CHAPTER VI

Embeddedness and Trust: Cooperation and Competition in Tiruppur, Kannur and Morbi

VI.1 Introduction

In the era of flexible specialisation we see vertical disintegration\(^1\) of industries, break-up of state monopolies into separate competing units and the easing of restrictions into market entry with low sunk costs\(^2\). The intensification of competitive pressures in intermediate and final product market and the growing demand for customisation have led supplier firms to make greater use of outsourcing and subcontracting of specialised services and components (Deakin and Michie, 1997). In this present state of functioning of an industrial space, cooperation, competition and conflict among firms are quite common. These are of significant import in the process of working towards higher efficiency, productivity and profit.

Our intention in this chapter is to look at the level of trust, cooperation and competition in the functioning of industrial spaces of the three towns of Tiruppur, Kannur and Morbi. We also intend to look at the role of institutions in enhancing trust and cooperation and solving the conflicts among the firms. There are two ways how business relations are formed among the firms. The process by which individual firms form trusting relationships with each other and the wider institutional framework within which trusting relationships are based and exercised. Here we intend to argue that the more effective congenial and contractual environment among the firms or within the domain of institutions under which the firms operate, will provide the basis for a greater potential for trust building. The key issue is how far diversity in the form of inter-firm relations may be explained by the role of social institutions. Trust is considered as the necessary ingredient in business relation because it guards against opportunistic behaviour, encourages better investment decisions and so ensures rapid and flexible responses to unforeseen demand fluctuations.

There have not been much work done on the concept of Embeddedness and Trust in the Indian context. In the West most of the work done recently, have

Most of the utilitarian traditions, including classical and neo-classical economics assume rational and self interested behaviour affected minimally by ongoing social relations. At the other extreme Granovetter (1985) argued what is called 'Embeddedness' that behaviour and institutions are constrained by ongoing social relations that to construe them as independent is a grievous misunderstanding. There are two views on the concept of 'Embeddedness'. One sees the economy as an increasingly separate, differentiated sphere in modern society. In the modern society rational calculations of individual gain is not effected by social and kinship obligations. The other view asserts that Embeddedness in earlier societies was not substantially greater than the low level found in modern society. Granovettors (1985) view diverges from both the schools of thought. “I assert that the level of embeddedness of economic behaviour is lower in non-market societies, than is claimed by substantivists and development theorists.” He in his analysis did not attempt to treat the issue posed by non-market societies. Since in non-market primitive society labour was the only factor of production, goods were exchanged in production to their labour costs—as in the general classical theory of exchange. Some anthropologist also remarked that economic behaviour in the tribal societies were independent of social relations. Granovettor did not go to address the issue of embeddedness of non-market societies. Instead he proceeds towards a theoretical elaboration of the concept of embeddedness, illustrated with a problem from modern society which is subsumed within a hierarchically organised firm and how transactions are carried out in market.

How the view of embeddedness alters our theoretical and empirical approach to the study of economic behaviour? Oliver Williamson (1975) noted that real economic actors engage not merely in the pursuit of self-interest
(Smithian view) but also in 'opportunism'. In recent years, there is a rise of imperfectly competitive markets characterised by a small number of participants with sunk costs and specific human capital investment. These firms are highly specialised with qualified workers who stick only to specific work. Such rigidity inhibits them to adapt to changing external circumstances. In such situations, the alleged discipline of competitive markets cannot be called on to mitigate deceit. In a self-regulating market, competitive forces could be imagined to suppress force and fraud (opportunistic behaviour). However, to Hirshman (1977) certain human motivations kept others under control and that in too in the pursuit of economic self interest- not through an uncontrollable passion— but in a civilized gentlemanly manner. “So the classical problem that daily economic life is riddled with mistrust and malfeasance has resurfaced again” (Granovettor, 1985). Classical economics operates with an individualistic conception of human action- and perfect competition disallowed social relations and all kinds of force and fraud. However, in the present day with the rise of imperfect competition there is a rise of opportunistic behaviour which led to mistrust and malfeasance. Here the role of social institutions come to generate trust to avoid malfeasance. Do such institutions guarantee malfeasance? We shall come to this in a short while.

VI.2 Role of Institutions in Trust Building

Social institutions and arrangements have been viewed as efficient solutions to certain economic problems. Malfeasance as a product of certain institutional arrangements can be easily averted. Institutional arrangements have been earlier interpreted as serving no economic functions, however, nowadays its role is being appreciated to discourage malfeasance. Apart from the institutional arrangements which can generate trust and avoid malfeasance, a rational individual could be motivated to develop clever ways to evade malfeasance. Social institutions and arrangements do not produce trust but instead are functional substitute of it (Okun,1981). Burchell and Wilkinson (1997) set the nature of trust against a background of social norms and legal institutions. Law is an important mechanism for dealing with essential riskiness of trust. “Legal
arrangements which led special attentions to particular expectations make them sanctionable ... lessen the risk of conferring task" (Luhmann, 1979). We shall come to this point in more details how contracts supported by law enhances cooperation and trust in the latter part of this discussion. Zucker (1986), suggests that even trust of a personal kind- which she defines as a ‘process-based’ in the sense of arising out of long standing relationships, need to be supported by modern economics by a form of trust which is rooted in stable institutions. This system of trust operates when trust is tied to formal, societal structure which have an existence separate from the immediate material preferences, motivations and actions of individuals. Institutional forms therefore, are not reducible to rational choice considerations but play an independent role in structuring individual agency. A distinction can be drawn between first, the process by which individual firms forms trusting relationships with each other and second, the wider institutional and organizational framework within which the individual relations are established.

