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POLICIES AND INSTITUTIONS TO PROMOTE INDUSTRIAL REORGANIZATION AND MERGERS: THE EXPERIENCE OF INDIA [1]

by

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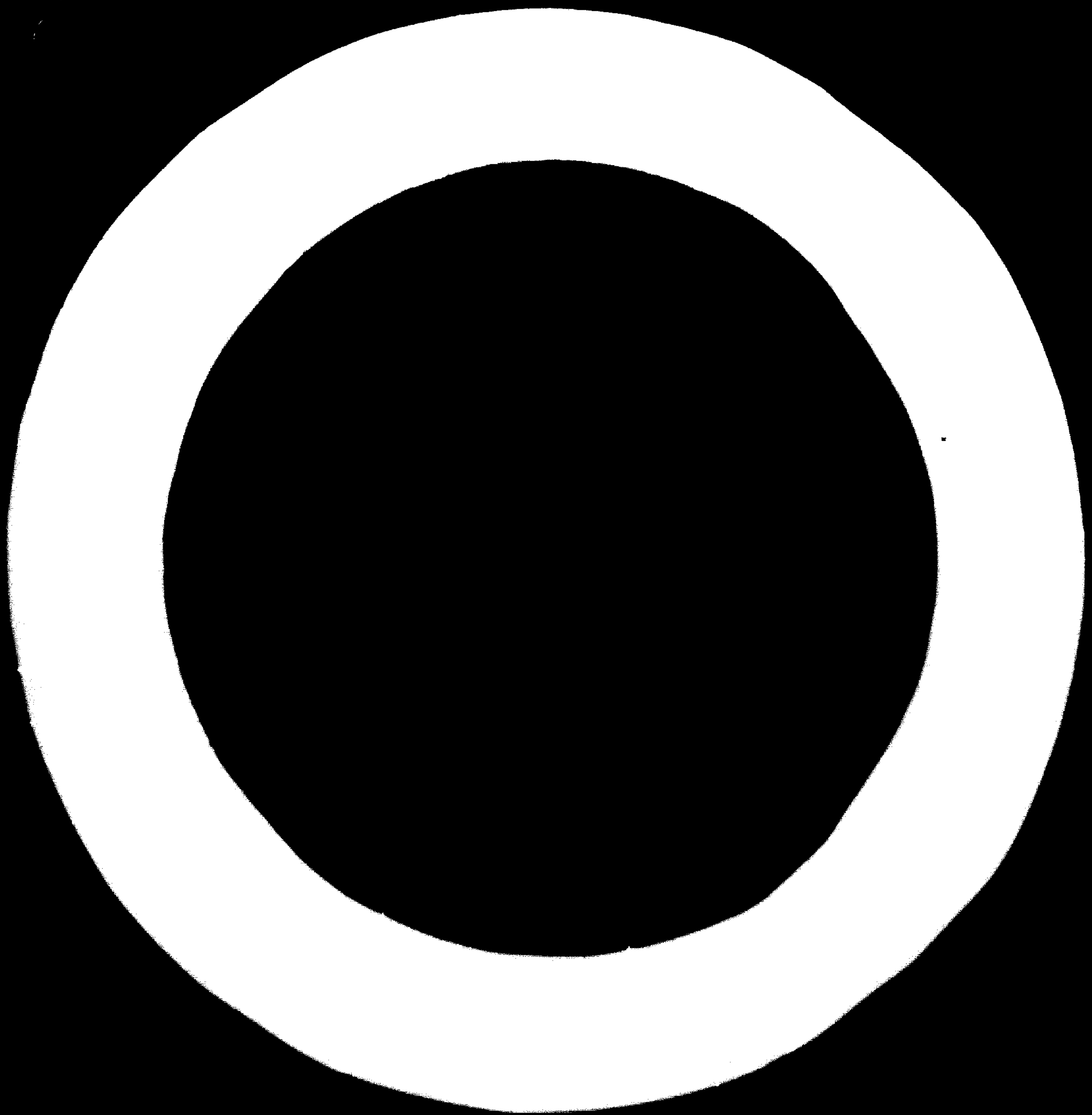

INDUSTRIAL REORGANISATION AND MERGERS.

1. Introduction

1.1. Capital, plant, knowhow, technology, dynamic management, mass production and large markets are among the essential elements of modern industrial enterprise. The primary objective of any progressive industrial organisation is to secure maximum production through optimum utilisation of scarce resources - financial, managerial and technological - to meet the growing demands.

1.2. The economic rationale for industrial reorganisation and mergers is the realisation of economies of scale and through them the benefits of mass production, adequate in volume and satisfactory in quality and competitiveness. A larger unit, as a rule, is in a better position than a smaller unit to mobilise the resources needed for research and development, on the results of which the future success of the enterprise hinges. The economies of scale depend, in their turn, on the size of the plant. The size of the plant is determined by technological considerations on the one hand, and demand considerations on the other.

