopted when India became independent. The initial institutional structure from which the corporate form evolved in India was the managing agency system. This system was characterised by the dominance of a few agencies, a large number of interlocking directorships, and the ability of the agents to control a large number of companies with very little financial stake. Together, these traits led to an increasing degree of monopolisation. Not surprisingly, these traits continued to characterise Indian capitalism in the interventionist era. The conglomerate or the business house, which arose out of the managing agency system, has constituted the predominant form of corporate governance during this period. Effective control of the conglomerate continues to be vested in the hands of the members of the founding family.

It was also observed that, typically, the promoters of a company do not directly hold a controlling interest in it. Along with its promoters, a typical Indian firm was owned by institutional investors, the public, and to a lesser extent foreign shareholders. The public, comprising of individual non-institutional investors held too little stake to be able to exert any influence on the company. By contrast, institutional investors held a large amount of equity in Indian companies and by virtue of their holdings have become very important players in the corporate economy. However, it was not clear whether these institutional investors had adequately served the interest of the millions of Indians whose savings they had mobilised. There are in fact, strong indications to the contrary. It was apparent, as far back in 1969 that the public financial institutions 'have denied themselves a part of the possible capital appreciation and also prevented the state from playing an increasingly active role in the industrial economy'.[27] There is also a fair bit of controversy over their involvement in situations of takeovers and acquisitions. Not surprisingly, perhaps, these institutions proved inadequate in discriminating

between material interests of the Indian public and the various political interests that surfaced during those takeover wars.

Next, I explored one of the most popular perceptions about Indian companies (and about companies in the developing world in general) – that they have suffered from a chronic problem of growth and profitability. My conclusions in this respect were that no *prima facie* evidence was available to demonstrate a chronic crisis. In relation to profits, I also considered the question as to whether Indian firms *could have* experienced higher profitability in the absence of state intervention. In this regard, my finding was that given the rather contradictory nature of state intervention in India, it is impossible to conclusively accept or reject this counterfactual claim.

A far more important analytical point constitutes the general relationship between high profitability and low macro-economic growth rates that has persisted throughout the two historical periods I examined. Twice during this period, India was confronted with a serious crisis of economic growth, once in the mid-sixties and once again in the beginning of the eighties. It is strongly believed in some quarters that these crises, and the persisting malaise of the Indian industrial economy, were caused by the *absence* of corporate profitability and corporate growth, rather than the reverse. As is well known, the popularity of this belief amongst the political elite led to the dismantling of the interventionist model in favour of a more liberalised, Anglo-American one. The latter model focuses exclusively on strategies to promote corporate growth and profitability, and is premised on the assumption that the processes through which corporate profitability is bolstered would automatically generate general prosperity.

What I wish to suggest is that such an exclusive emphasis on profitability is misplaced and is based on a rather partial reading of the impact of state intervention on the corporate economy. Such a partial reading, I hope to show in the next chapter, has resulted in a set of policies that is likely to result in the deepening of the contradictions of the interventionist model.

Finally, I examined, albeit somewhat indirectly, the issue of political power of capital. I began by observing that the primary source of capital's political power in India was its involvement in the nationalist struggle. As a result of this involvement, capital was able to exert substantial influence on the development strategy that India adopted. Since Independence, business has continued to exert similar influence on policy. This is not to say, as the classical Marxist view would suggest, that the state has been a passive tool in the hands of capital; and neither

is it correct to suggest, as the neo-liberals do, that capital is held captive in the hands of rent-seeking bureaucrats. Some authors have also argued that while the state might have had the intention of containing the political power of capital, it has been *constrained* by the demands of the *ruling coalition* (Bardhan, 1984). While this is a more nuanced argument, it does not seem to offer a theoretical explanation as to *why* the state might intend to contain capital's political power. The assumption seems to be that the state has an ideological stand against capital, but is politically constrained in its efforts to act on its ideological stand. The contradictions of state policy, some of which I have noted above, do not go very far in sustaining this argument.

As I hope to show in the next chapter, some of these theorisations of the Indian state need to be seriously revisited in light of the political and economic developments since the onset of liberalisation.

Statistical Appendix

Table 4A.1 Market Share of Top Four Firms in Selected Indian Industries

Industry	*1973–74*	*1985–86*	*1990–91*
Tea	36.6	45.2	30.5
Man-made fibre	100.0	100.0	100.0
Industrial chemicals	92.0	97.0	99.0
Automotive components	55.7	54.1	61.1
Metals	94.3	94.3	94.0
Electrical machinery	84.0	82.0	89.1
Transport equipment	95.0	95.0	97.1
LCVs	80.8	78.4	80.1
Jeeps	100.0	100.0	100.0
Malted foods	98.7	98.0	98.0
Soaps	85.0	94.0	n.a
Industrial yarn	100.0	84.2	n.a

Source: CMIE, *Markets and Market Shares*, 1992–93.

Table 4A.2 Relative Share of Cases Referred to the MRTP Commission by the Department of Company Affairs (DCA)

Year	*Total no. of proposals received by the DCA*	*Of which no. of proposals referred to the MRTP Commission*
1979	1639	3
1980	184	6
1981	250	6
1982	274	8
1983	284	7
1984	347	4
1985	325	Nil
1986	392	Nil
1987	Na	Nil
1988	352	Nil

Source: *MRTP Commission Annual Reports*, various issues.

Table 4A.3 Import Availability Ratios by Industry Groups

Value of Imports as per cent of total availability

Industry Groups	*1959–60*	*1965–66*	*1979–80*
Food	4.2	2.9	8.1
Beverages	15.8	7.5	0.7
Tobacco	1.5	0.9	0.0
Textiles	2.9	1.3	1.9
Wood products	22.1	4.5	2.9
Furniture	0.9	0.4	0.2
Paper	23.4	17.1	18.2
Leather & Fur	5.4	4.6	0.1
Rubber products	11.5	3.5	8.1
Chemical & prodts	30.2	17.2	19.5
Petroleum prodts	43.9	27.8	42.3
Non-metallic minerals	6.5	2.2	22.7
Basic metals	32.3	22.2	22.7
Non-electrical mach.	65.8	56.3	30.6
Electrical machinery	38.1	27.2	9.9
Transport equipment	25.7	15.8	11.1
Miscellaneous	18.8	15.6	16.7

Source: Based on Ahluwalia (1985:119).

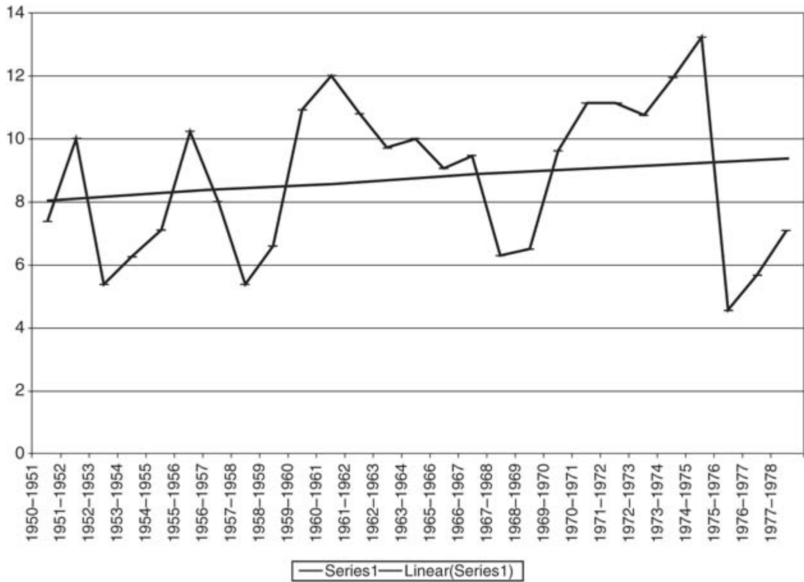


Figure 4A.1 Profits After Tax as Percentage of Net Worth: 1950–51 to 1977–78 Medium and Large Public Limited Companies
Source: Based on data from L. Arun Rede, *Structure of Profit Rates in Indian Manufacturing Industries*, Baroda: Rachana Book Emporium, 1984, pp.42–5.

Table 4A.4 Growth Rate and Employment Generation by the Private Sector

Period	*Percentage increase in paid-up capital of private sector companies*	*Percentage increase in employment generation*
1971 to 1981	57	9.8
1981 to 1991	404	6.1

Source: James, P. J. *Nehru to Rao*, Kerala: Massline Publications, 1995, p. 120.

Table 4A.5 Growth Rates of Assets of the Largest Indian Business Houses, 1980–90

Business House	*Assets in 1980 (Rs.millions)*	*Assets in 1990 (Rs.millions)*	*Average Annual Growth Rate (%)*
MA Chidambaram	438.10	12735.50	280.69
Reliance	1663.30	36002.70	206.45
United Breweries	969.00	11892.40	112.72
Larsen & Toubro	2160.30	16815.20	67.83
Bajaj	1792.60	13910.60	67.60
Modi	1988.20	13993.70	60.38
Thapar	3480.60	21771.50	52.55
TVS Iyengar	1886.40	11771.00	52.39
ITC	1562.90	9651.30	51.75
Birla	14319.90	84733.50	49.17
Tata	15390.00	85309.00	45.43
Hindlever	2193.00	12094.60	45.15
JK Singhania	4127.20	21390.00	41.82
Shri Ram	2410.00	9333.30	28.72
ACC	2745.10	9027.20	22.88
Mafatlal	4275.40	13435.50	21.42

Source: CMIE, *The Indian Corporate Sector*, 1996, p. 104

Table 4.A6 Capacity Utilisation and Profitability: Some Illustrative Data from ICICI-assisted Companies

Industry Group	*Capacity Utilization (per cent)*		*Gross Profits as % of Sales*	
	1989–90	1990–91	1989–90	1990–91
Automobiles & ancillaries	85.6	91.9	9.7	9.3
Cement	88.9	89.8	5.7	16.3
Chemicals & petrochemicals	112.9	115.3	10.9	10.2
Electrical equipment	64.4	73.4	10.3	11.2
Food prodts (excl. sugar)	53.7	48.3	7.9	7.6
Glass & pottery	85.0	87.7	11.2	12.2
Machinery manufacture	109.4	116.6	13.7	12.1
Metal products (ferrous)	109.0	108.8	17.0	15.8
Metal products (non-ferrous)	84.0	84.1	11.9	11.9
Pulp, paper, paper products	99.8	97.4	13.2	14.3
Rubber products	79.9	85.0	9.8	10.0
Sugar	43.5	54.0	11.3	14.7
Diversified	98.1	85.8	11.2	12.8
miscellaneous	42.4	43.5	15.5	15.7

Note: As mentioned in the text, the Industrial Credit & Investment Corporation of India (ICICI), is one of the major public financial institutions which finances large corporations in the private sector, usually with a minimum paid-up capital of Rs.50 million.
Source: ICICI *Annual Report*, 1992, p. 21 Table 25.

5
Corporate Capitalism in Post-Interventionist India: Paradoxes and More

In the previous chapters, I have attempted to delineate the contradictions of the Indian corporate economy as it existed until the eighties. The primary contradiction, I argued, was manifest in the fact that, despite considerable growth and expansion of the corporate economy, and fairly high levels of profitability, the effects of this growth were hardly evident on the rest of the economy. It is this contradiction that I take as the starting point for my discussion of the post-interventionist model. The thrust of my arguments can be summarised as follows.

While the post-interventionist model encompasses several fairly far-reaching institutional changes, the model is potentially highly capable of deepening the existing hiatus between the corporate sector and the rest of the economy. The potential is rooted in the particular assumption on which the post-interventionist model is premised, i.e., the key to unleashing the growth dynamics in India lies in increasing levels of corporate profitability. As in the interventionist era, there is little focus on the *content* of corporate profits, the various strategies that firms are likely to employ in order to realise increased profits. Will these profit strategies be based on increased innovation or, as in the previous era, on price and output manoeuvres? Will they increase employment and incomes? Will they involve patterns of corporate financing that free up scarce state resources for deployment elsewhere?

Obviously, none of these questions can be answered only at the level of theory. In fact, the theoretical answers that are available – from either the neo-classical or the institutionalist perspective – both seem somewhat simplistic in light of the complex realities of the post-

interventionist Indian economy. The institutionalist assumption – that a certain market logic can be set in motion by simply establishing an ensemble of legal/institutional mechanisms – is fraught with great contradictions. Most fundamentally, by leaving unproblematised the nature of the nature of the state, and the complex of motivations behind its attempts at institutional change, institutionalists provide us with few analytical categories with which to understand the specificities of the reforms as they unfold in each different context.

The fallacy of the neo-classical assumption is also equally apparent. As Kahler (1990) points out, the implementation of neo-liberalism requires a strong state that can 'manage' resistance not only from the 'popular sectors' but also from business. This 'orthodox paradox', as Kahler predicted, is becoming increasingly apparent in countries like India. At another level, the neo-classical assertions about the ability of the Anglo-American model to generate sustained economic growth seems largely contradicted by the experience of liberalisation in the Third World. As I will show below, this observation also holds true for the post-interventionist model in India. While corporate profitability has indeed increased in the post-interventionist period, it has not followed the trajectory predicted by neo-liberal theory. Paradoxically, this spurt in corporate profitability has occurred simultaneously with several recessions, unfolding in the midst of apparently strong macro-economic indicators.[1] Arguably, these cyclical fluctuations are endemic to market processes. However, even after allowing for cyclical fluctuations, what emerges as a critical structural characteristic of the post-interventionist era is a positive association between corporate growth and increased state support.[2]

This continuity with the interventionist era is rather striking. Indeed, it is manifest in the way public resources continue to be deployed in an otherwise 'liberalised' regime: through state-led demand management programs, through increased disbursement from financial institutions, through increased state spending on infrastructure, through sacrifices in the state's revenue incomes as a result of tax concessions etc.[3] The distributional (and political) implications of this are obviously complex and far-reaching. But leaving that aside for a moment, let us focus attention on how such a continuing relationship between corporate growth and state support disrupts the logic of the post-interventionist model. The premise of this model is that, by reducing direct economic participation of the state, the distortions of the incentive mechanisms that occurred under the interventionist regime can be corrected. Such a corrected, 'marketised' incentive mechanism will then generate growth.

As I will show below, the incentive mechanisms produced by the reforms do not reflect any substantial increase in the degree of marketisation; there is no clear evidence of increased competitive pressures on firms; further, there is no evidence at all that state involvement now is any less unidirectional than in the previous regime. In fact, the reverse may be true.

I will attempt to develop these arguments in four sections. As in the previous chapters, I begin by discussing the political-economic conditions under which the post-interventionist model emerged. Next, I examine in considerable detail the actual structural changes that have been implemented so far. I will examine changes at two levels: at the macro-level changes that will affect the external environment of firms; at the micro-level, changes that are likely to affect the internal structure of firms, i.e., structures of *corporate governance*. In the third section, I attempt an assessment of the impact of these changes – again at two levels – on the corporate economy as well as on the macro-economy. In the final section, I present my conclusions.

The emergence of the post-interventionist model

As indicated above, the emergence of the post-interventionist model is located in the contradictions of the previous regime. Primary amongst these contradictions was the dependence of industrial growth on government action:

> All growth of modern industry in India since the early twenties has been brought about under a protective regime. In planned industrialisation, protection is continued in a variety of ways, and the plan is articulated through selecting particular capitalists for particular fields and enabling them to acquire highly scarce resources of every type. Whatever the financial skill of the capitalist his success and progress are mainly created by state policy and maintained at public cost. Even so no attempt is made by the government to acquire control, to introduce an element of public ownership, or even to do anything to facilitate such a process in the future. Accumulation of gains and the rapid increase of economic resources and power in particular private hands can thus be described as a deliberate objective of state policy. . . . *Almost all government operation is based on the offer of incentives to private capital.*
>
> (Gadgil, 1972:304; my emphasis)

However, the continuous erosion of state finances that emerged as a direct consequence of this process became one of the primary reasons for a change in strategy. This coincided, unfortunately one would think, with the demands of globalisation from the North. As a number of theorists have argued, one major causal factor behind globalisation was a crisis in profitability, which urged firms to seek out larger markets in the South (Lipietz, 1984).[4] Obviously, countries like India emerged as prime candidates for this purpose, made more attractive by their own internal crises and vulnerability.

While catering to the demands of globalisation and economic liberalisation provided for the state an easy solution to its crisis, the willingness of Indian capital to do the same was much more contingent on what it could get in exchange for its cooperation. As such, the changes in economic policy had to be initiated in a manner that the immediate interests of the business community were not hurt. Most importantly, while market forces were to be unleashed, they were to be unleashed in conjunction with state support.

A *New Economic Policy* reflecting this careful balancing between state withdrawal and state support was developed first by Indira Gandhi in the early eighties, and carried further by Rajiv Gandhi who succeeded her as prime minister. Not surprisingly, it began with an extensive dose of demand management through state intervention rather than a withdrawal of the state. Tax concessions to higher income groups and to corporations were one of the primary instruments of demand management. Substantial increases in salaries in the government and government-related sectors (such as higher education) and an unprecedented expansion of employment in the public sector were other measures. Together, these generated a vast domestic market of 75–85 million people which, even though confined to the top 10 per cent of the population, was enough to attract the interest of domestic and foreign investors (Kurien, 1994:100).

As a result of these measures, industrial growth did revive, led by a phenomenal growth in consumer durables ranging from 8 to 22 per cent per annum during the period. Other sectors of industry also grew, particularly the capital goods sector, which had been the worst affected by the decline. An overall industrial growth of 8 per cent and an overall rate of growth of 5 per cent were recorded in this period, which was well over the trend growth rate of less than 4 per cent since the beginning of planned development.[5]

This 'new growth path' of the Indian economy was obviously laden with contradictions. For one, this was achieved through a

very significant increase in public expenditure.[6] Second, public expenditure was coupled with massive tax reductions so that the net result was a more-than-proportionate increase in public borrowing.[7] Third, there was a tremendous growth in import surplus, which eventually necessitated private commercial borrowing in addition to the borrowings from the IMF. The average interest rate on India's official debt increased from 2.4 per cent in 1980 to 6.1 per cent in 1982. In addition, the average maturity of loans declined from 40.8 years in 1980 to 24.4 years in 1989. However, external borrowings continued, increasing to about 21.5 per cent of the GDP ($56.3 billion) in 1989. Outstanding debts to private creditors increased ten-fold between 1982 to 1990 (to $22.8 billion in 1989), and debt service as a percentage of GNP increased from 9.1 per cent to 26.3 per cent over the same period. Fourth, the growth in employment fell to an all-time low during this period. In the private sector, where much of this new growth was located, employment declined in absolute terms; employment growth rate in agriculture fell to half of its previous levels (Kurien, 1994:98).

Thus the 'new growth path' of the Indian economy, comprising a combination of jobless growth and a huge debt, led quite directly to the crisis of 1991.[8] Bimal Jalan, who was then the Chairman of the Economic Advisory Council, identified the financial profligacy of the earlier regime and severe political instability as the primary cause behind this crisis (Jalan, 1992:1). In addition, the crisis of debt servicing and the falling maturity period of loans initiated a capital flight since 1989.[9] Foreign exchange reserves dropped to an all-time low and inflation crossed double-digits for the first time, resulting in a substantial reduction in India's credit rating (Jalan, 1992:3–4). It is important to note that the debt or the fiscal spending *per se* was not the cause of the crisis; rather, it arose from the particular ways in which these borrowed resources were deployed – in unproductive political management efforts rather productive investment that could over time, generate resources to retire the debt (Bhaduri and Nayyar, 1996).

It is in this context that Prime Minister Narsimha Rao and Dr Manmohan Singh as his Finance Minister turned to the IMF in 1991. As is well known, the conditionalities of the IMF loan required a serious structural adjustment of the Indian economy, of which economic liberalisation comprised an integral part. However, as already alluded to above, even the post-1991 programme failed much in the same way to accomplish what it allegedly set out to do: uncouple the state and the private sector in such a way that growth could be generated primarily by

the latter. There continues to exist political constraints on the ability of the state to withdraw financial support for private corporate growth. As I will argue below, state support, in particular in the form of project finance, infrastructural support and foregone tax revenues, remains crucial to corporate growth. Finally, there also appears to be serious constraints on the implementation of the micro-institutional/corporate governance changes sought by the programme. These changes, encapsulated in the *Companies Amendment Act* (1999) and the various legislative measures associated with it are supposed to affect corporate governance in a manner that bolsters the logic of the competitive market in the long run. Interestingly, however, there are several problematic aspects of the Companies Act which, when unreflectively transplanted from their Anglo-American context, are likely to act *against* the logic of competition rather than for it.

The post-interventionist model: an attempt at structural change?

Table 5.1 below summarises the main changes that have been implemented since 1991. Intense and prolonged debates have marked some of these changes, many of which are still not resolved. In what follows, let us analyse these changes in light of the broad issues I have raised above. I will first discuss the major macro-economic changes, discussing at some length the issue of capital market liberalisation. Next, I will discuss the micro-level issues, i.e., the changes in corporate governance that are sought in the new model.

Table 5.1 Changes Sought in the Post-interventionist Model

Changes in corporate governance, structure and ownership	*Changes in the macro economy*
• Free pricing of shares • Buyback of shares • Foreign ownership of corporate equities • Reduction of capital controls • Relaxation of controls on inter-corporate investments • Relaxation on limits to expansion and diversification of corporations	• Deregulation of the capital market • Deregulation of the banking sector • Deregulation of trade policy • Convertibility of the current and the capital account • Repeal of the Foreign Exchange Regulation Act (FERA) • Liberalisation of foreign investment and technology regimes

The macro-economic context

The capital market

The first major macro-economic change constitutes the liberalisation of the capital market. The theoretical (and normative) underpinnings for this are derived from the *financial repression* theses put forward by McKinnon (1973) and Shaw (1973), and some subsequent work undertaken by economists at the World Bank (Bond and Smith, 1996; Demirguc-Kunt and Levine, 1996a, 1996b; Demirguc-Kunt and Maksimovic, 1996 and Levine and Zervos, 1996a, 1996b). Their main arguments are (1) that equity finance is free from adverse selection and moral hazard effects, so that an investors can actually realise the returns they expect at the time they make the investment[10]; and (2) relative to financial intermediaries like banks, a capital market is better able to minimise transactions costs. These arguments, in particular the latter, have had great influence on reformers in developing countries like India (Gokarn, 1996; Sen and Vaidya, 1997), and is reflected in the reform programme quite directly. In what follows, let us examine the applicability of these arguments in the Indian context.

Until 1992 the price of share issues by Indian companies was fixed by the Controller of Capital Issues (CCI), a government agency, and was guided by the Capital Issues Control Act (1947). As one of first steps towards liberalisation, the CCI Act was repealed, and pricing of shares was 'set free'. As predicted by neo-classical theories of finance, the extent of public shareholding increased significantly with almost immediate effect, constituting what came to be known as the stock market boom. Market capitalisation of large Indian corporations responded accordingly. Capital issues by non-government public limited companies increased from Rs.65 billion in 1989–90 to Rs.200 billion in 1992–93.[11] While capital and premiums on the issuance of fresh capital accounted for only 10 per cent of the total resources raised until 1991–92, in 1993–94 and 1994–95, these accounted for 30 per cent of the total.[12]

Second, also as predicted by neo-classical theory, as soon as share prices were deregulated some new financial instruments began to operate in the Indian markets. Foremost amongst these was the instrument of preferential *allotment* (*preferential allotments* involve the offer of shares to the promoters of a company at prices substantially below the market price). As one author observes,

> Scores of promoters, both Indian and foreign have offered to themselves large blocks of shares at hefty discounts and enriched

themselves at the cost of the general public . . . over 30 large companies in which foreign promoters have stakes and almost double that number of companies with Indian promoters have issued shares on preferential basis to the promoters at heavy discounts. On a rough reckoning, the aggregate notional gain to these promoters is a staggering sum of about Rs.31 billion (approximately equal to $10 billion at the 1994 exchange rate).[13]

Note, in particular, that:

- Shares were offered to promoters at about 50 per cent less than the prevailing market prices.
- In several cases, particularly companies with foreign shareholdings, the preferential shares were allotted only with the intention of augmenting the promoters' stake and had absolutely no long-term plan for investing the amount raised.
- Indian company law did require, at the time, that shares could be preferentially allotted only after the allotment had been ratified at a shareholders' meeting. The inadequacy of this requirement under Indian conditions was clearly brought out in this process, although not much could be done.

Similar problems with deregulation was also reflected with respect to another financial instrument, namely *private placements*. Used fairly regularly in the Anglo-American markets, this instrument for project financing involves a *private sale* of debt or equity by a company, rather than a *public offering* through the capital market. From a firm's perspective,

Table 5.2 Private Placements in India

Year	*Amount raised through private placements (in rupees billion)*
1990–91	42.44
1991–92	44.63
1992–93	16.34
1993–94	74.65
1994–95	111.74
1995–96	133.61
1996–97	150.66
1997–98	300.60
1998–99	496.64

Source: *Reserve Bank of India Annual Reports*, various issues.

private placement is a cost and time-effective method, especially because it does not require detailed compliance with existing securities laws. Table 5.2 gives an indication of how this instrument became a dominant player in the Indian capital market.

This route to project financing has gained steadily in popularity as investor confidence plummeted, making it difficult for promoters to finance projects through public offers. In May 1997, a record of over Rs.30 billion was raised from the capital markets through privately placed debt issues, while public issues almost completely disappeared from the market (with the number of public issues dropping to ten during the same month).[14] During 1998–99, banks, financial institutions and public and private sector companies mobilised almost Rs.500 billion through this route (84.1 per cent of total resource mobilisation from the primary market), which was exceeded the previous year's record by 65 per cent. As indicated by the example below, this fairly common instrument of the Anglo-American economices has played havoc in the Indian market in the past, and remains vested with the potential to do the same in the future.[15]

The country's largest private placement deal was struck between Reliance Industries Limited and three of the major publicly owned financial institutions: The Unit Trust of India (UTI), Life Insurance Corporation of India (LIC) and the General Insurance Corporation (GIC) in November 1994. UTI took the largest chunk of the deal at Rs.7.7 billion, while LIC contributed about Rs.1.67 billion, followed by GIC (Rs.450 million). Reliance Industries had, on 4 November 1994, privately placed shares worth Rs.9.45 billion with the three state-owned institutions at a price substantially higher than the market price with a five-year lock-in period.[16]

It was later admitted by various authorities, including Finance Minister Dr. Manmohan Singh, that this had a been a rather significant misuse of public money. The UTI, LIC and the GIC, one may recall, are the three major institutions which mobilise resources from small investors. Historically, they have enjoyed a very high degree of investor confidence, and their involvement in a deal of this volume did serious damage to that history. However, more recent developments at UTI indicate that the problem may be more fundamental than simply one or two corrupt and unwise deals. Throughout 1997–98, UTI's portfolio underwent substantial erosion of its value by about 33.43 per cent, i.e., by about Rs.40 billion (approximately $1 billion). The primary reason behind this is the substantial shift in its portfolio towards equity to well over 50 per cent, the incomes from which are highly volatile. This

becomes even more problematic when we consider that the public's perception of UTI's mandate is to provide fixed, regular returns to its investors by putting their pooled money primarily into debt instruments. As one observer comments:

> Eager to capitalise on the stockmarket boom of 1994, UTI recklessly increased its equity holdings. Of course, being forced to sell large chunks of debt to meet the redemption pressure caused by corporate withdrawals in 1995–96, following a drying up of liquidity also skewed its portfolio further towards equity. Moreover, successive governments had used the UTI as their instrument for intervention in the stockmarkets to influence share prices. Now, as the quantum of withdrawals threatens to match the quantum of investments, all its past sins are weighing down UTI, leading it down the road to damnation, and taking the markets with it.[17]

The problem is, of course, complex. For our purposes, it is necessary at least to differentiate between two elements of the problem: (1) those that are necessarily short-term and constitute the usual instability associated with deregulation, and (2) those that are longer term, arising out of the structural characteristics of the corporate economy. It is only those of the former type that can be remedied by regulatory measures. The latter need regulation and restructuring of a more complex nature, with the ability to affect corporate behaviour. Our emphasis here is on the latter, and the example of the UTI's marketisation reveals a critical aspect of the problem. But before I address that, let us briefly consider one other major change associated with the development of the capital market, the entry of foreign portfolio investments (FPI) and foreign institutional investors (FII).