It can be reasonably argued that the more effective the contractual environment is in providing access to in the information and reducing conflict monitoring of risk from the individual relationships the greater will be the potential towards trust building (Burchell and Wilkinson, 1997). The key issue is how far diversity in inter-firm relations may be explained by the role of social institutions in sustaining cooperation (Arrighetti et al, 1997). Dei Ottati (1994) suggests that the smooth functioning of the market economy necessitates the presence of formal and informal institutions, which permits the formations and permanence of an economic and social environment in which constructive forms of cooperation and competition can prevail over destructive ones. Institutions effect the level of transaction costs within and organisation and hence influence business performances (North, 1990). It is suggested that cooperation is more easily achieved in social contexts where system of rules are mutually supportive and enjoy high level of legitimacy (Scott, 1995). Associations are viewed as a potentially highly important form of institutionalised mutual control (cooperation) between firms. This results from both formal regulations and more informal
behavioural norms and understandings. The legitimacy of institutions is enhanced if they enjoy government recognition as an effective representative organ. The system of formal and informal rules set up by the firms are mutually beneficial to all members of the institutions and associations.

VI.3 The Embeddedness Argument

The embeddedness argument stresses instead the role of concrete personal relations and networks of such relations in generating trust and discouraging malfeasance. The widespread preference for transacting with individuals of known reputation implies that few are actually content to rely on either generalized morality or institutional arrangements to guard against the trouble (Granovettor, 1985). In business relations, the degree of confidence must be more variable. Standard economic analysis neglects the identity and past relations of the individual transacts, but rational individuals know better relying on their knowledge of these relations. They are less interested in general reputations than on whether a particular other may be expected to deal honestly with them—mainly a function of whether they or their own contacts have had satisfactory past dealings with the other (Granovettor 1985). Granovettor gives more importance to social relations than institutional arrangements—that social relations are the structure that fulfills the functions of sustaining order. But it cannot guarantee the absence of malfeasance. The reasons as forwarded by Granovettor were—firstly, the trust engendered by personal relation presents by its very existence enhanced opportunity for malfeasance. In personal relations it is common knowledge that “you always hurt the one you love”, that a person’s trust in you results in a position far more vulnerable than that of a stranger. Secondly, force and fraud are most efficiently pursued by teams and the structure of these teams requires a level of internal trust. Both enormous trust and enormous malfeasance may follow from personal relations. Thirdly, the extent of disorder resulting from force and fraud depends very much on how the networks of social relations are structured. More extended and large scale disorder results from coalitions of combatants which is impossible without prior relations. Disorder and malfeasance do of
course occur when social relations are absent. But the level of malfeasance available on a truly atomized social situation is fairly low, instances can only be episodic, unconnected and small scale (Granovetter, 1985).

On the question of application of Embeddedness approach to economic life under what circumstances economic functions are performed within the boundaries of hierarchical firms rather than market processes that cross boundaries? Williamson (1975) asserts that money, time and energy that cannot be easily transformed to interaction with the other on different matters, are more likely to take place within a hierarchically organised firms. Repeated personal interactions across organisational boundaries support some minimum level of courtesy and consideration between the parties. In addition, expectations of repeat business discourages efforts to seek a narrow advantage in any particular transactions. Granovetter says that there is sufficient social overlay in economic transactions across the firms. The disputes are frequently settled without reference to the contract or potential or actual legal actions. You can settle any disputes if you keep the lawyers out of it (Macaulay, 1963). Settlement of disputes is eased by embeddedness of business in social relations. "Even where the parties have a detailed and carefully planned agreement which indicates what is to happen if, say, the seller fails to deliver on time often they will never refer to the agreement but will negotiate a solution when the problem arises as if there never had been any original contract" (Macaulay, 1963).

So, we have come across two views - institutions/organisations and embeddedness in personal relations that generate trust in economic behaviour. Let us come again to these two views in details with references to some recent studies, about formation and importance of trust, cooperation among the hierarchically organised firms.

**VI.4 Some Concepts on Trust and Social Relations**

Why is trust and cooperation important in an industrial space? Trust and cooperation in inter-firm relations improve business performances. The presence of trust transforms an exchange relations characterised by reducing the costs of specification, monitoring and guarding against opportunistic behaviour,
encouraging better investment decisions, and ensuring rapid and flexible responses to unforeseen events (Lyons and Mehta, 1997).