2. The situation in developing countries - some relevant considerations.

2.1. In developing countries, the limitations of domestic demand often impose a constraint on the optimum size of the plant as may be warranted by the most up-to-date technology. The requirement of optimum size of the plant can, no doubt, to a large extent, be taken care of by developing countries, where there is no pre-existing large industrial base, at

the stage of establishing new industries. Even here, because of the limitations of demand, the constraints of scarce financial and managerial resources, and the need to secure a fair measure of regional development, the alternatives may be either to have plants based on up-to-date sophisticated technology and of large capacities which may not be fully utilised or plants based on appropriate labour intensive technology suited to the local situation and of smaller capacities which bear a relation to the market. Alongside of these factors, the protection that has to be afforded to infant industries in developing countries by tariff, and more importantly import control, may also tend to create, over a period, a certain lack of awareness of cost considerations. These factors, combined together, result in a situation in many developing countries where the circumstances are weighted against economic production in the global sense. The concept of economic production (unless the industry is basically in a position to compete in export markets) may then have to be looked at in a national rather than international context.

2.2. Even where new enterprises are established, the manner in which they grow will depend on whether the items of production are such that in a developing country their demand will grow or export markets can be developed for them on advantageous terms. In other words, the manner in which enterprises will tend to become economic in size in developing countries depends on the types of products and whether they will have a growing domestic or export demand within a reasonable time. In a world of growing size of economic operations, the size of units in developing countries is almost always bound to lag behind economic

sizes in a global sense, and problems of reorganisation and mergers can never abate. But the process of industrial reorganisation and mergers is not a simple problem of industrial economics alone. Apart from individual instances of such mergers or reorganisations taking place on the initiative of entrepreneurs, any purposeful reorganisation or merger would need legislative as well as executive action on the part of the Government. When developing countries are grappling with the basic problems of establishing manufacture and absorbing technology, it is unlikely that they will be in a position to devote serious economic consideration to the problems of mergers and reorganisation as the industrial economy grows in size and diversity.

2.3. There is another sense in which the problem is likely to be faced by certain developing economies which have had a tradition of limited industrialisation in processing, extractive or other industries including those catering to export markets. In such industries, the machinery may have become obsolescent or the technology outmoded. The units may have become too small by modern standards and where the industry is export-oriented, its competitive power may be getting eroded. If the industries are those which the foreigners have left at the time the country achieved Independence and the successors do not have adequate managerial abilities, then again problems are likely to arise. In other words, industries as well as individual units may be subject to fluctuating fortunes arising out of trends in international trade or technology or merely out of lack of managerial effort. If the developing country is one which has a substantial portion of what may be called "previous generation industries" which are fraught with problems of obsolescence and rehabilitation, then the subject of industrial reorganisation and mergers assumes

a good deal of relevance. The advantages of industrial reorganisation and mergers in such a situation are obvious. The weeding out of uneconomic units, cutting out unnecessary selling costs, improving and ensuring quality, modernisation and technological improvements, solution to problems of maintenance and spare parts, and diversification of the production pattern to match the changing trends in demand are all possible.

2.4. At the same time, as has been mentioned earlier, developing countries or any country, for that matter, cannot look at such problems as purely a problem in industrial economics. Very often social and political aspirations of the people come into the picture. In developing countries, such reorganisation and mergers are generally bound to involve substantial changes in the pattern of ownership and control over the means of production. These changes at times give rise to sensitive problems such as monopolies and concentration of economic power in a few private hands. Hence what is important is to devise methods which will be practical and acceptable in the circumstances of particular countries and particular industries. The question, in essence, is how to reap the benefits of large scale enterprise without injury to broader national social objectives and interests.

2.5. Sometimes, the key to economic operation may not necessarily be mergers, but the expansion of uneconomic units, if demand conditions permit. The advantages of mergers will also vary depending on individual circumstances. The specific advantage, whether in terms of managerial integration or integration of the plant or cutting out selling costs or laying a base for research and development, will have to be identified and it will have to be seen whether this advantage will be realised

in the process of reorganisation and mergers. In other words, industrial reorganisation and mergers have to be regarded as means towards particular ends and not as ends in themselves.

2.6. Subject to these observations, specific fields of industries, particularly those relating to the export effort, can be identified in individual developing countries for purpose of reorganisation. But in each case, it will have to be seen whether what is really required is reorganisation or merger in the sense of changes of ownership pattern or merely modernisation and the induction of sound managerial and technological practices.

