A comparative study: Entrepreneurship in Pakistan and Indonesia, an institutional and resource based view

Introduction

This paper seeks, by way of a comparative approach, to explore parallels between the evolution of entrepreneurship in Pakistan and Indonesia. Entrepreneurship is often presented as the catalyst for economic development and yet the literature employs terms such as "Rent seeking" and "Infant capitalist" to describe indigenous capitalism in Pakistan and Indonesia. Why? Many scholars have offered unsatisfactory cultural explanations or hinted at institutional weakness without developing the analysis further. I will use institutional theory and a resource-based view of the firm to conceptualise the evolution of entrepreneurship, in the often neglected informal sector. This theoretical approach helps to explain the similarities that Rutten has found between rural capitalists in developing Asia and the entrepreneurs of Europe's early industrial revolution. Drawing on secondary sources and other examples to illustrate how the theory applies, I will briefly discuss the textile industry in each country before concluding. My finding is that entrepreneurship can enjoy sustainable competitive advantages -- even without government subsidies -- providing that intangible resources such as: tacit knowledge, access to markets and or cheap labour are available for emergent capitalists to exploit. My conclusion advocates the need for further research on small to medium-sized enterprises, with an emphasis on successful firms in the informal sector and the intangible resources that they leverage.

Pakistan and Indonesia: an opportunity for comparative study

Indonesia and Pakistan are the world's 4th and 6th largest countries by population and share a number of common features. They have predominantly Muslim agrarian populations; militaries with historically important roles in domestic politics and have suffered chronic economic underperformance (Booth1988, Al Haque 2007). They are culturally, linguistically and socially diverse and yet share an important Hindu historical legacy that predates the arrival of Islam. Faced with many variables and limited resources, the comparative method, as defined by Lijphart (Lijphart 1971), enables us to test macro-hypotheses generated from theory. This allows for the testing of insights developed in Indonesia to be applied in Pakistan and vice versa. When using the comparative method in social science, he cautions that it is important to be aware of its limitations but not be disabled by them. With these comments in mind I will explore the question: Why has entrepreneurship in both Indonesia and Pakistan not matched economic expectations?

In the introduction to his comparative study of rural entrepreneurship, Rutten (Rutten 2003) identifies limitations in the literature arguing that: "...variations in analytical emphasis in the entrepreneurship literature on different parts of South and Southeast Asia tend to mask the similarities on the ground – economic, political and social – that seem to unite the different business classes of various countries." (Rutten 2003:32) He argues that the literature on Southeast Asian entrepreneurship - often devoted to explaining the economic dominance of the ethnic Chinese - tends to be "Weberian" [i]or culture based. Meanwhile scholars focused on South Asia's system of caste, have drawn on class-based or structural models inspired by Karl Marx. Rutten observes that both of these analytical approaches, are powerful but have, in the absence of comparative studies, limited potentially more fruitful theoretical development and cross fertilisation.[ii] My working hypothesis is that the shape and character of entrepreneurship depends on the institutional environment and the intangible resources that are available.

Using a comparative approach to study the historical evidence from ancient Rome, early China, and the Middle Ages to Renaissance period in Europe Baumol found that in "the upper strata of society, rent seeking…gradually replaced military activity as a prime source of wealth and power" (Baumol 1990). Entrepreneurial behaviour, therefore, develops over time and can evolve from military to more benign *rentier* and even productive varieties depending on the institutional incentives or the "relative payoffs society offers to such activities" (Baumol 1990:895).

Describing the institutional implications for entrepreneurship Baumol states that "The rules of the game [are] a critical influence helping to determine whether entrepreneurship will be allocated predominantly to activities that are productive or unproductive and even destructive." But what determines whether the entrepreneurial process produces positive or negative results? To explore this question we need to recognise that the entrepreneurial process is evolutionary meaning that it depends the *diversity* (and abundance) of the entrepreneurial activity; the *selection* of activity defined by the institutional setting; and finally the accessibility of resources enabling *replication* and growth. I will argue that collective expectations play an important role in defining the institutional environment, the process of selection and the types of entrepreneurship that evolve.