Social relations between two parties exist when each party orients its behaviour on whole or in significant part to its expectations of behaviour of the other. Trust is a meaningful concept for the parties if at least one party is exposed to an element of behavioural risk. Trust is experienced by one party when it is uncertain about behaviour of the other (Lyons and Mehta, 1997). Given the existence of behavioural risk, trustworthiness is defined as the attribute of a party who would choose to refrain from opportunism and believes that the other is trustworthy. Why is this type of bond or cooperation necessary? It is because it can provide a viable alternative in circumstances of high transaction cost. The concept of cooperation has been neglected because both mainstream economic theory and large part of transaction cost literature have taken the view that market competition would suffice in the long run to ensure the evolution of optimal organisational forms. However, the real world situation is different. Smithian view of cooperation is that in society, it comes from own individual self-interest. The pursuit of individual self-interest in exchange in a free market society secures the level of cooperation necessary for the society as a whole. Contemporary analysis of industrial districts put much greater stress than what Marshall did on collectivist and institutional basis for successful coordination. Emphasis is placed on the community in guaranteeing standards of behaviour that endanger trust and cooperation and thereby strengthen inter-firm networks (Deakin and Wilkinson, 1997). Transaction cost concern is with organizational implications of the cost of making a transaction. Trusts enter into the argument of transaction cost because here cost is directly linked to the possibility that the economic actor will behave opportunistically. Lorenz (1988) says this is obvious enough in the case of contract enforcement, but perhaps less so in this negotiation and adaptation. If transaction cost are thought of as friction in the economy then trust can be seen as an efficient lubricant. Drafting of a comprehensive agreement that attempts to account for all possible contingencies take a lot of time money and effort. Williamson (1985) has made the point that in the absence of opportunistic behaviour there would be no need to attempt such costly planning. If both parties trust each other and behave honestly both will gain economically by avoiding the
transaction cost. A considerable amount of expenses may go into fashioning safe
guards designed to minimise the risks of being a victim of opportunistic behaviour
(Lorenz, 1988). These expenses could be avoided if there were mutual trust.

Thus Lyons and Mehta (1997) suggest that trust can be thought of as either
self interested or socially oriented. Trust supported by instrumentally rational
behaviour (expectations, of states of nature or the behaviour of other people) is
termed as Self-Interested Trust (SIT). Here where trust arises, it is carefully
calculated or incentives are created intentionally in direct response to the presence
of behavioural risk. The relative costs and benefits to being trusting or trustworthy
are measurable and they are evaluated within the boundaries of the exchange
relations. Another mechanism by which trust can be created and sustained is to
focus on social mechanisms which intentionally or inadvertently engender and
sustain trust and on the consequences of trust as they are realized by the
community of individuals. The recognition that behaviour is located within a
social arena leads to the notion of trust as norm based in orientation. This type of
trust is known as Socially Oriented Trust (SOT).

When does trust leads to cooperation? Is trust a result of cooperation rather
than a pre- condition? Gambetta (1988) says Cooperation makes some demands
on the level of trust, particularly of mutual trust. Depending on the degree of
constraint, risk and interest involved, trust as a precondition of cooperation can be
subjected to the demands of differing intensities. It may be needed to varying
degrees, depending on the force of the mechanisms that govern our cooperative
decision in general and on the social arrangement on which those decisions are
made. Higher is the level of trust higher the level of cooperation. However,
cooperative behaviour does not depend upon trust alone. It may come from social
relations and social institutions or from self- interest. Gambetta (1988) further
advocates that trust would be better understood as a result rather than a
precondition of cooperation. Trust would exists in societies and groups which are
successful because of their ability to cooperate, and cooperation could be triggered
not by trust, but simply by a set of fortunate practice, random at first and then
successfully retained. Our example of Tiruppur town largely reflects this. Then
why do we bother about trust when cooperation can be generated by other means.
Gambetta (1988) says it is not the question of bothering, instead concentrating on the manipulation of constraints and those conditions of cooperation we can intentionally and most effectively promote as much cooperation. This is possible by deploying some reasonable degree of coercion and by supporting arrangements which encourages cooperation through self-interest, thereby making small demand on trust. Cooperation can be achieved by other means like force also. However, such kind of cooperation is likely to be less efficient, more costly in future and more unpleasant (Gambetta, 1988). The strategy of looking at trust does not imply that we should wait for cooperation to evolve itself. We should set our sights on cooperation than on trust. We can promote right conditions i.e. mutual understandings for cooperation without assuming that the prior level of trust will eventually lead to cooperation.

Trust generates cooperation thereby reduces information and the monitoring costs. Trading partners tend to derive mutual benefits from cooperation in production but they compete over proceeds of production, because what one gets others cannot have. Every relationship is therefore by its nature both rivalrous and cooperative. The pursuit of distribution of self-interest could precipitate a retaliatory withdrawal of productive cooperation, a lowering of operational and dynamic efficiencies and a reduction of the proceeds from production (Burchell and Wilkinson 1997). Arrighetti et.al, (1997) found that contract law may play on important a role in underpinning long term, cooperative relationships and in fostering trust. The impact of contract law depends on the relationship between the legal system and other forms of institutional regulation.

VI.5 Firms, Cooperation and Trust

Cooperation is clearly necessary for the production process, particularly in vertically disintegrated firms, because individual firms here conduct only the specialised functions of a production process. The product passes through various stages in different specialised firms. So, in a vertically disintegrated production process mutual dependency among the firms is clearly necessary. The concept of inter-firm cooperation refers precisely to relations of mutual dependence between firms which retain their separate identity as legal or economic entities (Arrighetti et. al 1997). In vertical disintegration (flexible specialisation) the success is said to
depend on achieving a certain balance between competition and cooperation (Dei Ottiti, 1994). Competition between firms produces a higher degree of specialisation and a more extensive division of labour and a higher level of productivity (Loasby, 1994). The intensification of competition in product market is followed by increasing demands from buyers for greater customisation and flexibility in production and delivery of goods and services. For example, from our case study of the towns we found that many firms came into existence in Tiruppur after the export boom and that their survival in the market depended on how they changed their production structure according to the tastes of the customers. There is an increasing trend of diversification in product and design of garments.

