

The Issue of Small Firms' Innovation and Growth In Classical Informal Clustering

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Abstract

A paradigm shift was being observed from the perspective of location of the firms in the late 1960s to incorporate the study organizational behavior of the firms since 1970s. However, a revival of the discussion on location of industries appeared once again in the past few years since late 1980s. The rise of “alliance capitalism” with the growing prominence of intellectual capital raised the issue of new economic knowledge production. However, such discussions are solely concentrated to formal sector industries mostly of the developed nations. The present paper is an effort to analyze what strategies the small informal localized firms of the developing nations do adopt in order to get access in the new economic un-codified knowledge production in classical clustering to ensure their survival in the market. The established knowledge networks between small firms within an informal localization are sufficient enough to generate positive knowledge externality at the local level. To extract this, the tendency of a small informal firm is to locate within a spatial industrial cluster in order to incorporate successful knowledge spillover with the other firms of the same industry. Such un-codified non-market knowledge exchanges among informal firms are sufficient to promote growth of the existing industry.

Keywords: *Informal sector, Cluster economy, Externality, Location.*

JEL Classification: E26, F02, J61, R10.

I. Introduction

A paradigm shift was being observed from the perspective of location of the firms as analyzed in the late 1960s to incorporate the study organizational behavior of the firms since 1970s. However, a revival of the discussion on location of industries appeared once again in the past few years with the notification of the increasing pace of globalization since late 1980s and the rise of “alliance capitalism”ⁱ considering the growing prominence of intellectual capital as referred by Dunning 1998. However, such discussions are sole concentrated to formal sector industries mostly of the developed world. The present paper is a serious effort to analyze the phenomenon for small informal localized firms with their extended organizational networks at the local level. My present paper is an effort to detect the strategies that the small firms of informal localization of the developing nations do adopt in order to get access in the new economic un-codified knowledge production in classical clustering to ensure their survival in the market.

II. Methodology of Analysis

The logical argumentation of the study is based on literature support, case studies and primary survey results. The survey process is exhaustive. The survey is based on qualitative purposive sampling with semi-structured questionnaire and indirect interview method conducted in several spatial clusters of the Gems and Jewellery industry in West Bengal, namely Bowbazar (Central Kolkata), Sinthi (North Kolkata), Bhawanipur (South Kolkata), Domjur (Howrah) and Daspur-Ghatal (Paschim Medinipur). The micro-level field studies, sampling design and data analysis procedure are based on the standard model approach. The implication is that the selection of any sampling region of the study does not depend on data availability (or data non-availability) hence avoids any kind of error arising due to spatial homogeneity. The production units of a cluster within an industry in concern are considered to be non-homogeneous by nature. However, spatial distribution of the production units of a single industry under consideration is cross-sectional, given and known. Sometimes an ethnographic study has been approached due to data non-availability and non-responses in the sample survey area.

III. The Issue of Innovation in an Informal Localization

With growing prominence of the informal sector in several developing economies in the past few decades, the issue of ‘localized industry’ has attributed an important consideration in academic research and policy making. This is because a large part of informal sector production is carried out in informal localization. It becomes difficult for the small firms of the informal localized industries to get easy access to new economic knowledge production through executing innovation with their own R&D units thereby extracting positive externality in production – this is due to their insufficient fund to run large R&D units. Then the question appears: how in an “industrial district”, i.e. an area where a concentration of a large number of firms in a particular industry or in a group of industries, has already settled down. Here, the idea of industrial district does not refer simply to a “localized industry” formation but the idea actually refers that concentration of small informal firms in an industry or in a group of industries has already settled down.

One of the important characteristics of several informal localized industries is that often they are agglomerated in specific spatial clusters with concentration of decreasing average costs in production. The geographical concentration of several micro, small, medium and large enterprises producing same or similar type of goods and services strongly executes increasing returns to scale considering internal and external economies in production. However, the concept of agglomeration in the literatures of **Handerson** (1974, 1977, 1988, 2000), **Brulhart** (1998) and **Tabuchi** (1998) is accrued to positive external economies of scale which are often industry-specific. Then the same question appears: how the small informal firms of the localized industry with diversified characteristics distributed across several geographical spaces extracts positive external economies of scale. The question appears to be particularly relevant to deal with the share of a particular geographical location in a specific cluster industry to compare with the share(s) of the other location(s) of the same industry. Such analyses become vital to deal with the issues like formal-informal linkage analyses, cluster analyses, analyses of “Growth Pole” and several others.

