

This is the accepted version of an article which will be published in the journal *Business and Politics* published by De Gruyter: <http://www.degruyter.com/view/j/bap>

Accepted Version downloaded from SOAS Research Online: <http://eprints.soas.ac.uk/22126/>

Business and labor market flexibility in India: The importance of caste

Lawrence Sáez, SOAS, University of London

Introduction

Since the enactment of economic liberalization measures in India since the early 1990s, there has been an increased participation of the private sector in the Indian economy¹. The conventional stance in the literature on business attitudes toward liberalization generally emphasizes the importance of capital friendly attitude such as investment incentives, including flexible labor market to meet the challenges of global competition and a changing production system. The pressure for business friendly policies and factors market flexibility is enhanced —under conditions of increased economic globalization— due to the competitive pressures for attracting investments and greater policy space to business actors.

One of the observed outcomes of economic liberalization in India has been increasing divergence in economic performance often attributed to variation in investment climate and labor market flexibility across different states in India.² From the perspective of increased economic liberalization in transition economies, it would be plausible to link the demand for business

¹ Ahluwalia 2002

² Besley and Burgess 2004; Aghion et al 2008.

friendly policies including labor market flexibility with an increasing relevance of business in policy making, particularly if we view business as an interest group.³ As such, the choice of business groups as the explanatory variable would be a good starting point given its centrality in the context of economic globalization.⁴

Although there is merit to such an argument, this article argues that the influence of business on policy is determined by wider political dynamics. Using case studies from India, we argue that the presence of business in the social base of political parties, including the influence of caste on partisan orientation, has an influence in the policy process, specifically as it pertains to labor market flexibility. As the case study of subnational variation in investment incentives suggests, business influence is conditioned by the relation between business and the political party in government, which in turn is determined by the representation of business interests within parties. To put it simply, reforms understood through investment friendly policies and labor flexibility does not correspond to the size of the private sector (i.e., the material resources of business groups), but to the position of business classes and caste-based groups within the support base of political parties. We shall show that caste identification plays an important role on the position of political parties towards business liberalization policies. Such an outcome reflects the continued importance of partisan orientation in mediating public policies under conditions of globalization.

This article is arranged as follows. The first section deals with the broad theoretical terms, namely the dynamics of business and politics in the context of globalization. Section two elaborates on the business-policy dynamics with specific reference to India, which is followed by

³ Furlong 1997; Heinz et al. 1993; Spiller 1990; Yackee and Yackee 2006.

⁴ Hall and Soskice 2001; Held 1999.

the methodology and framework of analysis developed in section three. Section four presents the analysis based on a mixture of quantitative data and qualitative interviews of business actors across the four cases. Finally the conclusion presents the main findings through a historical-institutional understanding of the relative variation in business influence over government due to partisan orientation.

Globalization and Business

Globalization has been argued to be a beneficial process for capital or business since it strengthens the dominance of the market economy, constricts the role of the state, and expands the influence of transnational corporations.⁵ The increased economic inter-relation between states, global economic and technological changes along with the ideational reorientation has increased the scope of business relative to other social groups within societies. Theoretically, the process of globalization increases the political power of business relative to other social groups as well as the state through increased concentration of economic power, access to policy makers and threat of capital flight. Evidence suggests that bargaining between business and other social groups has been altered under conditions of globalization and scholars have often pointed out increasing policy relevance of “government-business” coalition which incorporates the role of business interests in the policy-making process.⁶ Furthermore, some argue that the process of globalization erodes the powers and the functions of the state. In this setting, multinational corporations can bargain favorably in relation to the state.⁷

⁵ Held 1999; Stiglitz 2002.

⁶ Mazumdar 2008.

⁷ Dunning 1997.

We define business here to refer specifically to the private sector of the economy — which although homogenous as a social group— is marked by a heterogeneous set of interests based on nature, size and location of the firm. As a category, business covers both trade and industry and ranges from small scale traders, medium sized firms to big industries. Intuitively we assume that not all businesses are affected in similar manner by globalization. Even studies on globalization —such as ‘*The Globalization Report*’— recognize that employers are poorly organized and fundamentally heterogeneous in their response to liberalization.⁸

In practice, the response of the business sector to liberalization in a reforming transition economy may vary as incumbent private business firms may be threatened by liberalization. For instance, firms that are favored during phases of import substitution industrialization may favor protectionism as against export oriented businesses that are likely to support liberalization.⁹ However, even though there are variations in business firms’ attitudes toward globalization, this should not be interpreted as opposition to globalization and liberalization per se.

The link between the phenomenon of globalization and the process of public policy involves two broad aspects, namely *internal liberalization* and *external liberalization*. Internal liberalization implies deregulation and the privatization of economic activity. Typically this process augments the importance of the private sector in the economy and policy making and as such is supported by private sector business firms. External liberalization, however, involves broader issues such as economic sovereignty, protectionism, and state promotion of export industries. This form of liberalization has evoked mixed responses from private sector firms

⁸ International Labor Organization 1997.

⁹ Katzenstein 1976.

business, particularly around questions of protecting domestic incumbents from international competition. Within this basic dichotomy, investment friendly policies and labor market liberalization represents a form of internal liberalization.

Business and Public Policies

Within the context of liberalization, private sector firms in reforming economies generally favor greater flexibility as competitive market economy requires adjusting the factor of production in accordance with market signals. As Martin and Swank point out, private sector firms resist any policies that interfere with their profitability by increasing tax burdens, or raising the wage floor of collective bargaining, or interfere with managerial control.¹⁰ In turn, strict labor regulations and trade unions often pose impediments to such profitability and market corrections. Although the necessity of some social regulation is accepted, it is argued that restrictive provisions have a negative effect on growth of business.¹¹ Increasing integration from trade and deregulation further creates competitive pressures on business to reduce costs by accessing concessions from the state and increasing flexibility. In short, globalization increases the pressure for internal liberalization and labor market flexibility.

In the context of India, the adoption of a market-led development strategy has increasingly led to structural pressures for business friendly policies and labor market flexibility. India —like other most transition economies— has a small industrial sector with an overwhelming dependence on the agricultural and the service sectors. As a labor surplus and capital scarce economy in contemporary global system, the state is under pressure to provide

¹⁰ Martin and Swank 2004.