Although the institution of contract law is commonly thought to be one of the principal mechanisms for enhancing the security of business transactions its precise role remains somewhat obscure. Particularly unclear is the relationship of law to trust. A dual role for contract law in supporting economic exchange may be identified. The law first creates a space within which the parties can plan the exchange, making due provisions for future contingencies. Secondly, it provides a set of sanctions aimed at inducing performance of the agreed obligations. Empirical research however has found the role of law in commercial transactions to be marginal (Arrighetti et al, 1997). Any resort to legal action carries a high price, particularly in the context of a long-term relationship. Litigation also raises implication of bad faith. The influence of contract law needs to be seen alongside that of other institutional factors which include the activities of trade associations and standard setting bodies, the cost and effectiveness of available systems of dispute resolution and the general level of macroeconomic stability (Arrighetti et al, 1997). Since, legal action carries bad faith all disputes can be taken care of by social and trading institutions like in Tiruppur by Tiruppur Exporters Association (TEA). Suggestions and findings of Arrighetti et al, (1997) support the fact that institutional norms are an important feature of the processes by which trust is developed and reproduced. More specifically institutional trust plays an important role in offsetting asymmetries of power between contract parties, promoting stability in trading relationships, and decreasing uncertainty. Hence, rather than seeing institutional forces as merely constraining individual agency, they should
also be viewed as channeling contractual behaviour (Arrighetti et. al, 1997). In Tiruppur many problems among the entrepreneurs are settled out of the court by TEA. This not only saves time and money of the entrepreneurs but also re-establish their business relationships.

In order to understand why firms enter into partnerships Arrighetti et. al, (1997) found that to realise certain advantages in terms of enhanced competitiveness called for price reduction increased customization of products, and enhanced collaboration over the development of new products and processes. Moreover long-term contracts were seen as a means of cementing such relationships into place. There was still a large segment of firms with little or no experience or interest in customising their products and for which both short-term contacts and relations were the norm. In some cases increase in the intensity of competition arising from external shocks or low entry costs, did not lead to improved quality of performance. There was a concentration on cutting prices at all costs, a process that threatened to undermine the quality provided by suppliers.

Our intention in this chapter to look at the level of trust, of cooperation and competition among the firms. The question that arises is do we need to tie trust to formal, social or trading institutions or tie with personal relations in our study towns? Are legal sanctions necessary to generate trust? Who generates trust? Social relations (Granovettor 1985,) or institutional arrangements (Okun,1981; Zucker 1986; Arrighetti, 1997; Burchell and Wilkinson 1997 etc.) both have their own arguments. We neither want to give sole importance to institutions nor social relations for generating trust. We accept the importance of both factors in the functioning of industrial space. Both arguments have their own role in a mutually supportive way to generate trust, cooperation and competition among firms. Trust and cooperation helps in improved business performances and competition for production of quality products not through price cutting which eventually leads to a deterioration of quality. Here we admit the role of institutions (trade association) for setting standard of quality and price, so that there is no unhealthy competition and disputes in the compromisation of quality and price.
In general, cooperation and good business relations can be achieved through personal and social relations by generating trust. These are desired and enhance the functioning of the industrial space. However, cooperation can be generated by legal institutions. This way too we can enhance efficiency but only applying by some kind of force. This is required when in a complex world, cooperation cannot be generated by mutual trust. Some illegal conditions i.e. manipulations of constraints, fraud cases also can generate trust with some kind of brute force. However, these are not desired for efficient functioning of an industrial space (Figure 6.1)

**Figure 6.1**

Path to Cooperation and Good Business Relations.

- **Personal Relations** → Trust → Cooperation and Good Business Relations (efficient functioning, desired).
- **Social Relations or Institutions** → Trust → Cooperation and Good Business Relations (efficient functioning, desired).
- **Legal Institutions** → Force? → Cooperation and Good Business Relations. (efficient functioning, desired when things go worse).
- **Some illegal conditions manipulations of constraints fraud cases etc.** → Force? → Cooperation (inefficient functioning, not-desired in an industrial space).

In the next portion of this chapter we shall try to apply all the issues we studied, empirically to our case study.

**VI.6 Trust, Cooperation and Competition in Tiruppur, Kannur and Morbi**

We have discussed in Chapters I and IV that flexible specialisation is characterised by vertical disintegration or networks of production functions. Competitive pressure in the product market and growing demand for customisation have led the supplier firms to make greater use of incontracting and
outcontracting. All firms here concentrate on one specialised activity. They subcontract out or take job works on some specialised part of the product produced in the town. Thus, they work together towards higher efficiency, productivity and profit.

VI.6.a Trust in Business Relations

We have divided the issue of trust in business relations in the towns into two parts. One deals with the internal production system (subcontracting, raw material acquisition) and the other with marketing of products, particularly in a non-local context.

