CHAPTER – I

INTRODUCTION

One of the major changes involved in development is industrialization. Industrialization is the key to restructure the economy. It is the advancement of a community along with involving new and better methods of production and expanding the size of the firm (Kirkpatrick, 1985). Industrialization is an effective instrument of growth and welfare. It has been defined as a process in which changes of series of strategic production functions are taking place. It involves three basic changes that accompany industrialization, mechanization of an enterprise, building of a new market and exploitation of a new territory. When we go deep into the process of industrialization the analysis of various operational aspects of the firm becomes imperative because a firm is the constituent unit of every industry and hence, plays a vital role in the industrialization, where as an industry consists of firms producing identical or close substitutes for some and relatively distant substitutes for all other outputs. Any such subgroup may be called industry (Bain, 1968). In the journey to economic growth of an economy, manufacturing sector plays a pivotal role. Hence, the importance of need to evaluate this sector is justified.

On the eve of independence in 1947, India inherited a highly restricted industrial structure comprising textiles, jute, sugar and iron and steel including some limited range of engineering in railways. The industrialization process in the pre-independence period manifested a distorted picture due to deliberate in built bias towards colonial rules, governing the growth of raw materials, smallness of the domestic market limited by low level of real income, lack of investment climate, absence of entrepreneurship and lack of financial and transport infrastructure. Thus, after independence, India accepted rapid industrializations as a policy goal for the rapid development and structural transformation of the economy.
In India, during the planning era, there has been a phenomenal growth of the industrial sector. Rapid industrialization of the country has been one of important objectives of planning since the second plan. The Second and Third Five Year Plans laid emphasis on the development of basic industries and the establishment of machine building capacity. Under the Fourth, Fifth and Sixth plans, although industrialization does not find an explicit mention among the objectives, perhaps for the reason that it is already an established fact in economic structure of the country, yet the basic strategy in this respect evolved in the Second Plan still hold good.

**Industrial Development in India**

Historically, industrial development in India has proceeded in three stages. In the first stage, secondary industry is concerned with the processing of primary products. "Milling grain, extracting oil, tanning, leather, spinning vegetable fibers’, preparing timber and smelting ones". The second stage in the evolution of secondary industries comprises the transformation of materials making bread and confectionary, footwear, metal goods, cloth, furniture etc. The third stage consists of manufacture of machines and other capital equipments to be used not for the direct satisfaction of any immediate want but in order to facilitate the future process of production.

In a country, like India consumer goods industries should have been given in priority to improve living conditions of the poor by expanding employment opportunities and supply of wage goods at the faster rate. Industrial development in India has been playing a crucial role towards structural diversification, modernization over the last forty five years and so has been a striking feature of the Indian economic development. Not only in India, but in all countries of world, it has been realized that industrialization is the major source of economic development and key for reconstructing the economy.

Since independence, India adopted a mixed type of economic system, in which public and private sector exist side by side. On the eve of independence, the agricultural sector was the main stay of Indian economy. Large extent (approximately, 72.1
percent in 1951) of the population was engaged in this sector and a major part of GDP (approximately 59 percent in 1950-51) was brought from this sector. In the post independence period, India started to develop its industrial sector. It was the Second Five Year Plan where the outstanding efforts were made to develop heavy and basic industries in the economy and the fruits of which may be distributed to other sectors of the economy. During the 20 years from 1950-51 to 1970-71, some basic and heavy industries such as iron and steel industry, heavy engineering industries were developed.

In the Industrial Policy Resolution of 1948, also known as economic constitution of India, announced on 6th April, 1948, special emphasis was laid on the development of cottage and Small Scale Industry (SSI). Besides proper steps were taken to design a suitable tariff policy, taxation policy and also for maintaining sound industrial relations between management and labour. Regarding foreign capital, the industrial policy recognized the need for security and participation of foreign capital and enterprise especially in respect of industrial technique and knowledge for enhancing the pace of industrialization in the country. However, the policy was to lay down the foundation of mixed economy with the participation of both public and private sector for accelerating the pace of industrial development in the country.