Why is Entrepreneurship seen as the catalyst for economic development?

The popular expectation of entrepreneurial activity is of a benign if somewhat wild force driving the economy. This view has been compounded by politicians who have championed entrepreneurs as 'national' heroes in the struggle for economic development in both recently formed nation-states but also in developed economies facing economic difficulties.[iii] According to Schumpeter's theory of 'creative destruction'(Schumpeter 1942) (p81-87), entrepreneurs are the drivers of economic growth that innovate by combining resources, revolutionizing economic behaviour, increasing productivity and, by extension, the nation's wealth. These idealised notions of entrepreneurship set the tone for my discussion on the role of government and institutions. It also helps explain the popular frustration with entrepreneurship when it fails to deliver positive results.

Why has "Rent seeking" and "Infant capitalist" been used to describe indigenous capitalism in Pakistan and Indonesia?

These 'national' and 'Schumpeterian' expectations of domestic entrepreneurship were fully present in newly independent Indonesia and Pakistan. They contrast strongly with both Baumol's historical perspective which allows for more varied outcomes. In contrast to the Schumpeterian hero of Western entrepreneurship, who leads a process of 'creative destruction', the entrepreneurs in Pakistan and Indonesia have been described as corrupt (Ul Haque) and apathetic (Koentjaraningrat 1969) by both international and local scholars (see also Rutten 2003:19-25). These negative attitudes towards local entrepreneurs are not confined to Pakistan and Indonesia and are symbolic of a wider misunderstanding of entrepreneurship and its origins.

Rutten's analysis of rural Gujarati traders shows how structural, often stereotypical, analyses have also been critical of small-scale trader-entrepreneurs in rural India. Their *lack of focus*, it has been argued, prevented them from "reinvesting their profits in the industrial enterprise [or]… to advance technology and increase the scale of industrial operations… [and] were said to be notoriously quick to shift investments into new fields in search of quick profits." (Rutten 2003:19) According to Rutten this "inclination to involve oneself in too wide a range of disparate commercial and industrial activities, whether successively or simultaneously" only reinforced the impression of Indian entrepreneurs as "commercialists" (Streefkerk 1985) who imitated to "fill a known gap in the production chain" (see Rutten 2003: 20).

Similar structural analyses, Rutten argues, were used in Malaysia and Indonesia to explain the poor performance of indigenous entrepreneurs. But because of the presence of successful ethnic Chinese businesses, cultural explanations were added to explain poor results. Typically these 'Weberian' arguments claimed that Confucian culture is entrepreneurial. These positions are somewhat ironic given that Max Weber had argued that Confucian culture limited entrepreneurial behaviour (Weber 1968). Nevertheless, this prompted the state, in the guise of economic planning, to cultivate select indigenous entrepreneurs, which Raillon called 'infant capitalists', with favourable policies. Raillon reasons that "strong government intervention… is not unexpected, as it is a rare thing to have spontaneous development of capitalism without state mediation." (Raillon 1991) (p 92). But state mediation is a form of *selection* and needs to be considered critically to explore our question further.

For example, Indonesia's *Benteng* policy of the 1950s was designed to favour *Pribumi* (indigenous) businessmen by awarding them monopolistic import licences.(Booth 1988)[iv] This policy prompted the formation of what popularly became known as Ali-Baba enterprises where Ali represented the *Pribumi* (Muslim) front man with political connections and Baba represented the Chinese Indonesian businessman with commercial know-how. Sadly these state policies encouraged *rent seeking* entrepreneurship and reinforced culture dominated views of entrepreneurship where the dependant and 'short-cut-ish mentality' of *Pribumi* politico-entrepreneurs were exaggerated (Rutten 2003:25) and extended to the wider population. This fed the belief, held both domestically and abroad, that *Pribumi* businessmen were incapable of advancement without state support. Pakistan's "Big push for industry" (1947-58) resembles Indonesia's experience and sets the tone for their respective post-independence development trajectories: "Various policy measures, such as tariff protection, import licensing schemes and other controls on imports, rather than enhancing productivity or encouraging industrialisation for growth, instead adversely affected the country by giving rise to a new elite—not entrepreneurs but rent seekers…" (Ul Haque 2007: 9)