The entire industrial space of Tiruppur is based on subcontracting and here everything is based on trust. In Chapter IV we have discussed the production process of Tiruppur knitwear industry. Such vertically disintegrated production process enables one to enter the business with low investment. Actually it is the motivation towards commercial or self-interest of each entrepreneur that they do business with small investments and on trust. However, the system in Tiruppur knitwear industry developed not with specific self-interest of the entrepreneurs. It developed spontaneously and all new entrants took up one specialised activity according to their working capacity and interest. As more export orders started coming to the town entrepreneurs were not required to worry for job work. Incontracting and outcontracting of jobs by the firms are done generally on verbal agreements. Local transactions worth lakhs of rupees takes place just through passing a slip. There was the instance of one exporter on how he had sent a single order worth rupees three lakhs through a cart puller. Altogether 51 firms out of total 57 (90 percent) we interviewed, reported that job working transactions are done purely on verbal agreement based on trust (Table 6.1) even though they keep an account of the quantity. Even the payments for the raw materials required by the firms were paid later on when payments primarily come from export earning.

For many firms in Tiruppur, working with low sunk cost, their survival depended on job working. The amount of job work of these firms on the other hand depended on accessibility and capacity to get orders by the export firms from the buyers. As doubted by Williamson (1975) are there any kind of malfeasance
because of the dependency on small job working firms by bigger firms and vice versa. In our case study we would categorically deny it. This is because survival of the small job working firms is entirely based on their reputation and credibility for not engage in any kind of malfeasance. On the other hand bigger firms also depend on such kinds of incontracting firms for specialized functions and prompt delivery. All networks in Tiruppur is based on personal relations. All individual firms form the trusting relationship and achieve cooperation among themselves. Are all theoretical assumptions as forwarded by different researchers, namely legal arrangements to avoid malfeasance, of cooperation and trust, irrelevant in the context of Tiruppur? We can in general say these were irrelevant. It is the behaviour of the firms at least in the internal context of Tiruppur located in social arena which constitutes a trust.

### TABLE 6.1

**Trust in Business Relations**

**Basis of Incontracting and Outcontracting**

<table>
<thead>
<tr>
<th></th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust and Informal Agreement</td>
<td>51 (89.5)</td>
<td>5 (33.3)</td>
<td>1 (6.7)</td>
</tr>
<tr>
<td>Kinship and informal Agreements</td>
<td>3 (5.3)</td>
<td>1 (6.7)</td>
<td>-</td>
</tr>
<tr>
<td>Formal Agreements</td>
<td>2 (3.5)</td>
<td>8 (53.3)</td>
<td>-</td>
</tr>
<tr>
<td>No Incontracting or Outcontracting</td>
<td>1 (1.7)</td>
<td>1 (6.7)</td>
<td>14 (93.3)</td>
</tr>
<tr>
<td>Sample size</td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>

### TABLE 6.2

**Trust in Business Relations**

**Raw Materials Acquisition**

<table>
<thead>
<tr>
<th></th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Immediate Payment</td>
<td>8 (14.0)</td>
<td>4 (26.7)</td>
<td>14 (93.3)</td>
</tr>
<tr>
<td>Post Payment</td>
<td>49 (86.0)</td>
<td>11 (73.3)</td>
<td>1 (6.7)</td>
</tr>
<tr>
<td>Sample size</td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>

* All figures in brackets are in percentage
* Sources of data - field work, 1997-98
However, in Tiruppur some entrepreneurs had reported that level of trust is declining now-a-days. Some firms are running away without paying the subcontractors their due. Even many firms delay their payments to subcontractors as a result there is unnecessary harassments. During our field visit there were some suppliers and jobworkers running around to recover their due and were forced to come on a latter date. In the Tiruppur network system if one exporter does not pay then whole jobwork network suffers. Some job work firms reported that they now do business only with known parties, who come regularly to them (repeated interaction) and provides timely guaranteed payments. After the export boom of late 1980s many jobworking firms have started their business in Tiruppur and there is competition to get the job work even by quoting low rates. Many big exporters know the helplessness of the jobworking firms for they have no alternative but to go to them for work. So these small job work firms are virtually compelled to do work on long term credit. This was the ground reality during our visit to Tiruppur in June 1997.

Do we need to say that institutional intervention is necessary to prevent such situations? Some contract laws are necessary to avoid such situations and to give protection to job working firms. Many associations of dyers, screen printers, Kaja button, apart from hosiery manufactures and exporters have organised themselves in Tiruppur. Yet Tiruppurs industrial space is based on trust in business relations (Table 6.1 and 6.2). Altogether 51 firms (about 90 percent) out of 57 firms we interviewed in Tiruppur reported that they do incontracting or outcontracting on trust and by informal agreements. Regarding raw material acquisition 49 firms (86 percent) reported that all payments are done latter. Only 3 firms had reported that they do incontracting or outcontracting on kinship basis, whereas only 2 firms reported that they do subcontracting by formal agreements. However we recommend the effective role institutions or law to safeguard business relationships among the firms.

Kannur on the other hand does not have a complex network like Tiruppur. The main exporters get the order and if it is beyond their capacity to deliver in time they subcontract it out to small jobworkers or to the cooperatives. Majority of the firms (8 in total or 53 percent, Table 6.1) reported that they subcontracts on
formal agreement, while the rest do it in an informal manner. Altogether 11 firms out of 15 we interviewed (about 73 percent) reported that they get raw materials on one month credit (Table 6.2). The reason they gave us was that agents who supply raw materials have to do business as well. For a month's credit they charge 2 percent interest, while immediate cash payments mean 2 percent discount.