After the proclamation of Industrial Policy Resolution of 1948, Indian economy had to face a series of economic and political changes, which necessitated the formulation of a fresh industrial policy of the country. In the mean time, the First Five Year Plan was completed and socialistic pattern of the society was accepted as a major objective of the country's social and economic policy. Thus, on 30th April, 1956, a second industrial policy was adopted in India replacing the policy resolution of 1948. The Industrial Policy Resolution (IPR) of 1956 had made a clear-cut provision for the expansion of both public sector and private sector enterprises in the country in coordinated manner with high degree of flexibility in its policies. Further, the policy resulted in the rapid expansion of the public sector in basic and heavy industries in the
country by establishing three Iron and steel plants with the foreign collaboration in Bhilai, Durgapur and Raurkela.

Industrial Policy Statement of 1973 was made in the context of a series of socialist policies including bank nationalization (1969) and Monopolies and Restrictive Trade Practices (MRTP) Act (1969). While it reiterated the philosophy of IPR of 1956, the statement made licensing stringent for large industrial houses. The recognition of the concept of joint sector was another step. A secretariat of industrial approval (SIA) was also established to provide single-window clearance. Industrial Policy Statement (IPS) of 1977 by Janta government emphasized the importance of small and cottage industries and reserved certain industries for these sectors. A tiny sector with (investments limit of Rs.1 lakh) was also recognized. The Statement had a strong bias against large scale and heavy industry. The establishment of a District Industries Centre (DIC) was another notable reform. These DICs have been considered to function as the nodal points for raw material distribution, credit facilities, and marketing for small scale and cottage industries. Borrowing by large scale industries for expansion/ modernization was severely restricted.

The new congress government drafted Industrial Policy Statement of 1980. It sought to reverse the ideological bias of the IPS of 1977 by reaffirming its faith in IPR of 1956. However, the statement was "outward looking" in its commitment to expert production and liberalization of licensing. It advocated coordinated development of small medium and large industries. Industries sickness was sought to be addressed by devising an early warning system.

Indian economy had reached a stage of deep crisis by June 1991, brought on by the Gulf War, lack of financial discipline by earlier governments, failure of monsoons and bunching of external payments obligations. India was for the first time, close to defaulting on its international commitments. India's credit rating was downgraded and she could not borrow from external commercial markets. The annual rate of inflation had touched 17 percent by August 1991. Foreign exchange reserves had plummeted
to a little above $1 billion, barely sufficient to meet the country's import bill for a week. Fiscal deficit had risen to 8.4 percent of GDP. Current account deficit in balance of payment was an unsustainable $9.9 billion. It was in this backdrop that India launched the New Economic Policy (NEP) announced by the Narasimha Rao government in Dr. Manmohan Singh's June 1991 budget. Broadly, the measures taken are classified into:

1. A short-term stabilization programme to bring the economy back on track;
2. A medium to long-term structural adjustment programme to correct structural rigidities and bottleneck in the economy.