In India, one of the major justifications for liberalising the capital market was the projected inflow of foreign capital. Having greater resources (to access information) and more financial clout than the average Indian investor, FIIs did show a significant interest in the Indian market. However, foreign portfolio investment (FPI) into India has been insignificant compared with other countries like Mexico, Korea and Thailand. Even so, Indian businesses and brokers have repeatedly complained that the impact of FIIs have in fact been 'destabilising', in the sense that they have usurped several Indian capital market intermediaries from their position of dominance.[18]

While much of the resistance to FIIs stems from immediate concerns about increased competition, there are serious reasons to worry about

the destabilisation caused by foreign inflows. As the experiences of Mexico, Korea and Thailand have shown, FII funds are primarily short-term, and therefore do add significantly to volatility. The most radical example is Thailand: the swing in the volume of FPI from 1995 (11.8 per cent) to 1997 (−7.9 per cent) corresponded to almost 20 per cent of its GDP. These swings of short-term investment were enough to dry up Thailand's foreign exchange reserves (Nagaishi, 1999). As Nagaishi and other authors warn, if there is further deregulation of the Indian stock market to attract more FPI, there seems to be no way to avoid falling into similar problems as these countries.

The primary problem with FPI is not only that it is oriented towards the short-term and quick profits, but that there is absolutely no control that national governments can have over their direction. This is true even in the case of Foreign Direct Investment (FDI), where most governments have put in place a mechanism for formal screening of proposals submitted by foreign investors. In India, the Foreign Investment Promotion Board (FIPB) has the institutional responsibility to evaluate proposals for foreign investment. In addition to the standard criteria applied to the evaluation of any business plan, the FIPB has the mandate to evaluate whether the proposed projects would be compatible with the development priorities of the country. As such, a significant portion of FDI projects that are approved by the FIPB are in priority sectors. However, there seems to be a puzzling disjuncture between *approvals* of FDI projects, and *actual inflows*. While the approvals are mainly in core sector industries, the actual inflow of FDI has been primarily into non-priority areas like domestic appliances, finance, services, electronics, food and dairy products, etc. (combined inflow into these sectors accounted for about 30 per cent in 1992–93, 44.9 per cent in 1993–94, 47.7 per cent in 1994–95 and 41.2 per cent in 1995–96).[19]

The situation is even worse for portfolio investment, since the very premise on which portfolio funds are attracted is that they are not subject to national control. Thus instability, volatility and perhaps most importantly the threat of takeover is in some ways endemic to portfolio investment. In India, one approach to solving these problems was to allow foreign investment in government debt.[20] The underlying assumption here was that by channelling the bulk of foreign portfolio investment into government-owned instruments would reduce the volatility in the stock markets. While the measure certainly succeeded in increasing the inflow of foreign capital, it has the potential to take the economy even further in the direction of volatility and vulnerability of the kind exemplified by Mexico.[21]

In view of these caveats, it is important to question more fundamentally the efficacy of stockmarkets for developing economies, and develop perhaps a set of criterion under which stockmarkets achieve the results they are expected to. India's experience certainly goes to validate some of the fears associated with liberalising capital markets in an ad-hoc manner.[22] Most importantly, the neo-liberal assertion that these problems emerge out of deficiencies in institutional design or incorrect sequencing of the reforms, and therefore can be corrected through regulatory measures needs to be challenged. Arguably, the problems can be taken as indicators of a chronic aggregate demand constraint. The neo-liberal model does not allow for any systematic solutions to such a demand constraint, indeed it resists even identifying the malaise as such; at best, it allows for ad-hoc artificial stimulants which stall these problems in the short-run, but cause them to resurface through many direct and indirect processes – and often in a greatly aggravated form. The most important effect of these oft-deployed artificial stimulants, one could argue, is the kind of systematic income inequality that is generated by increasing subsidisation of the corporate economy on the one hand, and negotiated wage increases for the top echelons of organised labour on the other (Kaplinsky, 1997; Shanta, 1999). Let us return to these issues in the last section, and for now, complete our discussion of the developments in the capital market.

As we saw above, the initial impact of deregulating share prices was quite devastating, leading eventually to the huge securities scam of 1992. The scam brought to light the immediate need for a regulatory body like the Securities Exchange Commission (SEC) of the US. As a result, the *Securities Exchange Board of India (SEBI)* was born, with the expectation that it will evolve over time into an institution like the SEC. However, SEBI encountered strong resistance from a number of key actors in the capital market, who opposed the exercise of any executive or regulatory power by SEBI. (For instance, the simplest possible regulation, i.e., the requirement that all brokers be registered, led to a strike in the capital markets on 10 April 1992 because the brokers were reluctant to divulge inside information to a statutory body.) Most members of the corporate community expressed a distinct preference for executive power to be vested with the government rather than an autonomous body like SEBI.[23] As a result, not only did SEBI's authority in key areas remain subordinate to the Department of Company Affairs, it also had virtually no executive authority.[24] Efforts to enhance SEBI's power were not only unsuccessful, but resistance to it also resulted in the repeal of several of its early statutes. As it currently stands, SEBI's decisions are

contingent upon and can be overridden by those of the Central Government.[25]

Paradoxically, the resistance to SEBI emerging as a powerful, autonomous body like the Securities Exchange Commission (SEC) in the US came from the private sector rather than the bureaucracy. The reason for this, obviously, lies in the nature of the historical relationship between the state and the private sector in India. Given the constraints imposed by this relationship, it is not surprising that the success of SEBI remains confined to producing the blueprint for a regulatory framework, which SEBI has done by issuing rules and regulations in a variety of key policy areas.[26]

SEBI's most substantive failure lies in its inability to stimulate investor confidence. Ever since the boom of 1992 revealed itself to be an artificial one, the Indian capital market seems to be ridden by a perpetual malaise.[27] Despite the continuous increase in the number of instruments and streamlining of procedures, a serious crisis in the confidence of investors seems difficult to reverse. The most immediate causes of the confidence crisis may have been located in the huge securities scam of 1992; even though fairly stringent measures were taken in its aftermath, including the establishment of SEBI, not much substantive change could be accomplished. For one, the prevalence of unethical practices by the various actors in the capital market remains a serious deterrent. For another, there often seems to be little corroboration between corporate performance, stock prices and dividend payments, rendering it even more difficult for the small investors to assess the viability of those investments.[28] Combined with a tradition where individual shareholders have virtually no say in the allocation of profits, or more generally in the management of the company, this provides a serious deterrent to investor confidence.

Other macro-economic changes

Several other important changes at the macro-level need to be considered, the foremost of which is the deregulation of the banking industry including the development banks. Recall that under the previous regime of development banking, banks were required to make decisions not exclusively on profit calculations, but also according to government directives designed to promote economic development (which required banks to channel funds to certain sectors, buy government securities, maintain high reserve requirements, etc.). Moreover, the banks imposed little discipline on defaulters as they themselves were under little

pressure to do so. The almost inevitable result was an extremely high rate of non-performing assets (NPAs) with much of it arising out of corporate sector defaults.

Recent banking reforms have addressed these problems through a two-fold strategy involving macro-policy reforms and micro-policy reforms. The former set of policies have included reducing cash reserve ratio, simplifying the maze of interest rates and a scaling-down of the directed credit programmes (Sarkar and Agrawal, 1997). Among the latter polices were the introduction of prudential norms to ensure greater transparency, the establishment of debt recovery tribunals, the re-capitalisation of banks and the introduction of Memoranda of Understanding (MOUs) between banks and the RBI to improve management of loan accounts. Banks seem to have responded positively to the reforms so far as is indicated by, among other things, a continuing drop in non-performing assets (from 26 per cent of total advances in March 1994 to 20 per cent in 1995 and further down to 16 per cent by March 1996) and an increase in the number of profitable public sector banks (Velayudham, 1997: 5–7).

However, serious problems of debt recovery continue to plague the banking system, especially with respect to large corporate clients.[29] More importantly, the primary purpose of these reforms, i.e., to signal an end to the soft credit regime and an inducement of greater dependence upon equity financing, remains largely unfulfilled. As numerous studies indicate, the corporate sector's dependence on debt and avoidance of equity remains almost as high as in the previous era.[30] This is also revealed in the high growth rate of sanctions and disbursements of volumes of debt by the development banks.[31]

A second area in which significant change has occurred with liberalisation is competition policy. As noted above, liberalisation brought an effective end to the infamous *licence-permit raj* and the removal of similar restrictions on investment and expansion that were part of the Monopolies and Restrictive Trade Practices Act (MRTPA). The few areas where controls remain involve regulations relating to pollution and other environmental considerations and the continued reservation of some industries for small businesses. Further, there has been a drastic reduction in the number of industries which were hitherto the exclusive domain of public sector enterprises; these have been opened up to private sector participation (and possibly, for some of them, complete privatisation in the future).

A third element of liberalisation has been a near-thorough overhaul of policies relating to foreign investment and foreign firms. At least four components of the policy need to be noted. First, there has occurred a

high degree of relaxation of foreign investment norms, with the government granting automatic permission for foreign ownership of up to 100 per cent in two of the most profitable industries (telecommunications and software). In addition, 74 per cent foreign equity ownership is permitted in 9 categories of industries, 51 per cent in 21 categories of industries and 50 per cent in 3 categories of industries. Second, the Foreign Exchange Regulation Act (FERA) has been repealed, being replaced now by Foreign Exchange Mechanism Act (FEMA). FEMA is accompanied by another important piece of legislation: the Prevention of Money Laundering Bill, and the two together are expected to facilitate the liberalisation of the capital account.[32] Third, there has occurred a very significant restructuring of the foreign trade and exchange rates regime. The complementary restrictions on import of raw materials and capital goods have been virtually abolished. Customs duties have been substantially reduced, with the peak rate falling from more than 200 per cent in 1991 to 65 per cent in 1994.[33] The liberalisation of imports, particularly of consumer goods, had emerged as the main source of conflict between the last Congress government and Indian business, and became one of the main planks of the BJP's economic policy.

Fourth, in 1997, the rupee was made convertible on current account so that the exchange rate is now market-determined subject to intervention by the Reserve Bank to contain excess volatility. In 1997, a committee on capital account convertibility was set up by the Reserve Bank of India (RBI) under the chairmanship of former RBI deputy governor S.S.Tarapore to prepare a road map towards capital account convertibility. The committee recommended a three-year time frame for complete convertibility by 1999–2000, down at the dawn of the twenty-first century many of the recommended steps has already been formalised.[34]

How exactly are these macro-level changes likely to affect corporate growth? Most fundamentally, the changes are intended to reduce the power of the state to impose constraints on corporate activity. However, at the same time they also threaten to expose Indian firms to unprecedented levels of market discipline and international competition. Indeed, Indian firms have been rather schizophrenic in their response to the reforms, contradicting quite directly the liberal argument that the exposure to increased competition and monitoring should have a salutary effect on Indian firms (Khanna and Palepu, 1999).[35] As we will see, the overall effect is fraught with contradictions; but before I take that up, let me briefly examine the changes at the micro-level that have occurred under the new regime.

Corporate governance

The macro-changes that I outlined above have been accompanied by changes at the micro-level, i.e., in structures of corporate governance. Broadly speaking, one may be able to identify two sources of change in corporate governance: (1) those emanating from the corporate sector itself – some of which are specific to specific companies, and (2) those contained in company law. With respect to the latter, substantial changes have been instituted through the Companies (Amendment) Act of 1999. The salient features of the Companies (Amendment) Act, 1999 are as follows.[36]

Box 5.1 Salient Features of the Companies (Amendment) Act, 1999

(1) Permission to companies to buy back their own shares or other specified securities subject to certain conditions;
(2) Permission to companies to issue sweat equity shares subject to fulfillment of certain conditions;
(3) Establishment of an Investor Education and Protection Fund;
(4) The constitution of a National Advisory Committee on Accounting Standards to advise the Central Government on the formulation and laying down of accounting policies and accounting standards for adoption by companies or class of companies;
(5) Permission to companies to make inter-corporate investments or give loans to other body corporates without prior approval of the Central Government.

Source: Department of Company Affairs, Government of India.

Let us examine these changes briefly, focusing on the two central issues: the buyback of shares and the takeover code.

Buyback of shares

Until 1999, section 77 of the Companies Act of 1956 imposed a blanket ban on companies, whether private or public, from buying their own shares. It was felt that such purchases would amount to 'trafficking' by

Box 5.2 Principal Regulations Regarding Buyback Under the Companies (Amendment) Act, 1999

- The buyback should not exceed 25 per cent of the total paid-up capital and free reserves of the company;
- The debt-equity ratio should be at least 2:1 after buyback;
- Such shares or other specified securities should also be fully paid-up;
- Companies are expected to make full and complete disclosure of all material facts at the general meeting, indicating the need for the buyback, the class of security intended to be purchased under the buyback, the amount to be invested under the buyback and the time limit for the completion of the same;
- Buyback must be authorised by passing a special resolution;
- The buyback should be completed within 12 months from the date of passing the special resolution;
- Companies have been given the freedom to effect buyback through different means and sources allotted under the employee stock option or sweat equity scheme can also be purchased by the companies;
- After completing the buyback operation, the company is prohibited from making a further issue of securities within a period of 24 months. This restriction, however, will not apply to issue of bonus shares, stock option schemes, sweat equity, and conversion of warrants, preference shares or debentures into equity shares;
- Promoters are not allowed to sell their shares if the buyback is through open market purchases;
- Buyback through subsidiary companies or any investment company is prohibited;
- Buyback is prohibited where the company has defaulted in repayment of deposits, redemption of debenture/preference shares or in repayment of term loans to any financial institution or bank and such default continues at the time of the proposed buyback;
- Failure to abide by these rules and restrictions may result in imprisonment for a period of two years or a fine of Rs.50,000 or both.

Source: Department of Company Affairs, Government of India.

the company in its own shares, and enable it to exercise unhealthy influences on the market price of its shares. The underlying idea was that creditors/contractors or other members of the public come to rely on the fact that the company is trading with a certain amount of capital and, therefore, they are entitled to assume that no part of the capital which has been paid into the coffers of the company has been subsequently paid out, except in the legitimate cause of its business.

The Working Group on the Companies Bill felt that the prohibition contained in the company law against buyback was antiquated and went against the long-term interests of both firms and shareholders. At a time when liberalisation is the driving force behind economic policy, the Group has considered it prudent to give a free hand to companies to decide whether the monies will be utilised for diversification or whether the surplus cash will be returned to shareholders so that they may invest the same in such manner that they may deem fit, subject to certain conditions (see Box 5.2).

The takeover code

Historically, Indian industrial policy has discouraged takeovers and mergers. While the reasons for this are not explicitly stated anywhere, they are not difficult to surmise. Indeed, the large size of the domestic market, bolstered by aggressive protectionist policies of the state made diversification or 'greenfielding' a much more feasible strategy than takeovers. More importantly perhaps, an active market for corporate control would not have been compatible with the 'balance-of-power' arrangement that had characterised the Indian corporate sector since its very inception. The 'balance-of-power' sentiment (that the dominant industrial empires will maintain a healthy distance from each other and respect each other's territories) was inscribed explicitly into Indian corporate law: the board of a company had the right to refuse transfers of shares to a particular buyer, thereby making it almost impossible for a transfer of control to occur without the consent of the existing management. The refusal of a transfer could be on two grounds: either that it went against the interest of the company or that it went against public interest. The definition of public interest in Indian law went beyond the simple interest of shareholders, but required that the proposed acquisition did not result in the creation of monopolistic conditions.

This situation has changed considerably since the eighties. From a level as low as 30–35 mergers in the late 1980s, merger activity touched a

peak of 430 merger announcements in 1995, and rose further to 552 mergers in 1997 (Khanna, 1999).[37] Primarily three factors are responsible for what is now increasingly being referred to as the 'first Indian merger wave': the abolition of restrictions on concentration, the availability of a large number of sick and weak firms and the entry of foreign capital. However, it is really the entry of foreign capital that fundamentally changed the scenario for corporate acquisitions in India. In what follows, I briefly present three events that illustrate critical developments in the relationship between state and capital in the post-interventionist era.

It was in 1993 that one of the major events in the history of acquisitions took place in India: the battle between the British multi-national BAT and its Indian partner ITC Limited over the control of the latter. At a meeting in London in late 1993, the CEOs of BAT and ITC (Martin Broughton and K. L. Chugh respectively) had allegedly come to an informal understanding that BAT will increase its stake in ITC from 31.4 per cent to 51 per cent. However, upon his return to India, Chugh reneged on his agreement and began to accuse BAT of seeking to reduce a powerful Indian company to a minor subsidiary of a MNC. Chugh also succeeded, in part at least, in amassing support from India's leading financial institutions (FIs) to resist BAT's takeover. The FIs jointly held 38 per cent of the stake in ITC and by virtue of their stake had three nominee directors on the board of ITC.[38] Like Chugh, the FIs were also resistant to any major change in ITC's hierarchy, and through a board resolution at an extraordinary meeting, they almost overnight increased the number of their nominee directors from three to five.

Subsequently, however, crises internal to ITC became so severe that even the FIs became convinced of the necessity of a change in ITC's management they voted for an exit package for Chugh valued almost at Rs.10 million. Soon after the new management and the new CEO took control, ITC was charged with a Rs.7 billion excise evasion case which, until today, remains pending before five Indian courts. Close in the heels of this came a FERA violation case involving $180 million. In the wake of these events, BAT suspended its battle for control for a few years, but has recently re-ignited its efforts to gain greater stake in ITC. This time its seems to have been more successful in garnering support from the crucial actors.[39]

Indeed, the BAT–ITC conflict marked the beginning of the takeover era in post-interventionist India. The most critical feature of the story is paradoxically, the role of the state as reflected in the participation of the

public financial institutions. The first point to note here is that in ITC, one of the largest private corporations in India, it is the public which holds the major financial stake. Second, it is this stake that the financial institutions are expected to safeguard through the appointment of the nominee directors. As such, their decision to support an existing management which was involved in corrupt schemes on such a grand scale gives us cause for serious concern. Finally, now that the practice of appointing nominee directors is on its way out, it is important to device other mechanisms that can effectively safeguard the public interest. Unfortunately, because the dual character of the involvement of nominee directors has hardly been recognised, the consensus seems to be that dismantling the practice will suffice.

A second determining event was the battle for control of INDALCO, the Indian subsidiary of ALCAN, Canada. In March 1998, Sterlite, a relatively young Indian firm, made an open offer for acquiring INDAL. It was a 'hostile' takeover bid, with INDAL's management clearly against the proposed acquisition by Sterlite. INDAL thus persuaded ALCAN to make a counter-offer: accordingly ALCAN offered to increase its stake at a price that initially matched and then exceeded Sterlite's offer price. However, Sterlite had offered to acquire about four times the stake that ALCAN had offered to buy, proposing thereby to inject a substantially greater amount of capital in INDAL. The critical decision rested with the three public financial institutions which held 36 per cent of INDAL's equity and they, along with the smaller shareholders, opted for ALCAN rather than Sterlite. It is estimated that the financial institutions incurred a loss of Rs.3.24 billion in cash by rejecting Sterlite's offer.[40] Moreover, this sale of equity by the institutions reduced their stake to below the 26 per cent level at which they would have the power to endorse/veto crucial resolutions by the INDAL board.[41] As of 1998, both ownership and management of INDAL rested unequivocally with ALCAN, with the institutions having very little participatory authority. In March 2000, ALCAN sold its entire stake to HINDALCO, the flagship company of the Aditya Birla group.

Contrast these two scenarios with a third one. In a complete reversal of their strategy to go along with existing management, six leading financial institutions are looking to offload to the highest bidder 44.5 per cent of the equity they collectively own in Modi Rubber Limited, a company promoted by one of the premier business families of India, the Modis. This act has moved two apex chambers of commerce the Federation of Indian Chambers of Commerce and Industry (FICCI) and the Associated Chambers of Commerce and Industry (Assocham), to appeal

to the government 'to throw away their high-minded advocacy of governmental non-interference in the working of the financial institutions (FIs)' and stop this sell-off. [42] The six FIs – IDBI, IFCI, ICICI, UTI, GIC and LIC – have for the last year been negotiating a price with the promoters but have not been able to agree on one. Now they have decided to sell the stake to the highest bidder. The Modis, the original promoters of the company, have objected to this, and claimed the right of first refusal and a negotiated price.

There are arguments on both sides as to what the role of the financial institutions should be with respect to their stakes in companies that do not perform. The neo-classical argument for disciplining management by activating the market for corporate control is by no means unequivocal (Singh, 1997). In the absence of laws preventing concentration, the market for corporate control is likely to aggravate oligopolistic conditions and work directly to contradict the logic of competition. More importantly, the very process through which the market for corporate control evolves from within an interventionist regime can result in a number of contradictions; as the cases above indicate, it becomes difficult to develop an universally applicable set of norms armed with the right kind of flexibility to balance a whole range of often contradictory priorities. A more complex issue, perhaps, is that the whole problematic of designing viable disciplining mechanisms is seen as a technical rather than a *political* task. This is where Kahler's 'orthodox paradox' becomes most relevant, and the institutionalists' indifference to the Neo-Marxist problematisation of the nature of the state takes on its salience.

So far, the development of the takeover code in India has proceeded through a rather contentious process. The code that is currently in practice is, however, heavily borrowed from the U.K. code and is replete with all the problems associated with the unqualified adoption of existing blueprints (see Box 5.3 below).

Box 5.3 Substantial Acquisition of Shares and Takeovers: Highlights of the SEBI Takeover Code

- A mandatory public offer is required when more than 15 per cent of the total stake is affected by the proposed change in control;
- An acquirer, including persons presently in control of the company, should make a public offer to acquire a minimum of 20

per cent in case the conditions for mandatory public offer mentioned above are valid;

- For the purpose of consolidation of holdings, acquirers holding not less than 15 per cent but not more than 75 per cent are allowed *creeping acquisition* up to 5 per cent in any period of 12 months. Any purchase for holding more than 51 per cent will have to be in a transparent manner through a public tender offer;
- Upon acquiring 5 per cent, disclosures must be made to stock exchanges and to SEBI;
- SEBI would not be involved in the pricing of offer. Pricing will be based on the parameters such as the negotiated price, average of the high and low price for 26 week period before the date of the public announcement, highest price paid by the acquirer for any acquisition during the 26 week period before the date of the public announcement, and the price for preferential offers, if any. Use of discretion by SEBI will be reduced to the bare minimum;
- The concept of Chain *Principle* has been introduced requiring a public offer to be made to shareholders of each company when several companies are acquired through acquisition of one company;
- Strong disclosure norms are mandated by the code, requiring disclosure of additional details of financial arrangements for implementing the offer, future plans of the acquirer for the target company etc. Disclosure of misleading information will be deemed a violation attracting penal action. Non-exercise of due diligence will also attract penalties;
- Conditional offer has been allowed subject to either a minimum mandatory acceptance of 20 per cent with differential pricing; or, with a deposit of 50 per cent of the value of the offer in cash in escrow, in cases where the bidder does not want to be saddled with the 20 per cent acquisition;
- The obligations of the board of the target company have also been spelt out. During the offer period, the board is precluded from inducting any person belonging to the acquirer or transfer shares in his name until all the formalities relating to the offer are complete.

Source: Government of India, *Economic Survey*, 1997 and 1999.

Codes of corporate governance

As I mentioned at the outset, structures of corporate governance are affected by developments in two realms: for one, there are developments in the realm of law which impose changes from the outside; for another, there are developments from within the corporate sector, which attempt to define changes from inside. The foremost of these attempts at self-regulation was the development of the *Code of Best Practice* developed by the Cadbury Committee in 1991. In 1997 a similar code for corporate governance was developed by the Confederation of Indian Industries (CII). Further to that the *Securities and Exchange Board of India* (SEBI) set up another committee on Corporate Governance under the chairmanship of Kumar Mangalam Birla in 1999. The task of this second committee was to focus specifically on issues related to the capital market. The principal recommendations of SEBI and CII are shown in Boxes 5.4 and 5.5 below.

Box 5.4 Kumar Mangalam Birla Committee on Corporate Governance: Some Mandatory Recommendations

- At the heart of the Committee's report is the set of recommendations which distinguishes the responsibilities and obligations of the boards and the management in instituting the systems for good corporate governance and restates the rights of shareholders in demanding corporate governance;
- The Committee recommends that the board of a company have an optimum combination of executive and non-executive directors with fifty per cent of the board comprising non-executive directors;
- The Committee recommends that the financial institutions should have no direct role in managing the company, and should normally not have nominees on the board, merely by virtue of their financial exposure by way of investment in the securities of a company. There is, however, a case for the term lending institutions to have nominees on the boards of the borrower companies, to protect their interests as creditors, in case of loan default or a potential of loan default, the determination of which may be left to the judgement of the lending institutions themselves. In such cases, the nominee directors should take an active interest in the activities of the board and

have to assume equal responsibility, as any other director in the board;

- The Committee recommends that a qualified and independent audit committee should be set up by the board of a company. This would go a long way in enhancing the credibility of the financial disclosures of a company and promoting transparency;
- The audit committee should have a minimum of three non executive directors, the majority being independent, with at least one director having financial and accounting knowledge; the chairman of the committee should be an independent director; the chairman should be present at Annual General Meetings to answer shareholder queries;
- The finance director, head of internal audit and a representative of external auditor should be present as invitees for the meetings of the audit committee;
- The board should set up a remuneration committee to determine on their behalf and on behalf of the shareholders with agreed terms of reference, the company's policy on specific remuneration packages for executive directors including pension rights and any compensation payment;
- That the following disclosures should be made in the section on corporate governance of the annual report:
- All elements of remuneration package of all the directors i.e. salary, benefits, bonuses, stock options, pension etc.
- Details of fixed component and performance linked incentives, along with the performance criteria;
- Service contracts, notice period, severance fees;
- Stock option details, if any – and whether issued at a discount, as well as the period over which accrued and over which exercisable.

Source: Securities Exchange Board of India, 1999.

Box 5.5 CII's Code for Desirable Corporate Governance: Highlights

- Maximising long term shareholder value.
- While acknowledging that there is a debate as to who the beneficiaries of corporate governance should be (e.g., shareholders, creditors, employees, local communities, suppliers, ancillary units, etc.), the Code argues that it is useful to limit

the claimants to shareholders and various types of creditors. The primary reason for this preference, according to the Code, is that the corpus of Indian labour laws are strong enough to protect the interest of workers in the organised sector, and both employees as well as trade unions are well aware of their legal rights. In contrast, there is very little in terms of the implementation of law and of corporate practices that protects the rights of creditors and shareholders;

- Any listed company with a turnover of Rs.1 billion and above should have professionally competent and acclaimed non-executive directors, who should constitute at least 30 per cent of the board if the Chairman of the company is a non-executive director, or at least 50 per cent of the board if the Chairman and Managing Director is the same person;
- There is no need to adopt the German system of two-tier boards to ensure desirable corporate governance. A single board, if it performs well, can maximise long term shareholder value just as well as a two- or multi-tiered board. Conversely, there is nothing to suggest that a two-tier board, per se, is the panacea to all corporate problems;
- No single person should hold directorships in more than 10 companies. This ceiling excludes directorships in subsidiaries (where the group has over 50% equity stake) or associate companies (where the group has over 25% but no more than 50% equity stake);
- In order to secure better effort from non-executive directors, companies should:
  (1) Pay a commission over and above the sitting fees for the use of the professional inputs. The present commission of 1% of net profits (if the company has a managing director), or 3% (if there is no managing director) is sufficient;
  (2) Consider offering stock options, so as to relate rewards to performance. Commissions are rewards on current profits. Stock options are rewards contingent upon future appreciation of corporate value. An appropriate mix of the two can align a non-executive director towards keeping an eye on short-term profits as well as longer term shareholder value;

  The above recommendation can be easily achieved without the necessity of any formalised remuneration committee of the board.