In Morbi, firms are generally vertically integrated. There is not much evidence of an incontracting and outcontracting system. In very few cases jobworks are done in other firms. As we have discussed in Chapter IV, like Tiruppur, in Morbi it is fairly easy to enter business with little investment. For the most part a moulding machine can be used to make the cabinet boxes for clocks, raw materials and the quartz which is imported or supplied by agents were needed to start the business. Therefore, subcontracting system and so trust does not arise in business relations in this regard. However, for all the raw materials acquired by the firms, payments have to be made immediately them (Table 6.2). Only one firm out of 15 in Morbi reported that they pay for the raw material at a latter date.

Till now we have discussed about trust in internal or local business environment. Let us now look at the marketing of products of the towns, which does not involve local transactions and so the level of trust in this case is likely to be different. The question is does geographical proximity enhances trust? Altogether 22 firms in Tiruppur (about 40 percent) reported Yes, and only 5 said (8 percent) No and 30 firms (52 percent) did not remark on it. In Kannur and Morbi, majority of the firms did not provide any comment on it (Table 6.2). Let us look at this matter in some depth.

<table>
<thead>
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<th>TABLE 6.3</th>
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<tbody>
<tr>
<td><strong>Trust in Business Relations</strong></td>
</tr>
<tr>
<td><strong>Geographical Proximity and Trust</strong></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
</tr>
<tr>
<td>N.A</td>
</tr>
<tr>
<td>Sample size</td>
</tr>
</tbody>
</table>

* All figures in brackets are in percentage

*Sources of data: field work, 1997-98
Is there any risk to getting the payments from export in Tiruppur? Do the firms give credit to their customers? Indeed 42 firms (about 74 percent) of the total 57 firms we interviewed reported that they give credit to customers (Table 6.4). However, recent loss and fraud cases were reported by many firms. This compelled exporters to take precautionary measure as initiated by Tiruppur Exporters Association (TEA). TEA has even come out with guidelines on how to do business in the export market. Many exporters suffered because of huge verbal and telephonic orders which were then frequently cancelled and also because of non-payments. That is why many exporters now stick to Letter of Credit (LoC) payment system, particularly in international transactions. Under the Letter of Credit system, the buyer’s bank commits itself irrevocably to honour its obligations under the credit. So there is no risk in doing business by Letter of Credit. With known and trustworthy buyers, with whom repeated interactions exits business is done with Documents on Payments (DP) and Documents on Agreements (DA) systems. Altogether 20 firms (35 percent) reported that they do business by Letter of Credit only. Only 4 firms out of 57 reported that they follow DP or DA systems. Altogether 8 firms reported that they get payments through their agents. Whereas majority of the firms we interviewed (25 in total or about 42 percent) reported that they get payments simply by cheques (Table 6.4).

**TABLE 6.4**

**Trust in Business Relations**

<table>
<thead>
<tr>
<th>Marketing of Products</th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Credit to Customer:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yes -</td>
<td>42 (73.7)</td>
<td>8 (53.3)</td>
<td>8 (53.3)</td>
</tr>
<tr>
<td>No -</td>
<td>15 (26.3)</td>
<td>7 (46.7)</td>
<td>7 (46.7)</td>
</tr>
<tr>
<td><strong>Mode of Payments:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Letter of Credit:</td>
<td>20 (35.1)</td>
<td>5 (33.0)</td>
<td>5 (33.3)</td>
</tr>
<tr>
<td>Delivery against Payments:</td>
<td>4 (7.0)</td>
<td>6 (40.0)</td>
<td>--</td>
</tr>
<tr>
<td>Agents:</td>
<td>8 (14.0)</td>
<td>4 (26.7)</td>
<td>10 (66.7)</td>
</tr>
<tr>
<td>Cheques:</td>
<td>25 (43.9)</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td><strong>Sample Size:</strong></td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>

*All figures in brackets are in percentage
*Sources of data: field work, 1997-98
In Kannur and Morbi 8 firms (53 percent) in each town, reported that they do marketing on credit. Again in both towns 5 firms (33 percent) of the total 15 we interviewed reported that they do business only by LoC. In Kannur DP system is more prevalent. This payment system is trustworthy. Because of repeated interactions with the buyers for many years has made this prevalent among Kannur entrepreneurs. In total 6 firms (40 percent) reported that they do business by DP or DA systems. In Morbi mode of payments in markets is mainly done agents through cheques. Altogether 10 firms (67 percent) had reported this (Table 6.4).

Did the firms enter into a litigation due to non-payment of their dues? In Tiruppur only 2 firms, in Kannur 3 firms and in Morbi 2 firms reported that they had to go for litigation (Table 6.5). Few had told us since law takes its own time it is better to avoid doing business with unknown buyers.

**TABLE 6.5**

<table>
<thead>
<tr>
<th>Litigation in the Past</th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>2 (3.5)</td>
<td>3 (20.0)</td>
<td>2 (13.3)</td>
</tr>
<tr>
<td>No</td>
<td>55 (96.5)</td>
<td>12 (80.0)</td>
<td>13 (86.7)</td>
</tr>
<tr>
<td>Sample size</td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>

*All figures in brackets are in percentage
*S Sources of data field work. 1997-98

What can we comment from this study on trust in business relations in the towns? Internal functioning of industrial activity through social relations is good and people generally want to maintain good business relations. However, in some case to avoid malfeasance, associations support is necessary. These are of not much relevance in Kannur and Morbi as the two towns do not have a complex network of production. However, due to the emerging trend of risk in non-local payments, we recommend that contract law is necessary in business relations. Social relations and repeated interaction need to be supported by legal institutional support, so that law in return guarantee relations and interactions rather than resort to time consuming litigations.
VI.6.b Cooperation, Competition and Social Relations

All firms exist in the towns to do business only and there is no charity. Still most of the entrepreneurs reported that they were friends too. Friendship and business are both different things. Particularly in Kannur and Morbi everybody know each other. As they were doing business, they had to fight for their own market. There can be two ways they can gain access to market. Through some positive practices like quality, design of the products, sales network, good bargaining prices and prompt delivery. Negative practices include copying design, wooing customers, misinforming rival producers. Compromising on quality through price cuts or low price quoting can be also considered as a negative practice. Let us look at these issues of competition in the three towns.