¹¹ Fallon and Lucas 1993; Besley and Burgess 2004.

incentives to capital for investment. Such a developmental model is reinforced by the proliferation of trade and investment regimes leading to creation of certain global norms based on a liberal market model. This is reflected in the repeated concerns from governments—as well as business organizations—about institutional impediments, such as complex labor laws and bureaucratic control in attracting investments and encouraging economic growth. As such, it can be assumed that a large private sector would significantly increase the pressures for investment friendly policies and labor market flexibility due to a mixture of economic reasons.

However, we suggest that the capacity of business to influence public policy as an interest group is not conditioned by economic considerations alone. The literature on interest group influence suggests that in democracies the power of any interest group is significantly determined by wider political dynamics, such as countervailing interests in society, linkages to government and so on.¹² Accordingly, we argue that industrial and labor policy are not merely structurally determined by the size of the private sector or by employer coordination, but also by the interaction of relevant social economic interests within the wider political process. Using the case of India, we will show that the caste identification of policy-makers shapes their predisposition to business-friendly policies. We will evaluate the role of business as a socio-political actor in a wider political matrix, especially in India, a country characterized by the historical weakness of economic interest groups and by a legacy of state presence in economic policy making.

Business and Politics: Determining Public Policy

¹² Becker 1983; Dahl 2005.

Approaching the issue of business influence on policy making, Godbole has distinguished certain broad ideological-political perspectives.¹³ The dominant neo-Marxist view considers that politics under capitalism is dominated by business and interconnected elite of financiers and directors. An important theoretical derivative that challenges the idea of a conscious ruling class has been the *structural dependence of the state on capital*. The dependence of governments on the performance of the voluntary market transactions of business for growth and employment create the necessary conditions for business inducement in liberal democracies. The privileges of business firms are not challenged, because restrictive government policies decrease investment, employment, government receipts, and economic growth.¹⁴

Contradicting the structural predominance of business over public policy, the *class organization hypothesis* considers business as an important and essential part of society with varying relevance over time reflected through state-market dynamics. The class organization hypothesis finds business influence on politics as dependent upon the resources at the disposal of business.¹⁵ Lucas argues that previous development strategies emphasized the importance of interventionist state capable of dominating social groups, including business as it was commonly assumed that business classes were weak and rent-seeking. However, contemporary trends privilege the role of the private sector as economic liberalization and international competition has shifted the balance of power between business and government.

According to the *partisan electoral view*, the relevance of business is a function of political-ideological dynamics is manifested through the party in power. Parties draw their

¹³ Godbole 2004.

¹⁴ Lindblom 1977.

¹⁵ Lucas 1997.

support from different socio-economic groups. The power of such groups fluctuates with the fortunes of their allied parties. As such it has been witnessed that composition of government in terms of ideological orientation and socio-economic basis have implications for macroeconomic policies such as level of unemployment, labor market rules, inflation, income distributions, growth strategies, and growth rates. Broadly the literature suggests that power of business or capital is much restricted under left party while it is greater under administration of right.¹⁶

Finally, another strand of literature advances a *political institutions* argument that government policies and institutions have implications for relative power and influence of interest groups over politics. It is pointed out that institutions of government have significant degree of autonomy and policies that are at odds with prevailing conceptions or objectives are unlikely to be pursued.¹⁷

Since the objective of this article is to determine the role of business interests in policy reforms, implicitly it is recognized that policy is not structurally determined by capital. Moreover, as the case study is based on sub-national comparison of structurally and institutionally similar units, the role of political institutions in policy can be argued to similar, if operational.

Determining business power in India

Empirical research on business-politics is confounded by the problem of identifying the mechanisms and sources of business influence. Business influence on policy may operate on an

¹⁶ Alvarez, Garrett, and Lange 1991; Garrett 1998.

¹⁷ Quinn and Shapiro 1991; Jenkins 2004.

individual as well as on a collective level, both manifestly and latently. Moreover, the effectiveness of business influence over policy is also determined by the type of policy at stake. The three major categories of public policy —distribution, regulation, and redistribution— tends to develop their own characteristic political structure, political process and group relations.¹⁸

The power of business emanates from its control over capital and consequently the forces of production. As explained earlier, modern governments everywhere for reasons of legitimacy have to ensure constant economic growth and, accordingly, must provide rewards to business to help foster that growth. Consequently, we can argue that that if the productive resources (e.g., capital, technology, industries) are under greater control of the government, then business is relatively marginalized. Therefore, the extent of public-private ownership of firms in an economy should provide some understanding of business power.

Expanding on the argument further, theoretically, economic reform should increase the political power of business class vis-à-vis the state. Similarly, in terms of foreign direct investment, the fact that multinational firms have become critical drivers of technological innovation, learning, and economic growth affords them a very “privileged position” in domestic policy. Thus, the increasing concentration of foreign investment as well as private capital should greatly expand the power of business under globalization. The objective of this article is to determine the sources of business influence that corroborate extent of reform specifically investment incentives and labor market flexibility in the selected states of Andhra Pradesh, Gujarat, Maharashtra, and West Bengal.

The specific case studies employed in this article have been selected for the purpose of investigating the relation between business presence and labor market reform. We compare

¹⁸ Godbole 2004.

institutionally and structurally similar political units with variations in labor market flexibility. In order to minimize state specific economic differences that may have an impact on labor market flexibility, the specific case studies of Andhra Pradesh, Gujarat, Maharashtra, and West Bengal mirror the cases selected in previous cutting-edge research on state-business relations in India.¹⁹ These four states are advanced industrialized states employing the largest number of workers in the manufacturing sector. Moreover, the industrial structure of the selected states, along with their respective growth rates and contribution of industry to net state domestic product, provides an important comparative dimension, as such they provide the most concrete example of variation in labor market flexibility.²⁰

Hence in order to compare the relative position of business across the states in India, we evaluate the data on the contribution of industry to the net state domestic product (NSDP), the share of public-private ownership of firms in the economy. We also measure the extent of FDI as proxy variables for material resources at the disposal of business. Further, data on the number of export oriented firms in the economy is also considered due to their privileged position as foreign exchange earner as well as to account for the differences in business orientation based on nature of industry.

4.1 Material resources of business in India

Any attempt to decipher potential influence of business in India should begin with an assessment of resources at their disposal. At the macrolevel, the control over economic resources

¹⁹ Sinha 2005.