- Consolidation of Group Accounts should be optional and subject to the FIs allowing companies to leverage on the basis of the group's assets.

The Code recommends highly detailed disclosure norms, as well as a compliance certificate endorsed by the CEO and CFO that disclosure norms have been complied with. The Code recommends policy packages that would facilitate takeovers to a much greater extent than is currently possible. In particular, it recommends increased availability of takeover finance so that the minimum bid could reflect at least a 51 per cent takeover.

Source: Confederation of Indian Industries, *Desirable Corporate Governance in India – a Code*, 1997.

It is, of course, too soon to speculate on the impact of the codes. However, since the elements of the codes are taken quite directly from the existing body of codes in the West (in particular, the Cadbury Code of Best Practice) certain tentative assessments may be warranted. First, the codes seem to share the two basic assumptions of the Cadbury Committee: (1) that self-regulation rather than statutory regulation and enforcement is the optimum way to improve corporate governance; and (2) financial markets rather than independent regulators provide a better way of penalising companies for their non-compliance with codes of governance (Sheikh and Rees, 1995). The Cadbury Committee's strong preference for self/market-based regulation as opposed to legislative control has been challenged even in its home ground. Most importantly, theorists have critiqued its inability to challenge the traditional theory of the firm, in which the '*dramatis personae*' are yet again the directors, shareholders and auditors. As is evident from Boxes 5.4 and 5.5 above, the authors of the Indian codes have also chosen to limit themselves in a similar way; in fact, each code focuses squarely on one set of stakeholders. This is also reflected in the rather selective nature of the committees that have developed the codes.[43]

In view of these caveats, it is difficult to be too optimistic about the codes as they now stand. As many studies have concluded, there is no clear evidence that the codes themselves have been able to affect corporate behaviour; rather the implementation of these codes is heavily contingent on how other stakeholders are able to make corporate boards more accountable.

Summing up: changes so far

In the above discussion I have attempted to delineate the major changes that took place in India since the late eighties. I analysed these changes at two levels: at the macro-level and at the micro or firm level. The latter comprised changes in corporate governance structures, as reflected in changes in company law, the development of the corporate governance code as well as other macro-institutional changes that are likely to affect the governance structures of corporations.

In the course of this discussion, I tried to highlight in each case the contradictions implied in these changes. The contradictions arise not from the changes themselves, but because of their application within a concrete historical structure. My intention here is not to advance a structuralist argument, but rather to assert, in the face of an unrelenting faith in the efficacy of institutional change and universal laws, that historical and contextual specificities do matter. (In this sense, it is important that the changes be assessed in conjunction with the last two chapters.) This becomes even more crucial in light of the broad question I have set out to answer: how do changes in the corporate economy affect the rest of the economy in redressing the long-term malaise afflicting it: the absence of macro-economic growth, the problem of unemployment, or more specific to the post-interventionist period, the phenomenon of jobless growth?

In the two sections that follow, I will assess the actual impact of these changes for the corporate economy and for the macro-economy respectively.

Ownership, control and corporate growth in the post-interventionist model: plus ca change?

Ownership and control

Let us try to assess the impact of these changes in terms of the structure of corporate governance that has emerged since 1991. My primary analytical concern, as in the previous chapters, is to detect if there has occurred a shift in the locus of control. Such a shift can be conceived at various different levels: that between management and the board of directors, between the management and the board on the one hand and the shareholders on the other, between workers and management, and between foreign and domestic capital.

Given the fact that we are still in an interregnum, the long-term impact of any of the changes cannot be grasped yet. It is useful, however, to map the changes that have occurred so far (Table 5.3 below).

In terms of control, the avowed thrust of all the above changes is the enhancement of shareholder democracy. However, the possibility of any palpable increase in shareholder democracy as envisaged by the proponents of corporate capitalism remains somewhat elusive. As Halbe (1999) argues:

Table 5.3 Governance Structures of Indian and Foreign Firms in the Post-interventionist Model

	Multinationals	*Indian firms*
Formal Mechanism of Governance	single-tier board of directors	single-tier board of directors
Structural/ Institutional Context	• stronger capital markets • banking system more oriented toward profit generation • relaxed controls on (foreign) ownership and profit repatriation	• stronger capital markets • banking system more oriented toward profit generation • relaxed controls on (foreign) ownership as well as portfolio investment • firms allowed to buyback their own shares through open market operations • takeover code • the corporate governance codes
Locus of Control *proximate*	• majority ownership (by foreign MNE) • minority ownership (by foreign MNE)	• minority ownership (by apex company)
ultimate	• parent MNE	• majority ownership (of apex company by controlling family)
Other Mechanisms of Control	• control of share offerings • discouraging shareholder participation	• interlocking boards • intercorporate investments • mergers (of group firms) • control of share offerings • discouraging shareholder participation

Source: Adapted from Herman (1981) and Reed (1998).

> Today, company law reforms, as they have unfolded so far, stand out for their unfriendliness to stakeholders apart from promoters. Owner-managers have systematically increased control over their companies. Virtually all restrictions needed to maintain a balance between them and other stakeholders, like creditors and small shareholders, have been done away with under the specious argument of unshackling of managers.[44]

It is important here to recall our earlier discussion with respect to the *ownership* of the corporation (see Chapter 2). As indicated there, the liberal, Anglo-American understanding of corporate ownership is that it is eventually the shareholders who own the corporation. In that sense, the shareholders' interest overrides any other concern the company may have, including the expansion of the company itself (recall the famous court case between Ford and the Dodge brothers). This 'classical' notion of ownership has undergone substantial change over the last few decades, and the present ethos under all models of corporate governance is to strike a balance between the interests of shareholders on the one hand and *other* stakeholders. In part, the potential problem of conflict of interest is corrected if more and more stakeholders become shareholders, and the existing model of corporate governance can guarantee that the shareholders can exercise (at least indirect) control over the company. Such an indirect control would foster the basic right of shareholders to have the firm run in their (collective) interests. Let us now try to evaluate the emerging Indian model of corporate governance using this criteria.

With respect to indirect control, the Codes of Corporate Governance and the Companies *(Amendment) Act 1999* together provide a number of provisions that could in principle help to improve the ability of shareholders to participate in the control of the firms. These include:

1) the requirement that all large companies have an audit committee (two thirds of whose members are to be non-executive directors);
2) an increase in the number of issues which need special approval by shareholders;
3) an increase in the financial disclosure requirements;
4) an increase in the number of non-executive directors; and
5) a greater role for proxies, including the right to speak at annual general meetings of the company.

There remains, however, immense cause for scepticism. Critics point out that, first and foremost, the 1999 Act was based on a bill 'which has been primarily written by corporates for corporates' (Halbe, 1997a; 1997b). While it can immensely simplify the management problems of big business (and large shareholders), it does so only at the expense of small shareholders and other stakeholders. As Halbe argues, many, if not most, of the changes that will promote better corporate governance are largely cosmetic. For instance, the increasing number of issues to be approved by shareholders really has no effect given that shareholder democracy is largely a myth. Second, critics argue, the new Act introduces a number of provisions which will have an adverse effect on the quality of corporate governance. These include a provision for the buy-back of company shares, an increase in the age limit for managing directors and directors, the dismantling of existing curbs on intercorporate loans and investments and an attempt to get around restrictions to limit the role of private trusts in helping business families maintain control of firms. Third, it is argued that the existing Act fails to take action in a number of key areas which could have improved corporate governance by altering the balance of power between management and dominant shareholders and small shareholders and other stakeholders. There is no mention of a possible role for employees in corporate governance – a move which could also have helped shareholders in the attempts to control management (Halbe, 1999). On the contrary, CII's code explicitly mentions that governance structures such as the German two-tier board are not useful in the Indian context where labour is already overprotected.

One significant shift that has occurred with liberalisation is the shift in the proximate locus of power among many subsidiaries of foreign MNCs. What has enabled this change is the liberalisation of the government's foreign investment policy (first, the automatic approval of 51 per cent holdings in 34 industries and then further measures allowing up to 100 per cent foreign ownership). As a result many parent companies have now tried to gain a majority interests in their subsidiaries or, more recently, have even established new wholly-owned subsidiaries which often run parallel with minority-owned subsidiaries.[45] As a result, the proximate locus of power in these firms is now majority ownership. The ultimate locus of control rests with the parent MNC.

In the case of Indian family business groups, liberalisation has induced a corresponding phenomenon in the form of intergroup mergers, which I shall discuss further below. Unlike in the case of subsidiaries of MNCs, however, this new trend to intergroup mergers has not

(at least yet) had any significant effect on the locus of control among Indian business houses. In most firms controlled by business families, the shareholdings of most promoters remain quite minuscule (see Table 5.4). As a result, the proximate locus of control in these firms remains a combination of minority holdings and strategic control (through managerial control by the business family). The ultimate locus of control still rests with the business family of the apex company. As Table 5.4 also demonstrates, in many of these large companies the share of the public in total shareholding has decreased, causing a further diminution of the possibility of public control on the Indian corporation.

One of the principal manifestations of lack of power of the ordinary shareholder is the substantive lack of accountability of corporations with respect to remuneration of managers and directors. While it is well known that remuneration packages reached new heights since the onset of liberalisation, the concern that shareholders might have goes beyond the absolute size of those packages; the real concern is whether remuneration is linked to performance, as well as whether the wealth of the company is distributed according to some reasonable notion of equity. In the West, a solution to the possible conflict of interest between the shareholders and the board in this regard is attempted by widening the shareholder base and allowing for shareholder activism. In the case of India it is harder to sustain this official myth as shareholdings are not nearly as widespread and the dominance of minority (and

Table 5.4 Structure of Shareholding of Selected Companies: 1996 and 1999

Company name	*D & R[a] 1992*	*D & R 1999*	*public[b] 1992*	*public 1999*	*CB[c] 1992*	*CB 1999*	*PFI[d] 1992*	*PFI 1999*	*foreign[e] 1992*	*foreign 1999*
ACC	0.01	0.01	44.67	43.54	0.03	19.08	55.29	30.82	0.01	6.73
Tata Ch	0.23	0.16	29.95	7.80	32.71	54.44	35.73	35.29	1.29	2.31
Nagarjuna	0.04	0.12	53.89	48.8	11.06	20.72	30.09	25.6	4.87	4.76
Grasim	0.23	0.84	18.78	17.82	24.51	22.64	31.96	33.61	24.52	25.77
Guj. Amb	2.29	2.13	23.91	18.21	29.96	24.69	25.01	20.06	18.83	36.02
ITC	0.009	0.61	22.96	17.29	1.11	0.81	34.95	36.57	41.31	45.33
TISCO	0.03	7.53	41.12	38.47	14.83	18.56	40.62	38.37	5.38	4.58
TELCO	0.07	0.76	20.15	19.39	17.31	16.34	33.44	30.77	28.06	33.48
Tata Tea	0.0	0.09	37.58	40.74	31.92	35.43	28.29	21.20	2.2	2.53
Bajaj Auto	9.66	5.93	33.53	27.99	33.36	32.41	7.71	7.86	15.74	18.03
RIL	1.82	0.71	27.37	22.89	29.5	29.95	19.16	17.61	22.12	27.75
Mafatlal	2.4	3.33	19.88	23.22	39.14	37.16	37.31	36.42	1.28	1.15

Notes: a. directors and relatives; b. shares owned by the public; c. other corporate bodies not included in d or e; d. public financial institutions; e. foreign ownership.
Source: Compiled from the *Bombay Stock Exchange Directory*, various years.

majority) shareholding groups over the board and management is undeniable. This is true both of foreign MNEs (which are controlled through minority or majority shareholdings by the parent company) and Indian business houses (which are controlled by business families).

Notwithstanding the restrictions on remuneration established by the Companies Act of 1956 (and subsequent amendments to it), managerial salaries have risen sharply in the period in question. The salaries of senior management rose by 42 per cent in 1996 alone (with the raise for the next tier of management being less, but still a substantial 37 per cent).[46] The concern for shareholders, of course, is whether these increases are justified or whether senior management is increasingly able to establish its own salaries independent of performance. Certainly, these raises have outstripped increases in the profits earned by corporations (not to mention the remuneration to employees at other levels). For their part, directors are being better compensated. More firms are choosing to pay their directors some per cent of the net profits in addition to fees for their participation in the board. An example of the level of recent compensation packages for directors was the famous instance where Hindustan Lever paid its three non-executive directors a full 1 per cent of its net profits, amounting to some Rs.35.3 million, equal approximately to $1 million. (Consider in this context CII's recommendation that directors' remuneration should be increased and that decisions regarding such increases could be legitimately made *without* a remuneration committee as in some other countries.)

A second manifestation of the total absence of control or influence by shareholders relates to financial irregularities. While it is generally difficult to prove financial abuse, one area in which dominant shareholders clearly took advantage of the deregulated capital market and abused the rights of minority shareholders is preferential share options. Between 1992 and 1994 dominant groups both in Indian and foreign firms took advantage of this device to earn thousands of crores, all in a perfectly legal manner. Thirty top foreign firms, for example, amassed more than Rs.3 billion through this device (see Table 5.5), while ten major Indian firms received Rs.15 billion (see Table 5.6). This abuse was largely curtailed in 1994 when SEBI ruled that the price of preferential offerings could not be below the average share price of the previous six months.

Corporate growth and profitability

It is not at all surprising, given the general thrust of the post-interventionist model, that corporate profitability would increase

Table 5.5 Major Foreign Beneficiaries of Preferential Share Offerings

Company	*Allotment date*	*Number of shares (Lakhs)*	*Gains to promoters (Rs.million)*
Alfa Laval	Jan 93	34.05	738.9
ABB	Nov 91	47.55	1378.9
Ashok Leyland	May 93	171.00	547.2
Bata	Feb 93	47.14	966.4
Colgate	Sept 93	112.93	7227.5
Castrol	Sept 93	35.38	3325.7
Cadbury	Sept 93	22.92	183.4
Coates of India	Dec 93	12.99	263.7
Coates Viyella	Nov 92	74.09	1444.7
Color Chem	Dec 92	1.69	206.2
CP Tools	Nov 93	10.25	374.1
Corn Product	Sept 92	3.45	155.2
E Merck	May 93	3.91	25.8
Glaxo	June 93	44.89	808.0
Hoechst	Jan 94	21.51	645.3
Indian Shaving	Jan 93	19.30	270.2
ITW	Sept 93	3.89	36.9
Kinetic Honda	Nov 92	48.04	288.3
Lipton	Dec 92	35.36	972.4
MRF	Jan 94	4.24	137.0
Nestle	May 93	47.52	1021.7
P&G	Aug 92	19.40	223.1
P&G	Jan 93	47.70	1097.1
Philips	Sept 93	76.84	1267.8
Reckitt & Colman	Sept 93	30.30	848.4
Sesa Goa	May 93	32.80	2968.4
Boots	Feb 93	18.18	536.3
Hind Lever	June 93	29.84	805.7
Ponds	Apr 94	9.31	1182.3
Stepan Chemicals	Jan 94	12.50	875.0
Total			30,821.6

Source: *Economic Times*, 8 August 1994.

in the changed circumstance. The actual results, however, have not been as unequivocal as suggested by neo-classical economic theory. Let us begin with some simple measures of corporate growth, viz., sales and fixed asset formation, as well as total output. Tables 5.7 and 5.8 illustrate substantial growth in corporate sales, although the pattern of growth has become much more volatile. This volatility is true of both sales (or output) and profits (see Table 5.9), whereas by comparison growth rates

Table 5.6 Major Indian Beneficiaries of Preferential Share Offerings

Company	*Allotment date*	*Number of shares (Lakhs)*	*Gains to promoters (Rs.millions)*
Nahar Spinning	Jan 94	88.00	7040.0
Essar Shipping	Dec 93	450.00	2700.0
Sol Pharma	Feb 94	60.00	1065.0
Ranbaxy	Feb 94	50.00	1000.0
CESC	Jan 94	50.00	940.0
Vysya Bank	Sep 93	24.00	907.2
Himatsingka Seide	Apr 94	21.14	784.3
Indian Rayon	Aug 93	34.00	510.0
Atul Products	Feb 94	50.00	425.0
DCL Polyester	Oct 93	33.00	132.0
Total			15,503.5

Source: *Economic Times* 8 August 1994.

Table 5.7 Corporate Sector Growth: Gross Sales per cent

Ownership groups	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*
Government	13.6	15.1	11.2	6.9	25.3	15.5	19.3
Central Government (CG)	13.7	15.1	11.1	6.8	25.6	15.6	19.5
Private Sector	16.6	20.3	13.9	18.5	28.3	26.1	12.8
Indian Private Sector	15.6	20.8	13.8	18.6	29.4	26.6	11.4
Indian Business Houses	16.2	21.1	13.5	18.6	27.6	25.5	11
Top 50 Business Houses	15.3	20.7	12	18.1	27.1	25	11.4
Other Business Houses	18.7	22.2	16.8	19.8	28.6	26.5	10.1
Other Private Indian	13.3	19.4	15.2	18.5	34.6	29.6	12.4
Foreign Private Sector	20.7	18.2	14	17.8	22.6	23.4	20

Source: Centre for Monitoring Indian Economy, *The Indian Corporate Sector*, 1998.

of gross assets formation has been relatively stable (see Table 5A.6 in the Appendix to this chapter).

Many observers take this volatility simply as an indication of the increasing marketization of the economy and ascribe to it a positive value. While there is some obvious validity in this view, it merits further analysis in light of two related trends that seemed to have emerged: first, that it has become increasingly difficult to get the economy out of a recession every time it enters into one, and second, since 1995 the recessionary trend has become somewhat of a semi-permanent feature of the Indian economy. In the initial years of recession following

Table 5.8 Corporate Sector – Profitability: PAT[a] /Net Worth – (per cent)

Ownership Groups	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*
Government	–0.8	–1.7	–3.2	–3.4	5	5.9	2
Central Government	–0.9	–1.7	–3.5	–3.8	4.9	5.9	2.9
Private	17.4	14.8	10	13.6	15.8	14.3	8.9
Indian Private Sector	16.4	14.1	9.4	13	15.4	13.6	7.9
Indian Business Houses	17.1	14.8	9.5	12.9	15.2	14.2	8.6
Top 50 Business Houses	17.1	14.4	9	12.7	15.6	15.1	9.8
Other Business Houses	16.9	15.9	10.9	13.3	14.2	12.2	5.8
Other Private Indian	13.7	11.4	8.9	13.5	15.9	11.8	5.7
Foreign Private Sector	22.8	18.5	13.9	18.1	19.5	20.9	18.1

Note:[a] profit after tax.
Source: as Table 5.7.

Table 5.9 Index Number of PBDIT: base 1985–86

Year	*Index*
1985–86	100
1986–87	110.9
1987–88	123.8
1988–89	152.1
1989–90	192.7
1990–91	216.7
1991–92	272.2
1992–93	312.6
1993–94	371.5
1994–95	483.2

Source: CMIE, *The Indian Corporate Sector*, 1996, pg. 19.

economic liberalisation it was possible, at least for the largest section of the corporate economy, to enjoy rising profits despite the recession. This is evident both from Tables 5.8 and 5.9. The latter shows considerable rises in the index of profitability both over successive years as well as in relation to 1985–86, which was by no means a low-profitability year.

However, more recent data from 1995–99 shows a rather striking inability of the corporate sector to maintain rates of profit. As Table 5.10 shows, companies with larger capital bases are doing relatively worse in terms of profitability. What is also important to note is that there is no obvious systematic relationship between the growth in sales to growth in profits. This becomes even more evident when one examines

Table 5.10 Growth Rates of Selected Variables of Selected Non-financial Companies According to Size of Paid-up Capital

(per cent)

Size of paid-up capital (Rs. millions)	*Sales 1997–98*	*Sales 1998–99*	*Gross profits 1997–98*	*Gross profits 1998–99*	*Interest 1997–98*	*Interest 1998–99*	*Profits after tax 1997–98*	*Profits after tax 1998–99*
Less than 10 m		4.8	69.1	−8.5	89.0	−0.6	56.5	−13.2
10–50 m	8.6	9.1	11.9	−5.7	5.5	8.7	22.0	−24.8
50–100 m	8.2	9.5	7.7	10.0	9.1	6.2	12.1	16.1
100–150 m	12.2	8.5	3.0	0.0	14.3	11.9	0.3	−15.8
150–250 m	11.8	11.4	9.6	3.0	7.5	19.8	13.2	−7.0
250 m+	6.4	7.9	−0.8	−0.1	11.8	19.2	−5.8	−18.7
All companies	8.0	8.6	2.3	0.8	11.6	16.6	−0.7	−14.7

Source: Reserve Bank of India, *Performance of Private Corporate Business Sector, 1998–99*, RBI Bulletin, October 1999.

industry-wise data: between 1991–92 to the present, no clear relationship between growth in sales and growth and profitability is discernible. What is the implication of this absence? As I mentioned in Chapter 4, this is an important characteristic of the Indian corporate economy which often goes unrecognised. While a lot more systematic research is necessary to analyse this relationship, an initial hypothesis may still be feasible: namely that the growth in sales, or more importantly, output, is not the primary source from which profits arise. I mentioned before that the growth in profits immediately following liberalisation was due, to a significant extent, to a spurt in *other incomes*, i.e., incomes derived from sources other than a company's primary line of business. The main sources of these incomes have been investments in real estate, commodities and other stocks, (which also had a very significant inflationary impact on these sectors).

Unfortunately, the standard measures of corporate performance do not reflect these structural properties of corporate profits. Most importantly, they cannot provide much indication as to whether any genuine *economic* value addition has occurred. This inadequacy of accounting profits has for some time now plagued institutional shareholders especially with regard to their investments in the developing world. The recent focus on *shareholder value* by management theorists, consultants

and institutional investors largely reflects this concern and has led to the adoption of indices of *economic* profits rather than *accounting* profits. In this context, let us briefly examine the notion of *Economic Value Added (EVA)*. EVA attempts to reflect the difference between a company's accounting profit and the cost of capital to indicate to shareholders whether their invested capital has been efficiently utilised, and indeed if there has been an addition to the market value of their capital. Developed by the American management consultant Stern Stewart, EVA has been popularised in countries like India, Brazil and Mexico, primarily to protect the interest of foreign investors. Since 1995, a large number of Indian companies have been using EVA and indeed, some startling results emerge when we compare companies on the basis of economic value rather than accounting value. A study undertaken in India in 1997 revealed the following:

- Of the top 100 companies that were studied, as many as 36 reported *negative economic profits*, i.e., they have reached a rate of return that is lower than the cost of capital invested.
- Three out of the top five value creators: Oil & Natural Gas Corporation (ONGC), Videsh Sanchar Nigam Limited (VSNL) and Bharat Petroleum Corporation Limited (BPCL) operate under monopolistic conditions. This seems to be the case worldwide: in the US the top three are Microsoft, Coca-Cola and Intel; in the UK, Shell, Glaxo and Lloyds TSB; in Brazil, Telebras, Telesp and Brahma.
- For most companies, there exist huge discrepancies between ranking in terms of their economic profits and their after-tax-profits.
- The discrepancies between economic and accounting profits are equally significant for public sector corporations and private sector corporations.

Table 5.11 presents the rank discrepancies revealed by the study.

These findings are indeed significant from the point of view of capital efficiency, and in particular from the point of view of the shareholder. Those who champion the EVA approach argue that a company should be rewarded/punished *only* according to whether it creates/destroys shareholder value. They go even further to argue that remuneration of managers be tied to their performance measured in terms of value creation. While these may be important arguments, and are certainly beginning to convince a number of leading Indian firms, a switch to a focus on capital efficiency or shareholder value is not likely to redress the problems of macro-level growth. In fact, it might even worsen the

Table 5.11 Economic Profits, Market Profits and Market-value Added of Selected Companies

Company	*Management*	*Rank by profit after tax (PAT)*	*Rank by economic profits (EP)*	*Rank by market value added (MVA)*
ONGC	Govt. Executives	1	1	1
IOCL	Govt. Executives	2	89	2
Reliance Industries	Ambanis	3	9	4
TELCO	Tatas	4	6	7
HPCL	Govt. Executives	5	16	9
VSNL	Govt. Executives	6	4	6
IPCL	Govt. Executives	7	43	29
SAIL	Govt. Executives	8	98	8
BHEL	Govt. Executives	9	90	11
NALCO	Govt. Executives	10	67	16
TISCO	Tatas	11	97	18
Bajaj Auto	Bajaj	12	3	14
BPCL	Govt. Executives	13	5	12
Hind Lever	Professional	14	2	3
Larsen & Toubro	Professional	15	96	17
Hindalco	Govt. Executives	16	30	10
ITC	Professional	17	10	5
Grasim	Birlas	18	85	37
Tata Chemicals	Tatas	19	71	25
Indian Rayon	Birlas	20	31	66

Note: (EP) = [PAT – weighted average cost of capital]/total capital; (MVA) = total capital employed [current value of company's shares and debt]
Source: KPMG–Business Standard Value Survey, published in *The Strategist Quarterly*, Jan–March 1998.

possibilities of growth. For, as the list of top performers indicate, high EVA–MVA rankings are associated with monopolistic firms which do not function on principles that are necessarily growth-generating. Further, the implications of shareholder-value-maximisation on the economy can be tenuous, since value can be easily maximised through a number of growth-impeding corporate strategies including retrenchment, sell-offs and mergers (recall from Chapter 2 our discussion of the British businessman Lord Hanson's strategies for shareholder value maximisation).

Of course, indices like EVA are not intended to reflect systematic differences between monopoly profits and competitive profits or between profits that arise from reducing the size of the workforce. As such, the shift to EVA-based strategising by companies cannot in itself provide much cause for optimism. What the move to EVA does signify is

a need perceived by Indian businesses to respond to the pressures of the times. This is what I examine below. Specifically, I will examine the strategies employed by Indian firms to respond to the changes discussed above. These strategies not only help explain the nature of growth that has occurred in the post-interventionist period, but more importantly point us toward the growth trajectory that might evolve in the near future.

Exit, voice, swadeshi

It is possible to identify three basic strategies adopted by Indian firms in the post-interventionist period, which I have labelled *exit*, *voice* and *swadeshi*. As the name suggests, the first refers to the decision of firms to leave the market. Not an insignificant number have chosen this route since the onset of liberalisation. The most prominent case of exit was the decision by Parle Export Brands, the dominant soft drink company in India, to sell out to Coca-Cola. There are of course different possible motivations for such decisions to exit the market, including personal reasons on the part of the promoters. The reason that is most frequently offered for this phenomenon, however, is that the promoters have seen the writing on the wall and have decided to exit while they could still command a good price. There is some concern within the business community that the latter might be the case, unless the government steps in to address the situation by offering some (temporary) relief. Indeed, increasing number of businesses have sold off all or part of their stake to foreign companies.[47] Some of the most critical and controversial sell-off decisions have come from the Tata group: between 1993 and now the Tatas have virtually exited from

- Pharmaceuticals – by selling off Merind Ltd. to Wockhardt (Rs.470 million)
- Personal care – by selling off Lakme to Unilever (Rs.2 billion)
- White goods – by selling off parts of Voltas to AB Electrolux, the Swedish domestic appliances major (Rs.2 billion +)
- Bearings – by selling off a division of Tata Timken to Timken Company, U.S. (Rs.1.8 billion)
- Cement – by selling off a division of TISCO to Lafarge SA, France (Rs.5.5 billion).

However, these exit strategies are fundamentally different from those followed by Parle's sell-off to Coke (or Duke Brothers who sold off to

Pepsi): the Tata's sell-offs are part of a restructuring process through which it is seeking an exit from older-style heavy industries into hi-tech and export-oriented sectors. As I will discuss below, this exit strategy is combined rather skilfully with other strategies which have enabled the Tatas to maintain and strengthen their stature as one of the top three business groups in India.

The second broad set of strategies adopted by Indian businesses, which I refer to as *voice* strategies, involves efforts to increase their competitive strengths. A number of different sub-strategies seem to have emerged, many of them reflecting dominant currents of management thought in the West. They can be categorised as follows:

- focus on core competencies
- offensive resistance to takeover bids
- formation of strategic alliances with MNEs
- adoption of new management and benchmarking techniques.