The aim of stabilization programme was to control inflation and remove Balance of Payment (BOP) deficit. It consisted of four distinct areas of action-fiscal policy, monetary policy, exchange rate policy and social sector policy. In fiscal policy, the objective was to reduce the government fiscal deficit by reducing government expenditure on one hand and increasing the tax base, on the other hand. An ambitious target of lowering the fiscal deficit from 8.4 percent in 1990-91 to 5 percent of GDP in 1992-93 was fixed. A review of food and fertilizer subsidies was undertaken. Chelliah Committee was appointed to look into the taxation on structure and suggest measures to augment revenue. Because of these measures, the fiscal deficit fell to 6 percent in 1991-92 and 5.6 percent in 1992-93. In monetary policy, credit was tightened by increasing interest rates. Narasimha Committee was appointed to recommend measures for financial sector reforms. RBI was given more autonomy and the automatic monetization of government's deficit was given up. In order to correct the exchange rate, rupee was devalued by 23 percent. In February 1992, the government announced the Liberalized Exchange Rate Management System (LERMS) to promote trade, and in next stage rupee was made convertible on current account in 1994-95 budget. In social sector policy the experience of countries in Latin America and Africa, which had undertaken stabilization programmes in the 1980s, had shown that due to the rigid public expenditure control and demand compression, which accompanied stabilizing the poor, suffered disproportionately, drastic cuts in
subsidies and increase in taxation impoverished the weaker and vulnerable sections. International Financial Institutes like the World Bank and IMF that recommended stabilization measure became unpopular on this account. It was UNICEF, which undertook a systematic study of the social cost of stabilization, and structural adjustment in late 1980s recommended adoption of a 'human face' for adjustment.

Structural Adjustment Programme (SAP) consists of a set of medium term policy measures that require stabilization on measures to be first adopted. It consisted of Industrial Policy Liberalization, Public Sector Reforms, Financial Sector Reforms and Trade Policy Reforms. Industrial Policy was drastically re-written in July 1991 with the abolition of licensing of industries on virtually all items except those constituting environmental problems, or involving security. MRTP legislation has been liberalized to encourage investment by large industrial houses. As a result of these measures, industrial production, which was virtually stagnant in 1991-92, grew to 9.3 percent in 1993-94 and 12.4 percent in 1994-95. Public Sector Reforms include getting out of areas where the private sector will be more efficient and disinvestment of equity in selected units. As public sector unit account for a large share in the government’s domestic debt a drastic reduction in the budgetary support to such units was another policy option. The list of the industries reserved for the public sector has been reduced from 17 to 6. Financial Sector Reforms are based on the recommendation of Narasimha Committee. The main features of these reforms are:

- To unshackle the banking system from excessive government control even without de-nationalizing, and to curtail the tendency of the government to rely on credit control measure as extra budgetary sources of inexpensive credit.
- Capital market reforms started with the establishment of Securities and Exchange Board of India (SEBI) in February 1992.
- Permitting Foreign Institutional Inventors (FIIs) to undertake portfolio investment and Indian companies to undertake Euro issues are other major steps.
All these efforts were made to unshackle the Indian industry from the unnecessary bureaucratic control and to enhance the competitiveness of Indian industry via increasing its efficiency and productivity.

**Manufacturing Competitiveness**

Competitive advantage is a firm's ability to transform inputs into goods and services at a maximum profit on a sustained basis, better than competitors. Comparative advantage resides in the factor endowments and created endowments of particular regions. Factor endowments include land, natural resources, labour, and the size of the local population.

In the 1920's, Swedish economists Eli Hecksher and Bertil Ohlin developed the factor-proportions theory, according to which a country enjoys a comparative advantage in those goods that make intensive use of factors that the country has in relative abundance.

Michael E. Porter(1980) argued that a nation can create its own endowments to gain a comparative advantage. Created endowments include skilled labour, the technology and knowledge base, government support, and culture. Porter's Diamond of National Advantage is a framework that illustrates the determinants of national advantage. This diamond represents the national playing field that countries establish for their industries.

A growing and competitive manufacturing sector has become the prime mover of modern economy. Both developed and developing countries have been focusing their strategies on improving their manufacturing sector and for an increased share in the global market. Manufacturing accelerates the effective use of primary products and drives both the industry and service sectors by inducing multiplier effects through numerous linkages. Manufacturing is essential for maintaining a balanced growth of the country. It can create large employment opportunities. As a result, the race for competitiveness in manufacturing among nations has gathered momentum supported
by a strong foundation for innovation, advanced technology, and high-end process development programmes. Fast reductions in the manufacturing cost have become one of the core aspects for increasing competitiveness in manufacturing sector. In a developing country like India, manufacturing activities help in providing better employment for those who belongs to rural and agricultural background. Therefore, manufacturing needs to occupy centre stage for providing the right type of employment and for effectively competing in the dynamic global markets. According to the latest World Economic Forum’s Global Competitiveness Report (2007), India has improved its global competitiveness and is ranked ahead of the other BRIC countries - Brazil, Russia and China. Among the BRIC countries India was the only country which had improved its ranking compared to the other three.