3. The Background in India.

3.1. The industrial base that had been developed in India prior to the Second World War consisted largely of processing industries such as plantation industries (tea, coffee etc), textiles, jute and sugar, extractive industries such as oil crushing, some mining industries (coal, iron ore, manganese and limestone), a few mine based industries, and a relatively small number of manufacturing and fabrication industries. Most of these industries were developed, owned and managed by British companies or entrepreneurs. There were, of course, isolated instances of pioneering efforts of Indian industrial enterprise, the most notable of which was the establishment of the Iron and Steel works by the Tatas at Jamshedpur. The size of manufacturing enterprises was generally small designed to cater primarily to the limited domestic demand. The general pattern of management that had been evolved and came to be known as the Managing Agency System consisted of

the performance by the so called managing agency firm or group of all the functions connected with promotion, finance and management of a number of units in different fields of industrial activity. Industrial growth in India in the years before independence was largely guided by the efforts of these managing agency houses. It has to be mentioned that while the Managing Agency houses promoted a sizeable number of industrial units under their umbrella, there was hardly any scope for rational integration in the operations of different units under any single managing agency calculated to promote economies in production or marketing. The system, however, resulted in control over sizeable areas of industrial activity vesting in the Managing Agency houses.

3.2. The impetus to industrialisation did not cease or slow down with the coming of Independence. But on the eve of Independence many foreign companies which owned and managed industrial undertakings in India adopted a policy of repatriation of their assets as a consequence of which several undertakings were bought over and passed on to the control of a few affluent Indian families. These families too found it to their advantage to adopt the managing agency system to control their newly acquired interests. The managerial abilities of the new Indian owners of the industrial undertakings naturally varied from one case to another. Some of them as also some of the foreign managing agency houses which continued in industrial ventures in India were motivated primarily by the desire to make quick and large profits out of the undertakings and devoted little attention to the need to rehabilitate and modernise their plant and machinery through replacements necessitated by wear and tear and the fast changing technology. The need to reorganise the structure of these production units to

respond to new situations and changing requirements was also generally not recognised.

3.3. Organised planning by the State in the post Independence period which sought to mobilise and harness all available resources to implement a programme of massive industrialisation at a rapid pace, also facilitated to an extent the establishment of new production units by these few well to do industrial houses who had by then acquired some experience of running industries. In view of their resources and experience, these houses were at a relative advantage compared to newer entrepreneurs in applying for and securing licences for starting new industries or for expanding their existing capacities. The policy of active encouragement to foreign collaboration in the early fifties also gave an edge to the established and well to do industrial houses as they found it easier to secure the collaboration of large and reputed companies abroad. Existence of limited markets for some articles, import restrictions necessitated by foreign exchange shortage and the need to protect national industries, exchange control and the then policy of banks to lend preferentially to the men of means and substance, all tended to help, to a greater or smaller extent, the established industrial houses to consolidate their hold and control over sizeable sectors of industry in the country. The Monopoly Inquiry Commission appointed by the Government of India in 1964 in their report submitted in 1965 pointed out that 75 prominent business groups controlled altogether 1536 companies having total assets worth Rs.2,606 crores* and a total paid up capital amounting to Rs.646 crores. According to the

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* A crore is ten millions

report, in 1963-64 these 75 groups controlled 44.1% and 46.9% of the total paid up capital and assets respectively of all non-government and non-banking companies in the country.

3.4. As has briefly been referred to earlier in this paper, an interesting point to note is that most industrial combines in India which really are groups of industrial units do not fall into any set pattern, i.e. horizontal, vertical, lateral or diagonal integration. The most common type of combine noticed in India is what may be called "conglomerate" wherein units altogether different and having no rational connection with each other, combine and are managed by an agency controlled by a Large House. For example, the Tata House controls not only a steel manufacturing enterprise, but it controls undertakings manufacturing soaps, cosmetics, edible oils, locomotives, textiles, automobiles, industrial machinery and machine tools, electricity generating units and a large spectrum of different types of enterprises. It is relevant to point out that by and large, these conglomerates are inconsistent with the modern concept of industrial reorganisation and rationalisation. A conglomerate with large investible resources does not necessarily invest in areas of the highest priority. It has little value from the angle of sound and efficient industrial growth. Conglomerate growth, on the other hand, results in the diffusion of scarce economic resources over a wide range of products irrespective of their importance and priority in the economy. One seldom comes across cases of mass production, product improvement and cost reduction in India as a direct result of conglomerate growth.