²⁰ Nagaraj 2004)

—namely capital and employment— constitutes one of the most important determinants of business influence. The contribution of industrial sector to the net state domestic product (NSDP) provides an important starting point for evaluating the potential influence of business in policy-making. Figure 1 identifies the state-wise share of the industrial sector in four Indian states (i.e., Andhra Pradesh, Gujarat, Maharashtra, West Bengal). [See Figure 1]

[FIGURE 1 ABOUT HERE]

As Figure 1 shows, the contribution of industry to NSDP is highest in the state of Gujarat. Since the initiation of economic liberalization policies in India in 1991, the industrial sector contribution has increased to more than 30 percent of NSDP in that state. Although economically Maharashtra continues to be the most powerful state in India, its share of industrial sector has varied little over the observed period, hovering at around 30 percent of the state's NSDP. Further disaggregated data reveals that since the 1980s the share of service sector in the economy has accounted for most of the NSDP growth which is consistent with the transformation of Mumbai from an industrial to the financial capital of India. In contrast, the contribution of the industrial sector is not dominant in West Bengal or Andhra Pradesh. In the case of West Bengal, the contribution of the industrial sector to that state's NSDP actually declined over time. Although starting from a small contribution, Andhra Pradesh shows an expanding industrial sector. Such an outcome has been often cited in favor of investment incentives including flexible labor markets.²¹

In terms of resources at the disposal of business, a greater share of public sector would imply lower business influence, not only on government, but also on the overall economy. As it

²¹ Iarossi et al. 2009 .

is difficult to get comprehensive state level data on the distribution between public and private sources of capital, instead we examine the data on employment share in public-private sector. The underlying logic for the selection of such a proxy variables remains that importance of business stems from both industrial investment and employment generation. As such greater levels of employment in the private sector would indicate greater leverage for the business sector. Figure 2 shows the statewise share of private sector as a proportion of employment in the economy from 1980 until 2005.

[FIGURE 2 ABOUT HERE]

Figure 2 shows that during the period 1980-2005, employment trends across the four selected states in India have remained more or less stable. Private employment is lowest in the state of Andhra Pradesh (around 47 percent as a proportion of the total labor force), while it is highest in Gujarat, reaching nearly 60 percent of the total employment in that state for the 2000-2005 time period.

It is clear from the data presented so far that business (i.e., the private sector) contributes relatively more to NSDP and factory employment in Gujarat and Maharashtra while their contribution in terms of NSDP is lower in West Bengal and Andhra Pradesh. An intuitive reading of these data suggests that the environment for investment in industry in Gujarat and Andhra Pradesh is thriving. Such an interpretation corresponds with a number of studies that summarize and compare the investment climate in Indian states.²² In order to determine the exact nature of the relationship between industry and business, it is necessary to look into the business-government dynamics at sub-national states from a historical perspective.

²² Iarossi et al 2009.

A final element to consider in identifying business strength is the variation in the impact of investment (including foreign direct investment) in the four case studies selected here. Table 1 shows that the number and value of industrial entrepreneur memoranda (IEM), a document that signals the intended investment in states by potential private sector investors. Table 1 also shows the number of export oriented units (EOU) that have emerged, primarily after the adoption of economic liberalization in India. Table 1 also shows the number and value of foreign direct investment (FDI) approvals reflect the choice of business over location and potentially the political economic orientation of states towards business. Table 1 shows the statewise share distribution in export oriented units, IEM implemented and FDI approvals in India from 1991 to 2005 [See Table 1].

[TABLE 1 ABOUT HERE]

Table 1 shows that since 1991 the state of Maharashtra has a higher amount of FDI and also hosts the largest number of EOUs. The states of Gujarat and Andhra Pradesh are positioned behind Maharashtra with relatively high levels of FDI approvals and the presence of EOUs. Among these four states, West Bengal has the lowest amount of FDI approvals as well as the highest number of EOUs. Table 1 also shows that if measured in terms of IEMs, Gujarat has been at the forefront of attracting businesses while West Bengal has been a laggard in courting business.

Broadly the data presented reveals that the resources at the disposal business appear to be highest in Maharashtra, followed by Gujarat and Andhra Pradesh. The resources at the disposal of business are lowest in West Bengal, however measured. It would be expected that the greater availability of material resources at the disposal of business could translate into greater leverage

for business. However, this is not the case with respect to the extent of labor reforms across the states. Existing studies on subnational variations in economic growth rate and policy reform have highlighted considerable variation across India's states, in policy design and implementation due to regional political and institutional dynamics.²³ As Kennedy succinctly points out "despite some mimicry in policies aimed at improving the business environment and increasing the attractiveness, a closer analysis reveals significant differences in the attitudes of political elites as well as regional diversity of instruments deployed."²⁴

There is substantial subnational variation can be noted in terms of labor market reforms across the states.²⁵ In a comparison of labour market flexibility across sub-national states of India, Shyam Sundar has classified West Bengal as the most regulated while Gujarat as the least regulated state. The states of Maharashtra and Kerala are fairly regulated positioned at 3 and 4 while Andhra Pradesh and Rajasthan are on the lower side of regulation at 7 and 8 out of 10 states considered.²⁶ Table 2 shows that there is an anomaly in the rank order of states. Maharashtra has greater industrial sector contribution to NSDP and greater private sector employment than Andhra Pradesh. However, Andhra Pradesh has greater labor market flexibility than Maharashtra [See Table 2]

[TABLE 2 ABOUT HERE]

²³ Sinha 2005, Bajpai and Sachs 1999, Kennedy et al. 2013.

²⁴ Kennedy et al. 2013.

²⁵ Besley and Burgess 2004, Aghion et al. 2008.

²⁶ Sundar 2008.

As Table 2 above shows, the material resources of business do not corroborate the relative variations in labor market flexibility, specifically between the states of Maharashtra and Andhra Pradesh. The lack of correspondence between the material resources of business and the degree of labor flexibility suggests the operation of some other causal variable that accounts for the lower level of labor market flexibility in Maharashtra relative to Andhra Pradesh. In what follows, we will evaluate whether the extent of business organization or the partisan orientation of state governments in India accounts for this anomalous outcome.