India’s economy is on the hinge of an ever increasing growth curve. With positive indicators such as a stable 8-9 per cent annual growth, rising foreign exchange reserves, a booming capital market and a rapidly expanding FDI inflows, India has emerged as the second fastest growing major economy in the world. The economy has been growing at an average growth rate of 8.8 per cent in the last four fiscal years (2003-04 to 2006-07), with the 2006-07 growth rate of 9.6 per cent being the highest in the last 18 years. Significantly, the industrial and service sectors have been contributing a major part of this growth, suggesting the structural transformation underway in the Indian economy. India’s manufacturing base, which is the fourth-largest among emerging economies, is among the fastest growing and has seen more investments as a proportion of gross domestic product than any country except China. After the IT boom, a manufacturing revolution has been well underway in the Indian economy, spurred on by the increasing presence of multinationals, scaling up of operations by the domestic companies and expanding domestic market. The sector has been averaging 9 per cent in the last four years (2004-07), with a record 12.3 per cent in 2006. The spurt in growth is evident in areas focussed on skill-intensive production processes, where India has an edge in the global market. These include electrical and power engineering, speciality chemicals, pharmaceuticals and auto components among others. The recent thrust on special economic zones (SEZs) is also expected to give a
boost to the manufacturing sector. This will be further fuelled by the investment by the big retail chains (World Economic Forum, 2007 and Economic Survey, 2007-08).

Also, manufacturers from across the world are looking at India as a potential manufacturing powerhouse. India's vast domestic market and availability of low-cost workers with advanced technical skills which has all the required skills in process, product, and capital engineering, thanks to its long manufacturing history and higher education system, has been instrumental in attracting the ever expanding number of multinationals who are setting up their manufacturing base in the country. The sheer size of the Indian market has obvious appeal.

India offers abundant engineering and technical manpower, producing annually about 4 lakh graduate engineers. Significantly, the technical workforce is set cross the two million mark this year, with the march from one million to two million happening in just about three years. With such a large technical workforce it is possible for the high skill-sectors to produce almost forty per cent of the manufacturing output in India. Taking advantage of this fact, several multinationals operating in skill-intensive industries requiring advanced technical expertise have set up their shop in India World Economic Forum, 2007).

The Government has taken several initiatives to accelerate growth in this sector and improve competitiveness of Indian industry in general and manufacturing in particular:

- Implementation of technology up-gradation schemes for various sectors such as small scale industries, textiles, food processing among others.
- Implementation of industrial infrastructure up-gradation programmes on cluster basis.
- Easier access to inputs at competitive prices and rationalization and reduction in duty rates.
- Encouragement to foreign technology collaborations and liberalization of FDI
in manufacturing activities.

- Launch of "Visionary Leadership in Manufacturing" programme to generate 300 visionary leaders in manufacturing in the next three years.
- Implementation of Special Economic Zones Act.
- Starting the construction of Delhi-Mumbai Industrial Corridor in cooperation with Japan External Trade Organization (JETRO).

To further encourage manufacturing growth, the Government plans to set up Manufacturing Investment Regions (MIRs) on the lines of Petroleum and Petrochemicals Investment Regions (PCPIR). In the case of exports also, Indian manufacturing sector has made substantial improvement in recent years.

