the pioneer
VIJAYAWADA | SATURDAY | MARCH 27, 2021

Private sector: From growth to innovation

The private sector has come of age with liberalization, outsourcing, and infrastructure development. The driver of this transformation in the private sector is the "growth machine". The idea of a growth machine was popularized by professors of Sociology John Logan and Harvey Molotch, who used the metaphor of an industrial machine to explain rapid economic growth in America.

Typical machines consist of moving parts arranged in a systematic way. This ordered arrangement consumes inputs, adds value, and turns out products of unvarying quality within timelines. In an economic system, the growth machine works in a similar way - it is a machine whose primary product is economic growth. Its parts consist of groups of industrial firms, local businesses, realtors, business organizations and governments working as entrepreneurs. Thegrowth machine adds value to land (raw material) by erecting new structures (final products), such as convention complexes, sports stadiums, riverfront development and the redevelopment of city centers.

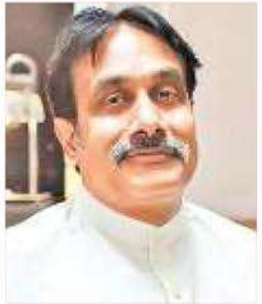
In order to produce consistent growth, multiple components of the growth machine have to be joined up in asystematic way. This is done by Government support in the form of laws and policies to attract and retain businesses. Specifically, such support includes regulatory and planning assistance,institutionalizing of pro-growth strategies and practices, and promoting connections through intermediaries (e.g. development finance institutions). The promotion of all these business activities occurs within a broad vision of public interest.

Globalization has increased the opportunities available to governments to attract "footloose capital" with a slew of new incentives and benefits to boost economic development.

Globalization has increased the opportunities available to governments to attract "footloose capital" with a slew of new incentives and benefits to boost economic development.

Most important of these is the transformation in the attitude of local officials, who have started to accept the dominant ideology of private sector-led growth.

An Indian version of the growth machine has also fueled India's growth story. The Indian growth machine is organized around entrepreneurial central and state governments, supported by corporates, industry associations, and other entities. Growth is sought to be achieved through the establishment of high development projects - export promotion zones (EPZ), retail malls, office plazas, schools, professional colleges, industrial complexes, highways and attracting investment in "hot sectors", such as IT and BT. The agenda is to attain high levels of growth, which is likely to create jobs, enhance incomes, and increase revenues for the governments. In turn, the increased government revenues will help to fund the increasing number of socio-economic development programmes.



DR. SAMEER SHARMA

The flip side is that growth machine-driven development opens up opportunities for gaming and cronyism, which retards economic growth in the long run. Malcolm Salter, at the Harvard School of Business Administration, has studied the ways in which gaming and cronyism are practiced by the private sector. Gaming has both rule-making and rule-following components. Rule-making (influence) involves lobbying with the government to include loopholes in new laws and rules and then exploiting the loopholes, even to the extent of subverting their original intent. Rule-following (compliance), on the other hand, involves technical compliance with existing rules while exploiting their ambiguities for self-interest, thus again subverting the rules' intent.

Cronyism occurs due to the confluence of contributions, personal connections and greed founded on uncompromising self-interest. Additionally, cronyism is built on the message that the actions of corporations always promote public interest and are in the broader interests of the nation.

One way of overcoming gaming and cronyism is to convert the growth machine into an "innovative machine". The key difference between the two is in the way private companies grow; in a growth machine, private companies rely on price to obtain competitive advantage and grow. On the other hand, companies in an innovation machines gain their competitive advantage by making innovation a part of their daily operations. Transmuting to an innovative machine requires switching policies in time by astute policy-makers.

Veteran economist, William Baumol, in his book 'The Free-market Innovation Machine', explains the way an innovation machine makes innovation a part of its routine activities. Companies do not leave innovation to chance, but make it a part of their ongoing business activities.This is accomplished by creating a "domain of memorandums, rigid cost controls, and standardized procedures". Innovation here is not the big-bang type (Eureka moments), but routinized. Routinized innovation generates "herd effects" where companies are aware of the activities and innovations of their rivals, and are forced by competitive pressures to respond to them. Thus, sustained growth is founded on sets of industries that have routinized innovation into a regular and predictable business activity. Over time, the innovative machine will lead to a more efficient allocation of resources and continuous growth that would potentially address equity issues, something that was missing in the growth machine partly because the machine was never really designed to address equity issues, at least directly.

(Author has a PhD from USA and a DLitt from Kanchi University. The article is based on his research and practice and views are personal)