The lack of government neutrality in managing national entrepreneurship initiatives created institutional imbalances and dependency which adversely affected the evolution of entrepreneurship in these countries. In the case of Indonesia the vocational tendency to favor salaried government employment, combined with popularist economic planning and hyperinflation described by Siregar (Siregar 1969) created a perfect storm for these imbalances. The economic and social consequences of *rent seeking* entrepreneurship, as a tax and source of corruption are well documented (Jacobs 1992; Khan and Jomo 2000). However, Ul Haque recognises that "at times rent-seeking might be preferred over Entrepreneurship" (see also (Baumol 1993)). The awarding of rents may enable political leaders to buy off potential rivals or entice collaboration from otherwise neutral parties. Recently formed nation-states contend with an array of divergent socio-economic forces and find ways to neutralise or pacify them, especially in those that are as diverse as Indonesia and Pakistan. Both governments have (over) relied on systems of patronage centralised around the executive and the military to maintain unity and this has come with a cost. Once an institutional environment that awards rents and monopolies has been established it is very difficult to change because a mutual dependency between the state and the private sector emerges. Cognitive lock-in, which occurs when close ties between agents filters out information which would reveal the negative contribution of their action, may also play a role in maintaining these arrangements. (Gargiulo and Benassi 2000)

To understand how the mutual dependency emerges we can consider the position of an entrepreneur presented by the government with the option of *rent seeking*. Monopolistic rates of return should appeal to his commercial sense but where implications for the common good are excessively detrimental and apparent; one would expect some reluctance to profit lest jealousies lead to retributions from rivals. However, the implications are often not immediately apparent and there are rationally bounded (Simon 1957) (P198) limits to what degree an entrepreneurs can investigate an opportunity. If the entrepreneur does not take advantage of the opportunity then a competitor might. Refusing to work with the government could also have negative consequences. Where rents are the norm, alternatives are limited and deals with the government expected, the entrepreneur will approach the government for deals and aggressively so because this is where the best opportunities lie. Crony capitalism also referred to as ersatz capitalism is essentially feudal in that it encourages the centralisation of power often at the expense of creativity and technical innovation (Yoshihara 1988).

Suharto, Indonesia's second President, inherited a chaotic economic environment from Sukarno in 1967[v] and set about changing Indonesia's institutions; further centralising commercial, political, economic, judicial and legislative power. He established a relatively stable patronage-based environment for business.[vi] Sidel describes the socio-economic environment: "Suharto presided over the continuous flow of capital, labour, and commodities, and the regular rotation of military and civilian personnel...it was precisely this steady circulation...that kept Indonesia in motion as Suharto stood still, for more than thirty years." (Sidel 1998)[vii]

Suharto's Indonesia went through the motions of holding elections and passing laws in parliament, with the interests of constituent groups selectively represented. The bureaucracy (government organisations) and businesses that evolved around the political system was geared to serve these chosen constituents and ultimately the Suharto establishment's interests. Built around a system of centralised patronage, Indonesia's economy grew, helped along the way by oil revenues in the 1970s, but the regime nevertheless squandered some spectacular opportunities for development.[viii] In 2004, the Asian Development Bank reported that "Indonesia's governance system" had, prior to the 1998 financial crisis, "operated under a regime in which state institutions neglected good governance and the rule of law, where the state managed essential parts of the corporate sector, and where corruption was allowed to rule over common interests." [ix]