3.5. India's experience in regard to industrial conglomerates or combines has been that while they have contributed to the establishment of a number of industries in the country, helped in the development of promotional and managerial skills and in securing foreign collaboration, they have led to the emergence of economic concentration with its attendant evils, viz. high prices, deterioration in quality and keeping out newer entrepreneurs from the field. Thus, the growth of industrial combines in India, by and large did not achieve the objectives for which rationalisation and expansion of certain industries are generally advocated, viz. product improvement, cost reduction, optimum use of capital and managerial talent resulting in better service to the consumer. It cannot, however, be denied that there were a few isolated instances of mergers which led to rationalization and improved corporate performance. Thus, in the thirties a large number of cement producing undertakings came together to form the Associated Cement Company which has since grown into one of the large corporate organisations in the Indian landscape and has been distinguished by good working results and profitability. In the fifties the Indian Iron Corporation and the Steel Corporation of Bengal were merged on consideration of scale and rationalisation. However, the impetus for reorganisation and merger in these cases stemmed from an awareness of the need to tone up the working of industrial production units and not in pursuance of any conscious policy of reorganisation of industries on rational and efficient lines.

3.6. To sum up, the problem of industrial reorganisation and mergers in India has historically had two dimensions: on the

one hand, in certain traditional industries like coal mines, cotton textiles and jute, the problem of modernisation, rehabilitation and reorganisation has arisen for reasons of obsolescence, mismanagement, loss of competitive advantage, the march of technological events, etc. The other dimension to the problem has been a process which is not strictly industrial re-organisation or merger but one of initial industrial expansion and eventual industrial hegemony exercised through conglomerates of companies resulting in problems of concentration of economic power.

4. Evolution of Government Policy.

4.1. Till Independence, the then Government of India did not show any great concern over the growth of industrial conglomerates and combines and had not evolved any policy towards them. After Independence, the economic policy of the country was re-oriented and the State took upon itself the responsibility to avoid concentration of economic power. One of the Directive Principles of State Policy as laid down in the Constitution of India requires that the "State shall, in particular, direct its policy towards securing that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment". The Industrial Policy Resolutions adopted by the Government of India in 1948 and 1956 had stressed the need "to accelerate the rate of economic growth and to speed up industrialisation and, in particular, to develop heavy industries and machine making industries, to expand the public sector, and to build up a large and growing co-operative sector." The 1956 Resolution further stated "equally, it is urgent, to reduce

disparities in income and wealth which exist today, to prevent private monopolies and the concentration of economic power in different fields in the hands of small numbers of individuals. Accordingly, the State will progressively assume a predominant and direct responsibility for setting up new industrial undertakings and for developing transport facilities."

4.2. In pursuance of the Industrial Policy Resolution, 1956, the Public Sector of Industry has been expanded substantially since the beginning of the Second Plan(1956). The planned and massive expansion of the public sector in recent years, apart from helping to check the concentration of economic power in private hands, has enabled the State to secure control over the management and growth of basic industries like steel, oil, fertiliser, heavy machinery, power generation equipment and machine tools. A net addition of Rs.481 crores in the paid-up capital of Government companies was made during the Second Plan period (1956-1961) and Rs.691 crores during the Third Plan period (1961-66). During the period after the Third Plan and upto 1970-71, a further sum of Rs.826 crores has been invested in the paid-up capital of the public sector companies. Thus, while at the beginning of the First Five Year Plan in 1950-51 the public sector companies accounted for only 3 percent of the total paid-up capital in the entire corporate sector, they accounted for 48 per cent as on 31st March, 1971.

4.3. But in the earlier years following the advent of Independence, no specific policy of industrial reorganisation or mergers was evolved. The attention of Government was largely focussed on the need to broaden and strengthen the industrial base and to the

development of a strong and vigorous public sector to cover the strategic and basic areas of industry. The stray mergers of industrial units, and reconstruction of the structure of a few units which took place were more due to the fluctuating fortunes of the industrial units which were involved and not as a result of any clear policy of reorganisation of any particular sector of industry on efficient and modern lines. The few cases of mergers, restructuring, and reorganisation which did take place were guided by the relevant provisions of the Company Law, which at that time were primarily regulatory in character.

4.4. In 1969 Government decided on clear and purposeful policies and initiated concerted measures calculated to reduce the concentration of economic power resulting from control over large industrial conglomerates by the large industrial houses. These measures included (i) the nationalisation of the major commercial banks in July, 1969 which deprived these large houses of their hold over the resources of many of the larger banks which were under their influence till then, (ii) the abolition of the system of Managing Agency and Secretaries and Treasurers with effect from 3rd April, 1970 which to a large extent, did away with the visible means of control of the large houses over the majority of the companies till then under their management and severed the management links between such companies; and (iii) Issue of Guidelines to the public financial institutions to govern their investment policies which provided for their increasing participation in the equity capital and in the policy making and management of private sector companies, thus assisting the process of the loosening of the affiliation of such companies with the Large Houses.