Indian manufacturing sector contributes about two-thirds of the total exports of the country. 'Made in India could become the next big manufacturing exports story' says a report by McKinsey. India, with its proven track record in the skill-intensive industries and the global trend to manufacture and source products in low cost countries, is well placed to emerge as one of the leading hub for manufactured exports. No doubt, the growth of the Indian economy largely depends on the manufacturing sector. The overall growth rate is tardy, shows downward trend from 1991 through 2005. This is a very depressing phenomenon in spite of few industries are showing a remarkable presence in the international markets with both products and investments.

**Barriers to Competitiveness of Indian Manufacturing Sector:**

A nation’s overall economic performance is enhanced or inhibited by the performance of the individual industry sectors. In the Indian context, manufacturing was recognized as the main engine of economic growth and creation of wealth and accordingly, emphasis was placed on growth of industry in the five-year plans. However, the share of manufacturing has stagnated at 17 per cent of GDP for over two decades. This is much lower than the share in other comparable economies.
One of the major reasons for this has been the inability of India to build and maintain competitiveness needed to meet the global challenges as well as to develop a larger domestic market through low cost production. Foreign direct investment (FDI) contributes to a country’s economic growth and development. It adds to the fixed capital formation and has a positive impact on balance of payments without the risk of debt creation or the volatility associated with short-term portfolio capital flows. It brings technology, know-how, managerial skills and access to global markets. It also increases the efficiency and competitiveness of local firms.

While the recent findings by Global Competitiveness Report, 2007 attest the inherent strength of the Indian economy and corroborate the potential of India in the global investment scenario, concerns expressed by them about the investment climate and related issues would also need to be addressed. These concerns include issues such as bureaucracy and political instability, weak/inadequate infrastructure and concerns about intellectual property rights, heterogeneous nature of Indian markets, and business regulations. India and China are the two most talked about Asian countries today in terms of economic growth, but FDI inflows into India is in no way comparable to China. Although India has made progress in some areas for improving the business climate, the most striking feature is that it ranks lower than its Asian peers in most of the categories. Therefore, India needs to seriously address the entry procedures for MNCs to set up a business in India.

Moreover, the linkage between trade and FDI indicates that FDI plays less important role in driving India’s export growth except the IT field. The FDI, which acquires large chunks of equity in Indian firms catering to the domestic market, uses these firms to market import-intensive branded products and then takes out large amount of foreign exchange in the form of technology payments and dividends. The government should streamline the FDI inflow. In terms of emphasis, the effort should be to encourage foreign investment that uses India as the outsourcing base for world market production with positive net effect of employment and balance of payments. If outsourcing in software and IT-enabled services is seen as such a major source of
strength for India, there is no reason why outsourcing in manufacturing should not be seen as positive, and provided more privileges than foreign investment catering primarily to the domestic market and regulated for balance of payment reasons.

Historically, India has had a highly fragmented industry structure. The manufacturing sector in India is characterized by a significant number of small scale and even unregistered manufacturing firms. Small and medium scale enterprises in India have received significant preferential treatment - both in terms of specific sectors being reserved exclusively for them and in terms of preferential excise and other fiscal concessions. Since the preferential treatment is contingent on these units remaining small, there is no incentive for these units to expand. This has eroded the competitiveness of Indian manufacturing and has prevented India’s market size from being translated into scale for manufacturing.

No doubt, the industrial policy should encourage small scale production with both employment linkage effects in mind. Protecting small scale production with the employment objective in mind in a labour-surplus economy is not a form of charitable intervention but rational economic policy. Protection of small and medium entrepreneurs (SMEs) would involve a rethink of excessive import liberalization in sectors where small-scale protection is viable, a restitution of measures of protection like reservation of production and differential tariffs, and a conscious direction of credit from the appropriate financial institutions to meet the investments and working capital needs. Corporate - SME linkage is a major thrust area for making the SMEs globally competitive and to protect from foreign substitutes. Backward and forward integration of SMEs with corporate should be mooted and a value chain should be created at the corporate level, so that, the SMEs will be protected and the possibility of growth of this sector will be tremendous.