The extent of business organization

An important factor that may account for the divergence in the degree of business influence over state policies pertains to business influence over policy makers. In a democracy, such policy makers include elected representatives as well as the bureaucracy and political parties. Thus, the study of wider political dynamics especially the nature of interest aggregation by organization and the business-politics linkages may provide important clues to understand the relative variation in business influence. The importance of such political dynamics in determining the influence of business at the subnational level in India has been pointed out in a number of studies.²⁷

A potential explanation for relative weakness of business in Maharashtra—in spite of having ample material resources—may be the nature of interest articulation by business. Like other interest groups, the capacity of business to effectively influence policy and outcome depends on the resources of the organization, freedom from government influence, level of

²⁷ Sinha 2005; Cali and Sen 2011.

centralization and existence of other contending interests. As such analysis of specific dynamics of business associations across the states may potentially indicate some causal factor.

The states under consideration are marked by multiplicity of business organizations based on region, industry and even rivalry across businesses in that state. Although all the states are marked by a multiplicity of business organizations, Gujarat and Andhra Pradesh are characterized by relative centralization of business organizations compared to Maharashtra and West Bengal. For example in Gujarat, the Gujarat Chamber of Commerce and Industry (GCCCI) is the apex organization not only in Gujarat, but also as the largest regional business organization in India. GCCCI offers an extensive range of diversified services providing information, acting as a channel of between business and government, acting as an interest group that presents budget-related memoranda to various state authorities.

In contrast, the state of West Bengal is characterized by a multiplicity of business organizations. These include the Bengal Chamber of Commerce, the Indian Chamber of Commerce, the Bengal National Chamber of Commerce, the Oriental Chamber of Commerce, the Federation of Small and Medium Industries. Among others, these chambers of commerce represent the various industry associations and provide the logistic support to business. Policy matters are directly taken up by the industry associations and chambers of commerce provides logistic support.²⁸ Similarly, Maharashtra given its history of industrialization also has a high degree of business organization decentralization. The business associations in that state reflect a diversity of regional interests, like the Deccan Chamber of Commerce, the Mahratta Chamber Of Commerce Industries & Agriculture; community chambers like Memon Chamber of Commerce,

²⁸ Mukarji 1989.

Zoroastrian Chamber of Commerce, Dalit Chamber of Commerce; along with statewide business interests through Indian Merchants Chamber, Bombay Chamber of Commerce, Maharashtra Chamber of Commerce and Hindustan Chamber of Commerce.

The extent of fragmentation or centralization could potentially explain the explaining variations in business influence. However, we are not persuaded that the extent of concentration of business is a reliable measure for business influence on policy. Greater business group fragmentation reflects factors like industrial composition, the extent of business coordination, the nature of business classes and similar historical institutional developments. As such, the organization of business as a variable in determining business influence can at best be marginal. What emerges as important from such a discussion is the variation in relative efficiency of the business organizations across the states. In an interesting study on state business relations, Cali and Sen have sought to compare the nature of relation based on an index of existence of business organization, investment promotion agency and expenditure on industry.²⁹ The findings of Cali and Sen in the four states under consideration for the period 1975-2008 reveal a high and increasing trend for Gujarat and Andhra Pradesh. SBR in Maharashtra is comparatively lower of these states while it is lowest in West Bengal. Such a SBR trend broadly correlates with our evaluation of business influence across the states.

A crucial question that emerges in this context concerns the conditions that augment greater coherence among business. In other words, what conditions led to greater centralization of business interests in Gujarat and Andhra Pradesh as opposed to Maharashtra? Such a question assumes relevance in the light of the fact that mere possession of resources by business does not

²⁹ Cali and Sen 2011.

translate into influence and points out the role of broader political processes particularly coherence in interest aggregation and business-party linkage.

Partisan orientation: business - party linkage

A conventional explanation regarding the subnational variation in investment incentives and labor market flexibility emphasizes on the nature of government.³⁰ The relation between business and government policy is not straightforward and just as greater business contribution should lead to influence of business, business decision to invest is influenced by government policies. Alvarez *et al* point out that *ab initio* expectations about labor and government may affect business strategy as capitalists may be less likely to invest in domestic economy when it confronts a strong labor movement and a leftist government.³¹ Naturally the nature of party in power has implications for the nature of business-party linkage. Although this theme could be elaborated further, here we will present some preliminary findings on the issue of business-party linkages in our four Indian states.

According to the literature on partisanship (i.e., the ideological orientation of government in terms of a left to right spectrum), economic programs have a significant relationship to macroeconomic characteristics. These include employment levels, monetary growth rates, income distributions, growth strategies, and growth rates.³² We argue that such differences in the programmatic orientation of parties in India emanate from the *differences in the social support*

³⁰ Alvarez, Garrett, and Lange 1991, Sinha 2005.

³¹ Alvarez, Garrett, and Lange 1991.

³² Quinn and Shapiro 1991.

base of parties. Partisan orientation of government can be explained through a combination of ideological and electoral imperative as political parties in democracy seek to represent groups in society on the basis of specific programs. Even though ideological and instrumental interests may change, these are relatively stable leading to stability in party system. Scholars, like Frieden and Rogowski, and Hankla, have pointed out the importance of the support base of the regime in the determination of policy in democratic systems.³³

The argument of partisan orientation is particularly relevant in the context of this analysis as the ideological difference in party program does not augment our understanding of the relative variations in labor market flexibility. As the case study reveal, major political parties in India — such as the center-left Congress Party and the center-right Bharatiya Janata Party (BJP)— have similar positions on economic reforms, but the outcomes of sub-national partisan regimes are visibly different between the Congress Party-led government of Maharashtra and the BJP-led government in Gujarat. Moreover, variations in government orientation towards reform can be identified across sub-national states despite same political party in government. A case in point is the Congress Party-led governments in Maharashtra and Andhra Pradesh which exhibit divergent outcomes in investment incentives and labor market reform.