Ul Haque's focus groups with businessmen across Pakistan, (2007:20-21) found that two themes emerged which suggest such a scenario has occurred in Pakistan despite relatively more changes in government over the same period of time: 1) "Business is not dynamic; few businesses seem to grow to be large conglomerates and multinationals" and 2) "Innovation which is the key to entrepreneurship seems to be nearly absent." He attributes this malaise to an established "rent-seeking culture" where "businessmen, rather than focusing upon innovation expect that the government will help." For example, he cites requests from the businessmen to the government for protection against cheap Chinese products and compensation to Sargodha merchants who lost customers to Lahore when the motor way was opened.

This view does not differ enormously with the situation for entrepreneurs in Indonesia. Gustav Papanek in his study of the Indonesian textile industry found that affirmative action programmes in Central Java "undermined entrepreneurial skills – innovation in relation to products, markets, technologies and management – and instead encourage cultivation of political and bureaucratic contacts." (Papanek 2006) But what of the entrepreneurs who are not part of the inner circle? To investigate this question I will present theory to examine the institutional environment inhabited by the multitude of small to medium-sized enterprises[x] in the rural-industrial fringe of society which Ul Haque refers to as the informal sector[xi].

What does institutional theory and the resource-based view of the firm suggest about the challenges facing entrepreneurship in the informal sector?

South and Southeast Asian farmer-come-entrepreneurs, Rutten discovered, resemble early European industrialists on three counts[xii]. They progressively withdraw from their villages to settle in towns and cities; distance themselves from labour and employ workers from outside their immediate communities (Rutten 2003:207-208). This severing and redevelopment of relationships is, I will argue, driven by an entrepreneurial need for resources in the shape of new institutions. To understand rural entrepreneurship from an institutional perspective I will combine the contributions of Alice Dewey, Douglas North, and Janet Landa to institutional theory, before briefly integrating a resource-based view.

In the 1950s, the anthropologist Alice Dewey, investigated trade and social control in Java and asked: "why there was such a huge difference between the prosperity of Chinese traders and Javanese traders?" Dissatisfied with the prevailing cultural explanations she examined trade using social control theory. Dewey found that "the one factor which consistently differentiated Javanese and Chinese traders was the way in which informal social sanctions operated." She formulated the hypothesis that systemic differences in the social environment of the Chinese Indonesians and the indigenous traders could explain responses to economic opportunities (Dewey 1962). According to Dewey's argument social sanctions were more commercially effective amongst Chinese Indonesian traders than amongst indigenous groups because, as an ethnically and religiously distinct minority, the consequences of social sanction or exclusion from their community would be catastrophic. The relatively high degree of co-operation amongst Chinese Indonesians lowered transaction costs and facilitated access to more profitable types of trade which in turn stimulated the formation and reinforcement of group identity and enterprise. "The more profitable the group ventures are the more effective is the sanction of the threat of exclusion from future groups. This sanction reinforces group solidarity, lowers the risks, and makes group operations more effective." (Dewey 1962:178)

New Institutional Economics (NIE), especially the work of Douglass North (North 1990), drew indirectly on the principle of social control theory. He defined institutions as: formal constraints based on written laws and contracts; meanwhile, informal constraints are based on codes of conduct. Institutional environments are hybrid by nature but a given 'transaction type' will dominate depending on the social environment. There are, according to his model, three types of transactions between organisations, or individuals (1990:34-5) with increasing scope for economic specialisation:

- Type one transactions occur in villages or tribes and are reciprocated through social favours and limited monetary exchange
- Type two transactions occur between members of same social network, such as guilds and ethnic minorities, are supported with third party enforcement and may be monetized
- Type three transactions are usually monetised with *anonymous* third party enforcement by way of legal precedent and or written contracts

TYPE ONE

According to this NIE framework, transactions that occur in villages or tribes are reciprocated through social favours and do not favour diverse entrepreneurial activity. For example, within an economically isolated village environment, North argues, the market is so small that poor economies of scale preclude all but the most rudimentary specialisation. While his classification sometimes exaggerates the absence of money it highlights the importance of social exchange and by extension social status. The dense social network enables villagers to know one another's business, making shirking difficult and status important. When an individual takes initiatives to specialise (diversifying entrepreneurial behaviour) he will encounter the institutional limitations of this environment.