4.5. Further, under the new Industrial Licensing Policy which became operative in February, 1970, certain limitations were imposed on undertakings belonging to foreign majority concerns and the twenty Larger Houses (listed in the Industrial Licensing Policy Enquiry Committee's Report). In accordance with this policy, these undertakings were expected to utilise their resources for the development of industries in the 'Core and Heavy Investment Sectors'● and for substantially export-oriented production. Definite policy orientations calculated to promote small scale industries and encourage new entrepreneurs in the medium scale sector were also given. The reservation of an increasingly larger number of industries for future development in the Small Scale Sector, the exemption from licensing of industries with investments below Rs. 1 crore for all but the Larger Houses and Foreign Majority companies, the encouragement given to new entrepreneurs and the increasing financial assistance granted to small scale units, all helped to create conditions for widening the base of industrial entrepreneurship and promoting broad-based ownership and control over industrial production.

4.6. Prior to the enactment of the Monopolies and Restrictive Trade Practices Act, 1969, the Government had no specific policy towards industrial integration and mergers. Government had neither expressly favoured nor disapproved of such combinations as a matter of policy, and under the Companies Act, mergers

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● The Core Sector of industry which has been so designated in view of the highest priority assigned for its development has been listed. The heavy investment sector is that sector where in individual units the capital investment is Rs. 5 crores or more.

or amalgamations were left to the initiative of industrial units and to the decisions of Courts on merit. Certain industries like coal, iron and steel and banking, however, implemented schemes of amalgamations and mergers at the instance of Government as such a step was considered beneficial for increasing efficiency. Similarly, formation of joint deals and export trade associations was also encouraged by the State. Thus the economic advantages of rational combines were not lost sight of even in the absence of any clear policy enunciation.

4.7. Earlier legislative measures, however, did provide for the guided growth of industries on planned basis and for regulation of various aspects of the functioning of industries in the broader national interest. The Industries (Development and Regulation) Act, 1951 has provisions enabling the Government to take over industrial undertakings if they are found to be working to the detriment of the public. The Companies Act has, apart from the detailed provisions to regulate the functioning of joint stock companies, a string of provisions to govern the procedures to be adopted in the case of mergers and amalgamations.

4.8. The Industries (Development and Regulation) Act, 1951 through a recent amendment and the Companies Act have provisions to facilitate and regulate industrial re-organisation and mergers. Section 18 FC of the Industries (Development and Regulation) Act provides that in the case of an industrial undertaking the management of which has been taken over by the Government, on receipt of a report on the affairs and working of the undertaking, if the Government are satisfied that (a) in the interests of general public, or (b) in the interests of the shareholders,

or (c) to secure the proper management of the company owning the undertaking, it is necessary so to do, they may, by order, decide to prepare a scheme for the reconstruction of the company owning the industrial undertaking. Section 395 of the Companies Act, 1956 provides that if a scheme of merger is approved by nine-tenth majority of shareholders, it shall be binding on all. Section 396 empowers the Government to compel two or more companies to amalgamate in the national interest. In case the scheme of merger involves the use of re-issue of capital, approval of the Controller of Capital Issues is also necessary. Under the Banking Companies Act, 1949, in the interest of efficient conduct of business, the process of merger of banks has been simplified; recourse to law courts has been obviated, legal formalities have been minimised and the risk of a few shareholders holding up the scheme of merger has been eliminated. By a subsequent amendment of the Act, the Government have assumed necessary powers to effect compulsory amalgamation of a bank with the State Bank of India or with any other bank. However, any scheme of merger of banks requires prior approval of the Reserve Bank of India.

4.9. Amalgamation and mergers under the above-noted legislative enactments have been used in India previously with a view to giving de jure recognition to a de facto situation in which the companies concerned were already interlinked by virtue of control exercised by the same group. Not only companies under the same managing agency were merged with each other, but even two or more managing agency companies were amalgamated. Such mergers, however, resulted in large concentration of economic power in the hands of certain management groups. Some examples of such amalgamations are those of Jardine Henderson Ltd., Macneil and Barry Ltd., and Martin Burn Limited.

It has to be pointed out that the regulatory provisions in the Companies Act under which these mergers were facilitated failed to take into consideration the economic and social aspects of mergers.

5. <u>The present policy towards reorganisation and mergers.</u>

5.1. The Monopolies and Restrictive Trade Practices Act, 1969 for the first time vested in the Central Government the authority to approve or disapprove of mergers or amalgamation involving companies which are covered by the provisions of the Act relating to concentration of economic power. One of its important objectives is to regulate mergers and expansion schemes of the larger houses. Schemes of mergers or amalgamation of an undertaking whose assets are not less than Rs.20 crores or an undertaking which is either a dominant undertaking or which after the proposed merger is likely to become such, require approval by the Central Government under section 27(2) before the court can sanction them. In approving of the merger applications, the Central Government has to take into account all matters which appear in the particular circumstances to be relevant and, among other things, give adequate consideration to the need consistent with the general economic position of the country -

a) to achieve the production, supply and distribution, by most efficient and economical means, of goods of such type and qualities, in such volumes and at such prices as will best meet the requirements of the Defence of India, and home and overseas markets;

b) to have the trade organised in such a way that its efficiency is progressively increased;