In order to determine the dynamics of business-political party linkage, we examine the representation of business within support base of parties through the proxy variable of parliamentarians elected across the states over the period 1980 to 2004. Since members of the national parliament (the *Lok Sabha*) are directly elected across the states during the same time, such data not only indicates the share of proprietary classes in the political system, but also helps

³³ Frieden and Rogowski 1996; Hankla 2006.

to overcome state specific political conditions in each state. Such a methodology is supported in the literature on political parties that suggest candidate selection by parties reflect their support base both at the level of ideas, as well as identity. As Hazan and Rahat point out parties seek to address the issue of representation through candidate selection and selected candidates, not only reflect the political belief of their voters, but also share descriptive characteristic similar to those they represent.³⁴

In the context of the present study, such an analysis is augmented by socio-political specificities which are characteristic of business associations with specific ethnic or religious communities. As Damodaran has pointed out, the historical patterns of social stratification in India have led to broad correspondence between occupational groups and caste (endogamous occupational groups within Hindu society) structures within society.³⁵ As such, an analysis of the caste identification of elected representatives (MPs) could potentially indicate the nature of support base of parties and consequently the extent of business representation within parties. We suggest that greater representation of business castes among elected representatives should lead to greater business influence and vice versa.

Partisan orientation: representation of business within party

An analysis of business representation across parties based on social composition of elected members of parliament confirms the partisan orientation hypothesis. As we will show below, the extent of business friendly reform and labor market flexibility across the states seems to correspond to the variations in presence of business castes as a support base for parties. In

³⁴ Hazan and Rahat 2006.

³⁵ Damodaran 2008.

other words, the data suggests that *states where business castes constitute a dominant base for the dominant political parties in state government are marked by greater reform and flexibility.*

In contrast, if business castes do not constitute a politically dominant support base due to reasons such as existence of strong countervailing groups or marginalization of business their influence appears low.

In sum, the findings suggest that influence of business under stood through policy reforms towards investment incentives and labor flexibility is a function of political relevance of business. The argument becomes clear if we consider each sub-national state separately and analyze the dominance of business from a historical-political perspective. In this context it is important to point out that dominance of particular castes or groups within parties is influenced by wider political dynamic (such as the party system, the nature of political mobilization, and the structures of social stratification).

Case study 1: Andhra Pradesh

According to literature industrialization in Andhra Pradesh occurred mainly under the auspices of the state under economic planning and until 1970s the regional elite of the state were not keen on industrialization which has been attributed to their association with land. As Alivelu *et al* point out it was only after the green revolution, particularly in the fertile region of the state that one finds the emergence of an agriculture turned industrial class along with an urban educated middle class. Such a development marked the emergence of a regional business class and increasing participation of private sector in the economy.³⁶

³⁶Alivelu et al. 2009.

Interestingly due to specific historical-social reasons peculiar to the state the emergent agriculturalist turned industrial section was largely dominated by two castes —the Kammas and the Reddys— with some presence of the Kapus. From a political perspective, the Reddys, a landed aristocracy turned industrial caste, has traditionally dominated the leadership echelons of the Congress Party. The historic rivalry between Kamma and Reddy caste groups meant that the Kammas could not really find space in the Congress-dominated political regime and largely supported the opposition. Eventually the emergence of the Telegu Desam Party in the 1980s provided the Kammas a political platform and large sections aligned with the TDP.³⁷ The political assertion of the Kammas through the TDP explains the visible increase in the representation of business among MPs in the state during early 1980s.

The assertion of this regional bourgeoisie became decisive during the post-liberalization period reflected through the leadership change in the Telugu Desam Party (TDP) when N.T. Rama Rao, the founder leader was displaced by his son-in-law, Chandrababu Naidu. Observers of Andhra politics have pointed out that the leadership contest between NTR who represented opposition to reforms and Chandrababu Naidu who favored increased reforms signified a wider social contestation where the business classes played a crucial role.³⁸

An analysis of the support base of parties based on elected representative in the state corroborates the dominance of Reddys and Kammas in the politics of the state. As Table 3 shows the Reddi, Kamma, and (to a lesser extent) Kapu constitute the dominant caste groups within the state (S.C and S.T seats are constitutionally reserved) and tend to be represented by the two major political parties [See Table 3].

³⁷ Kohli and Bardhan 1988.

³⁸ Suri 2004.

[TABLE 3 ABOUT HERE]

Table 3 shows that 45.7 percent of Congress Party MPs were either members of the Reddy or the Kamma caste groups. Likewise, 42.2 percent of TDP MPs came from these two caste communities. Since these castes also constitute the major business communities in the state, business interest within support base of both Congress and TDP is dominant. In terms of relative variance between the support bases of the parties, the Congress Party appears to be characterized by a somewhat more heterogeneous support base than the TDP. Overall, though, Reddy and Kammas also represented 42.6 percent of the total number of MPs from Andhra Pradesh from 1980 to 2004.

A chi-square test of independence was performed to examine the relation between political party affiliation and caste in Andhra Pradesh. The relation between these variables was significant, $\chi^2(28, N = 272) = 97.57, p < .01$. As such business groups in Andhra Pradesh by virtue of their dominance in the support base of major parties can be argued to have greater influence over public policy. The relatively greater labor market flexibility in the state despite lower business resources seems to be explained by this greater political influence of business. The situation in Andhra Pradesh suggests that competing business castes constitute important support base for competing political parties. In terms of inter-party difference in support base, the Congress Party has relatively heterogeneous support base compared to the TDP.

Case study 2: Gujarat

Detecting partisan orientation in the context of labor market reforms in Gujarat is difficult as the material resources of business already suggest a dominant role for business. However, an historical overview reveals that Gujarat has been characterized by the political dominance of the regional bourgeoisie, which can be traced even before liberalization. According to Sinha, a class of capitalist farmers who later turned into industrial class (*Patidar Patel*), the artisan – trader (*Bania*) class and the backward castes constitute the regional bourgeoisie in the state.³⁹ This regional business class developed and gained in strength—even during the stage of Nehruvian economic planning— due to conscious policy choice of regional political elites. In fact the greater share of private sector and relative lack of public sector investments was a conscious policy to strengthen the business classes by ensuring larger share of the economy.⁴⁰

Since the mid-1980s, after a brief period of political turmoil, the state has witnessed a stable two party competition between Congress Party and the BJP. Given the reformist economic orientation of the BJP and continuous BJP rule in the state since 1990s the increasing labor market flexibility in the state is quite expected. However, it is interesting to note that labor flexibility appears to have increased even prior to economic liberalization. This outcome can be attributed to the hegemonic dominance of business castes in the politics of the state.