Foremost amongst these is the focus on *core competencies*, which involves a somewhat substantive shift from the strategic emphasis on diversification that characterised the earlier regime.[48] The post-interventionist climate has rendered diversification both unnecessary and infeasible, leading companies to sell of ventures not directly related to their primary competencies.[49] Important here, among other things, has been the increasing necessity of ensuring a proper balance between businesses which generate funds and those that will demand investments. This kind of restructuring has emerged as particularly important in light of the new regime of financing in the post-interventionist period. Previously, firms were able to rely on soft debt finance from the public financial institutions. With the deregulation of interest rates, equity financing has emerged as a cheaper option for many projects. In particular, companies have been keen to exploit debt markets overseas, where interest rates are substantially lower.

The second type of voice strategy – resistance to takeover bids – is probably the one that has received the most publicity. I discussed the famous battle between BAT, UK and ITC, India. Similar conflicts have occurred between Gillette, USA and HLM Private Ltd, INDAL and Sterlite India. The Indal–Sterlite story represents a rather remarkable voice strategy, in that it is a case where an Indian company wanted to increase its stake in a subsidiary of a MNC (ALCAN of Canada).

A third type of voice strategy involves the adoption of management practices and benchmarking techniques such as EVA, total quality

management (TQM), business process reengineering, supply chain management, etc.[50] Often, changes such as these have been ushered in by members of the younger generations who are more 'professionally' orientated than their predecessors.

A fourth and related type of voice strategy is reflected in the efforts of Indian business houses to professionalise. This concern is particularly salient for family business houses insofar as the holders of the top offices, whose performance can make or break a firm, tend to receive their places not on the basis of merit, but family ties. As noted above, family firms have been trying to address this issue by ensuring that the younger generation are professionally qualified. Paradoxically, the move toward the professionalisation of younger generation has come to coexist with an increasing number of serious and disruptive family feuds within Indian business families, especially when the issue of succession has been at stake.

Liberalisation has certainly increased the pressure on Indian business families to become more competitive. The willingness and/or ability to do so, however, remains open to question. A recent study, employing the types of measures mentioned above as criteria, has attempted to assess the prospects of survival for Indian business families.[51] The findings were not particularly encouraging. The study found that not one of the top 50 business houses was sending out a *powerful* survival signal, while only 14 of them could be considered to be emitting a *strong* survival signal. At the other end of the spectrum, more than 20 out of the top 50 houses were found to be *downright weak*. Thus, while liberalisation has increased competitive pressures on Indian firms, they are proving to be not entirely willing and/or able to respond. This fact helps to account for a third strategy which Indian firms have employed to address the challenge of liberalisation.

The third set of strategies which Indian firms have sought to exercise can be categorised as *swadeshi*, which literally means home-grown or indigenous. The ruling sentiment of India's independence movement, *swadeshi* has been reinscribed into the political discourse by the BJP since 1991. The BJP's aim was to distinguish itself from the Congress' avowed commitment to IMF-style liberalisation and structural adjustment programmes. In particular, the BJP became vocal about its strategies to contain the power of international capital. Underlying BJP's *swadeshi* stance were two factors: (1) its relationship with the Indian Merchants Chamber which has historically represented factions of capital most closely alligned to the *swadeshi* movement led by Mahatma Gandhi; and (2) an awareness that the *swadeshi* sentiment was fairly

widespread amongst the business community and could be congealed into a political force.

This the BJP did rather successfully and in a way that sought to balance carefully the threats and opportunities associated with global capital. As I have argued elsewhere, this was achieved by charting out a relationship between sections of Indian capital and a particular class of foreign investors, viz., the non-resident Indians (NRIs).[52] The NRIs saw in *swadeshi* a rather unique possibility for gaining special treatment by the Indian state and Indian capital. From the point of view of Indian businesses, the NRIs provide a way to establish linkages with global capital without having to succumb entirely to the uncertainties of unfettered foreign competition. This fortuitous coincidence of interests was probably first noted by Rajiv Gandhi, the official author of post-interventionist political-economy in India; however, it is the BJP, along with its cultural outfit, the *Vishwa Hindu Parishad* (World Council of Hindus), which has been actively trying to build bridges between the NRIs and the 'motherland'. Specifically for this purpose, an organisation called the *Overseas Friends of the BJP* was formed in 1994 to launch the *Saffron Vision 2000* in the US. The aim of this project is to educate NRIs in the US about the economic policies of the BJP.[53]

Two main elements of the BJP's economic policy are particularly appealing to business: privatisation and protectionism. The philosophical roots of this protectionism are derived from a synthesis of Gandhian socialism and the thoughts of a lesser known nationalist ideologue, Deendayal Upadhyaya, both of whom emphasise *swadeshi* and self-reliance.[54] In line with the idea of self-reliance, the BJP's economic policy recommends restrictions on the entry of foreign capital into consumer goods sectors and only qualified entry into other sectors of production. This is where the BJP most sharply distinguishes itself from the Congress, and thereby draws support from the largest faction of Indian domestic capital. In 1993, when it embarked most aggressively upon its bid for political power, the BJP planned a 'boycott' of goods manufactured by MNCs, executed by way of a much-publicised burning of imported goods deliberately evocative of the nationalist struggle. Initially, the BJP had also planned a negative list of sectors where foreign investment would not be allowed and imports were to be restricted.[55]

Most importantly, the BJP has endorsed a policy of preferring investment by NRIs over other types of foreign capital. In the states governed by the BJP and its alliances, explicit policies have been pursued to attract NRI investment. Between 1991 and 1995 about Rs.4 billion (approximately $119 million) of NRI investment has flown into Gujarat, which is

one of the richest and most industrialised states in India ruled by the BJP.[56] This impressive inflow of capital is a result of the Gujarat government's special incentive package for NRIs, which a special branch of the Ministry of Industries of the Gujarat state has been set up to administer. The incentives include priority in allotment of cash subsidies and loans from financial institutions, as well as special allotment of resources like electric power and land. As the Ministry of Finance's key document, *The Economic Survey (1998–99)* states:

> A number of liberalization measures have been taken to promote portfolio investment. In order to avoid NRIs being crowded out by FIIs, the aggregate ceiling for investment in a company by all Non-Resident Indians (NRIs) / Persons of Indian Origin (PIOs)/ Overseas Corporate Bodies (OCBs) has been raised from 5 per cent to 10 per cent of the paid-up capital of a company. In case of listed Indian companies, the ceiling can be raised to 24 per cent of paid-up capital under a General Body Resolution. Also, the investment limit by a single NRI/PIO/OCB has been raised from 1 per cent to 5 per cent of paid-up capital.[57]

The development of the special regime for NRIs constitutes only one element of the *swadeshi* strategy. The other elements involve special measures to enable Indian firms to fight off hostile takeover bids (e.g., buybacks, non-voting shares), restrictions on public financial institutions so that they can sell their stakes only to Indian firms, (continued) tariffs on imports and restrictions on FDI (especially in consumer goods), and (continued) export subsidies.

The design and implementation of *swadeshi* is, of course, made possible by the active participation by some Indian industrialists, most notably the House of Bajaj, the Shahs, the Ruias, the Mahindras as well as a whole complex of medium and large businesses based in Western India. By mediating a political relationship between this particular class of global investors and local capital, the BJP has successfully managed to acquire political power which seems fairly robust in the face of myriad destabilising forces.

In conceptualising *swadeshi* as a strategy for Indian corporate capital, one needs to carefully avoid the two common theoretical pitfalls: neither the view that the BJP is being instrumentally deployed by Indian capital, nor the view that the responses from capital are mere reactions to economic policy formulated autonomously by the BJP seem accurate reflections of reality in this case. What is critical to note is how a

particular vision of the relationship between capital, state and society get politicised at particular points in time, because it has the potential to bring together a number of diverse interests.

The post-interventionist model and the question of development

Let us now try to form a general assessment of how the post-interventionist model has impacted the rest of the economy. Recall the set of general criteria set out at the beginning to assess the models:

- a sustained increase in assets, incomes and skills of workers;
- a substantive transition of labour–management relationships in such a way that there occurs gradual democratisation of the realm of production.

In the particular context of the post-interventionist model, the expectation would be that labour market conditions would come to simulate those in the more liberalised Anglo-American markets. This could imply two contradictory processes: on the one hand, there is reason to expect an erosion of the power of labour unions; on the other hand, there is also reason to expect a 'tightening' of the labour market, i.e. increase in levels of employment because of the expansion of industrial activity accompanied by a tighter relationship between wages and the marginal productivity of workers.

At least three conditions need to be satisfied if the above is to occur. First, it needs to be ensured that profits cannot be generated without the continuous expansion of productive capacity. Second, the expansion of productive capacity will have to be based upon a judicious balance between capital and labour intensity. Third, in order that continuous expansion becomes viable, there will have to be a corresponding expansion of aggregate demand. This will have to occur through redistributive processes emanating from both the market and the state (by the market through increases in wages and corporate asset ownership, and by the state through taxation).

It should be somewhat obvious from the discussion that trends so far have not conformed to any of the criteria above. The most dramatic impact has been on the earnings of workers employed in the corporate sector. As Table 5.12 shows, wages as a value of production have declined uniformly across all types of corporate firms, from 10.43 per cent in 1985–86 to 6.75 per cent in 1994–95. It has also been uniform

Table 5.12 Share of Wages in the Total Value of Production (per cent)

	1985–86	*1989–90*	*1990–91*	*1991–92*	*1992–93*	*1993–94*	*1994–95*
Public Sector	9.79	9.83	9.61	9.54	9.44	9.32	6.53
Private Sector	11.16	9.04	8.68	8.16	8	7.42	6.85
Indian Private Sector	11.46	9.18	8.84	8.28	8.03	7.36	6.77
Large Houses	11.28	9.27	9.03	8.52	8.34	7.87	7.31
Other Private Cos.	12.28	8.82	8.13	7.47	7.11	6.05	5.32
Foreign Companies	11.83	9.81	9.01	8.51	8.47	8.34	7.73
All Companies	10.43	9.44	9.13	8.81	8.65	8.22	6.75

Source: CMIE, *The Indian Corporate Sector*, 1996, p.50.

across both large corporations (especially MNCs), as well as smaller, private firms (where the share of wages has declined from 12 per cent to 5 per cent).[58]

In the largest section of the corporate economy, voluntary retirement schemes worth Rs.1 billion have been administered each year between 1993 and 1997.[59] This is particularly true of sectors where high growth is envisaged in the coming years, and the permanent exclusion of a class of Indian workers from these sectors merits some concern.

Of course, each of these companies has had to seek approval from state governments for the respective schemes they have administered and state governments usually do not ratify the schemes unless they have support from the trade unions. There exist, however, very significant contradictions in Indian labour law. First, the law requires companies to pay only up to 15 days salary for every completed year of service and state government approval is almost never given if this is the proposed compensation. Second, the actual practice of state intervention has worked in a manner that makes it more feasible for companies to shut down whole operations/plants/branches rather than lay off a section of the workforce.

In the public sector, a total of 1,29,049 workers had availed of the VRS by April 1999. The amount released for this purpose was Rs.23 billion between 1992–93 and 1998–99. During 1998–99 a budgetary provision of another Rs.2.9 billion has been made for VRS with the expectation that a similar amount would have to be set aside every year for the next five years. Of the total number of workers retrenched, about 11,367 (approximately 10 per cent) have been redeployed over the past six years (at the rate of approximately 2000 workers per year as against a retrenchment rate of 21,000 per year).[60]

The retrenchment of workers through various voluntary retirement schemes in a market where unemployment is already high is not likely to favour the democratisation of production in any serious way. In fact, it has resulted in the reversal of some of the material and political gains secured by the Indian workforce. However, a certain class of skilled workers have made substantial financial gains, even if the political equation between labour and management has shifted in favour of the latter. The reasons behind this shift are several. First, the increasing presence of the MNCs are having a twofold effect: one the one hand, there is a tremendous increase in salaries; on the other hand, there is a movement toward more flexible employment, less job security, sub-contracting etc. Second, domestic businesses have been lobbying for a long time for a viable exit policy, modelled after the bankruptcy laws in the U.S. While there is certainly a movement in that direction, the existing laws do not work as much to protect workers as they appear to.

As indicated in Chapter 4, existing policies seek to protect employment by inducing companies to seek help from the public financial institutions and the *Board for Industrial and Financial Reconstruction* (BIFR). Once signs of 'industrial sickness' begin to appear, boards and managements of companies are expected to approach the financial institutions and the BIFR to put together a revival strategy that involves fresh financing and concessions. While the intentions behind these measures are commendable (protection of employment and investments made out of public money), there is ample evidence that the possibility of receiving these concessions have induced firms to use them for financing corporate restructuring.[61] But more importantly, there is evidence that the roles played by the government and its various agencies, including the BIFR, is not equivocal; broadly speaking, they have tended to respond much better to revival plans proposed by managements/promoters rather than workers. In one particularly illustrative example, workers had put up equity amounting to Rs.90 million out of their wages to finance the revival of an ailing jute mill. The proposed scheme got no attention from the various authorities for about three years, a delay that compromised the viability of the scheme and the earnings of the workers in a very significant way.[62]

On balance, the shift towards the post-interventionist model provides little room for optimism even with the stringent requirements of development that I have set out. As I will argue in the next chapter, growth rates of demand, output and employment have reached unprecedented levels of volatility – a volatility I think can be directly attributed to the changes in the corporate economy. Of course, this is to be expected from

the particular model of corporate capitalism that is being implemented in India. The question is whether this model is preferable to the less volatile yet perhaps the more stagnationist model that preceded this.

As it appears in hindsight, the interventionist model was rendered an unsustainable one because of the historical/structural constraints on which it remained highly contingent. The post-interventionist model proposes to break with this history in a very substantive way by dismantling some old institutions and putting in place an ensemble of new ones. The vision behind this transition is that, unless free of interruptions, the logic of capital is unable to deliver its promised goods; and when interrupted, it unless itself out in distorted and paraoxical ways. However perverse, there may be a certain logic to this argument. The question, of course, is what exactly such an uninterrupted logic of capital can deliver.

One can answer this question from both ends of the political spectrum; both answers, however, are likely to be simplistic, and both could contain substantive elements of truth. A more complex answer needs to incorporate at least two sets of issues: (1) the specific ways in which the 'fetters' on the logic of capital emerge and the ways in which their removal is sought; and (2) the specificities of the new system that emerges, in particular, the specificities of the *altered* conditions under which capital now has to operate.

The final chapter offers some thoughts on these issues.

Statistical Appendix

Table 5A.1 Assistance Sanctioned and Disbursed by Development Banks

Year	*Growth Rate of Sanctions (per cent)*	*Growth Rate of Disbursements (per cent)*
1981–82	8.2	28.8
1982–83	20.3	14.8
1983–84	24.5	23.8
1984–85	35.5	19.3
1985–86	14.9	40.6
1986–87	23.3	14.8
1987–88	13.1	17.9
1988–89	53.2	35.9
1989–90	6.7	5.9
1990–91	32.7	33.0
1991–92	20.3	30.2
1992–93	45.4	39.5
1993–94	23.2	14.6
1994–95	49.0	26.2

Source: Industrial Development Bank of India, *Report on Development Banking in India 1994–95*, Table 2.1, p. 5.

Table 5A.2 The Top Ten Zero-Tax Profit Makers in 1994–95

Company	*Profit Before Tax (in million rupees)*
SAIL	11085.7
Reliance Industries	10648.5
State Bank of India	7154.9
Essar Gujrat	975.1
National Aluminum	3002.0
Tata Chem	2866.5
Tata Iron & Steel	2641.9
Nagarjuna Fertilisers & Chemicals	1928.9
Great Eastern Shipping Company	1733.5
Century Textiles and Industry	1591.7

Source: *Business Today*, 22 December 1995.

Table 5A.3 Major Foreign Beneficiaries of Preferential Share Offerings

Company	*Allotment Date*	*Number of Shares (Lakhs)*	*Issue Price (Rs.)*	*Market Price on Issue Date (Rs.)*	*Pref. Issue Amount (Rs. cr.)*	*Market Value of Pref. Allotment (Rs. cr.)*	*Gains to Promoters (Rs. cr.)*
Alfa Laval	Jan 93	34.05	73.00	290.00	24.86	98.75	73.89
ABB	Nov 91	47.55	60.00	350.00	28.53	166.42	137.89
Ashok Leyland	May 93	171.00	50.00	82.00	85.00	140.22	54.72
Bata	Feb 93	47.14	35.00	240.00	16.50	113.14	96.64
Colgate	Sept 93	112.93	60.00	700.00	67.76	790.51	722.75
Castrol	Sept 93	35.38	110.00	1050.0	38.92	371.49	332.57
Cadbury	Sept 93	22.92	100.00	180.00	22.92	41.26	18.34
Coates of India	Dec 93	12.99	112.00	315.00	14.55	40.92	26.37
Coates Viyella	Nov 92	74.09	65.00	260.00	48.16	192.63	144.47
Color Chem	Dec 92	1.69	700.00	1920.0	11.83	32.45	20.62
CP Tools	Nov 93	10.25	25.00	390.00	2.56	39.97	37.41
Corn Product	Sept 92	3.45	200.00	650.00	6.90	22.42	15.52
E Merck	May 93	3.91	34.00	100.00	1.33	3.91	2.58
Glaxo	June 93	44.89	75.00	255.00	33.67	114.47	80.80
Hoechst	Jan 94	21.51	70.00	370.00	15.06	79.59	64.53
Indian Shaving	Jan 93	19.30	120.00	260.00	23.16	50.18	27.02
ITW	Sept 93	3.89	120.00	215.00	4.67	8.36	3.69
Kinetic Honda	Nov 92	48.04	30.00	90.00	14.41	43.24	28.83
Lipton	Dec 92	35.36	105.00	380.00	37.12	134.37	97.24
MRF	Jan 94	4.24	1027.0	1350.0	43.54	57.24	13.70
Nestle	May 93	47.52	70.00	285.00	33.26	135.43	102.17
P&G	Aug 92	19.40	225.00	340.00	43.65	65.96	22.31
P&G	Jan 93	47.70	120.00	350.00	57.24	166.95	109.71
Philips	Sept 93	76.84	40.00	205.00	30.74	157.52	126.78
Reckitt & C.	Sept 93	30.30	100.00	380.00	30.30	115.14	84.84
Sesa Goa	May 93	32.80	120.00	1025.0	39.36	336.20	296.84
Boots	Feb 93	18.18	110.00	405.00	20.00	73.63	53.63
Hind Lever	June 93	29.84	105.00	375.00	31.33	111.90	80.57
Ponds	Apr 94	9.31	180.00	1450.0	16.76	134.99	118.23
Stepan Chem	Jan 94	12.50	125.00	825.00	15.62	103.12	87.50
Total					860.22	3942.83	3082.16

Source: *Economic Times*, 8 August 1994.

Table 5A.4 Major Indian Beneficiaries of Preferential Share Offerings

Company	Allotment Date	Number of Shares (Lakhs)	Issue Price (Rs.)	Market Price on Issue Date (Rs.)	Pref. Issue Amount (Rs. cr.)	Market Value of Pref. Allotment (Rs. cr.)	Gains to Promoters (Rs. cr.)
Nahar Spinning	Jan 94	88.00	25.00	825.00	22.00	726.00	704.00
Essar Shipping	Dec 93	450.00	30.00	90.00	135.00	405.00	270.00
Sol Pharma	Feb 94	60.00	75.00	202.00	45.50	151.50	106.50
Ranbaxy	Feb 94	50.00	400.0	600.00	200.00	300.00	100.00
CESC	Jan 94	50.00	142.0	330.00	71.00	165.00	94.00
Vysya Bank	Sep 93	24.00	22.00	400.00	5.28	96.00	90.72
Himatsingka	Apr 94	21.14	79.00	450.00	16.70	95.13	78.43
Indian Rayon	Aug 93	34.00	200.0	350.00	68.00	119.00	51.00
Atul Products	Feb 94	50.00	65.00	150.00	32.50	75.00	42.50
DCL Polyester	Oct 93	33.00	25.00	65.00	8.25	21.45	13.20
Total					603.73	2154.08	1550.35

Source: *Economic Times*, 8 August 1994.

Table 5A.5 Growth in Gross Fixed Assets of the Indian Corporate Sector (per cent)

Ownership Groups	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*
Government	11.09	11.83	7.78	5.82	11.46	14.27
Central Government	11.09	12.70	7.70	5.24	11.33	14.39
Central Government Takenover	13.95	7.751	1.00	−10.87	5.35	0.043
Central Government Others	8.79	13.17	9.859	5.84	11.5	14.8
Private Sector	30.72	24.59	31.89	40.28	24.25	11.38
Indian Private Sector	31.63	25.77	32.99	41.07	24.74	10.55
Indian Business Houses	31.42	26.35	30.52	35.84	23.44	11.98
Top 50 Business Houses	30.64	23.97	27.31	34.59	23.26	15.75
Other Business Houses	33.39	32.29	38.01	38.52	23.82	4.160
Other Private Indian	32.43	23.54	42.66	59.84	28.68	6.345
Foreign Private Sector	25.01	16.80	24.06	34.25	20.33	18.29

Source: CMIE, *The Indian Corporate Sector*, 1996, p.17.

Appendix note: market value and additions to market value

Following the development of the stock market, a lot of emphasis has come to be placed on the market capitalisation of firms. The level of market capitalisation, defined as price per share times total shares

outstanding, is being increasingly used to assess firms. The larger the level of market capitalisation, the more efficient is a company in creating 'value for its shareholders'. In this context, it is necessary to be aware of some of the pitfalls of this measure. For instance, if we compare the market capitalisation figures of the largest Indian companies as they are listed in the Bombay Stock Exchange (BSE), with figures published by the International Finance Corporation (IFC), we see a huge difference (see Table 5A.6).

What explains this difference? As IFC states in its *Emerging Markets Yearbook*, a number of adjustments to market capitalisation are necessary to arrive at a better estimation of the amount of a company's stock that is in the market. First, from the perspective of IFC and the global investors it represents, statutory limits on foreign ownership need to be excluded, since this means that a certain percentage of the equity is not available to foreign investors. Second, IFC also adjusts for capital owned by government. This is important in the Indian case, since an average of 30 per cent of stocks in large companies is held by the government and government-owned financial institutions. What this means for the investor is that, when a decision has to be made for or against a takeover bid, these institutions would have ultimate control on a substantial block of shares which would override the decision of individual investors. Third, and most important, is the adjustment for *cross-holdings*.

Table 5A.6 Market Capitalisation of Largest Indian Companies: IFC versus the Bombay Stock Exchange (BSE)

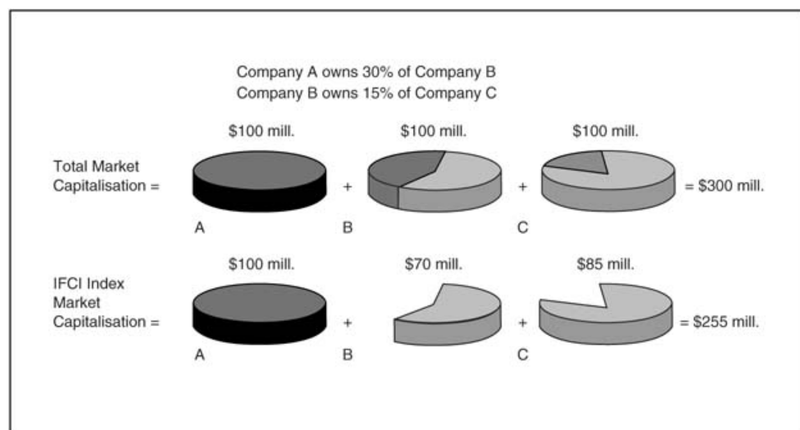
Company	*IFC $mn*	*$million BSE*
BAJAJ	374.6	1693.25
HIND.LEVER	1818.39	6659.22
HINDALCO	215.82	1625.56
IDBI	146.44	1558.31
ITC LTD.	972.95	3385.78
RELIANCE	590.4	3916.44
HDFC	188.26	966.31
TATA STEEL	168.61	1516.42
TATA ENGG	140.28	2034.28
LARSEN & TOUBRO	203.99	1173.41

Conversion rate: 1$=Rs.40
BSE market capitalisation are averages for 1997–98

Source: IFC, *Emerging Markets Yearbook, 1998* and BSE Directory.

Conceptually, *cross-holding* (or cross-ownership) is defined as the situation where one company owns stock in a second company (see Figure 5A.1 below). Since typically one company's holdings of another company's stock are included in the overall market valuation of the former, there is an element of double counting whenever cross-holding is present. Company A is valuable because it owns part of company B, and counting both A and B at their observed market capitalizations would be deceptive. Furthermore, an investor could buy all of A and B for less than the sum of their observed market capitalisations, since by buying all of A this investor would automatically acquire part of B. Hence, any weighting scheme based on market capitalisations would firstly tend to overstate the weight associated with companies involved in cross-holding, and secondly would overstate the weight in a composite index of any country with greater than average cross-holding generally. This insight is particularly important with respect to India, where cross-holdings are high and transparency is low. As we saw, there were some restrictions on cross-holdings and inter-corporate loans and investments in the interventionist regime, which have been liberalised in the Companies (Amendment) Act of 1999. The full implications of these measures need to be factored in when considering market capitalisation.

Figure 5A.1 IFC Indexes: Adjusting for Cross-ownership



Part III

This page intentionally left blank

6
The Paradox of Profits: Some Tentative Conclusions

As suggested in Chapter 5, there is one central paradox that has come to characterise India's corporate economy today. On the one hand, the regulatory framework through which the Indian state had historically managed accumulation stands dismantled. On the other hand, some highly problematic continuities with the interventionist era remain. For those of us who believe in history, perhaps such a paradox is to be expected; nonetheless, the importance of this paradox – of the co-existence of some elements of state intervention *simultaneously* with weak regulatory powers of the state – needs to be assessed carefully.

The most important implication of this co-existence, I wish to suggest, will be evident in the nature of corporate profitability. Contrary to the claims of neo-liberal economics, the reforms are not likely to alter the sources of corporate profitability of Indian firms in any significant way. For a variety of reasons, the only exception here may be the knowledge-based sectors; however, with respect to the euphoria about the knowledge-based economy, two caveats are in order. First, at least in the medium term, it is unlikely to comprise any more than one small, exclusive niche within the Indian economy. Second, despite the astounding increases in the levels of market capitalisation, profits, and personal wealth of key firms/players in this economy, the overall effect of these increases for the rest of the economy is far from clear. As Peter Evans concludes from his study on the Indian software industry:

> Taken as a whole, India's software exports go to the heart of the ambiguities of the new internationalisation .... Leaving aside packaged software ... the custom side of the business ranges from routine code writing, which is a low-return use of skilled intellectual labour, and the design and implementation of complex information systems,

> which is essentially very high level consulting work and reaps commensurately high return ... a substantial portion (perhaps the majority) of India's software 'exports' were in reality contracts for migrant intellectual labour, pejoratively known as 'bodyshopping' .... Bodyshopping produced neither proprietary return nor a contribution to organisational or entrepreneurial infrastructure of India's domestic industry. It also exacerbated India's brain drain.
>
> (Evans, 1995:194–5)

Let us, then, set our euphoria aside for a while and return to the main arguments of the work. As I tried to show in my examination of the three historical models, profits in India have arisen primarily from non-market forces, as well as from market manoeuvres associated with distorted market structures. As I also attempted to show, the interventionist state had a critical role to play in making these profit strategies viable. In this regard, the role of the Indian state has been criticised quite correctly by authors on both sides of the political spectrum. The essence of both these arguments is well known. From the right, the primary argument is that state intervention resulted in inhibiting the growth potential of the corporate sector, thus preventing it from contributing to macro-level growth. While these authors generally concede that India's highly distorted industrial structure pre-empted the development of healthy competition, they recommend state policies and corporate strategies which could further distort the underlying structures. More importantly, few of these authors have actually offered a systematic analysis of profit strategies of Indian firms. The few studies that exist confirm our hypothesis that the trajectory of profits of Indian firms do not reflect competitive market behaviour (Kambhampati, 1998).