Today the public sector in India is characterized by its inability to face up to competition in an increasingly competitive environment, brought about by the LPG reforms. Wrong investments in men and machinery and failure of management to
appreciate the need for changing corporate culture in an era of global competition have also led to the situation. Global competitiveness of most of the public sector units is very poor, even at the domestic level. Of course, the performance has improved in the last two fiscal, but it has been due to the emergence of few public sector units including the ‘navratnas’. The survival of the public sector units would depend on strategies aimed at restructuring -business operations, organizational management, technology upgradation, labour management and financial reengineering.

Some initiatives are taken by the government to improve the infrastructure, which is the foremost factor for the corporates to be globally competitive. One success story is the initiatives taken at Indian ports. At the major ports, container operations have been privatized; as a result, there is dramatic difference in the cargo handling facilities in recent years. True is the case with roads. It is estimated that the efforts put by the former NDA government to make the NHs into quadrilateral, if successfully carried out by the present UPA government; the road haulage time will be reduced to half of its current levels. If road haulage time drops dramatically and port turnaround time is nothing to complain about, it will open up new export opportunities for many Indian corporates and many MNCs will quicken their operations in India because of the saving of both time and cost. Meantime, the progress on the airports and airlines has been slow. For instance, the leasing of airports to private parties has made slow progress and the privatization of Air India and Indian Airlines has come to a copper. As a result there is a severe constraint on business travel and poor facilities for handling air cargo.

Adoption of latest technology and infrastructure is also very poor with many firms especially worse in the case of most of the PSUs. Because of long gestation period, and many social implications, the infrastructure sector compares unfavourably with manufacture and many other sectors. Specific policies in this area are needed to make infrastructure attractive. Clearly, for many firms, there is a wide gap between the potential demand for infrastructure for high growth and the available supply. In order to make the core sector attractive for FDI, the government’s move to modify the 49 per
cent cap on foreign equity in the infrastructure sector to render fund mobilization easier is a welcome move.

Since the initiation of economic reforms, India’s outward orientation has increased considerably. The destination pattern of Indian exports has remarkably changed whereby the importance of developing countries as an export market has improved a lot. There is, however, some concern that India has not been able to fully utilize its potential in international trade. Indian exports have a steady increase over the years but India’s share in global trade did not arise as impressively and the major components of India’s exports remain almost unchanged.

Moreover, unlike the East Asian countries where manufacturing sectors have been the major driver of export growth, the contribution of manufacturing exports in India has been comparatively low. The reasons attributed are: small-scale industry reservations, high transaction costs, inflexible labour laws and other industrial bottlenecks. Therefore, despite the recent strides, Indian manufacturing has a long way to go before its exports truly become an engine of growth.

The ability of Indian corporates to prosper and be competitive internationally has a lot to do with the home base. Corporates, which don’t have a vibrant, dynamic environment at home, cannot compete internationally. Moreover, many firms are doing excellent business in India. They are heroes in India, but zeros when they are exposed to the boundaries beyond India. Indian exports are growing, but the growth is dominated by growth in service exports and in particular IT-related services, but they are not indicative of the broader economies. The other notable areas are jewellery, precious metals, textiles/apparels, fish, construction, metals, components and pharmaceutical. Though we have attained significant growth in the above mentioned industries, in terms of world trade the share is too low. Indian firms have to realise the realities and expose themselves fit to the world market.

It must be remembered that we are starting from a relatively-low base of manufacturing. The manufacturing sector has remained quite subdued in India over
the past couple of years (2005-06). No doubt, the manufacturing sector is important to an economy like India’s. If the Indian economy is to grow at 8 percent plus, then manufacturing sector has to start growing faster than the 8-9 per cent it has logged in the last couple of years but the government does have a plan to kick-start the sector. The National Strategy for Manufacturing, a comprehensive plan developed under the National Manufacturing Competitive Council (NMCC), aims to enhance manufacturing sector growth.