The dominance of Patidar-Bania-Brahmin caste alliance has meant that irrespective of political parties, the developmental orientation of the state has always incorporated business interests. The point becomes clear if we consider the data on the dominant caste composition of the elected members of parliament in the state. [See Table 4]

³⁹ Sinha 2005.

⁴⁰ Sinha 2005.

[TABLE 4 ABOUT HERE]

Table 4 shows the data certain castes particularly Patels (Patidar) and Kshatriyas dominate politics in the state. From 1980 until 2005, 68 percent of MPs from the Congress Party were from the Kshatriya and Patel caste groups. These caste groups constitute the core of the state's regional bourgeoisie. Accordingly, business groups emerge as dominant support base for parties. The dominance of business castes as support base appears to be greater in case of the BJP. From 1980 until 2005, 60.9 percent of BJP MPs from Gujarat were Kshatriya and Patels. This corroborates commonplace characterization of the party as the party of *baniyas*. The support base of Congress Party however is not devoid of representation of business castes although there is greater representation of backward and scheduled castes. However, such difference cannot obviate the across party dominance of business castes and groups.

A chi-square test of independence was performed to examine the relation between political party affiliation and caste in Gujarat. The relation between these variables was significant, $\chi^2(14, N = 176) = 58.1, p < .01$. Just as was the case with respect to the impact of caste groups in Andhra Pradesh, we show that caste identification and political representation are not statistically independent. We have shown that business caste groups are dominant within the Congress and the BJP, the two more dominant parties in the state. The case study of Gujarat affirms partisan orientation in terms of business domination. However specific to Gujarat, the linkage between business and politics transcends partisan divisions as business influence seems endure political alteration.

Case study 3: Maharashtra

Among the cases being evaluated in this study, Maharashtra is the most interesting case as it is the state has been historically one of the frontrunners in terms of economic growth and industrial development. Given the large and vibrant industrial sector in the state business should have been comparatively more influential in bringing about greater labor flexibility. However, as we showed earlier, Maharashtra is marked by comparatively lower labor market flexibility; lower than Andhra Pradesh, for instance. Although business constitutes an important and powerful social group in the state, it has not emerged as a hegemonic group as it has been the case in Gujarat.

The influence of business, in spite of a large private sector, appears lower because of the peculiar political dynamics of the states. Observers of Maharashtra politics have pointed out that numerically dominant Maratha-Kunbi caste —a traditional middle peasant agrarian group— constitute the most important political group in the state. According to Palshikar and Deshpande, formal political power has been vested with the numerically dominant Maratha-Kunbi caste group in the state.⁴¹ However, the material interests of the brahmins (predominantly regional bourgeoisie- industrial and urban middle class) have also been preserved by the government through an elaborate patronage network.

The argument can be elaborated through the data on the dominant caste composition of the elected members of parliament in the state of Maharashtra. As is evident from the data, the agrarian caste of Maratha-Kunbi dominates politics in the state in an overwhelming manner and consequently business interests although powerful is not hegemonic. In terms of partisan variation in support base between the two major political alliance blocks namely Congress-NCP and BJP-Shiv Sena it is evident that the support base of the former is relatively more

⁴¹ Palshikar and Deshpande 1999.

heterogeneous with greater representation of scheduled castes and marginalized communities.
[See Table 5]

[TABLE 5 ABOUT HERE]

As Table 5 shows, the Maratha-Kanbi caste group has a disproportionately large representation in the national legislature. From 1980 until 2005, 38 percent of Congress Party MPs from Maharashtra came from the Maratha-Kanbi caste group. Similarly, 31 percent of BJP MPs from Maharashtra came from the same caste group. Compared to the previous two states (Gujarat and Andhra Pradesh), the presence of a dominant business caste group is much lower in Maharashtra.

A chi-square test of independence was performed to examine the relation between political party affiliation and caste in Maharashtra. The relation between these variables was significant, $\chi^2(44, N = 317) = 76.1, p < .01$. Once again, we have shown that there is no statistical independence between caste and political party affiliation. Given the dominance of the Maratha-Kanbi caste group in the state's parliamentary representation in the Lok Sabha, it is clear that business interests are less well represented because the interests of a business caste (such as was the case in Andhra Pradesh and Gujarat) are less prevalent in Maharashtra.

In due course, the argument of dominance of Maratha-Kunbi agrarian caste in politics leading to a lower influence of business interests will need scrutiny as sections of the Maratha-Kunbi have shifted from agriculture to industry. As Damodaran points out Maratha castes have gradually entered industrial mainstream through co-operative ventures, particularly in

sugarcane.⁴² If this trend continues, then we shall hypothesize that there will be a greater influence of business interests in policy-making. Thus, Maharashtra presents a situation where business castes-class despite material resources and representation has been unable to exert commensurate influence on policies. The situation in Maharashtra confirms the partisan orientation argument as material or organizational strength of business seems to be counteracted by its weakness to emerge as dominant social base for political parties. The case study of Maharashtra indicates that mere presence of business interests is not adequate for political influence and the wider support base of parties need to be considered in analysis.

Case study 4: West Bengal

The state of West Bengal represents a stark contrast to the other states discussed in this article (particularly Gujarat) where business interest groups have had a marginal political influence. The data on business representation reveals that business has practically no presence measured in terms of proportion of businessmen elected as MPs. Such an outcome becomes somewhat comprehensible in the light of the fact that the state has been ruled continuously for the last 34 years by the Left Front- an alliance of left parties dominated by the Communist Party of India (Marxist).

According to Sinha, the peculiar politics in the state can be understood through the overwhelming dominance of the Bhadrak community in the politics of the state which meant that industrial elites were precluded from the political scheme. The social position of the bhadrak, in the urban governmental professions and middle class status with historical legacy

⁴² Damodaran 2008.

of cultural renaissance, nationalist fervor and Marxism induced ideas significantly radicalized the ideational discourse in the state. Given the ideological nature of the regime business especially large industries were not particularly welcome and small scale sector along with public sector was encouraged. [See Table 6]

[TABLE 6 ABOUT HERE]

A chi-square test of independence was performed to examine the relation between political party affiliation and caste in West Bengal. The relation between these variables was significant, $\chi^2(40, N = 289) = 159.09, p < .01$. Once again, there is a strong relationship between caste and party affiliation. The strong representation of non-business caste groups in West Bengal's parliamentary representation creates the conditions for negligible interests by business groups. Moreover, since there is no business caste group being represented in the national parliament, then there is not a surprise to learn that the data on employment reveals that compared to the other states, the share of private sector employment in industry is not only lower, in fact share of overall private sector employment has actually declined in the state. As such both in terms of resources and political influence business have not been able to exert any significant influence on public policy. Thus, the marginal influence of business in West Bengal can be attributed to the relative absence of business interests within the main political parties.