Authors from the left, while agreeing on the hypothesis of distorted market structures, disagree both on the causes and consequences of such distortion. In their view, the distortion of market structures that occurred under the interventionist regime should not be seen as an outcome of the state's efforts to control capital, but as an outcome of the state's efforts to *aid* certain factions of capital. The ultimate effect of this, according to critical scholars, is a net transfer of resources and assets from state (and society) to capital. Obviously, this stands in direct contradiction to the neo-liberal claim that intervention helps the state amass resources at the cost of capital.

We need now to move beyond this debate, but before we do that, let us acknowledge that capital in India has made substantial gains during the interventionist period, perhaps both despite and because of the state. It is

clear, however, that these gains have not penetrated into Indian society at large, through the creation of employment and incomes, an increase in assets of workers, or their general standards of living; most importantly, the skill level of the average Indian worker did not improve much over the last five decades. In sharp contrast to the East Asian tigers, Indian firms both in the private and the public sector depended on capital-intensive technologies and emphasised the accumulation of physical rather than *human* capital. As Table 6.1 shows, the reforms have in no way been able to put the economy on a trajectory of steady growth.

In the preceding chapters I tried to develop an argument to explain why capitalist development in India followed the trajectory it did. It is time now to see how these findings compare with the extant literature in the field. There are several strands of literature I wish to consider, each of which offers explanations as to how modern corporations may contribute to development. In what follows, I will discuss five approaches to the question: (1) the organisational learning argument (as advanced by Chandler, Amsden *et al*); (2) the transaction cost argument (as developed by Coase and Williamson); (3) the classic finance-theoretic arguments about the centrality of shareholder value maximisation (Friedman, Miller *et al*); (4) the corporate strategy-centred argument that critique the finance-theoretic model (Porter and Prahalad); and (5) the

Table 6.1 Industrial Growth Rates: Use-based Classification, 1980–81 to 1998–99

Sectors	1980–81 to 1990–91[a]	1990–91 to 1994–95[b]	1994–95	1995–96	1996–97	1997–98	1998–99
Basic Goods	7.86	−14.18	8.9	10.7	3.1	6.5	1.4
Capital Goods	11.30	11.73	5.7	4.1	9.3	5.3	12.7
Intermediate Goods	5.87	−4.91	5.3	19.1	8.1	8.1	5.9
Consumer Goods	6.57	5.55	11.8	12.3	5.2	4.6	2.4
Consumer Durables	13.66	−2.17	16.2	25.8	4.7	7.8	4.7
Consumer Non-Durables	5.34	9.13	10.8	9.3	5.3	5.2	1.8

Source: CMIE, India's Industrial Sector, January 1996, p. 5;
Government of India, Ministry of Finance, *Economic Survey*, various years.
Notes: (a) and (b) are compound annual growth rates based on 1980–81=100; the figures for 1994 to 1998–99 are based on the new index of industrial production 1993–94=100.

aggregate demand argument (articulated by a wide range of theorists who accept some of the basic postulates of both Keynes and Marx, albeit in varying degrees). Next, I will consider these arguments in light of the recent developments in India. I will then conclude by reflecting on these developments in somewhat greater detail in order to identify some of the forces and actors that condition the trajectory along which the Indian corporate economy is likely to evolve, in the near future.

The arguments

Consider first the Chandler-Amsden theses that emphasise the following aspects of the corporate form:

- its ability to exploit economies of scale
- its ability to recruit and develop the kind of human capital necessary for commercialising new technologies as soon as they come into existence
- its ability to become the primary drivers of technological advances and the seat of continuous learning

As is well-known, Chandler emphasises the superiority of the corporate form with respect to its ability to 'learn' and commercialise technology, and argues that despite the fact that the rise of the large corporation led to the early emergence of distorted market structures, such distortion – aided – rather than hindered – overall industrial growth rates in the US. Amsden makes this argument (in my view, even more powerfully) in the context of ('late') development; she demonstrates exactly how the organisational strengths of oligopolistic enterprises were harnessed by the Korean state, while at the same time *it was able to deter typical profit strategies associated with oligopolistic behaviour from dampening the speed of growth.* This point is absolutely critical, I think, in understanding the dynamics of growth through big business in East Asia. It provides not only an explanation of East Asian growth, but can also give us important pointers as to why such growth was also conducive to increasing the material wellbeing of East Asian workers, as well as a continuous enhancement of their skills and abilities. This could explain in turn, why East Asia's record of income distribution has been much better than that of the US. However, none of these East Asian successes can take away from the essentially undemocratic political structures to which East Asian workers (and civil societies) were

subjected, especially during the miracle years (although assessing them simply by contrasting them to the structures of formal democracy in the West is not likely to be useful).

Why was it the case in East Asia that growth-dampening oligopolistic behaviour could be contained? Several answers are available in the literature. Amsden, for instance, argues that the answer lies in the particular abilities and visions of the East Asian bureaucracy. Others draw upon the uniqueness of Confucian ethics. Business historians and corporate strategists offer yet a third explanation: namely that East Asian companies place little value on market profits relative to the expansion of size, assets and 'corporate honour'. As McCraw points out:

> If there is any one key to the Japanese economic miracle, it lies in the maintenance of a fever pitch of inter-firm competition that by the 1990s had persisted without abatement into its fourth decade. This remarkable aspect of Japanese capitalism is insufficiently understood in the West, and its importance is often underestimated even by Japanese scholars. It is a competition that emphasises market shares as much as profit, if not more. It is a ceaseless, almost obsessive drive to uphold the status of the company – not for the purpose or with the aim of driving domestic competitors out of business, but of maintaining position and corporate honour, and of avoiding shame.
>
> (McCraw, 1997:543)

Those who espouse this latter view attempt to break with the strong statist interpretation of East Asian success, which portrays business as a passive partner in the process of development (Johnson, 1982; Evans *et al.*, 1985; Amsden, 1989; Haggard, 1990). Not surprisingly, business historians often find it necessary to reject this passive image, as they salvage from the archive of corporate histories the various corporate (as opposed to state) strategies, decision-making processes and value systems that contributed to the growth process (McCraw, 1997). In any case, the fact remains that the East Asian economies were able to prevent some of common growth-retarding effects of oligopolistic behaviour (the most important of which was to retain price-based competition) which in turn was predicated on continuous 'learning'. This ability, it may be argued, also accounts for the more egalitarian distribution of income that it produced (at least) relative to the US and other parts of the developing world – despite the absence of any state-administered redistributive measures.

As has often been argued, this technology-centred argument is necessarily incomplete in that it ignores the other side of the equation, i.e., the problem of demand. What made this continuous learning, expansion and commercialisation feasible? What guaranteed the requisite increases in the size of the market? The answer to this question is fairly straightforward in the East Asian case: markets were found abroad. As is well-known, a number of scholars have identified this outward-orientation of the East Asian regimes as its primary source of growth, and the inward-orientation of countries like India as the primary reason for their stagnation (Krueger, 1978; Bhagwati, 1988; Bhagwati and Srinivasan, 1999).

In the case of the West, however, it is not enough to point to the importance of exports; the dynamics of the domestic market also must be explained. Neither Chandler nor the other growth theorists of his genre address this issue in a fully satisfactory way. Was there anything particular to classic Fordist capitalism that ensured the expansion of aggregate demand? As Boyer argues, the fact that in the Fordist model productivity gains were directly translated into wage increases led to a synchronisation of productivity gains and aggregate demand. In addition to Continental Europe where this certainly was the case, Boyer argues that this held true even in the US – at least until the seventies; thus, the 'golden age' in the US was marked by an unprecedented reduction of wage differentials which resulted in the synergy between growth of productive capacity and aggregate demand as in the Continent (Boyer, 1996: 51). Boyer then goes on to make an even stronger argument. Contrary to the neo-liberal assertion that the redistributive elements of Fordism are responsible for its decline, the truth may in fact be the reverse: it is exactly those elements of redistribution, rather than technological learning, that accounts for the 'golden age' of capitalism, both in the US and the Continent.

While I accept the general thrust of Boyer's theses, it is important to add to it the economic relationships between the Third World and the West that also contributed to rising aggregate demand during the golden age. Let us return to the question of aggregate demand at a later point, and for now, go on to consider several other strands of relevant literature. I wish to consider next the Coase-Williamson type of argument that corporations create wealth because they are able to minimise transaction costs. As is well known, Coase's seminal work focused attention on the fact that it is the hierarchical nature of corporate organisation – in particular the employer-employee relationship – that allows such cost minimisation (Coase, 1937). However, this

Coasian insight (and its political implications) was not ascribed a central place in the core of transaction cost economics which emanated from Coase's work – and the formal development of which is attributable primarily to Williamson (Williamson, 1975; 1985). Williamson's major contribution was to offer transactions cost economics as an alternative to the neo-classicist and contract-theoretic analysis of economic organisations, and is regarded as highly useful for designing mechanisms/ governance structures where ordinary contractual arrangements are likely to fail. In developing countries, its insights are being applied – in quite an extensive way – in the designing of economic institutions for the post-interventionist regimes. There remain however, several serious problems with the straightforward application of the transactions cost approach to developing country contexts. Despite its *analytical* differences with neo-classical economics, transactions cost economics remains normatively and epistemologically within the neo-classical tradition, imbued very much with the same functionalism, ahistoricity and avoidance of the issues of power and political economy. As such, it gives us no theory as to why particular transaction costs evolve in particular economies – or more generally why particular institutions emerge in particular contexts. Neither can it explain why 'inefficient' institutions persist over long periods of time (Bardhan, 1989; 1993). Recall here my discussion of the managing agency model in colonial India. While a transaction cost view could indeed explain its function in the colonial economy, what such an explanation would exclude is the extreme skewness in the ownership of capital that made the institution viable. In my view, such exclusion takes away substantially from a full analysis of the impact of the institution in question.

Next, consider the classic value maximisation argument put forward by Friedman, Miller *et al*. The essence of the argument is, of course, as old as corporate capitalism itself, namely that businesses create value by maximising wealth for their shareholders. In this model, there is no possibility of a shortage of aggregate demand; according to a tenet that economists call Say's Law, this model is premised on the belief that an increase in supply automatically creates an increase in demand.

This finance-theoretic value maximisation model argues that as providers of equity capital, shareholders are the *residual claimants* who bear most of the risk, and they accordingly should receive the lion's share of the rewards. Other corporate stakeholders – customers, employees and local communities – should be *adequately* compensated and no more. Implicit in this view is a clear hierarchy of corporate objectives in which

the maximisation of shareholder value reigns supreme, and 'the ultimate scorecard for managers becomes the current stockprice – or more precisely, stockholder returns over a definite time horizon' (Prahalad, 1997:51).

This orthodox finance-theoretic model has been strongly criticised by corporate strategists like Porter, and more recently Prahalad (1997). Porter's argument – which I touched upon in Chapter 2 – is that in order to contribute to economic growth, companies must remain globally competitive. Global or macro-competitiveness in turn depends on how well companies invest in *intangibles* like the building of strong networks, process improvements, employee training etc. In Porter's view, the US system, with its focus of near-term profitability and shareholder value, discourages investment in intangibles and hence undermines the prospects for the long-term growth of the economy. Prahalad (1997) puts forward an even stronger argument: that no significant change in corporate behaviour can be brought about unless we acknowledge that corporations must add value in a way that all its stakeholders' interests are ascribed equal primacy. This would imply eschewing the hierarchy of stakeholders in which shareowners reign supreme and corporate goals are oriented towards the maximisation of shareholder value.

Both Porter and Prahalad note that the East Asian and European systems of corporate governance are better equipped to discourage short-termism and allocate investment in favour of intangibles. This is because both these systems are able to control the extent to which the capital market is able to shape corporate and even some social objectives. However, they also acknowledge, particularly in the wake of Eurosclerosis and the Asian crisis, that those systems are also flawed in that there is too little external disciplining (this in fact is the immensely popular thesis advanced by Paul Krueger). What they propose therefore is an amalgamation of the two models; their suggested model, however, is quite different from the one that seems to evolving in Europe, East Asia, and in other parts of the developing world. While they suggest designing governance mechanisms that combine the interests of the various stakeholders – with a clear reduction in the importance of the *stockholder* – what is occurring in reality is quite the opposite. As the Indian case clearly demonstrates, the *maximisation of shareholder value* is overwhelmingly the shared objective of all the critical actors: the state, business, international donors, foreign institutional investors as well as a fairly large and influential community of scholars working in leading institutions in India and abroad. Echoes of a similar commitment

to shareholder value can be heard in Mexico, in Brazil, in South Africa and in much of the developing world, as well as in the transitional economies of Europe. Of crucial importance here is also the global emergence of mechanisms that seek to *legitimate* the concern for shareholder value, especially in the developing world, through the creation of codes, norms of governance and the various schemes intended to demonstrate corporate social responsibility.

Let us consider now how exactly the above arguments apply to India. The Chandler–Amsden thesis could provide, in some sense, an obvious explanation for the retarded development trajectories of countries like India. However, it is not clear that technology by itself would have been sufficient. While it is true that East Asian patterns of 'learning' did not occur in India, a fair amount of technology and capital was accumulated in both the public and private sectors. What remains absent, however, is the diffusion of this technology in a manner that enhances the skills of the average Indian worker. In the light of this observation, it seems deeply ironic that Indian corporations enjoy significant tax concessions for investment in research and development (notwithstanding its record-breaking profit rates, India's most aggressively growing corporation – Reliance Industries – has qualified for *zero* taxes for a number of years on that basis).[1]

As some authors have already pointed out, the transaction cost approach appears fairly unsatisfactory with respect to India. It needs to be acknowledged, however, that the approach enjoys a lot of credibility amongst policy-makers and academics of a certain kind. It is strongly believed in these circles that certain elements of the reform programme – particularly those related to the financial sector – have been conducive to significant reductions in transaction costs. This belief is affirmed every time the stock market 'soars', and strangely enough, even every time the market 'plummets'. (The argument in the latter case is that transaction costs have not been reduced enough to remove all information asymmetries that characterise markets undergoing reforms.) While it is true that in the context of certain specific sectional issues, the approach can have some limited validity, it is certainly inadequate in explaining macro-economic or distribution effects of corporate capital.

Let me turn now to the argument that has come to comprise the basic tenet of the neo-liberal reforms: that corporations add most to society when they maximise shareholder value. There are several implications of this in the Indian context. On the one hand, even though there has been considerable growth in the number of shareowning households

in India, the proportion of such households remain quite low relative to the Indian population. On the other hand, the growth of this share-owning population – and most importantly the decision to allow employees' provident funds and pension earnings to be invested in corporate securities – ascribes a new salience to the issue. These funds comprise the life-savings of millions of working Indians and are currently estimated to amount to Rs. 2 trillion (approximately $46 billion).[2] Historically, these funds could be invested only in government securities and tended to earn low returns. The decision to bring this rather significant amount to the capital market and make it available to the corporate sector raises some very important dilemmas.

First, it is possible that the objective of shareholder value maximisation will yield substantive benefit to the average Indian shareholder, both directly as well as indirectly, by increasing the value of his pension funds. However, as I have argued, such value maximisation the world over comes about at very serious costs, the most important of which is corporate restructuring (including mergers and acquisitions) along with large-scale retrenchment. As I also showed, in most cases value maximisation must be associated with distorted market structures, the negative effects of which are serious. Further, in a developing country like India, there is great potential for maximising shareholder value through insider trading and price manipulation. Needless to say, the kind of shareholder activism or government regulation that would be required to exclude the possibility of value maximisation through these mechanisms is unlikely to emerge in India in the near term.

These considerations point us to the importance of perspectives that are critical of the wealth maximisation approach. I mentioned two perspectives above: the strategic arguments of business theorists like Porter and Prahalad and the demand-theoretic arguments put forward by left Keynesians. The first set of arguments are important in that they come from within the corporate community, and being cast in terms of corporate strategy, may find a better hearing. However, the strategic orientation of these arguments is also the source of their potential weakness, since they do not address the broader questions as to how strategic interests of capital are contingent upon history and structure.

This brings us to the demand-theoretic arguments of left Keynesians. In conjunction with these arguments it may be also useful to consider a wide range of development theorists who have commented on similar issues (Bagchi, 1982; 1994; 1999; Bardhan, 1993; Nayyar, 1994; 1997; Singh, 1994; Stiglitz, 1999). Common to all these authors is the recogni-

tion of the importance of aggregate demand, and the analytical assertion that at least in the context of a less-developed economy supply does not create its own demand. In this sense, they argue that economic reforms – being comprised of policy measures that intend to increase labour market flexibility through wage cuts and retrenchments – are inherently inimical to the expansion of aggregate demand in the long run.

Now, the macro-economic aspects of this problem have already been widely discussed and it is increasingly being admitted by all – even the IMF – that macro-economic management is a necessary pre-condition for the success of reforms. What I attempted to bring to the analysis was a focus on the *micro*-economic elements of the problematic. The thrust of my argument was that the impact of macro-economic policies are realised through the various profit strategies corporations employ, and unless those policies are aimed *directly at* altering profit strategies, the intended outcomes of those policies are unlikely to be realised. To a large extent, such a direct targeting of micro policies was exactly what was done in East Asia and remains, I think, one of the most enduring legacies of the 'miracle'. That said, one has to acknowledge the centrality of two factors in determining the success of these strategies – the authoritarian political framework within which they were implemented, and the exploitation of East Asian labour.

There is likely to be little disagreement that these elements are neither desirable nor possible, given the advances in political democratisation in countries like India. But there is an essential contradiction embedded in this process of democratisation: it is directed against state intervention in a manner that justifies the withdrawal of the state from political and economic life. As I tried to show in Chapter 5, the withdrawal of the state is not necessarily a simple devolution of power to civil society; rather, it is a redistribution of power from one social group to another, with very serious consequences on the relationships between these groups. In the specific context of economic reforms, this has meant a distribution of power away from labour to capital, from unorganised, skill-deficient labour to organised, high-skilled labour, from small capital to large capital, and most visibly perhaps, from productive to speculative capital.

This reconfiguration of power hardly reflects, I think, a reduction in state power but rather the emergence of a 'new' alliance between bureaucracies, corporations and certain factions of civil society who do not share a developmental objective. How are corporate goals and objectives to be influenced in an era of this 'new alliance'? Two broad

sets of answers are currently available. One represents the (neo) liberal view that asserts that under conditions of democracy, the prevalence of a particular set of goals/objectives reflects a societal preference for the same; hence any efforts to influence them undermine the democratic premise. The other represents critical perspectives, which suggest looking for fissures or contradictions within extant structures; such contradictions, when seized upon through concerted political action, are perhaps the only real sources of substantive change. Taking from this critical premise, it may be useful to conclude by identifying some 'fissures' in the structure of contemporary corporate capitalism in India.

Contradictions and possibilities

Let me begin by examining the role of one of the central agents in contemporary corporate capitalism, namely the investor. One of the critical developments with respect to the role of the investor – both globally, as well as in India – has been the emergence of institutional investors. In the US, institutional investor holdings have soared from $770 billion in 1980 to $15.4 trillion at the end of 1998, with 48 per cent of this amount coming from pension funds. Amongst these pension funds, the *public* pension funds (like CalPers) are active shareholders and have managed to affect corporate strategies in some cases quite significantly. In 1988, public pension funds accounted for only 7.1 per cent of the total equity market but by the end of 1998, they accounted for 10.3 per cent of total equities. By comparison, corporate pension funds actually lost ground as a percentage of total equity ownership: in 1988 they held 15.5 per cent of total equities, which had declined to 13.3 per cent by 1998.[3]

The importance of this global development can be seen as follows. On the one hand, it represents an effort to harmonise the interests of labour and the interests of other investors who might enable corporations to adopt profit strategies that labour otherwise might oppose. On the other hand, this also creates a stronger basis for labour (and allied factions of civil society) to oppose certain strategies of capital accumulation. As is not often recognised, these efforts at 'integrating' labour into the circuit of capital may manage to expose the underlying structural relations between capital and labour, thereby enabling a more fruitful confrontation between the two.

As alluded to above, in India there is a very serious on-going debate around the issue. The salience of the issue derives not only from the significant amount of capital involved, but also because at present there

are absolutely no mechanisms through which workers' organisations can intervene in structures of corporate decision-making. It is also not clear whether one can expect the development of such mechanisms over time, particularly in view of the increasing insecurity of the conditions of work and the withdrawal of the state as an arbitrator between labour and capital.

That said, it needs to be acknowledged that while the onset of globalisation has weakened the power of unions, it does not seem to have completely undermined them. A recent occurrence in India is a case in point. With regard to the proposed restructuring of nationalised banks, the Confederation of Indian Industry (CII) – the leading Indian Chamber of Commerce – had recommended the closure of a number of such banks whose capital base had been eroded significantly. In response, the bank employees' unions threatened to release the (currently confidential) list of corporate defaulters who owe the public banking system a significant sum (estimated conservatively at Rs.586 billion or approximately $14 billion at the current exchange rate). This immediately led the government and the CII to withdraw those recommendations, and most importantly, has resulted in a public release of the defaulters' list by the Reserve Bank of India. What happens hereafter is, of course, a matter of active politics. But the critical point, in my view, is that the Reserve Bank's decision to release the confidential defaulters' list may reflect an urgency to harness impulses from civil society in order to solve the otherwise insoluble fiscal crisis in which the state finds itself enmeshed. As the bank unions have accurately surmised, the recommended closure of the banks brings no gains to the state, with the latter held responsible for financing a huge retirement scheme for the retrenched workers, threats of political unrest, increased unemployment, and no possibility of ever recovering the defaulted sums of money. There is no obvious reason why a state that is already mired in a fiscal crisis would not seize this impulse from an important faction of civil society for its own advantage. However, the interests of the state are not always that unequivocal, and the eventual outcome in situations like this can hardly be predicted a priori.

A third and related indication of fissures in the seemingly glorious reign of global capital constitute the mobilisation around the WTO talks in Seattle. To a large extent, these mobilisations symbolise an authentic people's radicalism in response to the material impact of globalisation. There is, however, an unfortunate contradiction in the process: the genuine anti-West stance of the victims of neo-liberal policies is being used as an excuse to institutionalise anti-labour

policies at home. The government's stubborn resistance to attempts to link core labour standards and environmental protection with international trade reflects more its determination to allow the exploitation of cheap labour by Indian industries rather than any genuine opposition to global capital. At least seven WTO-related pieces of legislation were in the pipeline at the time of the Seattle events. These include the proposed amendments to the Industrial Disputes Act, Trade Union Act, Contract Labour Wages Act, etc. These changes reflect a confluence of interests of the Indian capital and the Indian state, where both agree on the need to increase 'labour market flexibility' in order to profit from globalisation.

To summarise this discussion so far, let me say that at least two sets of contradictions are visible in the process of economic reforms that is currently underway in India. The first comprises the co-existence of rapid growth in profits and incomes of certain actors in the corporate economy, with increasing problems of stabilising and sustaining macroeconomic growth rates. The second comprises a problem of legitimacy: there are continuous manifestations of the fact that the new regime is being perceived by several factions of civil society as unfair and undemocratic.

The latter constitutes probably the most potent source of change in the long-term. What is required to strengthen these political practices is the simultaneous development of a *proactive* strategy bringing together two themes: (1) an evaluation of the extant model of corporate capitalism *vis-à-vis* other possible models of corporate capitalism; and (2) an evaluation of corporate capitalism *vis-à-vis* other forms of production. At the current conjuncture, the latter would unfortunately be perceived to be of little value by most factions of civil society; the former, by contrast, is likely to find a better hearing. As I mentioned already, re-evaluation of the Anglo-American model *vis-à-vis* other models of corporate capitalism is actively underway with respect to most advanced economies *even when there seems to be global shift towards this model*. This shift, which was at its extreme ascendancy before the Asian crisis, has clearly weakened since. Numerous analyses of the crises in Asia and Europe have now converged on the view that much of that crisis may indeed have been caused by the decision to embrace the Anglo-American model in an unplanned, historically insensitive manner.

Let me conclude by returning to the point with which I began this chapter: the problem in India (and in most LDCs) is not simply the emergence of the Anglo-American model and the withdrawal of the

state. It is also the emergence of a new kind of interventionism where the state impacts upon society as much through its active presence as through its absence. The contours of political and economic power under this new interventionism need to identified – and indeed acted upon – in ways that encompass both these dimensions.

Notes

Preface

1 Legitimation is often confused with the state's distributive actions with respect to the relatively disadvantaged groups in society. This, in my view, leads to fallacious analysis. While a lot of analytical attention has been paid to the state's distributive role in relation to disadvantaged, relatively little attention has been paid, outside of the Marxist tradition, to the state's distributive intervention for those groups who already benefit from the market mechanism, especially in mixed economies.

1 India in the Past-interventionist Era: Towards a New Political-Economy?

1 For views from the left, see Bagchi, A.K. *The Political Economy of Underdevelopment* (Cambridge: Cambridge University Press, 1992); Kurien, C.T. *Global Capitalism and the Indian Economy* (New Delhi: Orient Longman, 1994). For views from the right, see Ahluwalia, I. J. *Industrial Growth in India: Stagnation Since the Mid-Sixties* (New Delhi: Oxford University Press, 1985); Bhagwati, J. and P. Desai *India: Planning and Industrialization* (New Delhi: Oxford University Press, 1970).
2 Government of India, *The Seventh Plan* (New Delhi: Planning Commission of India, 1985).
3 As one example of the strength of capital, consider that the average real rate of return in the private sector between 1976–77 to 1986–87 was as high as 22.6 per cent. By contrast, public sector profitability was only 5 per cent (Cassen and Joshi, 1995).
4 Several dimensions of this crisis are mentioned in the literature: the all-time low foreign exchange reserves, the all-time high fiscal deficit, the huge losses suffered by public sector enterprises, the ever-expanding web of subsidies, etc. For a summary see Jalan (1992).
5 As examples, see Cassen and Joshi (1995); Evans (1995); Jalan (1992).
6 Chandra, B. *Nationalism and Colonialism in Modern India* (New Delhi: Orient Longman, 1979). Ray, R. K. *Industrialization in India: Growth and Conflict in the Private Corporate Sector, 1914–47* (London: Oxford University Press, 1982).
7 The category 'foreign capital' constitutes foreign corporations, MNCs, foreign institutional investors and international financial institutions like the IMF, the World Bank, the WTO, etc.
8 Friedman, M. 'The Social Responsibility of Business is to Increase Its Profits', *New York Times*, 12 September 1962, p. 126.
9 See Johnson, C. *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925–75* (Stanford, California: California University Press, 1982) for a classic discussion of Japanese planning. It shares with socialist planning the

following features: (a) centrally determined allocation of resources between consumption and investment; (b) detailed allocation of investment capital across different sectors; (c) use of an input-output model to determined exact volumes of primary, intermediate and final goods to be produced in each plan period. For a fuller discussion, see Johnson (1988), pp.51–68.

10 Lal, D. *The Hindu Equilibrium. Vol 1. Cultural Stability and Economic Stagnation, c.1500 B.C. – A.D.1980* (Oxford: Clarendon Press, 1982).

11 For an exposition of this view, and the way in which its straightforward application can lead to fallacious conceptualisations of the state in the Third World, see Alavi (1982; 1983).

12 This version of dependency has in fact been criticised on many counts, most fundamentally for having displaced the very locus of Marxist analysis from an analysis of class relationship emanating from the realm of production, to an analysis of *exchange* relationship between *nations* (Warren, 1976). For our purposes here, the more salient point is their problematic theorisation of capital and the state in post-colonial societies.

13 Zeitlin, M. 'Corporate Ownership and Control: The Large Corporation and the Capitalist Class', *American Journal of Sociology* 79, 5 (March 1974): 1073–119.

14 Scott, J. *Corporate Business and Capitalist Classes* (Clarendon:Oxford University Press, 1997), p.313.

15 See Zeitlin, M. *The Large Corporation and Contemporary Classes* (Cambridge: Polity Press, 1989); Hamilton, N. *Limits of State Autonomy* (Princeton: Princeton University Press, 1982); Hazari, R.K. *The Structure of Corporate Private Power* (New Delhi: Planning Commission of India, 1966). Bagchi A. K. *Private Investment in India 1900–39* (Cambridge: Cambridge University Press, 1972).