IV. Innovation and Social Skill

The issue of innovation attributes to skill which is the learned capacity (or abilities) that one possesses. Sometimes skill becomes domain-specific, i.e. skills useful only for a certain job in any particular job – e.g. the Bengal Gems and Jewellery industry workers are renowned for their skill that refers to the incorporation of finer hand-made craft works while preparing jewelleryes with simple tools the use for cutting and fitting stones, carving out of intricate designs, coloring and finishing of the semi-finished ornaments etc. Such social skills facilitating interaction and communication and learned within a socio-economic stimuli sometimes becomes location-specific, for instance, the artisans of the “Growth pole” of Domjur in the Howrah district in West Bengal are specific in diamond setting, executing external economies of scale in agglomerated small scale informal industries allowing linkage effect [**Francois Perroux** (1949)].

The workers become keen to acquire social skill (both qualitative and quantitative dimension) since it often expresses worker's expertise, specialization, and innovative capacity measures their labour productivity that is reflected in their wages. The process of learning such knowledge endowment inherent within social skill acquired often requires some cost-effective socio-environmental stimuli in the form of community (social capital) networks between workers and between producers and workers in the frame of socialization with some already existing social rules, norms, reciprocity, co-ordination, organizations, belongingness, relations and interactions created, communicated, and changed in verbal and nonverbal ways.

V. Social Skill and Tacit Un-codified Knowledge Spillover

What is the problematic here is that the informal bonding and belongingness among the group members or community workers in an informal set up, knowledge endowment generates knowledge spillover in the form of easy knowledge flow in absence of formal paper works and patent laws - it even appears often in gossiping in streets and tea stalls. Such a knowledge and information spillover arising out of labour market pooling makes it easier for the rival firms to get access to innovation appeared in the form of new tacit or un-codified classical knowledge production function since marginal cost of transmitting tacit knowledge is the least with frequent

social interactions and communications appearing in an informal set up [**Jacobs (1969), Glaeser et al (1992)**].ⁱⁱ

VI. Tacit Un-codified Knowledge Spillover and Sticky Knowledge Externality

The tacit knowledge is uncertain in nature since it can spill over easily. With easy facilitation of network migration, the informal worker of the parent firm not only switches over to a new firm for higher wages and better work conditions but also presents himself in the new workplace along with his acquired skill and knowledge endowment acquired in the parent firm. The new firm reduces its costs of discovery, innovation and Marshall-Arrow-Romer (MAR) externality. In absence of formal paper works and patent laws, the small informal firms minimize the inherent stochastic behavior of this uncertain sticky knowledge production function [**Von Hippel (1994), Manski (2000)**] through transmission of direct and face-to-face interactions among the informal workers with the presence of their frequent and repeated non-market contacts which is easier within a spatial cluster by maintaining emotional tie-up and effective communication with the labourers. This is the only way by which the small informal firms of an informal localization execute positive “pecuniary” externalities in knowledge production which is non-exclusive and non-rival in use [**Scitovsky (1954), Arrow (1962), Romer (1986), Krugman (1991), Lucas and Rossi-Hansberg (2002)**].

VII. Knowledge Externality and Informal Localization Growth

One implication of the positive execution of industry-specific external economies is that it can rationalize city system through circular or cumulative causation of investment [**Myrdal (1957), Glaeser et al (1992)**]. However, each industry has its optimum size - sub-optimization of any informal localization city may lead to welfare-improving profit-opportunity based mobility of entrepreneurs [**Becker and Handerson (2000)**]. It leads to the establishment of a core in the region with large market and a periphery – for instance, the “core” location of Bowbazar and the periphery Sinthi location in Central and North Kolkata in case of the Gems and Jewellery industry in West Bengal [**Dicken and Lloyd (1990)**]. Such a formal-informal linkage within the

“core” and between the “core” and the periphery extracting positive externality allowing complementary core-periphery linkage model causes growth of the entire localized industry.

VIII. Conclusion

In case of localized informal industrial production, a successful execution of location-specific firm-specific positive knowledge externality by the small firms may ensure the existence of decreasing cost industry. The knowledge networks between small informal firms within an informal localization are sufficient enough to generate positive knowledge externality at the local level. To extract this, the tendency of a small informal is to locate within a spatial industrial cluster in order to incorporate successful knowledge spillover with the other firms of the same industry. Such un-codified non-market knowledge exchanges among informal firms are sufficient to promote growth of the existing industry.

End Notes:

- i. Alliance capitalism includes both strategic alliances and acquisition exchange deals between firms [Cantwell, 1999].
- ii. Here, we have to keep in mind Krugman’s famous argument that “knowledge flows are invisible, they leave no proper trail by which they may be measured and tracked”.

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