7. Conclusion

The central argument of this article is that the power of business to influence policy is structured by the salience of business castes as an electorally relevant group. We have argued that states where business castes form the support base for political parties and have access to

decision-makers are the states characterized by greater labor flexibility. In turn, another key finding of this article reveals that the extent of reform and flexibility across the sub-national states in India does not correspond to the size of the private sector in the economy. In other words, the material resources at the disposal of business do not explain the relative variations in business influence among policy-makers. A disaggregated analysis of four Indian states reveals that in terms of economic structure, the power of business should have been greater in Maharashtra and Gujarat compared to West Bengal or Andhra Pradesh. However, as the data suggest, labor flexibility is significantly higher in Andhra Pradesh compared to Maharashtra despite the former having a comparatively smaller private sector than the latter.

The presence or absence of endogenous business castes across the states could be attributed to historical-institutional developments. The literature highlights the role that the caste system in India plays in confining business activities to certain groups within Hindu society.⁴³ There is also existing literature emphasizing on developments consequent upon colonialism and post-Independence policies that affected the class-caste structure of the Indian state.⁴⁴ Kochanek has pointed out that industrialization under colonialism had consequences for the pattern, timing, nature of capital and entrepreneurship in different regions of India. Our paper, however, specifically focuses on labor market reforms under conditions of economic liberalization. We argue that the differences in business influence in determining policies appear to be a function of political dynamics, specifically the representation of business castes in the support base of political parties.

⁴³ Damodaran 2008.

⁴⁴ Kochanek 1974.

The article has offered an important explanation to account for the variation in labor market flexibility across subnational states in India. As an explanatory variable we show the relevance of political and social dynamics. We have shown the relevance of such political and social dynamics through a comparative case study of *most like* cases. Using four case studies in India, we have shown that variation in labor market flexibility stems from the presence or absence of business castes within the government. As such, the article is not about the processes through which business groups influence labor policies, but rather by establishing the relation between the presence/absence of business groups and labor reform. Our sub-national analysis of business representation suggests that the existence of assertive and dominant business caste-class within the major parties in Andhra Pradesh and Gujarat have led to greater pro-business orientation. In contrast, the near complete absence of business classes in the politics of West Bengal has meant marginal influence of business in public policy. However, as the situation in Maharashtra reveals, the mere presence of business interests within political parties is not a sufficient condition to guarantee adequate business influence. Rather the ability of business castes-classes to emerge as a dominant support base (i.e., electorally relevant constituency) is crucial for business influence.

The analysis of business presence in support base of political parties (i.e., the partisan representation across states) reveals some important dimension of business politics linkages across the states of India. The relevance of contending social groups in determining business influence and attitude may be identified from the difference in business attitude reflected across the states. For example, in terms of labor market flexibility, policy outcomes emphasize socio-economic equality, often recognizing the adverse effect of liberalization of labor. Business in West Bengal and Maharashtra although strongly endorsing labor flexibility for attracting

investment and efficiency seem to approach the issue at a social level. In contrast, the approach of business towards questions of flexibility in Andhra Pradesh and particularly Gujarat resembled the classic neoliberal paradigm where much more faith appears to be on operation of market and its beneficial impact. As a result of the impact of business caste elites in the national parliament, most policy in Gujarat emphasizes on the benefits of growth reflected through enlightened interaction between business and labor that resulted in very low confrontation. In Gujarat, businesses have shown a preferred individual interaction with labor with relative marginalization of organized labor.

Our article suggests that parties tend to cater to business interest in labor policies more whenever there is greater representation of business in politics. Our argument is based on the analytical classification of the electoral base of political parties and the dominant base within parties. We have argued that in terms of policy orientation, the interests of the dominant base have greater leverage than that of the electoral base. To support this claim, we have measured the composition of elected members of parliament (e.g., the leadership) in terms of profession and caste composition.

We think that the argument of partisan orientation can be theoretically substantiated as interest groups in India have developed along pluralist lines and were often divided along nature of capital, regional concentration, and even caste. The post-independence legacy of *dirigisme* had meant that the influence of interest groups dependent on their capacity to influence parties in government and electoral outcomes. As such the relevance of business within electoral support base for parties emerged as critical to determine its influence. Labor market reform is ideally determined through an interaction of business, labor, and the state. Given the state-dominated institutional structure that has evolved in the four decades after India's independence, the state

has a crucial role in determining the outcome of the negotiations between labor and capital. As we have shown, then business has greater leverage over the state legislature, there is greater labor market flexibility. This argument can be extended to claim that the power of organized labor to prevent labor market reforms is contingent upon its own capacity to mobilize as well as its capacity to influence the state.

The principal finding developed in this article challenges the conventional notion of variegated business influence across subnational states by highlighting the role of caste in explaining variations in policy. The relative power of business across the states appears to vary due to the relation between business and government which in turn is structured by the salience of business castes as an electorally relevant group. States where business castes form support base for parties and has access to decision makers are the ones characterized by greater labor flexibility. As such the partisan orientation hypothesis appears to be most relevant explanation for variations in business influence. However, the exact relation between the presence of business castes as a support base and the extent of its influence is contingent upon the composition of broader socio-economic support base for the regime should be explored in further research.