16 *Directly Unproductive Profit-seeking Behaviour* (DUP) arises in a situation where the state sets up a system of controls such that profits arise out of an actor's interaction with this control system and the bureaucrats who operate it, rather than activities which create productive value. The more elaborate the system of controls are, the greater the amount of resources that are diverted from direct-productive to direct-unproductive activities. See Bhagwati, J. N., 'Directly-unproductive (DUP) activities', in *Journal of Political Economy,* October, 90, 1982.

17 The developmental state paradigm takes as its epistemological starting point, the core of 'modernisation theory' as developed by Weber, Parsons, Geschenkon *et al*. While it diverges significantly from the mainstream American renditions of modernisation theory as developed by Almond and Verba, it does accept, and builds upon some of the central assumptions of modernisation theory in the Weberian tradition. For a discussion of its roots, see Evans, P. *Embedded Autonomy* (New Jersey: Princeton University Press, 1995).

18 In some ways, the institutionalists focus on the corporate form *in isolation from* the general dynamics of capitalism reverses the problem associated with versions of Marxist analysis which tend to focus away from the specificities of different organisational forms. While both positions can be defended from within their respective theoretical schemes, both pose a problem for analysing or assessing the impact of specific organisational forms under capitalism.

19 'Alfred D. Chandler, Jr., defines the modern business enterprise as an economic institution that owns and operates a multiunit system and that relies

on a multilevel managerial hierarchy to administer it. The definition is not only simple but powerful; it clearly brings out the essential nature of the modern firm, namely its hierarchical structure, hints at the resulting centralisation of assets within a few large industrial companies and focuses sharply on the basic research question. When this definition is accepted, the study of the modern firm becomes a study of when, where and why business hierarchies were established...' See Herman Daems, "The Rise of the Modern Industrial Enterprise: A New Perspective", p. 203, in A. D. Chandler, Jr. and Herman Daems (eds) *Managerial Hierarchies: Comparative Perspectives on the Rise of the Modern Industrial Enterprise*, (Cambridge Mass., and London, 1980 Harvard University Press).

20 It is possible however to apply the approach in a more dynamic fashion, or to explain the existence of a wide range firm structures in a single capitalist economy. As examples, see Chang (1994) on South Korea.

21 For a long time, this argument has been advanced by the dependency writers as well as French regulation theorists in the context of Western economies. Since the onset of globalisation and the hegemonic rise of the 'convergence hypothesis', the argument has found resonance in a much wider community of scholars (Berger and Dore, 1996). Broadly speaking, there are two versions of the convergence hypotheses, both of which are particularly relevant in the context of neo-liberal reforms in the Third World. One version proposes the inevitability of the convergence of all national systems towards the Anglo-American model; the other version does not argue a logical inevitability, but attempts to demonstrate empirically that this is in fact the case. For a critique of the hypothesis, see the essays in Berger and Dore (1996), especially those by Boyer, Dore, Gourevitch and Streeck).

2 Corporate Structures, Corporate Control, Corporate Power: Some Conceptual Explorations

1 The earliest and clearest statement that indicates this is found in German corporate law. The German Stock Corporation Act of 1937 contained a provision which made the management board responsible not only for the shareholders' interest, but also for that of the workforce and the public good (Hopt, 1998:237).

2 In this famous case, the Dodge Brothers had sued the Ford Motor Company in their capacities as shareholders, with the allegation that Henry Ford, who controlled Ford's board of directors, was not sufficiently concerned with the welfare of its shareholders. After paying $1.2 million in dividends on $2 million on of capital, Henry Ford had decided that Ford would suspend further dividend payments indefinitely. At the time, the company was retaining $58 million in profits, allegedly to expand its business and lower the price of its products. Mr. Ford was quoted in the press as saying that the purpose of the corporation was to produce good products cheaply and to provide increasing employment and good wages and 'only incidentally to make money'. The Dodge Brothers asserted that the shareholders owned the enterprise and they were entitled to force the directors to pay out some of their accumulated profits. The court decided in favour of the plain-

tiff, asking Henry Ford to pay out the dividends as demanded by Dodge Brothers.

3 Allen, W. T. "Our Schizophrenic Conception of the Business Corporation", in R. Monks and N. Minow, *Corporate Governance* (Cambridge, Mass: Blackwell Publishers, 1995).

4 This was followed in 1855 by the Limited Liabilities Act. As is well known, the limited liability concept was a rather innovative legal mechanism through which directors and other shareholders were made to bear only a limited liability for all company debts.

5 Germany adopted a far more prescriptive and tightly controlled model which lacked the flexibility of English common law. Shareholders' interests were represented and protected by a board of supervisors, quite separate from the management of the firm. Scandinavian countries also adopted the basic German model, heavily circumscribed by the concept of societal control on the corporation. See Charkham, Jonathan P., *Keeping Good Company: A Study of Corporate Governance in Five Countries* (Oxford: Clarendon Press, 1994).

6 See the various essays in the *Cambridge Journal of Economics*, 1998, vol. 22.

7 Note that the model presented here is extremely stylised and there are many variations in the relationships between holding companies and subsidiaries within and across countries.

8 In sifting through these various forms of corporate control, we should keep in mind that the need for inter-corporate control arises from the need to 'abide' by the anti-monopolistic concerns of society and perhaps more importantly, to protect the individual pieces of a corporate empire from takeover threats. When I examine the Indian corporate structures in detail, we shall note the existence of particularly complex and interlocutory structures that are highly capable of protecting smaller units from takeover threats. The question we would need to ask in that context is why such protective structures exist in economies like India, where takeover threats are fairly low.

9 'The core element of this group is the managerial hierarchy which centralises management perspectives, co-ordinating performance and structural adjustments . . . the group expresses the hierarchical principle in its federal structure, and hence by its very nature, presents itself in a variety of forms. . . . There is then no "unifying desirable characteristic" (or virtus), but rather a mutable, highly differentiated morphology, finding its unitary form either in its transactions or in its organisation, depending on the ends that the regulatory centre wishes to attain' (Sapelli, 1990:198).

10 *Transaction costs* are all costs associated with the design, implementation and monitoring of voluntary contracts in market economies. These costs, which Williamson describes as being 'akin to frictions in physics', arise in the absence of 'hierarchies' or organisations to monitor individual contracts. Factors that increase the incidence of transactions costs are (1) that economic agents act with bounded rationality, (2) that economic agents are opportunistic and (3) that there exists asset specificity. See Williamson (1985) for a discussion.

11 See Sugarman, D. and Gunther Teubner, *Issues in the Governance of Complex Groups*: introduction (Baden-Baden: Nomos Verlag Ges; Firenze: European University Institute, 1990) p.20

12 One has to be really cautious in making this claim. While in these economies the regulation of corporations has been limited, the relationship between state and capital have been far from *liberal*; in particular, the role played by the state in augmenting corporate profitability (especially of large capital) is indeed much more pro-active and significant than that conceptualised by neo-classical economics.
13 Excerpted from *Made in America: Regaining the Productive Edge*, The Massachusetts Institute of Technology Commission on Industrial Productivity, 1989, cited in Hampden-Turner and Trompenaars, 1993:184.

3 Corporate Capital in Colonial India: Genesis, Structure and Transformation

1 Bagchi, A. K. "European and Indian Entrepreneurship, 1900–30", in *Elites in South Asia* edited by Edmund Leach and S. N. Mukherjee (Cambridge, Cambridge University Press, 1970); Ray, R. K. *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).
2 Markovitz, C. *Indian Businessmen and Nationalist Politics 1931–39* (Cambridge: Cambridge University Press, 1985); Kochanek, S. *Business & Politics in India* (Berkeley: University of California Press, 1974).
3 Lal, D. *Cultural Stability and Economic Stagnation: India, c.1500 BC – AD 1980* (Oxford [England]: Clarendon Press; New York: Oxford University Press, 1988).
4 Morris, D. "Indian Industry and Business in the Age of Laissez-Faire" in *State and Business in India: a Historical Perspective*, edited by Dwijendra Tripathi (New Delhi: Manohar Publications, 1987).
5 Desai, Ashok V. "The Origins of Parsi Enterprise", in *Indian Economic and Social History Review*, vol (4), 1967.
6 Ray, R. K. *Entrepreneurship and Industry in India 1800–1947*, pp. 65–7.
7 One major problem in comparing rupee and sterling share of paid-up capital lay in the continuous fluctuations of the exchange rate. Also, since much of the Indian corporate sector at this time was controlled by foreign interests, rupee and sterling shares of capital should not be equated with foreign and Indian interests.
8 A. K. Sur, *Diamond Jubilee Volume*, the Calcutta Stock Exchange.
9 As Lokenathan explains, given the 'imprimatur' of the managing agency system, stocks floated by managing agents were invariably oversubscribed within a day or two of the prospectus issue. Oversubscription and the existing sharemarket regulations made it simple for a managing agency to split up shares in such a way that it could control the company in spite of owning as little as 10 per cent of the stock. All it had to ensure was a large percentage of relatively small stockholders, friends or otherwise, who would gladly give their voting power to the managing agents for an assured annual dividend.
10 Ghosh, S. K. 'Indian Bourgeoisie and Imperialism' in *Economic and Political Weekly*, Special Number, November 1988, 2445–58.
11 Leading industrialists like G. D. Birla were particularly notable. In one of his letters to a friend, he wrote, 'I need hardly say I am a great admirer of Gandhiji. In fact I am one of his pet children. I have liberally financed his

khadi (cottage industry) movement and untouchability activities . . . I wish I could convert the authorities to see that he is greatest force in the side of peace and order. He alone is responsible for keeping the left wing in check' (Birla, 1953:56–7).

12 See Birla's quote above.

13 Interlocking directorates refers to the practice of individuals having multiple directorships and there being an overlap of such directors on the boards of firms (both within a given business house or conglomerate and/or across them).

14 'The Great Firms, were possessed of large resources disposed of through a large number of branches scattered throughout India, and occasionally abroad, and involved simultaneously in a large number of lines of trade and economic endeavour. . . . It is perhaps best not to think of them as single firms, since typically they were a conglomerate of interacting firms belonging to closely-related members of one family' (Timberg, 1994:129). 'Each branch of the firm functioned as a separate unit – though several branches in the same town might be under the general supervision of a single clerk. Each branch manager had full authority to run his branch as he saw fit'. (Timberg, 1994:132).

15 'Why did the Indian houses prove so much more forward than the expatriate firms in manufacturing the newly profitable industrial products for the domestic market? It was not that the latter did not possess the necessary marketing channels. But during the Depression, the expatriate firms which had a strong presence in the inland trade were compelled by falling profits to withdraw their presence from the interior to the colonial ports, leaving the entire inland business to the bazaar nexus of the shroffs and arhatiyas. The new Indian industrial houses had more ramified connections in the bazaar, were better able to mobilise financial resources by shifting investments from the depressed trade sector, and were altogether less deterred by the business difficulties of the period as they were impelled by the great determination, grit and growing commitment to the process of Indian industrialisation' (Ray, 1994:56–7).

16 'In terms of profitability the two major export industries jute and tea were going down steadily in the thirties, while a variety of protected industries . . . were experiencing investments booms on account of rising profits at the end of the depression' (Ray, 1994:56)

17 Ray (1994) makes the same argument as Goswami. For a similar argument in the context of Mexico, see Haber (1989).

18 The key provisions of this act with respect to managing agencies included: 1) a limit on the term of a managing agent up to a maximum of twenty years (and the right of shareholders to remove the managing agent in the case of a non-bailable offence); 2) no provisions for compensation to managing agents except in the case of the termination of the contract due to a liquidation of the firm (which was not due to negligence on the part of the managing agent); 3) the elimination of the ability of managing agents to transfer agreements; 4) the acknowledging of three distinct sources of remuneration for managing agents (viz., commission, office allowance and payment for other services) and a recommendation that the commission to agents be based upon a percentage of the net profit (rather than gross profits, sales,

output, etc.); 5) a restriction on managing agents appointing more than one third of the directors; 6) a prohibition on guaranteeing loans and investing in companies in which the managing agent has an interest (without the unanimous approval of the board); 7) a prohibition on loans to managing agents and members of their boards of directors and 8) a prohibition on managing agents engaging in any business which was similar to or competed with the managed firm (Sharma and Chauhan, 1965:185–6).

4 Corporate Capitalism in Independent India: the Interventionist Model and its Contradictions

1. The confrontation of 'development' and 'growth' has been and continues to be at the centre of the development debate. Broadly speaking, growth implies a sustained increase in the volume of output and income of a society over time. This notion is not concerned with the distributive implications of income expansion. Development, on the other hand, is a more comprehensive notion, comprising growth, distribution, and a general increase in the standard of living of all classes, especially the weaker ones (Myrdal, 1957; Chapter 2).
2. Partly because of its association with the Communist Party, and partly because of the violent tendencies inherent in grass-roots mobilization in a situation of gross inequities, the movements led by the radical faction were becoming increasingly violent. This brought tremendous opposition from Gandhi, not only because it went against his principles of non-violence, but also because of his opposition to a Communist alternative. Gandhi's opposition was shared by the conservative faction, and was successful in significantly moderating Jawaharlal Nehru's committed socialist stance, even though it could not reduce the strength of the radical faction as a whole (Frankel, 1978:65). The strength of this radical faction, and Nehru's commitment to it, were reinforced immediately after Independence when Nehru, 'in a striking departure from Gandhi's strategy – and his own earlier prudence – permitted a radical formulation of the Congress Party's ultimate goals.' (Frankel, 1978:68). The Congress Committee on *Objectives and Economic Programs* passed a resolution that provided for substantial land reforms, nationalization of existing private enterprise (particularly monopolies) and the establishment of heavy industries under public ownership. In addition, the Committee envisaged that the state would exercise substantial control on the functioning of private enterprise (Frankel, 1978:68).
3. These linkages were not equally strong or influential in policy-making. The linkage of the radical faction to the urban and agrarian poor was weak and amorphous, while the industrial elite was obviously much more organised in representing itself. Recently however a series of studies on the nature of grass-roots mobilisation during the period of state formation have brought to light the fact that the extent of involvement of the rural and agrarian poor was quite substantial, even though localised and amorphous (Guha, 1984).
4. The attrition of the radical faction began almost immediately after Independence, despite the dramatic resolution passed by the Congress in 1947 under

Nehru's leadership. One reason was Nehru's political office. The second reason was a very significant increase in the membership of the Congress Party at the local and village levels, where most of the members came from the propertied classes. Third, the conservative faction within the Congress moved for and was able to pass a resolution that 'no member of the Congress Party could be the member of any other political party, communal or other, which has separate membership, constitution or program'. This was directed at, and succeeded in considerably attenuating the strength of the Congress Socialist Party whose members were all members of the workers' and peasants parties – formal and informal – and were linked to the Forward Bloc, the party of the radical nationalists of Bengal (Frankel, 1978:70–2).

5 Nehru, according to some authors, was 'co-opted' by an alliance between the political and industrial elite led by Mahatma Gandhi and G. D. Birla. (Chandra, 1978). 'Jawaharlal Nehru's rhetoric of socialism had already been assessed at its true worth by G. D. Birla and the rest of the business elite as far bach as 1936. Nehru often openly indicated his willingness to go along with the designs of big business – who were the framers of the Bombay Plan of 1944 – for example, he publicly opposed the direct tax provisions of the Budget, in spite of a prior agreement to the contrary' (Bagchi, 1991:612).

6 The goals of the Act were several, including: 1) regulating private industrial development in accord with government planning; 2) directing investment to priority areas; 3) discouraging economic concentration; 4) encouraging the dispersal of industry to under-developed regions; 5) the promotion of small scale and cottage industries; 6) optimising scarce foreign exchange resources; and 7) facilitating government takeover of firms not operating in the public interest.

7 Government of India, *Second Five Year Plan* (New Delhi, 1955).

8 These included arms and ammunitions, atomic energy, iron and steel, heavy castings, heavy plants and machinery for iron and steel, mining and machine tools, heavy electrical plants, coal and lignite, mineral oils, various mining activities, aircraft, rail and air transport, shipbuilding, communication devices (telephones, telegraphs) and the generation and distribution of electricity.

9 These included aluminium and all other minerals and non-ferrous metals not included in Schedule A, machine tools, ferro-alloys and tool steels, basic and intermediate products for the chemical industry (dyestuffs, drugs, plastics), antibiotics and essential drugs, fertilisers, synthetic rubber, carbonisation of coal, chemical pulp, and road and sea transport.

10 In addition to their ability to exert control over firms through equity holdings, PFIs also held considerable powers as lenders. These included: 1) the right to appoint one or two nominees to the board of directors (generally a total of only two nominees are appointed by all institutions combined); 2) the right to require the borrowing company to broaden its board of directors; 3) the right to approve the (re-)appointment of the managing director; 4) the right to approve certain other key appointments (e.g., finance director, technical director); 5) the right to specify what matters may be submitted for the board's approval; 6) the right to restructure the top management set-up; 7) the right to approve selling/purchasing arrangements; 8) the right to appoint management/technical consultants and auditors who will report directly to

the shareholders; and 9) in the case of the IFC, the right to take over management in some circumstances (Gupta, 1989:129–32).

11 Prof. R. K. Hazari has defined a business house as follows:

'A business house may be defined as consisting of units which are subject to decision-making power of common authority. There may be a wide range of variation in the degree of control or influence which the decision-making authority exercises over the different units. The decisions by this authority generally cover prices, investments, production, purchases and sales, employment and labour. The implementation of the policies and working out of the details may be delegated to subordinate authorities, but the extent of the delegation and the allocation of functions at various levels are themselves matter of policy.' (Hazari, 1966:5).

12 Not surprisingly, it is rather difficult to obtain data on shareholding patterns of Indian companies for this period. It is only since the late eighties that the Bombay Stock Exchange Directory has begun to publish such data. The data presented in this table is mostly for 1989–90 and some for 1991–92.

13 There are primarily two mechanisms through which inter-corporate investments occur. The first is direct interlocking of equity between two companies belonging to the same house. The second is building circular chains of investment between companies of the same group.

14 See '*Performance of Assisted Companies*' published by both ICICI and IDBI, various years.

15 This analysis is based on the share distribution schedules obtained from the companies. For purposes of obtaining the share of public sector funds, the shareholdings of insurance companies, term lending institutions, UTI, nationalised banks, central and state governments and government companies have been taken together.

16 The purpose of having nominee directors, in the opinion of the Dutt Committee, was twofold: to help prevent economic concentration and to ensure that the public interest and not merely private profit guided corporations. The functions which they are assigned are succinctly summarised by one author as follows:

1. They should be able to devote their whole-hearted attention to the affairs of the firms on whose boards they are nominated.
2. They should not only safeguard the interests of the institutions, but also serve the interests of sound public policy.
3. They should be accountable to the institutions which they represent.
4. They should keep themselves fully acquainted with the affairs of the concern. Without undue interference in day-to-day affairs, they should give constructive suggestions to the management in all-important operational matters.

Any abuse of powers by the promoters and pursuit of policies detrimental to the interests of the concern like diversion of funds, etc. should be prevented by the nominee director (Sengupta, 1983:222–3).

17 Several committees were set up at this time, enquiring into particular cases of investment by public financial institutions. The Vivian Bose Commission's investigation of the government-owned Life Insurance Corporation's

investment in the Mundhra group was a case in point. The Report of the Vivian Bose Commission was also the first systematic inquiry into the informal linkages used by the private sector to circumvent policy (Bambhri 1982:153).

18 Bombay Stock Exchange Directory, July 1999.

19 See Mukherjee Reed, A. 'In a Neo-Classical Bind', *The Telegraph*, 22 September 1997.

20 These figures differ somewhat from Amsden's figures on Korean profitability. According to Amsden, profitability has varied between 10 per cent for heavy industry and 13 per cent for light industry over this period. See Amsden (1989), p.89, Table 4.2. In any case, Indian profit rates compare quite favorably with Korea.

21 'Sick' industrial firms are defined as firms which (a) have earned cash-losses for three subsequent years; (b) have high current liabilities relative to their current assets and (c) have had their net worth eroded by 50 per cent or more or have suffered an erosion of their paid-up capital. See Reserve Bank of India *Report of the Committee to Examine the Legal and Other Difficulties faced by Banks and Financial Institutions in Rehabilitation of Sick Industrial Undertakings* (1984:70).

22 Chatterjee (1980).

23 CMIE (1990 and 1996).

24 *India Development Report*, p. 201.

25 Even with more comprehensive samples, such as those based on the corporate finance statistics published by the Reserve Bank of India, a systematic relationship between growth and profitability is not readily discerned. See Rede, 1984.

26 South Korea's labour movements have, of course, been the most successful. Labour movements in other East Asian countries have also been significant. See M. Kumazawa (ed.), *Portraits of the Japanese Workplace: Labour Movements, Workers, and Managers* (Colorado: Westview Press, 1996); Hewison, K. & G. Rodan, 'The Decline of the Left in Southeast Asia', *Socialist Register* (London: Merlin Press, 1994).

27 Report of Committee on Public Financial Institutions, Government of India, 1969:186.

5 Corporate Capitalism in Post-Interventionist India: Paradoxes and More

1 'Why is the Economy Not Growing?' Cover Story, *Business Today*, November 7–21, 1997.

2 For instance, with respect to the deceleration in GDP in 1997–98, the *Economic Survey* states that 'the deterioration of growth is perhaps even worse, if one takes into account the fact that fully one percentage point of growth is attributed to the 20 percent increase in real value added in the 'public administration and defence subsector' arising chiefly from pay increases to government servants' (*Economic Survey 1999*, Ministry of Finance, Govt. of India, Chapter 1, p.1).

3 See Tables 5A.1 and 5A.2 in the Appendix to this chapter.

4 Lipietz, A. 'The Globalisation of the General Crisis of Fordism', #8413: CEPREMAP Working Papers, 1984.
5 The data here is primarily from Jalan (1992), various chapters.
6 Public expenditure rose from Rs.178 billion in 1980–81 to Rs.820 billion in 1989–90 (*Reserve Bank of India Bulletin*, various years).
7 The fiscal deficit in 1986–87 touched an all-time high of 9 per cent of the GDP (*Reserve Bank of India Bulletin*, 1988).
8 The jobless nature of the growth derived out of two factors. First, the expansion of the public sector comprised income increases for existing employees, rather than the creation of new jobs. Second, since most of this income expansion was targeted to the urban middle-class, it resulted in an increased demand for consumer durables. Since this demand expansion was also associated with the liberalization of imported inputs, most of the consumer durable production was achieved by assembling inputs imported from abroad. Some domestic production also occurred, but mostly with the help of labour-saving techniques.
9 The flight amounted to $102 million in October 1990, went down to $11 million in February 1991, but then shot up to $373 million in April and to $330 million in June. The total added up to $1.33 billion (*Economic Survey* 1992–93, cited in Kurien 1994:100).
10 Adverse selection occurs when a negotiation between two people with different amounts of information, i.e., asymmetric information, restricts the quality of the good traded. This typically happens because the person with more information is able to negotiate a favourable exchange; moral hazard occurs when a person changes behaviour to the detriment of another person, *after* an agreement has been reached.
11 IDBI, *Annual Report*, 1992–93, p.8.
12 CMIE, 1996, p.59.
13 A. Mehta, "Promoters" Bonanza At Public Cost', *Economic Times*, 1 August 1995.
14 *Business Line*, according to a study by Centre for Monitoring the Indian Economy Pvt Ltd (CMIE).
15 K. Ramesh, 'Private Placement: Promoters' Joy, Investors' Pain', *Business Line*, 28 January 1996.
16 S. Swain, 'CBI closes file on Reliance–Unit Trust Rs.945–cr private-placement deal', *Indian Express*, 23 July 1998.
17 'Shattered', *Business Today*, 17 July 1998. Also see, Bagchi, A.K. 'Globalisation, Liberalisation and Vulnerability: India and Third World', *Economic & Political Weekly*, 6 November 1999.
18 'Stress on larger role for Indian investors', *The Hindu*, 24–08–1996; 'Who's Afraid of FIIs?', *Outlook*, 31 July 1996.
19 See *India Development Report* 1997, p.134.
20 'FIIs allowed to invest in Government Debt Instruments', *Times of India*, 31 January 1997; 'Mixed Response to Removal of Curbs on FIIs', *Business Line*, 1 February 1997.
21 'FII debt funds set to cross $1.3–billion mark', *Economic Times*, 31 March 1997.
22 Singh, A. (1997), 'The Stock Market, Industrial Development and the Financing of Corporate Growth in India' in D. Nayyar (ed.), *Trade and*

Industrialisation, Oxford University Press. (1998), 'Liberalisation, the Stock Market and the Market for Corporate Control: A Bridge too Far for the Indian Economy?' in I. J. Ahluwalia and I. M. D. Little (eds), *India's Economic Reforms and Development: Essays for Manmohan Singh*, Oxford University Press.

23 Section 4 of the Act lays down the constitution of the management of SEBI. The board of members of SEBI shall consist of a chairman, two members from amongst the officials of the Ministries of the Central Government dealing with Finance and Law, one member from amongst the officials of the Reserve Bank of India constituted under section 3 of the Reserve Bank of India Act, 1934, two other members to be appointed by the Central Government, who shall be professionals and interalia have experience or special knowledge relating to securities market.

24 *Business Today*, 22 February 1992.

25 Section 17 of the Act empowers the Central Government to supersede SEBI, if on account of grave emergency SEBI is unable to discharge the functions and duties under any provisions of the Act, or SEBI persistently defaults in complying with any direction issued by the Central Government under the Act, or in the discharge of its functions and duties under the Act and as a result of such default. the financial position of SEBI or its administration has deteriorated, or in public interest.

26 The more important of these with respect to the promotion of more responsible corporate governance include: *Guidelines For Disclosure And Investor Protection* (1992); *Prohibition Of Insider Trading Regulations* (1992); *Form Of Annual Statements Of Accounts And Records Rules* (1992); *Foreign Institutional Investor Regulations* (1995); *Venture Capital Funds Regulations* (1996); *Mutual Funds Regulations* (1996); *Substantial Acquisition Of Shares And Take-Overs Regulation* (1997).

27 'It is a harsh reality that millions of investors have turned away from the capital markets after being deceived by unscrupulous companies, fly-by-night operators, high premium issues and siphoning (out) of funds by promoters immediately after the public issues, etc. The investor has suffered losses so badly in the market that he is no more willing to further invest in the capital market. 'Policy makers either in the government or in the SEBI board realise the ground realities of the integrity and quality of promoters and issuers who were given full freedom of access to raise capital under the free pricing mechanism. It has brought havoc in the Indian capital market which is in an early stage of development and growth', quoted from a report by a Parliamentary Standing Committee on Finance, in *The Economic Times*, 10 March 1997. See also 'No Direction In The Capital Market', *Times of India*, 13 January 1997.

28 As a study of 1400 companies in October 1996 indicated, high dividend payouts and good corporate growth were in fact inversely related. High dividends were paid by companies which performed quite badly, while well-performing companies paid fairly little by way of dividends. The problem is further compounded by the fact that small shareholders have little or no say in profit appropriation. See 'Dividend Yields – The High-Payout-Low-Growth Syndrome', *Business Li*ne, 13 October 1996.

29 'As of March 31, 1994, the Industrial Development Bank of India (IDBI), the Industrial Credit and Investment Corporation of India (ICICI), and the

Industrial Finance Corporation of India (IFCI) have run up a list of 99 defaulters between them who had failed to pay the institutions over Rs.2 billion that was long overdue. Some of the top industrial houses in the country figure on the list of defaulters, some more than once and some several times over. Yet, even when the group has defaulted more than once, institutions happily channelled public funds into other or similar schemes set up by the very industrialists' in 'Who Does the Money Belong to Anyway', *Financial Express*, 31 July 1994.