(c) to ensure the best use and distribution of men, materials and industrial capacity in India;

(d) to effect technical and technological improvements in trade and expansion of existing markets and the opening up of new markets;

(e) to encourage new enterprises as a counteracting force to the concentration of economic power to the common detriment;

(f) to regulate the control of the material resources of the community to subserve the common good; and

(g) to reduce disparities in development between different regions and more especially in relation to areas which have remained markedly backward.

5.2. The Central Government may, before according their approval, send a case to the MRTP (Monopolies and Restrictive Trade Practices) Commission for further enquiry where such enquiry is considered necessary. The Central Government has dealt with several cases of merger under these provisions. In one case, viz. the merger between Forbes Forbes Campbell and Company Limited and two of its subsidiaries, Warrior (India) Limited and Auto Accessories Limited, the merger has been allowed on the ground that the industry will thereby be organised more effectively, will ensure the best use and distribution of men, materials and industrial capacity and reduction in cost of production and management. In another case a proposal for amalgamation of Bengal and Assam Industries Limited, J.K. Agents Private Limited and Madhya Pradesh Industries Limited was not allowed on the ground that it would not

serve any special public purpose and would on the other hand increase the concentration of economic power in the hands of the controlling group to common detriment.

6. Criteria for identification of industries in which reorganisation and mergers would be desirable:

6.1. Before identifying the criteria for the selection of industries in which re-organisation and mergers would be desirable, it merits repetition that Government's primary objective is that the integrated or merged units should function efficiently within the broad framework of the accepted social objectives of the country and national priorities. In evolving a policy in respect of industrial integrations, Government have to take into account all the relevent facts, particularly their long range impact on distribution of income and wealth, and employment.

6.2. Within the broad perspective mentioned above, it is possible to delineate areas or industries where mergers or combinations may be fruitful. On a broad reckoning, it is felt that it would be advantageous to have industrial reorganisation and mergers under the following circumstances or in the areas of industry mentioned below:

i) Where the manufactured products and/or the physical equipment used in their production are large, e.g. steel, automobiles, ships, public works contracting;

ii) where the production involves a number of successive processes of manufacture or operations on the raw material, and there are economies from having all the processes under one roof, or controlled by one administration e.g. Steel;

iii) where expensive research activity is important to competitive power - e.g. chemicals;

iv) where the product is fairly standardised and can, therefore, be produced on a mass scale in long runs by specialised machines;

v) where the markets are geographically concentrated or transport costs are low in relation to the unit value of the product;

vi) where production involves several different operations and the existence of occasional large indivisibilities creates a balancing problem;

vii) where there is a large excess capacity in different manufacturing units manufacturing similar products;

viii) where there are large number of uneconomic units in the same line of manufacture competing with each other in the same markets; and

ix) where the total demand including export possibility is sufficient to support only a few firms of economic size.

7. A brief review of mergers and amalgamations in selected sectors in India:

7.1. In some of the Indian industries like coal, jute, cotton textiles and in respect of banks, mergers in the past did prove useful. In the case of these industries, there were a preponderance of small-sized units and many of them were ill-equipped and uneconomic. In order to work out definite proposals for the amalgamation

of collieries, a Committee on Amalgamation of Collieries was appointed in the year 1955 which recommended that small collieries should be amalgamated and brought under unified control for their reorganisation and modernisation. The Government followed up this recommendation by constituting a Committee to promote voluntary amalgamation of small coal mines.

7.2. So far as the textile industry is concerned, the Cotton Textile Inquiry Committee, 1958 recommended that mills of uneconomic size should be made economic by proper balancing or by amalgamation with some other units which could afford to purchase and instal the machinery and plant needed. Similarly, steps have been taken in the jute industry to eliminate the uneconomic units by transferring their loom-hours to other mills working on double shifts with greater economy. This trend towards closing down less efficient units and concentrating production in more economic and modernised units deserves to be noted. But in all such cases of reorganisation, what was sought to be secured was the better and more economic functioning of the concerned industrial units which had a potential for improvement in performance through replacements, rehabilitation and modernisation and wherever necessary through expansion of the size of operation. In the process such units which had hardly any potential for improved performance had to be closed down. Essentially the scheme of reorganisation was centered on individual industrial units in the industry and was not a scheme designed for a reorganisation of the structure of the industry as a whole. The efforts nevertheless resulted in better and more economic production in the particular sector of industry.