Bibliography

- Aghion, Philippe, Robin Burgess, Stephen J. Redding and Fabrizio Zilibotti. 2008. *The Unequal Effects of Liberalization: Evidence from Dismantling the License Raj in India*. *American Economic Review* 98(4):1397-1412.
- Ahluwalia, Montek S. 2002. "Economic Reforms in India Since 1991: Has Gradualism Worked?". *Journal of Economic Perspectives*, 16(3): 67-88.
- Alivelu, G., K Srinivasulu and M Gopinath Reddy. 2009. "State Business Relations and Performance of Manufacturing Sector in Andhra Pradesh – A Case Study." Discussion Paper Series. Manchester: University of Manchester.
- Alvarez, Michael, Geoffrey Garrett, and Peter Lange. 1991. "Government Partisanship, Labor Organization and Macroeconomic Performance." *American Political Science Review* 85(2): 539-556.
- Bajpai, Nirupam and Jeffrey Sachs. 1999. "The Progress of Policy Reform and Variations in Performance at the Sub-National Level in India", Development Discussion Paper No. 730, Harvard Institute for International Development.
- Becker, Gary. 1983. "A Theory of Competition Among Pressure Groups for Political Influence." *Quarterly Journal of Economics* 98(3): 371-400.
- Besley, Tim and Robin Burgess. 2004. "Can Labor Regulation Hinder Economic Performance? Evidence from India." *Quarterly Journal of Economics* 119(1): 91–134.
- Cali, Massimiliano and Kunal Sen. 2011. "Do Effective State-Business Relations Matter for Economic Growth? Evidence from Indian States." *World Development* 39(9): 1542-1557.
- Dahl, Robert A. 2005. *Who Governs?: Democracy and Power in an American City*. New Haven: Yale University Press.
- Damodaran, Harish. 2008. *India's New Capitalists: Caste, Business and Industry in a Modern Nation*. Houndsmill, Basingstoke, U.K.: Palgrave Macmillan.
- Datta Chaudhuri, Mrinal. 1996. "Labor Markets as Social Institutions in India." IRIS-India Working Paper No. 10. College Park, MD: University of Maryland.
- Dunning, John. 1997. *Governments, Globalization, and International Business*. Oxford: Oxford University Press.
- Fallon, Peter and Robert Lucas. 1993. "Job Security Regulations and the Dynamic Demand for Industrial Labor in India and Zimbabwe." *Journal of Development Economics* 40(2): 214-275.
- Frieden, Jeffrey and Ronald Rogowski. 1996. "The Impact of the International Economy on National Policies: An Analytical Overview." In *Internationalization and Domestic Politics*,

- edited by Helen Milner and Robert Keohane. Cambridge, Cambridge University Press: 25-47.
- Furlong, Scott. 1997. "Interest Group Influence on Rule Making." *Administration & Society* 29(3): 325-347.
- Garrett, Geoffrey. 1998. "Global Markets and National Politics: Collision Course or Virtuous Cycle?" *International Organization* 52(4): 787-824.
- Godbole, Madhav. 2004. "Good Governance: A Distant Dream." *Economic and Political Weekly* 39(11): 1103-1107.
- Hall, Peter and David Soskice. 2001. *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*. Oxford: Oxford University Press.
- Hankla, Charles. 2006. "Party Strength and International Trade: A Cross-National Analysis." *Comparative Political Studies* 39(9): 1133-1156.
- Hazan, Reuven and Gideon Rahat. 2006. "Candidate Selection: Methods and Consequences." In *Handbook of Party Politics*, edited by Richard Katz and William Crotty. London: Sage.
- Heinz, John, Edward Laumann, Robert Nelson, and Robert Salisbury. 1993. *The Hollow Core: Private Interests in National Policy Making*. Cambridge, MA: Harvard University Press.
- Held, David. 1999. *Global Transformations: Politics, Economics, and Culture*. Stanford, Stanford University Press.
- Iarossi, G., P. Mousley, et al. 2009. *An Assessment of the Investment Climate in Nigeria. Directions in Development, Private Sector Development*. Washington, D.C.: World Bank.
- International Labor Organization. 1997. *World Labor Report, 1997-98: Industrial Relations, Democracy and Social Stability*. Geneva: International Labor Office.
- Jenkins, Rob. 2004. "Labor Policy and the Second Generation of Economic Reform in India." *India Review* 3(2): 333-363.
- Katzenstein, Peter. 1976. "International Relations and Domestic Structures: Foreign Economic Policies of Industrial States." *International Organization* 30(1): 1-45.
- Kennedy, Loraine, Kim Robin, and Diego Zamuner. 2013. "Comparing State-Level Policy Responses to Economic Reforms in India: A Subnational Political Economy Perspective." *Revue de la régulation. Capitalisme, institutions, pouvoirs* Spring (13), consulted 15 april 2014. URL : <http://regulation.revues.org/10247>
- Kohli, Atul, and Pranab Bardhan. 1988. *India's Democracy: An Analysis of Changing State-Society Relations*. Princeton, N.J.: Princeton University Press.

- Lindblom, Charles. 1977. *Politics and Markets: The World's Political Economic Systems*. New York: Basic Books.
- Lucas, John. 1997. "The Politics of Business Associations in the Developing World." *Journal of Developing Areas* 32(1): 71-96.
- Martin, Cathie Jo and Duane Swank. 2004. "Does the Organization of Capital Matter? Employers and Active Labor Market Policy at the National and Firm Levels." *American Political Science Review* 98(4): 593-611.
- Mukarji, Nirmal. (1989). "Decentralisation below the State Level: Need for a New System of Governance." *Economic and Political Weekly* 24(9): 467-472.
- Palshikar, Suhas and Rajeshwari Deshpande. 1999. "Electoral Competition and Structures of Domination in Maharashtra." *Economic and Political Weekly* 34(34/35): 2409-2422.
- Quinn, Dennis and Robert Shapiro. 1991. "Business Political Power: The Case of Taxation." *American Political Science Review* 85(3): 856-871.
- Shyam Sundar, K. 2008. *Labour Regulation in Indian Industry*. Edited by T. S. Papola. 10 vols. New Delhi: Bookwell on behalf of ISID.
- Sinha, Aseema. 2005. *The Regional Roots of Developmental Politics in India: A Divided Leviathan*. Bloomington, IN: Indiana University Press.
- Spiller, Pablo. 1990. "Politicians, Interest Groups, and Regulators: A Multiple-Principals Agency Theory of Regulation, or "Let Them Be Bribed." *Journal of Law & Economics* 33(1): 65-101.
- Stiglitz, Joseph. 2002. *Globalization and its Discontents*. New York: W. W. Norton.
- Suri, K. C. 2004. "Telugu Desam Party: Rise and Prospects for Future." *Economic and Political Weekly* 39(14/15): 1481-1490.
- Yackee, Jason and Susan Yackee. 2006. "A Bias Towards Business? Assessing Interest Group Influence on the US Bureaucracy." *Journal of Politics* 68(1): 128-139.