The foremost test of global competitiveness is the ability of the firms to withstand foreign competition at home markets. In order to become the economic superpower of the world, India needs to sustain the annual growth rate continuously for the next decade or so. Such a high level of sustained growth cannot be achieved solely on the basis of the service industry. It is here that the manufacturing sector has a crucial role to play. Its growth will provide the thrust needed to take the economy forward to the next higher level and create employment opportunities for the people. The IT industry provided the impetus to economic growth, but it cannot by itself grow the economy and provide enough job opportunities for millions of people in the employment market. It is the manufacturing industry that holds the promise of creating jobs for the millions and meeting the needs of a developing country like India. So, there is a need to enhance competitiveness in manufacturing sector.

Conventional economic theory makes a case for competitive markets on the grounds of efficiency. The concept of competition is central to mainstream economic theory, has been the pivot around which production is organized and prices and incomes are determined. In fact, “In economic life, competition is not a goal: it is a means of organizing economic activity to achieve a goal. The economic role of competition is to discipline the various participants in economic life to provide their goods and services skillfully and cheaply” (Stigler, 1968).

Competition exists only when there are a large number of sellers and buyers and no one individual can influence prices. The economic case for competition is, therefore, made on the grounds that a competitive market system solves both the resource
allocation and income distribution problems through its pricing mechanism. This pricing mechanism has an in-built process through which it maximises consumer and producer’s surplus thereby taking care of the welfare problem. While the homogeneity of the product and an atomistic market structure are sufficient conditions for the existence of pure competition, an additional characteristic is the absence of barriers to entry by new firms. This was recognized by early industrial economists and emphasized repeatedly (Bain, 1956 and Geroski, 1990).

It is therefore clear that competition can be encouraged only when entry into an industry is not hampered by entry barriers. In other words, barriers to entry are essential for the existence of non-competitive behaviour since free entry is bound to create competitive conditions. Entry plays crucial role in ‘Theory of Firm’ and has aroused extensive interest in Industrial Economics. Entry not only helps to decrease monopoly power of incumbent firms, it helps in reducing prices, eliminates excess profit, helps in decreasing inefficiency, stimulates innovations and technical progress. Entry which is guided by factors like market structure, profit possibilities, performance and behaviour of incumbents, prevailing economy conditions, and government policies has always aroused interest of policy makers. The study of entry offers a deep insight into the working of market forces. Not only the market forces but exogenous transitory factors such as policies of industrial regulation, state of economy, capital market determines the entry to a larger extent.

**Entry Barriers and Industrial Policy**

Indian industrial sector had been sheltered by protection through tariffs, quantitative restrictions, industrial licensing etc. the entry into manufacturing sector was merely governed by non-market forces during the ‘license raj’ and it was issued to specific groups. Policies initiated in the year 1980 brought about overhauling of industrial and trade policies bringing in changes in the form of reduced barriers to entry and promotion of competition. The process of change was initiated in early 1980’s but the changes were brought slowly into the system by late 1980’s. The licensing procedure was streamlined and the time frame of issues of license was reduced. By 1981-82 the manufacturing equipment of exploitation of alternative sources of energy was de-
licensed. In 1983-84, nine industries were exempted from provisions of section 21 and section 22 of the MRTP act. The major changes implemented were in form of capacity expansion, exemption from MRTP clearance in backward regions with high priority industries. By March 1985, 25 categories of industries were de-licensed. By late 1985, de-licensing extended to 82 categories. Industries like drug and drug formulation were brought into list.