7.3. The case of banking and insurance companies received special consideration, because of their special position in the national economy. A large section of the banking industry and a major portion of insurance business had already been integrated with the establishment of the State Bank of India and the Life Insurance Corporation respectively. More recently 14 other important private banks and lately all the general insurance companies were nationalised. Here the scheme of reorganisation and integration in stages covered a major segment of the Banking Industry and practically the whole of the Insurance industry. A sectoral approach was adopted here on broader policy considerations and the scheme of reorganisation was not centered on individual units in the industry on the basis of their relative performance.

8. Decision to set up holding companies in selected industries to facilitate their reorganisation for rapid and coordinated growth:

8.1. Recently, Government have decided to set up a Holding Company for Steel and associated input industries like coking coal, iron ore, manganese ore, etc. This company will own all the shares in public sector corporations dealing with these industries, own all Government shares in the relevant joint sector companies and will act as the nominee of public sector financial institutions which hold shares in private sector units in the sphere of iron and steel and associated inputs, refractory units and small steel producing organisations. The Holding Company will be responsible for the working of the steel plants in the private sector, in which the public financial institutions have a substantial share. This decision has been taken in order to ensure the rapid and orderly growth of the steel industry.

8.2. The Holding Company will formulate long-term programmes of development, arrange for effective channelling of surpluses into further expansion of the industries, finance necessary technological changes and innovations and coordinate and supervise the operations of the various companies under it. It would thus achieve economies of vertical integration and ensure coordinated growth at least cost. For the machine tool industry too, Government have decided to establish a holding company to secure similar objectives. In the light of the experience gained in these two important sectors, the extension of this system of reorganisation to other important areas of industry would be considered.

8.3. As is evident from the decision to establish holding companies in the steel and machine tool sectors, Government have recognised the need for reorganisation in the iron and steel and machine tool industries by facilitating vertical integration in such industries. The plants in the iron and steel industry in the private sector are sufficiently large; hence, any further horizontal expansion of the industry will only lead to concentration of production in the existing units with no proportionate advantage in the shape of economies of production. Vertical integration will, it is expected, facilitate achievement of economies in investments and ensure coordinated growth. This is largely true of the machine tool industry also. As has earlier been mentioned, the need and scope for similar reorganisation in other industries, say engineering industries, paper, cement, fertilizer, drugs and pharmaceuticals, non-ferrous metals, etc. will require examination in the light of the experience gained in regard to steel and machine tools. But in any scheme of reorganisation as may be demanded by the

needs of a particular industry, due care will have to be taken to ensure that the resultant economies are significant and real and there is no further accretion to the concentration of economic power in private hands.

9. Some other aspects of
<u>reorganisation of industries.</u>

9.1. Due encouragement may also have to be given for diagonal expansion of industrial units to provide for the necessary ancillary facilities for their efficient functioning. For instance, the scope for integration of ancillary and service industries like coal washeries, and transport agencies with collieries for the coordinated development of the coal industry deserves examination. To derive the full advantage of the economies of integration, the integrated units should be situated within a readily accessible geographical region, as there is a close relation between integration and location of integrated units. The economies to which a reference is made here are those related to production, purchase and supply of raw materials and management. If the units are situated at wide distances, common technical staff cannot be employed, raw materials cannot be purchased in bulk from one market centre, by-products cannot be economically transported to other factories processing them and common managerial staff cannot supervise and guide the operations of all the integrated units. There could of course be some economies in distribution and sales depending on the type of industry and the location of markets and consuming centres.

9.2. Inter-connections between Companies through linkages in management secured through

inter-corporate investments and interlocking of directorships resulting in conglomerate growth as distinct from any rational integration, have in the past only contributed to undesirable concentration of economic power and not resulted in any economies in production, purchases, sales or use of managerial and technological resources. In any rational scheme of future planning and reorganisation, such conglomerate growth has not only to be discouraged but positive steps may have to be considered to restructure the management of industrial units forming part of existing conglomerates which serve no economic purpose and only create social problems and tensions.

10. Decentralisation of production suggested as the most suitable form of reorganisation in certain cases.

10.1. In industries which involve assembly of a large number of components, any future scheme of reorganisation designed to achieve economies in production should take note of the need and scope for economic decentralisation of production through establishment of a number of large units solely for the manufacture of ancillaries and components. Mass production of components and ancillaries in factories specially designed for their manufacture and their supplies to different assembly units will help in achieving better economies in production then by concentrating manufacture of all the components within an integrated production cum assembly plant. Encouragement to the establishment of a large number of units for mass production of different

ancillaries and components will, apart from achieving significant economies of scale in their production, also help in broad-basing entrepreneurship and in planned location of such industries taking due note of the need for balanced regional development. Economies and social benefits accruing from large scale sub-contracting of ancillaries and components have begun to be recognised and a healthy trend in the shape of developed countries sub-contracting the manufacture of labour intensive components to developing countries with large man power resources has begun to emerge. Dispersal of ancillary industries will also avoid problems arising out of employment of a very large labour force within a single factory. In a case of this type, rational reorganisation would consist of decentralisation of production in contrast to integration of production facilities.