30 'The analysis of balance sheets of 7295 companies (as on March 31, 1997) shows: (a) The equity capital of the corporate sector was to the extent of 11 per cent, while loan/borrowing was as high as 44 per cent of the total assets; (b) the dividend on equity was about 9 per cent while the interest to borrowing ratio was about 20 per cent; (c) the profit margin of non-financial companies was about 40 per cent and if the financial companies are included it was about 44 per cent; (d) return of equity was 24.5 per cent. These parameters clearly indicate that there is sufficient scope for expanding the equity capital', J. Dash, 'Performance of the Corporate Sector 1996–97', in *Economic and Political Weekly*, 31 July–6 August 1999. The *India Development Report* of 1997 comes to the same conclusion. See J. Sarkar and P. Agrawal, 'Banking: The Challenges of Deregulation', in K. Parikh (ed.), *India Development Report* 1997 (Delhi: Oxford University Press and Indira Gandhi Institute of Development Research), p. 206.

31 See Table 5A.1 in the Appendix to this chapter.

32 In an important deviation from the Foreign Exchange Regulation Act (FERA), there is a complete elimination of criminal proceedings for violations of FEMA. Only adjudication and penalty up to twice the contravention involved have been prescribed as against five times the contravention and simultaneous criminal proceedings in FERA. In cases where the contravention cannot be quantified, the penalty is up to only Rs.100,000. However, the adjudicating authority has been given the powers of detention for failure to pay the penalty within the prescribed time limit, a provision that is not there in FERA. The Enforcement Directorate will be the agency to enforce FEMA. In a major deviation from FERA, the Central Government has been given the powers to suspend/relax any permission granted or restriction imposed under the new law if it considers it to be in the public interest. Under FERA, the statute is supreme and the Government cannot notify any suspension/relaxation of provisions of the Act. This provision now gives overriding powers to the Government. The FERA board, which is the appellate authority, is sought to be disbanded and a new Appellate Tribunal for Foreign Exchange is sought to be established. Adjudication will also be done by authorities appointed by the Central Government. The FEMA Bill envisages repeal of FERA, but offences committed under the repealed Act shall continue to be governed by the provisions of the repealed Act as if that Act had not been repealed. See 'FEMA to allow deals in some capital accounts', *Business Line*, 31 July 1998.

33 Government of India, Ministry of Commerce, *EXIM Policy 1997–2002*.

34 RBI press release dated 3 June 1997.

35 T. Khanna & K. Palepu, 'Emerging Market Business Groups, Foreign Investors, and Corporate Governance', NBER Working Paper No. W6955, issued February 1999.

36 The Department of Company Affairs, *Annual Report*, 1998–99.

37 The data is taken from a database being compiled at the Indian Institute of Management, Calcutta. As the author warns us, caution must be exercised in interpreting this data. Firstly, the data for the pre-1991 period is not strictly comparable to the post-reform data, which is far more comprehensive. The pre-1991 data is based on announcements in fortnightly business journals and company law board files only. Secondly, if a firm has three bidders and the press reports these at different points of time, the database will have three different entries. This provides for some firms appearing in the database two or three times. Thirdly, no claim is made that the merger is actually achieved or realised, since many bids are fruitless or take years to be consummated.

38 'Transition At ITC', Editorial, *Business Line*, 13 December 1995.

39 'There is a renewed effort to permit BAT Plc, the UK-based multinational, to hike its holding in ITC, its Indian joint venture. The initiative to see this through has been taken up by over 40 parliamentarians who have recommended that UTI be allowed to square up its holding in ITC. While the MPs make no mention of BAT as a possible buyer of the stock, it is learnt that UTI had offered a portion of its stock to BAT at a premium late last year. This deal had been struck down by the ministry of finance then.... Last November, the finance ministry had directed UTI against selling a part of its holding in ITC to BAT as it would lead to a larger presence of the foreign promoter. UTI had intended such a sale as it needed to reduce the equity weight in some of its schemes. While rejecting UTI's plan, the finance ministry had argued that a higher BAT holding – from about 32 per cent at present – would lead to increased tobacco capacity, which was undesirable on health grounds. This argument was considered invalid given that ITC had doubled its capacity a few months before. The MPs, who have said that UTI should be allowed to go about with its deals, as the trust, 'passing through an acute financial crisis,' is in need of funds.... These developments come at a time when Rothmans and BAT have decided to merge worldwide. If UTI is permitted to sell its equity – 14 per cent – to BAT, the UK company's holding would go up from 32 per cent to 46 per cent. With an additional 2 per cent coming in from Rothmans, the holding would increase to about 48 per cent, giving it near complete control over ITC. This obviously brings into reference the foreign equity cap for the cigarette sector, which is 100 per cent.' See 'MPs batting for UTI May Help BAT up stake in ITC', *Economic Times*, 18 January 1999.

40 'Learn from the Indal experience', *Economic Times*, 25 September 1998.

41 'Sebi should ask Sterlite, Alcan to start once again', *Economic Times*, 10 June 1998.

42 'The Market for Corporate Control', Editorial, *Economic & Political Weekly*, 6 November 1999.

43 Names of the members of the committee: Shri Kumar Mangalam Birla, Chairman, Aditya Birla group – Chairman of the Committee; Shri Rohit Bhagat, Country Head, Boston Consulting Group; Dr. J. Bhagwati, Joint Secretary, Ministry of Finance; Shri Samir Biswas, Regional Director, Western Region, Department of Company Affairs, Government of India; Shri S. P. Chhajed, President of Institute of Chartered Accountants of India; Shri Virender Ganda, President of Institute of Company Secretaries of India; Dr. Sumantra

Ghoshal, Professor of Strategic Management, London Business School; Shri Vijay Kalantri, President, All India Association of Industries; Shri Pratip Kar, Executive Director, SEBI – Member Secretary; Shri Y. H. Malegam, Managing Partner, S. B. Billimoria & Co; Shri Narayanan Murthy, Chairman and Managing Director, Infosys Technologies Ltd.; Shri A. K. Narayanan, President of Tamil Nadu Investor Association; Shri Kamal Parekh, Ex-President, Calcutta Stock Exchange; Dr. R. H. Patil, Managing Director, National Stock Exchange Ltd.; Shri Anand Rathi, President of the Stock Exchange, Mumbai; Ms D. N. Raval, Executive Director, SEBI; Shri Rajesh Shah, Former President of Confederation of Indian Industries; Shri L. K. Singhvi, Sr. Executive Director, SEBI; Shri S. S. Sodhi, Executive Director, Delhi Stock Exchange.

44 Halbe, S. R. 'Company law reform loses its way', *Business Standard*, 7 September 1999.
45 *Business World*, 25 December 1996–7 January, 1997.
46 *Business India*, 23 September–6 October 1996.
47 *Business World*, 25 December 1996–7 January 1997.
48 G. Hamel & C. K. Prahalad *Competing for the Future*, Harvard Business School Press, 1996.
49 *Business World*, 1–15 May 1997.
50 *Business Today*, 7 January–2 February 1998.
51 *Business Today*, 7 January–2 February 1998.
52 Mukherjee Reed, A. 'The State As Charade: Political Mobilisation in Today's India', *Socialist Register*, 1997.
53 'Building Bridges', *Business Today*, 22 July–6 August 1993.
54 Basu *et al* (1993).
55 'Building Bridges', *Business Today*, 22 July–6 August 1993.
56 *The Economic Times*, 3 August 1996
57 Government of India, Ministry of Finance, *The Economic Survey 1998–99*, Chapter 6, p.3.
58 CMIE, *The Indian Corporate Sector*, 1996, p.50.
59 The figures are estimated from CMIE's data on some major restructuring efforts in the private sector, and VRS schemes of the public sector discussed in the media. CMIE, *The Indian Corporate Sector*, 1996, p.50, Table52.
60 Government of India, Department of Industrial Development, *Annual Report 1998–99*.
61 Dunlop India Limited is a major case in point. See story entitled 'Tyre major Dunlop India declared sick by Board for Industrial & Financial Reconstruction', *The Economic Times*, 23 June 1998.
62 Narayanan, M. S. 'Industrial Sickness: Review of BIFR's Role', *Economic & Political Weekly*, 12 February 1994.

6 The Paradox of Profits: Some Tentative Conclusions

1 In general, it has been observed that 'investments in research and development (R&D) fell as a proportion of GDP through the decade of the 1980s; the share of the private sector in industrial R&D fell from 58 per cent in 1980–81 to 54 per cent in 1990–91' (Kaplinsky, 1997:686).

2 Prime Minister's Council on Trade & Industry, 'Reforms in the Financial Sector and Capital Markets', Chapter 7, para 7.4.
3 *Institutional Investment Report* – Financial Assets and Equity Holdings, Vol. 3, no. 1, August 1999.

Bibliography

Agrawal, P. 'Labour Policy: Striking A Balance' in K. Parikh (ed.) *India Development Report* (Delhi: Oxford University Press, 1997).

Ahluwalia, I. J. *Industrial Growth in India: Stagnation since the Mid-Sixties* (New Delhi: Oxford University Press, 1985).

Ahluwalia, M. 'India's Economic Reforms', in R. Cassen and V. Joshi (eds) *India: The Future of Economic Reforms* (Delhi: Oxford University Press, 1995).

Alavi, H. 'The Structure of Peripheral Capitalism' in H. Alavi and T. Shanin (eds) *Introduction to the Sociology of Developing Societies* (New York: Monthly Review Press, 1982).

Alavi, H. 'Colonial and Post-Colonial Societies', in T. Bottomore (ed.) *A Dictionary of Marxist Thought* (Cambridge, Mass.: Harvard University Press, 1983).

Alchian, Armen A. and H. Demsetz, 'Production, Information Costs, and Economic Organization', *American Economic Review* vol. 62, no. 5, Dec. 1972.

Allen, William T. 'Our Schizophrenic Conception of the Business Corporation', in R. A. G Monks and N. Minow (eds) *Corporate Governance* (Cambridge, Mass.: Blackwell Publishers, 1991).

Amin, S. 'Accumulation and Development: A Theoretical Model' *Review of African Political Economy*, 1974, pp. 9–26.

Amsden, A. H. 'The Acquisition of Technological Capability in South Korea', Mimeo (Washington, DC: Development Research Department, Productivity Division, World Bank, 1985a).

Amsden, A. H. 'The State and Taiwan's Economic Development', P.B. Evans, D. Rueschemeyer, and T. Skocpol (eds) *Bringing the State Back In* (Cambridge: Cambridge University Press, 1985b).

Amsden, A. H. 'Republic of Korea Stabilization and Adjustment Policies and Programmes', *Country Study* No. 14 (Finland: World Institute for Development Economics Research of the United Nations University, 1987).

Amsden, A. H. *Asia's Next Giant.* (Oxford: Oxford University Press, 1989).

Bagchi, A. K. 'European and Indian Entrepreneurship, 1900–30', Leach, E. and S. N. Mukherjee (eds) *Elites in South Asia* (Cambridge: Cambridge University Press, 1970).

Bagchi, A. K. 'Long-term Constraints on Industrial Growth in India 1951–68' in M. Kidron and E. A. G. Robinson (eds) *Economic Development in South Asia* (London: Macmillan, 1970).

Bagchi, A. K. 'The Theory of Efficient Neocolonialism', *Economic and Political Weekly,* VI (30–32), Special Number, July 1971.

Bagchi, A. K. *Private Investment in India: 1900–39* (Cambridge: Cambridge University Press, 1972).

Bagchi, A. K. (ed.) *Economy, Polity and Society* (Oxford: Oxford University Press, 1988).

Bagchi, A. K. *The Political Economy of Underdevelopment* (Cambridge: Cambridge University Press, 1982; 1992).

Bagchi, A. K. 'The Discourse of Planning and Political Economy in Post-Colonial India', *Economic and Political Weekly,* Annual Number, March; 1991.

Bagchi, A. K. 'Rent Seeking, New Political Economy and the Negation of Politics', *Economic and Political Weekly,* 21 August 1993, pp. 1729–36.

Bagchi, A. K. 'European and Indian Entrepreneurship in India 1900–30', in Ray, R. K. (ed.) *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).

Bagchi, A. K. 'Globalisation, Liberalisation and Vulnerability: India and Third World', *Economic and Political Weekly* 6 November 1999.

Baig, N. *The Pattern of Company Management In India* (Aligarh: Navman Prakashan, 1971).

Baker, C. Johnson, G. and A. Seal (eds) *Power, Profit and Politics: Essays on Imperialism, Nationalism and Change in Twentieth Century India* (Cambridge: Cambridge University Press, 1981).

Balassa, B. *et al.* (eds) *In Development Strategies in Semi-industrial Countries* (Baltimore, Md.: Johns Hopkins University Press, 1982)

Bambhri, C. P. *Politics in India* (New Delhi: Asia Publishing House, 1982).

Baran, P. and E. J. Hobsbawm, 'The Stages of Economic Growth', *Kyklos*, 14, 1961, pp. 234–42.

Baran, Paul A. and Paul M. Sweezy *Monopoly Capital: an Essay on the American Economic and Social Order* (New York: Modern Reader Paperbacks, 1968).

Bardhan, P. *The Political Economy of Development* (Oxford: Oxford University Press, 1984).

Bardhan, P. 'The new institutional economics and development theory: a brief critical assessment', *World Development* v. 17 Sept 1989, p. 1389-95.

Bardhan, P. 'Economics of Development and the Development of Economics', *Journal of Economic Perspectives*, vol. 7, no. 2, pp. 129–42, Spring 1993.

Basu, T. *et al. Khaki Shorts Saffron Flags* (Hyderabad: Orient Longman, 1993).

Bengal Chamber of Commerce, *Report of the Industrial Survey Committee*, (Calcutta: 1946 and 1948).

Berger, S. and R. Dore (eds), *National Diversity and Global Capitalism* (Ithaca and London: Cornell University Press, 1996).

Berle, Adolf A. and Gordiner C. Means, *The Modern Corporation and Private Property* (New York: Macmillan, 1932).

Bettleheim, C. *India Independent* (New York: Frank Cassell, 1968).

Bhaduri, A. *The Economic Structure of Backward Agriculture* (Delhi: Macmillan, 1984).

Bhaduri, A and D. Nayyar, *The Intelligent Person's Guide to Liberalization* (Delhi: Penguin, 1996).

Bhagwati, J. and P. Desai, *India: Planning and Industrialization* (New Delhi: Oxford University Press, 1970).

Bhagwati, J. N. 'Directly-unproductive (DUP) activities', *Journal of Political Economy,* October, vol. 90, 1982.

Bhagwati, J. N. 'Export-Promoting Trade Strategy: Issues and Evidence,' *World Bank Research Observer*, vol. 3 (1), pp. 27–57. (1988)

Bhagwati, J. N. and T. N. Srinivasan. '*Outward Orientation and Development: Are the Revisionists Right?*' Yale University, Economic Growth Center (New Haven, Conn.: 17 September 1999).

Birla, G. D. *In the Shadow of the Mahatma: A Personal Memoir* (Bombay: Orient Longmans, 1953).

Bombay Stock Exchange Database, several years.

Bond, J and B Smit (1996): The Coevolution of the Real and Financial Sectors in the Growth Process', *World Bank Economic Review,* 10 (May 2).

Boyer, R. 'The Seven Paradoxes of Capitalism. Or is a theory of modern economies still possible?' CEPREMAP, Paper no. 9620, October 1996.

Brandeis, L. Dembitz, *Other people's money and how the bankers use it* (New York: Harper & Row, 1967).

Brenner, R. 'The Economics of Global Turbulence', *New Left Review,* no. 229, May–June 1998.

Brewer, A. *Marxist Theories of Imperialism: A Critical Survey* (London and New York: Routledge, 1990).

Buchanan, James M. *et al, Toward a Theory of the Rent-Seeking Society* (College Station Texas: Texas University Press, 1980).

Buchanan, D. H. *The Development of Capitalist Enterprise in India* (New York: Macmillan, 1934).

Cable, V. 'Indian Liberalization and the Private Sector', in R. Cassen and V. Joshi (eds), *India: The Future of Economic Reforms* (Delhi: Oxford University Press, 1995).

Cardoso, Fernando H. 'On the Characterization of Authoritarian Regimes in Latin America', in David Collier (ed.), *The New Authoritarianism in Latin America* (Princeton, NJ: Princeton University Press, 1979).

Cardoso F. and Faletto, E. *Dependency and Development in Latin America* (Berkeley, Calif.: University of California Press, 1979).

Carnoy, M. *The State and Political Theory* (Princeton, NJ: Princeton University Press, 1984).

Cassen, R. and V. Joshi (eds) *India: The Future of Economic Reforms* (Delhi: Oxford University Press, 1995)

Chandler, A.D., *The visible hand: the managerial revolution in American business,* (Cambridge, Mass. : Belknap Press, 1977).

Chandler, A. D. Jr. and Herman Daems (eds) *Managerial Hierarchies: Comparative Perspectives on the Rise of the Modern Industrial Enterprise* (Cambridge, Mass., and London: Harvard University Press, 1980).

Chandler, A. D, F. Amatori and T. Hikino (eds). *Big Business and the Wealth of Nations* (Cambridge: Cambridge University Press, 1997).

Chandra, B. 'The Indian Capitalist Class and British Imperialism', R. S. Sharma (ed.) *Indian Society*: *Historical Probings* (New Delhi, 1974).

Chandra, B. 'Jawaharlal Nehru and the Capitalist Class', *Economic and Political Weekly,* Special Number, August, 1975.

Chandra, B. *Nationalism and Colonialism in Modern India* (New Delhi: Orient Longman, 1979).

Chandra, B. *The Indian Left* (Cambridge: Cambridge University Press, 1982).

Chang, H. J. *The Political Economy of Industrial Policy* (London and Basingstoke: Macmillan, 1994).

Charkham, Jonathan P. *Keeping Good Company: A Study of Corporate Governance in Five Countries* (Oxford: Clarendon Press, 1994).

Chatterjee, R. *Union, Politics and the State: A Study of Indian Labor Politics* (New Delhi: South Asian Publishers, 1980).

Chatterji, B. 'Business and Politics in the 1930s: Lancashire and the Indo-British Trade Agreement' in *Power, Profit and Politics: Essays on Imperialism, Nationalism*

and Change in Twentieth Century India, Cambridge: Cambridge University Press, 1981 pp. 527–574.

Chaudhuri, A. *Private Economic Power in India: A Study in Genesis and Concentration* (New Delhi: Peoples Publishing House, 1975).

Chew, D. H. (ed.), *Studies in International Corporate Finance and Governance Systems: A Comparison of the US, Japan, Europe* (New York: Oxford University Press, 1997).

Clement, W. *The Canadian Corporate Elite: an analysis of economic power* (Toronto: McClelland and Stewart, 1975).

CMIE (Centre for Monitoring Indian Economy), *The Indian Corporate Sector*, 1990 1996, and 1998.

Coase, R. 'The Nature of the Firm', *Economica*, 4(1937): pp. 386–405, reprinted in G.J.Stigler and K.E. Boulding (eds) *Readings in Price Theory* (Homewood, Ill.: Richard D. Irwin, 1952).

Coates, D. *Models of Capitalism* (Cambridge: Polity Press, 1999).

Colander, David C. (ed.) *Neoclassical Political Economy: An Analysis of Rent-seeking and DUP Activities* (Cambridge, Mass.: Ballinger, 1984).

Confederation of Indian Industries, *Desirable Corporate Governance in India – A Code* (New Delhi: 1997).

Corporate Studies Group, Institute for Studies in Industrial Development, '"Functioning of the Industrial Licensing System: Capacity and Production in Organized Industry"' in *Economic and Political Weekly*, 30 April, 1983, pp. 694–706.

Demirguc-Kunt, A. and R. Levine, 'Stock Markets, Corporate Finance and Economic Growth', *World Bank Economic Review*, 10, 2 May, 1996.

Demirguc-Kunt, A. and R. Levine, 'Stock Market Development and Financial Intermediaries: Stylised Facts', *World Bank Economic Review*, 10, 2 May, 1996.

Demirguc-Kunt, A. and V. Maksimovic, 'Stock Market Development and Financing Choices of Firms', *World Bank Economic Review*, 10, 2 May, 1996.

Desai, Ashok V. 'The Origins of Parsi Enterprise', *Indian Economic and Social History Review*, vol. v (4), 1967.

Desai, P. B. *Planning in India* (Delhi: Concept Publishers, 1979).

Deshmukh, C.D. *Economic Development in India, 1946–1956* (Bombay: Asia Publishing House, 1957).

Deyo, Frederic C. (ed.) *The Political Economy of the New Asian Industrialism* (Ithaca: Cornell University Press, 1987).

DiMaggio, Paul J. and Powell, Walter W, 'The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields', *American Sociological Review*, 48, 2, April 1983, pp. 147–60.

Dutt, R. Palme *A Guide to the Problem of India* (London: Victor Gollancz, 1942).

Engels, F. *Anti-Duhring* (Moscow: Foreign Languages Publishing House, 1959).

Evans, P. *Dependent Development* (Princeton, NJ: Princeton University Press, 1979).

Evans, P. 'The State as Problem and Solution: Predation, Embedded Autonomy and Structural Change' in Haggard, S. and R.Kaufman (eds) *Politics of Economic Adjustment* (Princeton, NJ: Princeton University Press, 1992).

Evans, P. *Embedded Autonomy* (Princeton, NJ: Princeton University Press, 1995).

Evans, Peter B., D. Reuschemeyer and T. Skocpol (eds) *Bringing the State Back In* (Cambridge: Cambridge University Press, 1985).

Fama, E. and M. Jensen, 'Separation of Ownership and Control', 26, *Journal of Law and Economics*, 1983, pp. 301–26.
Federation of Indian Chambers of Commerce and Industry (FICCI), *Annual Reports: 1927–1947* (New Delhi).
Frank, A.G. 'The Sociology of Development and the Under-development of Sociology' in J. Petras and M. Zeitlin (eds) *Latin America: Underdevelopment or Revolution?* (New York: Fawcett, 1969).
Frankel, Francine R. *India's Political Economy, 1947–1977: The Gradual Revolution* (Princeton, NJ: Princeton University Press, 1978).
Friedman, M. 'The Social Responsibility of Business' *Capitalism and Freedom* (Chicago: University of Chicago Press, 1962).
Friedman, M. 'The Social Responsibility of Business is to Increase its Profits' *The New York Magazine*, September 13, 1970.
Gadgil, D. R. *Planning and Economic Policy in India* (Poona: Gokhale Institute of Politics and Economics, 1972).
Gerlach, M. L. *Alliances and the Social Organization of Japanese Business* (Berkeley, Calif.: University of California Press, 1989).
Gerschenkron, A. *Economic Backwardness in Historical Perspective* (Cambridge, Mass.: Harvard University Press, 1962).
Ghosh, S.K 'Indian Bourgeoisie and Imperialism' in *Economic and Political Weekly*, Special Number, November, 1988, pp. 2445–2458.
Gokarn, S: 'Indian Capital Market Reforms, 1992–96: An Assessment', *Economic and Political Weekly*, 31 (15, 13 April).
Gopal, M. H. *The Theory of Excess Profits Taxation* (Mysore: Bureau of Economic Research, 1947).
Goswami, O. '*Sahibs, Babus and Banias*: Changes in Industrial Control in Eastern India, 1918–50' in Ray, R. K. (ed.) *Entrepreneurship and Industry in India 1800–1947*, (Delhi: Oxford University Press, 1994).
Goswami, O. *Corporate Bankruptcy in India: A Comparative Perspective* (Paris: Organization for Economic Co-operation and Development, 1996).
Government of India, *Conference on Industrial Development in India* (New Delhi, Government of India, 1947).
Government of India, *The First Five Year Plan* (New Delhi: Planning Commission, 1951).
Government of India, *The Companies Act* (New Delhi: Ministry of Law, Department of Justice and Company Affairs, 1956).
Government of India, *The Second Five Year Plan, 1956–61* (New Delhi: Planning Commission, 1955).
Government of India, *The Third Five Year Plan, 1961–66* (New Delhi: Planning Commission, 1959).
Government of India, *Report of Justice Vivian Bose Commission* (New Delhi: 1963)
Government of India, *Report of the Industrial Development Procedures Committee* (New Delhi, 1964).
Government of India, *Report of the Monopolies Inquiry Commission*, (New Delhi, 1965).
Government of India, *Final Report on Industrial Planning and Licensing Policy* (New Delhi, 1967).
Government of India, *Report of the Industrial Licensing Policy Inquiry Committee* (New Delhi, 1969).

Government of India, *The Fourth Five Year Plan, 1969–74* (New Delhi: Planning Commission, 1970).

Government of India, *The Fifth Five Year Plan, 1974–79* (New Delhi: Planning Commission, 1976).

Government of India, *Report of the High Powered Committee on Companies and MRTP Acts* (New Delhi, 1978).

Government of India, *The Sixth Five Year Plan, 1980–85* (New Delhi: Planning Commission, 1981).

Government of India, *Report of the Committee on Trade Policies* (New Delhi: Ministry of Commerce, 1984).

Government of India, *The Seventh Five Year Plan, 1985–90* (New Delhi: Planning Commission, 1985).

Government of India, Department of Company Affairs, Ministry of Law, Justice and Company Affairs, *Annual Reports*, various years.

Government of India, Ministry of Finance, *Economic Survey* (New Delhi: various years).

Grossman, S. and O. E. Hart, 'The Costs and Benefits of Ownership: a Theory of Vertical and Lateral Integration', *Journal of Political Economy*, vol. 94, 1986, pp. 691–719.

Guha, R. *Subaltern Studies: writings on South Asian history and society* (Delhi and New York: Oxford University Press, 1984).

Gupta, L.C. *Corporate Boards and Nominee Directors*, (New Delhi: Oxford University Press, 1989).

Haber, Stephen H. *Industry and Underdevelopment: the industrialization of Mexico, 1890–1940* (Stanford, Calif.: Stanford University Press, 1989).

Habermas, J. *Legitimation Crisis* (Boston: Beacon Press, 1975).

Haggard, S. *Pathways from the Periphery: The Politics of Growth in Newly Industrializing Countries*, (Ithaca, New York: Cornell University Press, 1990).

Halbe, S. R. 'A law for the corporates and by the corporates' *Business Standard*, 8, August 1997 (a).

Halbe, S. R. 'Much ado about nothing' *Business Standard*, September 1997 (b).

Halbe, S.R. 'Company law reform loses its way', *Business Standard*, 7 September, 1999.

Hamilton, N. *The Limits of State Autonomy: Post-Revolutionary Mexico* (Princeton, NJ: Princeton University Press, 1982).

Hampden-Turner, C. and Trompenaars, A. *The Seven Cultures of Capitalism: value systems for creating wealth in the United States, Japan, Germany, France, Britain, Sweden, and the Netherlands* (New York: Currency Doubleday, 1993).

Hanson, A.H. *The Process of Planning: A Study of India's Five Year Plans* (Oxford: Oxford University Press, 1972).

Hazari, R.K. *The Structure of Corporate Private Power* (New Delhi: Planning Commission of India, 1966).

Herman, E. *Corporate Control, Corporate Power* (Cambridge: Cambridge University Press, 1981).

Holland, Daniel M. (ed.) *Measuring Profitability and Capital Costs: An International Study* (Lexington, Mass.: Lexington Books, 1984).

Hollingsworth, J. Rogers and R. Boyer (eds) *Contemporary Capitalism: the Embeddedness of Institutions* (Cambridge and New York: Cambridge University Press, 1997).

Hopt, Klaus J. *Comparative Corporate Governance: the state of the art and emerging research* (Oxford: Clarendon Press, 1998).

Huntington, S. *Political Order in Changing Societies* (New Haven, Conn.: Yale University Press, 1968).

Imai K. and H. Itami, 'Interpenetration of Organization and Market: Japan's Firm and Market in Comparison with the US', 2, *International Journal of Industrial Organization*, pp. 285–310, 1984.

Industrial Development Bank of India, *Annual Reports*, various years.

Industrial Finance Corporation of India, *Annual Reports*, various years.

Investors' India Year Book, cited in R.K. Ray, *Industrialization in India: Growth and Conflict in the Private Corporate Sector, 1914–47* (Delhi: Oxford University Press, 1979).

Jalan, B. *India's Economic Crisis: The Way Ahead* (Oxford: Oxford University Press, 1992).

Johnson, C. *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925–1975* (Stanford, Calif.: Stanford University Press, 1982).