Altogether 46 firms (about 80 percent) of the total 57 firms interviewed in Tiruppur reported that quality was their prime concern in market competition. While 10 firms (17.5 percent) reported that they depended on quoting low prices to face competition (Table 6.6a). Design of products, low price quotation, prompt delivery, sales network came in second priority for some firms. For the Kannur firms, both quality and design were seen as first priority especially when issues of competition came to the fore. Out of total 15 firms 14 had reported that quality is their main concern along with the design. One firm did not show its concern for design. However few rely on low price quotation to get the market for their products. Morbi scene is different from Tiruppur and Kannur. Since on the technical part most of the firms depend on assembling of imported quartz of clocks, quality has not much to do. It is design of the clock which gives market to the firms. So most of the firms we interviewed (11 in total or 73 percent) emphasised their concern for design as a basis for competition in the market. Only 4 firms out of 15 firms interviewed (26 percent) showed concern for quality.

TABLE 6.6
Issues of Competition
(a) Positive Practices

<table>
<thead>
<tr>
<th></th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quality</td>
<td>46 (80.7) Pl.</td>
<td>14 (93.3) Pl#</td>
<td>4 (26.7) Pl</td>
</tr>
<tr>
<td>Design</td>
<td>1 (1.8) Pl, 21 (36.8) PII</td>
<td>13 (86.7) Pl#</td>
<td>11(73.3) Pl; 4 (26.7) PII</td>
</tr>
<tr>
<td>Sales Network</td>
<td>1 (1.8) PII</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Price</td>
<td>10 (17.5) Pl, 17(29.8) PII.</td>
<td>1 (6.7) Pl; 1 (6.7) PII</td>
<td>2 (13.30 PII)</td>
</tr>
<tr>
<td>Prompt Delivery</td>
<td>3 (5.3) PII</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sample Size</td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>
Issues of competition

(b) Negative Practices

<table>
<thead>
<tr>
<th></th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Copy design</td>
<td>-</td>
<td>-</td>
<td>13 (86.7)</td>
</tr>
<tr>
<td>Wooing Customers</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Misinforming Rival</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Producers etc.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sample Size</td>
<td>57</td>
<td>15</td>
<td>15</td>
</tr>
</tbody>
</table>

* All figures in brackets are in percentages
* Sources of data field work, 1997-98
* PI - First Priority
* PII - Second Priority
# In Kannur gives equal importance to both quality and design.

Are there any negative practices that firms follow to get access to the market? Both Tiruppur and Kannur firms reported that they do not follow negative practices. However, most of the Morbi firms (13 or 87 percent) reported that they copy designs for their products (Table 6.6b). Though nobody had reported about negative practices in Tiruppur, Kannur and in Morbi (apart from copying design) such practices were prevalent in all the three towns. Many firms attempt to misinform the rival firms and woo the potential customers. Interference on others market is the main cause of dispute in these towns. These facts came to be known when matters were discussed the matters with the Associations and some citizen of the towns. One office bearer of Tiruppur Exporters Association (TEA) had told us that they tried to solve many a dispute rather than going to the law. Some firms in Kannur and Tiruppur had reported that good personal relationship with buyers gives the market for the product. The transaction done with the parties for generations helped them to gain the market. One exporter in Tiruppur told us that competitions are tackled by quality, agents and good personal relations. In Morbi competitions in the market is taken care of by the agents who market and sell the products for commissions.

VI.6.c Cooperation and Social Relations

Apart from the highly complex network of production in Tiruppur from where all firms get mutual benefit there is not much cooperation among the firms in Tiruppur. Only 14 firms (25 percent) of the total 57 firms reported that they share job when bulk order has to be delivered on time. Very few (only two in total) had reported that they help each other financially, materially and in labour matters (Table 6.7). However there were incidences of financial help to set up
units, particularly on kinship line. Earlier in Chapter III we had pointed about that whole knitwear industry in Tiruppur is dominated by Gounder caste, where entrepreneurs, labourers all were Gounders. So on caste lines there were incidences of cooperation when one wanted to set up a unit. In our sample not many had reported this. Probably our sample could not come across such situations. In Kannur 9 firms (60 percent) told us that they share jobs. But they did not report about other cooperation like financial help, input and workforce sharing (Table 6.7). We could not find out any form of cooperation in the case of Morbi as such.

