Replicating IT Success in Manufacturing

What is the issue?

- India has witnessed extraordinary growth in the information technology (IT) sector in the recent decades.
- In this context, it is essential to understand, in comparison, the manufacturing sector - the shortfalls, potentials and the measures needed.

What led to the IT sector's growth?

- There is a widely-held myth that growth in the IT sector was possible as the sector had no intervention from the government.
- But in reality, the government, at the outset, did the necessary things, needed for IT' sector's success.
- **Internet** - The government spent public money in creating high-speed internet connectivity of global standards with the U.S. for the IT software parks.
- This was done years ahead of telecom modernisation in India.
- Creating islands of high-speed connectivity for a nascent industry independent of the telecom system was a bold move then.
- This enabled the seamless integration of the Indian IT industry into the US market.
- **Trade** - The government brought trade in services into the regulatory framework of imports and exports.
- It allowed the IT industry to import duty-free both hardware and software.
- It also gave it all the incentives that were being provided to exporters of goods.
- This enabled the Indian IT industry to get integrated in the dynamic US market without any disadvantage.
- **Regulations** - In addition to the above, the IT industry was able to function under the Shops and Establishment Act.
- It was, therefore, not subject to the over 40 laws relating to labour and the regulatory burden that these impose.
- **Human capital** - Further, the IT sector had the benefit of low-cost high-value human capital.
- This was actually created by the investments made a generation earlier in higher scientific and technical education.

What do these imply?

- Certainly, the IT success story was possible only because of planned government interventions and did not happen all on its own.
- So the key lesson is that the state can take steps to nurture competitive advantage in a sector; in manufacturing too.
- But there is a false ideological divide of 'state' verses the 'market' and a growing faith in the latter.
- In effect, this argument is hampering the task of replicating the IT success for manufacturing.
- In comparison, to boost manufacturing, China created world class infrastructure.
- This included Special Zones along the coast and even housing for workers.
- It supported them in getting foreign and domestic investment in manufacturing.
- Within a few years, it started becoming the factory of the world and now becoming an economic superpower.

What is the challenge in India?

- In India, development of industrial areas has been the responsibility of the States.
- But there exists the political need to spread scarce resources equitably across regions.
- So the creation and maintenance of globally competitive infrastructure for manufacturing remains a challenge.
- The Central government did recognise this problem, but efforts at addressing this have been feeble.
- Moreover, the efforts are constrained by an excessive faith in the potential of private investment.

What are the shortfalls in the approach?

- **SEZs** - The Special Economic Zones (SEZs) were conceived and promoted from the year 2000.
- These had a zero import duty regime along with no taxes on profits.
- With these, the government provided a favourable regulatory regime.
- But it assumed that the private sector would develop these zones successfully.
- The private sector succeeded in the IT sector as the land and investment needed were modest.
- But other than the IT SEZs, only few manufacturing ones with scale really took off.

- The private sector did not have the scale to create globally competitive physical and social infrastructure for manufacturing to be competitive.
- Here, if the Centre in partnership with the States had taken the lead in assembling land and investing adequately, the outcome could have been quite different.
- The private sector could have been roped in only where it had the potential to.
- **Industrial Corridor** - In 2005, the ambitious Delhi Mumbai Industrial Corridor was set up.
- The initial decision was to get the private sector to invest and develop industrial areas along the Delhi-Mumbai Dedicated High Speed Freight Corridor.
- But it was eventually found that private investment on the scale needed would not be forthcoming.
- The need for Central government financing for the trunk infrastructure was soon realised, but is yet to be developed.
- This is the case with Kolkata-Amritsar and Bengaluru-Chennai Industrial Corridors as well.
- The same applies to the recently proposed idea of developing large economic zones with world-class infrastructure around sea ports.

What should be done?

- A successful IT park equivalent for manufacturing will have to be developed.
- The physical and social infrastructure should be comparable to the best in the world and help connect to the global markets seamlessly.
- Workers' housing which is key to productivity should become an integral part of industrial area development.
- [The software SEZs having housing and workplaces within walking distance had contributed significantly to its success.]
- In addition, such an industrial area needs to be large enough to have the critical mass for generating positive externalities and the increasing returns to scale that follow.
- This has been the key to China's success - such economies of scale have resulted in unbeatable prices for a wide range of manufactured products.
- India needs to build new and large world-class manufacturing areas speedily, especially in the industrial corridors and along the ports.
- These are critical for the competitiveness needed for being part of the global manufacturing supply chain.
- The economic returns and job creation from such investment will be tremendous.

Source: BusinessLine