Johnson, C. 'The Japanese Political Economy: A Crisis in Theory' *Ethics and International Affairs*, 2, 1988, pp. 79–98.

Joshi, V. and I. M. D. Little. *India's Economic Reforms 1991–2001* (Delhi: Oxford University Press, 1996).

Kahler, M. 'Orthodoxy and Its Alternatives: Explaining Approaches to Stabilization and Adjustment' in Joan M. Nelson (ed.) *Economic Crisis and Policy Choice: The Politics of Adjustment in the Third World* (Princeton, NJ: Princeton University Press, 1990).

Kambhampati, U.S. *Industrial Concentration and Performance: A Study of the Structure, Conduct and Performance of Indian Industry (1970–85)* (Delhi, Oxford University Press, 1996).

Kambhampati, U.S. 'Market structure dynamics in Indian industry', *Bulletin of Economic Research*, April 1998 v.50 no. 2, p 133(21).

Kaplinsky, R. 'India's Industrial Development: An Interpretive Survey', *World Development*, Vol 25, No 5, pp. 681–694, 1997.

Kaviraj, S. 'A Critique of the Passive Revolution', in *Economic and Political Weekly*, Special Number, November, 1988, pp. 2429–44.

Keynes, J.M. *The General Theory of Employment, Interest and Money* (London: Macmillan, 1936).

Khanna, T. and K. Palepu. 'Emerging Market Business Groups, Foreign Investors, and Corporate Governance', NBER Working Paper No.W6955, February 1999.

Kidron, M. *Foreign Investments in India* (London: Oxford, 1965).

Kling, B. 'The Origin of the Managing Agency System', in Rajat K. Ray, *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).

Knight, Frank H. *Risk, Uncertainty and Profit* (Boston, Mass.: Houghton Mifflin, 1921).

Kochanek, S. *Business & Politics in India* (Berkeley, Calif.: California University Press, 1974).

Kothari R. *Politics in India* (London: Little, Brown & Company, 1970).

Krueger, Anne O. 'The Political Economy of the Rent-Seeking Society', *American Economic Review*, vol. 64, no. 3, 1974, pp. 291–303.

Krueger, Anne O. *Foreign Trade Regimes and Economic Development: Liberalization Attempts and Consequences* (Cambridge, Mass.: Ballinger, 1978).

Kurien, C.T. *Global Capitalism and the Indian Economy* (New Delhi: Orient Longman, 1994).
Kurien, M., 'Class Character of the Indian State', in Kurien, M. (ed.) *India–State and Society* (Bombay: Orient Longman, 1975).
Kuznets, S. *Modern Economic Growth* (New Haven, Conn.: Yale University Press, 1966).
La Porta, R., F. Lopez-de-Silane and A. Shleifer. 'Corporate Ownership Around the World', *National Bureau of Economic Research*, W6625 June 1998.
Lal, D. *Cultural Stability and Economic Stagnation: India, c. 1500 BC – AD 1980* (Oxford: Clarendon Press; New York: Oxford University Press, 1988).
Lall, S. *Learning to Industrialize: The Acquisition of Technological Capability in India* (London: Macmillan, 1987).
Leach, E. and S.N. Mukherjee (eds) *Elites in South Asia* (Cambridge: Cambridge University Press, 1970).
Leibenstein, H. *General X-efficiency Theory and Economic Development* (New York: Oxford University Press, 1978).
Levine, R and S Zervos (1996): 'Stock Market Development and Long Run Growth', *World Bank Economic Review*, 10 (May 2).
Levkovsky, A.I. *Capitalism in India* (Delhi: Peoples' Publishing House, 1966).
Lewis, W.A. 'Economic Development with Unlimited Supplies of Labour' in A.N. Agarwala and S.P. Singh (eds) *The Economics of Underdevelopment* (London: Oxford University Press, 1954).
Lindblom, C. *Politics and Markets* (New York: Basic Books, 1977).
Lipietz, A. 'The Globalisation of the General Crisis of Fordism', No 8413: CEPREMAP Working Papers, 1984.
Lokanathan, P.S. *Industrial Organisation in India* (London: G. Allen & Unwin, 1935).
Mahalanobis, P.C. *Talks on Planning* (Bombay: Asia Publishing House, 1961).
Mani, S. 'New Industrial Policy: Barriers to Entry, Foreign Investment and Privatization', *Economic and Political Weekly*, August 29, 1992, pp. M–86 to M–94.
Markovitz, C. *Indian Businessmen and Nationalist Politics 1931–39* (Cambridge: Cambridge University Press, 1985).
Marx, K. and F. Engels, *On Colonialism* (London: Lawrence & Wishart, 1961).
Masani, M.R. *The Communist Party of India, A Short History* (London: Derek Verschoyle 1954).
Mathews, John A. 'Fashioning A New Korean Model out of the Crisis: the rebuilding of institutional capabilities' *Cambridge Journal of Economics*, 1998, 22, pp. 747–59.
McCraw, T. 'Government, big business, and the wealth of nations' in Chandler, A.D., F.Amatori and T.Hikino (eds) *Big Business and the Wealth of Nations*. New York: Cambridge University Press: 1997.
McKinnon, R. *Money and Capital in Economic Development* (Washington, DC: Brookings Institution, 1973).
Mehta, M.M. *The Combination Movement in Indian Industries* (Allahabad: Friends' Book Depot, 1952).
Mehta, M.M. *Structure of Indian Industries* (Bombay: Popular Book Depot, 2nd edition, 1961).
Miliband, R. *The State in Capitalist Society* (London: Weidenfeld & Nicolson, 1969).
Miller, Merton H. 'Is American Corporate Governance Fatally Flawed?' in Donald H.Chew (ed.), *Studies in International Corporate Finance and Governance Systems: A Comparison of the US, Japan, Europe* (New York: Oxford University Press, 1997).

Mitra, A. ‘Class Relations and the Growth of Output’ in Singh, B. and V.B Singh (ed.), *Social and Economic Change* (Bombay: Asia, 1968) pp. 451–8.

Mitra, A. *Terms of Trade and Class Relations* (Calcutta: Rupa, 1979).

Mohan, R. and V. Aggarwal, ‘Commands and Controls: Planning for Indian Industrialization, 1951–1990’, *Journal of Comparative Economics*, vol. 14, 1990, pp. 681–712.

Monks, Robert A.G. and N. Minow, *Corporate Governance* (Cambridge, Mass.: Blackwell Business, 1995).

Morris, D. ‘Indian Industry and Business in the Age of Laissez-Faire’ in Ray, R.K. *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).

Mukherjee, A. and Mukherjee, M. ‘Imperialism and Growth of Indian Capitalism in the Twentieth Century’ in *Economic & Political Weekly*, 12 March 1988, pp. 531–546.

Mukherji, S. ‘The Private Sector and Industrial Policy in India 1946–56, in A.K Bagchi (ed.). *Economy, Polity and Society* (Oxford: Oxford University Press, 1988).

Mukherjee Reed, A. *Liberalisation from What? The State-Business Nexus in India (1947–1990*), Unpublished Ph.D dissertation, University of Southern California, 1994.

Mukherjee Reed, A. ‘The State As Charade: Political Mobilisation in Today’s India’, *Socialist Register*, 1997.

Mukherjee Reed, A. ‘In a Neo-Classical Bind’ *The Telegraph*, 22 September 1997.

Munshi, M.C. *Industrial Profits in India: 1936–1944* (New Delhi: FICCI, 1948).

Myrdal, G. *Economic Theory and Underdeveloped Regions* (London: Duckworth, 1957).

Nader R., Mark Green and Joel Seligman. *Taming the giant corporation* (New York: Norton, 1976).

Nagaishi, M. ‘Stock Market Development and Economic Growth: Dubious Relationship’ *Economic & Political Weekly*, 17–23 July 1999.

Nandy, A. ‘The Political Culture of the Indian State’ *Daedalus*, *Journal of the American Academy of Arts & Sciences*, vol. 118, no.4, 1989.

Nayyar, D. (ed.), *Trade and Industrialisation* (Delhi: Oxford University Press: 1997).

Nayyar, D. (ed.). *Industrial Growth and Stagnation: The Debate in India* (Bombay: Oxford University Press: 1994).

Nelson, J. M (ed.) *Economic Crisis and Policy Choice: The Politics of Adjustment in the Third World*, (Princeton, NJ: Princeton University Press, 1990).

Nurkse, R. *Problems of Capital Formation in Underdeveloped Countries* (Oxford: Oxford University Press, 1953).

O’Connor, J. *The Fiscal Crisis of the State* (New York: St. Martin’s Press, 1973).

Offe, C. *Contradictions of the Welfare State* (Cambridge, Mass.: MIT Press, 1984).

Parikh, K. (ed.) *India Development Report* (Delhi: Oxford University Press, 1997).

Patnaik, P. ‘Imperialism and Growth of Indian Capitalism’ in R. Owen and R.B. Sutcliffe (eds), *Studies in the Theory of Imperialism* (London: Macmillan, 1972).

Pavlov, V.I. *The Indian Capitalist Class* (New Delhi, 1975).

Porter, Michael E. *The Competitive Advantage of Nations* (New York: Macmillan, The Free Press, 1990).

Porter, M.E. 'Capital Choices: Changing the Way America Invests in Industry', in Donald H. Chew (ed.), *Studies in International Corporate Finance and Governance Systems* (New York: Oxford University Press, 1997).

Poulantzas, N. *Political Power and Social Classes* (London: New Left Books, 1968, 1974).

Poulantzas, N. *State, Power, Socialism* (London: New Left Books, 1978; 1980).

Prahalad, C.K. 'Corporate Governance or Corporate Value Added: Rethinking the Primacy of Shareholder Value', in Donald H. Chew (ed.), *Studies in International Corporate Finance and Governance System* (New York: Oxford University Press, 1997).

Raj, K.N. *New Economic Policy* (Delhi: Oxford University Press, 1986).

Rao, V.L. *Progress of Development Banking in India* (Allahabad: Chugh Publications, 1986).

Ray, R.K. *Industrialization in India: Growth and Conflict in the Private Corporate Sector, 1914–47* (London: Oxford University Press, 1982).

Ray, R.K. *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).

Rede, L.A. *The Structure of Profit Rates in Indian Manufacturing Industries* (Baroda: Rachana Book Emporium, 1984).

Reed, D. *Three Historical Models of Corporate Governance: An Evaluation of Corporate Economic Responsibility in India* (Calcutta: Indian Institute of Management, 1998).

Reich, Robert B. *The Next American Frontier* (New York, NY: Times Books, 1983).

Reserve Bank of India, *Annual Reports* (Bombay: various years).

Reserve Bank of India, *Performance of Private Corporate Business Sector, 1998–99* RBI Bulletin (Bombay: October 1999).

Reserve Bank of India, *Report of the Committee to Examine the Legal and Other Difficulties faced by Banks and Financial Institutions in Rehabilitation of Sick Industrial Undertakings* (Bombay, 1984).

Robinson E.A.G. and M. Kidron (eds), *Economic Development in South Asia* (London: Macmillan, 1970).

Rostow, W.W. *The Stages of Economic Growth: A Non-Communist Manifesto* (Cambridge: Cambridge University Press. 1960).

Rungta, R.S. *The Rise of Business Corporations in India: 1851–1900.* (Cambridge: Cambridge University Press, 1970).

Sandesara, J.C. *Industrial Policy and Planning, 1947–91* (London and New Delhi: Sage Publications, 1992).

Sapelli, G. 'A Historical Typology of Group Enterprises: The Debate on the Decline of Popular Sovereignty', in D. Sugarman and Gunther Teubner (eds), *Regulating Corporate Groups in Europe* (Baden-Baden: Nomos Verlagsgesellschaft, 1990).

Sarkar, J. and P. Agrawal. 'Banking: The Challenges of Deregulation', in K. Parikh (ed.) *India Development Report* (Delhi: Oxford University Press, 1997).

Schumpeter, Joseph A. *The Theory of Economic Development*, Harvard Economic Studies, vol 46 (Cambridge, Mass.: Harvard University Press, 1961).

Scott, J. *Corporate Business & Capitalist Classes* (Oxford: Oxford University Press, 1997).

Scott, J. *Corporations, Classes, and Capitalism* (London: Hutchinson, 1979).

Securities Exchange Board of India, *Report of the Kumar Mangalam Birla Committee on Corporate Governance* (Bombay, 1999).

Sen, K. and R.R. Vaidya. *The Process of Financial Liberalisation in India* (Delhi: Oxford University Press, 1997).
Sengupta, N.K. *Changing Patterns of Corporate Management* (New Delhi: Vikas Publishing House, 2nd revised edition, 1983).
Shanta, N. 'Growth and Significance of the Private Corporate Sector', *Economic & Political Weekly*, 31 July – 6 August 1999.
Sharma, M.K. *Business Environment in India* (New Delhi: Commonwealth Publishers, 1989)
Sharma, T. and S.D. Singh Chauhan *Indian Industries* (Agra: Shiva Lal Agarwala & Co., 1965).
Shaw, E.S. *Financial Deepening in Economic Development* (New York: Oxford University Press, 1973).
Sheikh, S. and W. Rees. *Corporate Governance and Corporate Control* (London: Cavendish Publishing, 1995).
Shirokov, G.K. *Industrialization in India* (Moscow: Progress Publishers, 1973).
Simon, H.A. *Models of my Life* (New York: Basic Books, c.1991)
Singh A. *Corporate Financing Patterns in Industrializing Economies: A Comparative International Study* (Washington, DC: IFC, 1994).
Singh, A. 'The Stock Market, Industrial Development and the Financing of Corporate Growth in India' in D Nayyar (ed.), *Trade and Industrialisation* (Delhi: Oxford University Press,1997).
Singh, A. 'Liberalisation, the Stock Market and the Market for Corporate Control: A Bridge too Far for the Indian Economy?' in I. J. Ahluwalia and I. M. D. Little (eds), *India's Economic Reforms and Development: Essays for Manmohan Singh*, (Delhi: Oxford University Press, 1998).
Singhania, V.K. *Economic Concentration through Inter-Corporate Investments* (Bombay: Himalaya Publishing House, 1980)
Sinha, N.K. *The Economic History of Bengal*, vol. II (Calcutta: Firma K. L. Mukhopadhyay, 1962).
Sinha, N.K. 'Indian Business Enterprise: Its Failure in Calcutta (1800–1848)', in Ray, R.K. *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).
Stark, D. *Recombinant Property in East European Capitalism*, Public Lectures No.8, Collegium Budapest, Budapest, 1994.
Stiglitz, J. 'Labor Participation and the East Asian Crisis', presented at the Seoul Conference on *Democracy, Market Economy and Development*, 26–27 February 1999.
Sugarman, D. and G. Teubner (eds) *Issues in the Governance of Complex Groups* (Baden-Baden: Nomos Verlag Gesellschaft; Firenze: European University Institute, 1990)
Teubner, G. 'Regulating Corporate Groups in Europe' in D. Sugarman and G. Teubner (eds) *Issues in the Governance of Complex Groups* (Baden-Baden: Nomos Verlag Gesellsschaft; Firenze : European University Institute, 1990)
Teubner, G. 'The Many-Headed Hydra: Networks as Higher-Order Collective Actors', in J. McCahery, S. Picciotto and C. Scott (eds) *Corporate Control and Accountability: Changing Structures and the Dynamics of Regulation* (Oxford: Clarendon Press, 1993).

Thakurdas, P., J. R. D. Tata, G. D. Birla *et al.*, The Bombay Plan for India's Economic Development, a Brief Memorandum Outlining a Plan of Economic Development for India (London: Penguin, 1944).

Timberg, T. A. 'Three Types of the Marwari Firm' in Ray, R. K. *Entrepreneurship and Industry in India 1800–1947* (Delhi: Oxford University Press, 1994).

Tomlinson, B. R. 'Colonial Firms and the Decline of Colonialism in Eastern India, 1914 to 1947' in *Modern Asian Studies* 15 (3), 1981 pp. 455–486.

Toye, J. *Dilemmas of Development: Reflections on the Counter-Revolution in Development Theory and Policy* (Oxford: Blackwell, 1987)

Tripathi, D. and M. Mehta *Business Houses in Western India: A Study in Entrepreneurial Response* (New Delhi: Manohar Publications, 1990).

Veblen, T. *The Theory of Business Enterprise* (New York: C. Scribner's Sons, 1904).

Veblen, T. *Absentee Ownership and Business Enterprise in Recent Times: the case of America* (New York: B.W. Huebsch, Inc., 1923).

Velayudham, T.K. 'Prologue,' in R. Subramanian and T.K. Velayudham (eds) *Banking Reform in India: Managing Change* (New Delhi: Tata McGraw-Hill, 1997).

Verma, H.S. *Industrial Families in India: An Enquiry into the Nature of Their Entrepreneurship* (New Delhi: Concept Publishing, 1987).

Wade, R. *Governing the Market* (Princeton, NJ: Princeton University Press, 1990).

Wallerstein, Immanuel M. *The Capitalist World-Economy: Essays* (Cambridge and New York: Cambridge University Press, 1979).

Warren, B. *Imperialism: Pioneer of Capitalism* (London: New Left Books, 1980).

Westphal, L. and K.S. Kim. 'Korea' in B. Balassa, *et al.* (eds) in *Development Strategies in Semi-industrial Countries* (Baltimore, Md.: Johns Hopkins University Press, 1982).

Williamson, O.E. *Markets and Hierarchies: Analysis and Anti-trust Implications* (New York: Free Press, 1975).

Williamson, O.E. *The Economic Institutions of Capitalism* (New York: Free Press, 1985).

World Bank, *India: Stabilizing and Reforming the Economy* Report No. 10489–IN.(New Delhi, 1992).

World Bank, *South Korea: Managing the Industrial Transition*, Volume II (Washington, DC: 1987).

Zaidi, A.M. *The Great Upheaval, 1969–72* (New Delhi: Orientalia, 1972).

Zeitlin, M. 'Corporate Ownership and Control: The Large Corporation and the Capitalist Class', *American Journal of Sociology* 79, No 5 (March 1974), pp. 1073–119.

Zeitlin, M. *The Large Corporation and Contemporary Classes* (Cambridge: Polity Press, 1989).

Index

agglomeration 34, 35
aggregate demand 45, 47, 92, 119, 172, 188, 189, 193
ALCAN 148, 168
Ambani, D. 113
Amsden, A. H. xii, 17, 43, 48, 55, 106, 185, 186, 187, 191
Anglo-American model 11, 12, 19, 50, 68, 106, 130, 196
apex company 32, 33, 101, 107, 156, 159
ASSOCHAM 63, 64, 149

Bagchi, A. K. 16, 53, 54, 58, 59, 61, 71, 72, 78, 79, 91, 94, 97, 170, 192
Bangurs 106
bania 60
banian 61
Bardhan, P. 14, 125, 189, 192
BAT 147, 148, 149, 168
bazaar 69, 73, 74, 79
Bengal Chamber of Commerce 65, 92
Bengali businessmen 61, 65
Bengali nationalist entrepreneurs 62
Berle, A. A., and Means, G. C. 15, 24, 25
Bhaba Committee 89
Birla, Aditya 148
Birla Brothers 59, 85
Birla, G. D. 63, 64, 65, 66, 94
Birla, Kumar Mangalam 151
Birlas 60, 84, 104, 110, 112, 113
BJP 143, 169, 170, 171
Board for Industrial and Financial Reconstruction (BIFR) 174
Bombay Plan 95, 112
Bombay Stock Exchange 179
Bombay Stock Exchange Directory 159
Boyer, R. 11, 188
business houses 109
buyback of shares 144–6

Cadbury Committee 151, 152, 154
Capital Issues (Control) Act 99, 100, 135
capital market 134, 135–41, 138, 140, 141
Carr, Tagore & Co. 67
chaebol 30
Chandler, A. D. 18, 19, 29, 185, 186, 188, 191
Chandra, B. 54, 56, 63, 97
Chatterjee, R. K. 120, 121
Chettiars 65
Classical Marxist view xiii, 124
Coase 185, 188, 189
Companies Acts 82, 90, 91, 98, 105, 106, 144, 160
Companies Amendment Act (1999) 134, 144, 157
Company Law Board 106
Confederation of Indian Industries (CII) 151, 152, 154, 160, 195
Controller of Capital Issues (CCI) 100, 135
conglomerate 6, 20, 28, 100, 101, 110, 112, 123
Congress xii, 66, 94, 112, 113
convertibility clause 110–11
corporate control 50
  types and mechanisms 25–9
corporate economy 84, 119, 123
corporate governance 21, 23, 55, 93, 100, 131, 133, 134, 151, 155, 190
  in the post-interventionist model, codes of 144–50, 151–4, 155, 156, 157
corporate groups 50
  definition 30
  emergence of 34–7
corporate structures 31
  umbrella and interlocking structures
  see also satellite structures 103

Dalmia, R. K. 65
Dalmia-Jains 84, 85
Dalmias 60, 83
dedicated capital 48
deindustrialisation 79
Department of Company Affairs 114, 126, 140, 144, 146
deregulation 9, 10, 13
development banking 108, 110, 111
  development banks 110, 141, 176
developmental state xii, 17
directly unproductive (DUP) activities 17

economic reforms 3, 6, 9
economic value 164,
Economic Value Added (EVA) 165–7, 168
enucleation 34, 35,
excess profits tax 76
export promotion 108

FICCI 63, 64, 65, 66, 92, 113, 148
finance-theoretic value maximisation model 185, 189–191
  see also shareholder value maximisation
financial institutions
financial control 23, 27–28, 30, 107, 130, 137, 147, 149
  see also public financial institutions
five-year plans 3
fluid capital 48
Fordist form 15
  Fordist capitalism 188
foreign direct investment (FDI), 139, 171
Foreign Exchange Mechanism Act (FEMA) 143
Foreign Exchange Regulation Act 99, 134, 143, 147
Foreign Investment Promotion Board (FIPB) 104, 139
foreign portfolio investments (FPI) 138, 139
foreign institutional investors (FII). 10, 138, 139
Friedman, M. 11, 12, 185, 189

Gandhi, Indira 4, 64, 132
Gandhi, Rajiv xii, 4, 132, 170
General Insurance Corporation (GIC) 100, 137, 149
Goenkas 106
Goswami, O. 60, 74, 75
Government control 28
Gujaratis 65

Hazari, R. K. 16, 103, 104
Herman, E. 156
Hindustan Lever 160
holding company 31,

IMF 4, 133, 169, 193
INDALCO 148, 168
Indian Chamber of Commerce 65
Indian labour law 120, 122, 173
Indian Merchants Chamber 65, 169
Industrial Credit and Investment Corporation of India (ICICI) 97, 100, 104, 110, 117, 128, 149
Industrial Development Bank of India (IDBI) 100, 104, 110, 111, 149, 176
Industrial Finance Corporation of India (IFCI) 97, 104, 110, 111, 149
industrial licensing 108
Industrial Licensing Policy Inquiry Committee (ILPIC) 101, 102
Industrial Policy Resolution of 1956 98
Industries (Development and Regulation) Act 97
inner circle 84
innovation 42
institutional investors 104, 123, 194
institutionalist political economy 19, 129, 130
institutionalists 13, 129, 130
inter-corporate control 28
  investments 28, 32, 71, 72, 80, 102, 103, 105, 107, 156
  loans 84, 86
  networks 71, 72
interlocking directorships 28, 71, 72, 80, 84, 102, 105, 123
interlocking structure 31, 103
  inner circle, outer circle and complex 103, 104
International Finance Corporation (IFC) 179, 180
interventionist model
  definition of 93
  emergence of 93–7
ITC 147, 168

Jains 104

Keynes, J. M., Keynesians xvii, 47, 78, 186, 192
Kling, B. 67
Knight, F. H. 42, 43
Kochanek, S. 53, 63, 64, 94, 113

late development 48, 186
legitimacy 14,
legitimation xiii, 3, 94,
  deficits xiv
Leibenstein, H. 47,
Levskovsky, A. I. 62, 63
license-permit-quota regime 98, 107, 142
Life Insurance Corporation of India (LIC) 100, 110, 137, 149
Lokanathan, P. S. 68, 87

Madras Chamber of Commerce 65,
management (or managerial) control 24, 25, 30, 86
managerialism 15, 16, 25
managing agencies 72
  British and Indian 69–70
managing agency model 55, 66, 80, 84, 87, 189
managing agency system 66, 81, 82, 85, 87, 88, 89, 91, 99, 123
managing agents 62, 72, 81, 82, 90, 101
marketisation 9, 10, 13, 131
Markovitz, C. 53, 66
Marwari firms 73, 74
Marwaris 56, 59, 60, 64, 65, 71, 73, 75
Marx, K. 186

Marxist political economy 13, 18
McCraw, T. 187
Mehta. M. M. 71, 83, 99, 106
Miller, M. M. 185
minority control 27,
mixed economy 3, 4
Modi Rubber Limited 148
Monopolies and Restrictive Trade Practices Act (MRTPA). 142
Morris, D. 54, 56, 69
MRTP Commission 126
MRTPA 142
Mukherjee A., and M. Mukherjee 63, 94
multiple directorships 71

nationalised banking 109
Nehru, Jawaharlal xii, 4, 96, 97
neo-classical economic theory 8, 43, 135, 161
neo-classical economics 189
neo-classical perspective 129, 130
neo-liberal economics 7, 44, 183
  claim 184
  model 140
  policies 195
  reforms 5, 191
neo-institutionalist economics 21,
neo-utilitarian political economy 13, 16, 17, 19, 112
network 28,
New Economic Policy 132
nexus of contracts 25
nominee directors 28, 104, 107, 111, 112
non-performing assets (NPAs) 142
non-resident Indians (NRIs) 170, 171

orthodox paradox 130, 149

parent company 30
Parsis 56, 59,
peripheral capitalism 14, 44,
Porter, M. E. 45, 48, 186, 190, 192
Prahalad, C. K. 186, 190, 192
preferential allotment 135
private placements 107, 136, 137
profits, pure 42
  market 42
  Marxist theories of 43
  sources of 76
promoter 101, 123, 135, 136, 137, 146
public financial institutions 100, 101, 111, 123

Rao, Narsimha 4, 133
Ray, P. C. 65
Ray, R. K. 53, 54, 57, 58, 64, 72, 73, 76
reciprocity 106–8, 110, 111
Reed, D. 69, 71, 86, 89, 107, 156
Reliance Industries 113, 137, 191
rentier incomes xv, xvi,
rents 13, 16, 17
rent-seeking 47, 111, 112, 114, 125
  hypothesis 16
  school 18
Reserve Bank of India (RBI) 82, 116, 117, 136, 142, 143, 164, 195
residual claimants 189
Rungta, R. S. 68, 72, 80, 82, 87, 88

Sarabhai, A. 65
satellite structure 31, 33
Schumpeter, J. A. 42, 43, 47
SEBI 9, 140, 141, 149, 150–2, 160
shareholder value 86, 164, 165
  maximisation 166, 185, 190–2
sick industries 118, 119,
Simon, H. A. 84
Singh, Manmohan xii, 4, 133, 137
Singhania 83
Sinha, M. K. 62
state autonomy 14,
State Bank of India (SBI) 99
Sterlite 148, 168
Stiglitz, J. 48, 49, 192
straight-line structure 31, 32
subsidiary 30, 31, 32, 40, 146
Surajmall Nagarmalls 60,
swadeshi 167, 169, 170, 171

Tagore, Dwarkanath 61, 65
takeover code 146–150
Tata, J. N. 59, 78, 82
Tata, J. R. D. 65, 87, 95
Tatas 58, 84, 85, 110, 112, 113, 147, 167, 168
Thakurdas, P. 63, 64, 65, 71, 95
Timberg, B. R. 73, 74
Tomlinson, B. R. 59, 66, 84
transaction costs 18, 188, 191

unidirectionalism 106–7
Union Bank 61
unionisation 120
Unit Trust of India (UTI) 100, 137, 138, 149

Veblen, T. 47
Vivian Bose Commission 84, 85,
voluntary retirement schemes (VRS) 173, 174

Williamson, O. E. 18, 19, 185, 188, 189

zaibatsu 30
Zeitlin, M. 15, 16