**TABLE 6.7**

Cooperation and Social Relations among Firms

<table>
<thead>
<tr>
<th>Cooperation</th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Help:</td>
<td>2 (3.5)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Input Help:</td>
<td>2 (3.5)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Lending Machine:</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Labour exchange:</td>
<td>1 (1.8)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Job sharing</td>
<td>14 (24.6)</td>
<td>9 (60.0)</td>
<td>2 (13.3)</td>
</tr>
</tbody>
</table>

* All figures in brackets are in percentage
* Sources of data: field work, 1997-98

**TABLE 6.8**

Cooperation and Social Relations among Firms

<table>
<thead>
<tr>
<th>Social Relations</th>
<th>TIRUPPUR</th>
<th>KANNUR</th>
<th>MORBI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Solidarity in decision:</td>
<td>18 (14.0)</td>
<td>49 (86.0)</td>
<td>15 (100.0)</td>
</tr>
<tr>
<td>Business Gossips:</td>
<td>31 (54.4)</td>
<td>26 (45.6)</td>
<td>6 (40.0) 9 (60.0)</td>
</tr>
</tbody>
</table>

* All figures in brackets are in Percentage
* Sources of data field work, 1997-98

All the firms in the three towns take on individual decisions regarding their production. Do they have solidarity in decision taking in certain cases like price fixation, labour problems, about some government regulations? Regarding these
matters generally firms under association take common decision. Most of the firms in Tiruppur are not members of an association (particularly of TEA) and so their decision making in this regard is not affected by others. In Kannur too apart from some common problems like fixation of wages for labour, in other matters they are not influenced by others. In production process they take individual decisions. In Morbi we did not find any active association, in operation and rarely they took common decisions regarding the functioning of the industry in the town.

Do the entrepreneurs in the towns gossip and share experiences about their business with fellow entrepreneurs. In total 31 entrepreneurs (54 percent) in Tiruppur reported us that they gossip with each other regarding price fixation, labour problems. In Kannur 6 firms (40 percent) reported that they gossip with each other (Table 6.8). They also discuss about price fixation and labour problems. They told us that they gossip because they were all friends. Whereas those who do not gossip also told us that they all were friends. So it was better not to have any discussion with friends. We did not find Morbi entrepreneurs entering into any form of business gossip with each other.

VI.7: Implications

What are the implications of our study on Embeddedness in industrial space? Our study towns were successful in terms of generating employment and foreign exchange earnings. These towns have grown without much government regulation and interventions. The initiative set by some enthusiastic entrepreneur and tradition to maintain it in the social arena made the towns successful. Granovetter is right that embeddedness in personal and social relations generate trust in business relations to give the required sustainability. Earlier there is no role of institutions either social or legal in fostering business relationship. However, with the present rise of extreme competition in the towns, particularly to gain access to the market by firms have led to some disputes among them. Moreover incidences of non-payments in business relations compelled the firms to think about the futility of personal relationships. Some firms have started reporting such incidences. So who can give assurance against such malfeasance apart from concrete personal relationship? Is it social or trading institutions or it is legal institutions? Since every relationship by its nature is both rivalrous and co-
operative (firms have to compete over proceeds of production) for the smooth functioning of the industrial space, institutional support is necessary. Many things regarding cooperation and competition can be handled by institutions in a social context. In this context we take the example of Tiruppur Exporters Associations. Litigation brings bad name to the firms. If personal relationship fails to solve some disputes (Granovettor was optimist about this) institutions can help to solve such disputes (TEA is a good example). So to maintain trust and relationship, concrete personal relationship can be the first line of defence and social institutions came in later to support if the former fails. We had discussed in this chapter how important is the role of trust in the functioning of industrial space for efficiency and higher productivity.

What can be the role of law or legal institutions in the industrial space? Can we call it as third line of defence? Law can give space within which firms can work and law sets out obligations of the firms to avoid any malfeasance. Since litigation and law can bring bad name to the firms, some researchers (Arrighetti et al, 1997) want it to keep it at a minimum level. But such contract and law is now increasingly becoming necessary, particularly in a non-local marketing context because of the non-payment against the delivery of goods. Sometimes even good personal relationships fail to get the payments due. That is why many exporters in our study towns stick to the letter of credit (LoC) system.

So at the end we can comment that concrete personal relationship, social institutions and legal institutions of law have their own role in generating trust and assuring business and good business relationship in an industrial space. For efficient functioning and a reputation of a successful industrial space there are several yardsticks to be kept in mind. Intense competition might lead the firms to resort to price cut thereby compromising on quality. Such a bad reputation can be disastrous not only for the firms but for the whole town. Here social institutions and law have their role to play.

1 Vertical disintegration means segregation of production functions of a firm, through the development of a diffused subcontractors net.

2 Low sunk cost means – not very highly specialised in specific investment so that they adopt to changing external environment.
3 Classical and neo-classical economics operates with an atomized, individualistic undersocialised conception of human action. They disallow impact of social structure and relations on productions, distribution or consumption.

4 One incentive is not to cheat, is the cost of damage to one's reputation. Individuals with whom one has a continuing relations have an economic motivation to be trustworthy, so as not to discourage future transactions.

5 Departing from the pure economic motives, continuing economic relations often become overlaid with social content that carries strong expectations of trust and abstention from opportunism.

6 What makes behaviour more predictable – because departing from pure economic motives, continuing economic relations often become overlaid with social content that carries strong expectation of trust and abstention from opportunism. This closes of some fears that create difficulties among strangers- in human relations the degree of confidence must be more variable.

7 Atomized social relations – here in the absence of sustained social relations – one could expect only minor conflicts. In atomized or individualistic social situations, one expects them to be grouped together as a team to pursue force and fraud.