For industries yet to be de-licensed, broad banding was extended in stages and by January 1986, the number covered was some 28 industry groups which increased to 40 by 1988-89. Moreover, the asset threshold bringing a unit under the purview of the MRTP act, which was set at Rs 20 crore in 1969 was raised to Rs 100 crore in March 1985. In addition to a general policy thrust, important policy measures were undertaken in some key sectors of the industry. In September 1986, de-licensing was extended to certain chemical industries. The industrial policy reforms in late 1980s emphasised the need to ease entry or expansion of incumbent firms and recognised the importance of efficient scales of production. The policy of minimum economic capacity (MEC) was ushered in to prevent fragmentation of capacity and reduce cost inefficiency. By 1988-89, MEC was prescribed for 84 industries, which went up to 108 by 1989-90. However, the main thrust to the reforms in the industrial sector came with the announcement of the new industrial policy in July 1991. The new policy package initiatives removed industrial licensing in all industries except those reserved for the public sector, for the SSI sector and those under compulsory licensing, subject to minimal locational conditions. Restrictions on investment by MRTP and FERA companies were also removed. The most important aspects of this policy package are: (i) Across the board de-licensing and the proposed repealing of the MRTP act, expected to reduce barriers to entry into the Indian industrial sector, (ii) A broader attitude towards foreign collaborations, technical as well as financial and especially the open door policy towards FDI, (iii) policies aimed at reforming the public sector. These policies of industrial regulation were supposed to play a major role in fostering the right market environment to increase competition and reduce barriers to entry. However, some [e.g., Mani 1992, 1995] feel that the New Industrial Policy (NIP) is
still to go a long way in fulfilling the above-mentioned objectives - which only time can tell - especially given the fact that industrial production in the recent past suffered due to import compression, rise in the cost of imports, the BOP crisis, the uncertain atmosphere on investment due to the events in 1992 and 1993. Though economic theory has recognized the importance of the influence of entry on economic performance, direct and systematic statistical evidence of factors that affect entry is meager. It is mainly because formal models of entry suffer from the problem of their lack of testable implications and most of the empirical work is based on such models, which do not permit precise hypothesis testing [Kessides 1991]. However, the small yet growing body of empirical literature throws some light on the various factors that affect the entry phenomenon and presents considerable evidence on the extent and barriers to entry across markets in a number of countries. Empirical work on entry has made significant contributions in the direction of recognising the long run tendencies of entry and its associations with various elements of markets structure in cross-sections of industries [e.g., Orr 1974; Gorecki 1976; Hilke 1984; Kessides 1986; Baldwin and Gorecki 1987; Highfied and Smiley 1987; Schwalbach 1987; Shapiro and Khemani 1987]. More recent empirical studies have broadened this traditional work to include some dynamic aspects of entry through the use of longitudinal and panel data [e.g., Highfied and Smiley 1987; Lieberman 1987; Dunne et al. 1988; Geroski 1988].

In spite of the flurry of empirical research accompanied by interesting results on the international front, it is surprising to note that nothing substantial has been done to study entry and its barriers in India. Keeping in view the changes in the Indian policy framework during 1980s and the NIP of 1991 – aimed at reducing barriers to entry and promoting competition – the present study intends to achieve the following main objectives:

1. To discuss various theoretical issues relating to entry barriers.
2. To explain inter-industry differences in entry patterns in Indian manufacturing sector.
3. To identify and estimate various barriers to entry in Indian manufacturing sector.
4. To distinguish between the impact of various causal factors on the incidence vis-à-vis extent of entry.
5. To suggest various policy measures to enhance healthy competition in manufacturing sector.

Plan of the Study

The study is divided into seven chapters including the present one which consists of introductory aspects of manufacturing sector, industrial policy and competitiveness of manufacturing sector. Second chapter deals with theoretical issues relating to entry barriers. Third chapter reviews the empirical studies consisting of studies on barriers to entry in relation to economies of scale, concentration, product differentiation; capital intensity etc. Fourth chapter gives the outline of database and methodology. In fifth chapter an attempt has been made to study inter-industry differences in entry patterns in Indian manufacturing sector. Sixth chapter analyzes the key barriers to incidence and extent of entry entry. Seventh chapter summarizes the findings and brings out the implications.