10. Conclusion

Indian experience shows that while selective application of policies relating to industrial reorganisation and mergers may be useful and necessary for particular industries in given historical circumstances, the formulation of any overall general policy in this regard will have to take note of the socio-economic implications of the concentration of economic power that might result. What can be useful as a tool in selective circumstances cannot be a general remedy, still less a panacea for industrial efficiency and growth. A study of the needs, requirements and potentialities of individual industries is an inescapable exercise for policy makers in developing countries, the need for which gets reinforced by what we have stated above in regard to industrial reorganisation and mergers.

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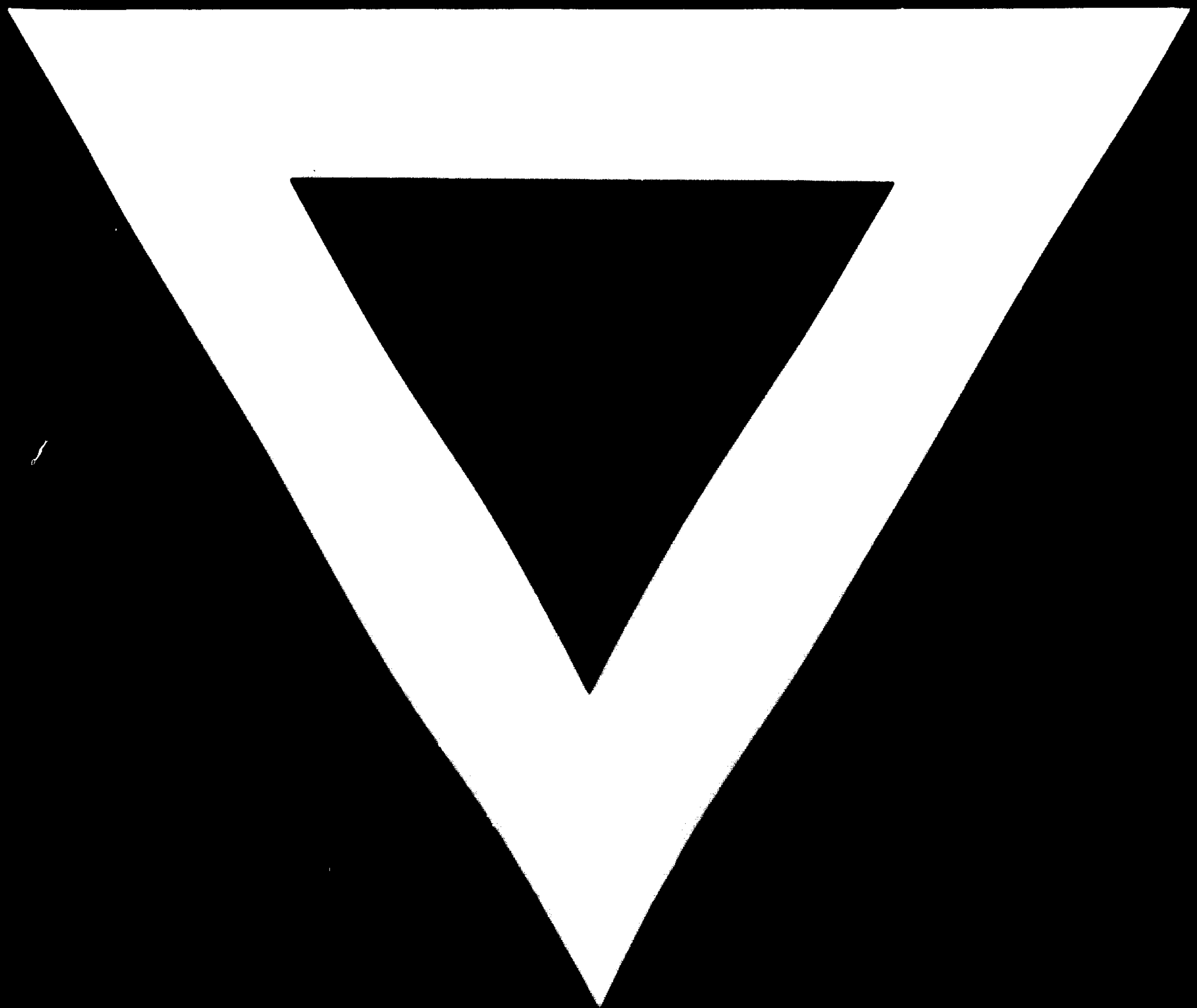

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