For example, Dewey found that institutions which enable trade within the village can hinder the would-be trader from achieving scale and specialisation. She describes how a villager, aspiring to sell his harvest of bananas in the local town, attracts neighbours who attempt to relieve him of excess supply in return for coconuts next week. This usually well intentioned exchange introduces a degree of uncertainty to the would-be entrepreneur's planning process. For the stockpiling of the harvest to proceed smoothly, a change in local institutions is needed where the anticipated financial exchange in the market takes precedence over the social exchange in the village. Alternatively the would-be trader can, assuming he has the resources, distance himself from the village environment to avoid unwanted transactions. This might not initially mean quitting the village but it may oblige the trader to be absent for extended periods while he establishes institutional relationships that would support his more specialised role. There are precedents for this kind of economic migration. For example, Indonesia's Minangkabau people, known for their entrepreneurial flair, have a tradition where young men migrate to other parts of Indonesia in search of opportunities to start their own businesses (Naim 1971).

TYPE TWO

Migrant entrepreneurs often provide a good illustration of type two transactions. Chinese Indonesian traders, even when dispersed geographically, relied on "external pressures and internal allegiances" Dewey argued, "to create communities in which the members [had] considerable control over each other." (see also Hannah Papanek's 1972 analysis of Pakistan's Muhajir business elite[xiii].) Dewey recognised that, as if in a village, the "pattern of reciprocal duties and obligations" meant that social or financial accounts were kept open as the relationships between members were expected to endure for life. Hierarchy and status play an important role in these transactions and along with codes of conduct - as opposed to written laws - are the dominant heuristics in determining the terms of trade. This equates with what North calls type two transactions.

As most Chinese Indonesian agricultural traders in the 1950's had recently migrated from villages in Fujian, it is not surprising that they displayed institutional behaviour which resembled that found in villages. However, the act of migration to a new institutional environment prompted innovation because the Chinese Indonesians faced new opportunities and could not rely on *all* of the institutions they had relied on in China. The nature of the social environment in Southeast Asia meant that new transactional approaches had to evolve. Migration to Indonesia therefore, provided an institutional shock for these individuals that changed the rules of the game at a faster rate than which was possible in their home villages which remained underdeveloped until recently.[xiv]

The economist Janet Landa (Landa 1981), inspired by Dewey's social sanction theory, developed a transaction cost model to explain the trading practices of ethnically homogeneous middlemen groups in rural Malaysia. These ethnic Chinese also relied on codes of conduct for contract enforcement and, based on cultural identity, discriminated between insiders and outsiders. By way of heuristic screening techniques, that determined the degree of "social distance" and reliability, they judged the risk premium associated with their counter party. Outsiders had to pay cash to transact meanwhile insiders might be granted favourable credit. According to this theory, caste, religious and ethnic boundaries may serve as useful proxies to determine counter-party status and reliability. Landa also showed that as the size of the trading coalition expands transaction costs increase because more effort is required to determine the risk of default. Therein lies the limitation of type two transactions and the degree to which specialisation is possible. A 'commercialist' strategy makes a great deal of sense for entrepreneurs limited to type two transactions. Eventually however, opportunities for arbitrage diminish as trading networks become saturated with type two transactions and competition. The result is poor productivity as entrepreneurs expend their energies seeking trades rather than 'reinvesting their profits in industrial enterprises'. The returns to identity-based type two transactions eventually suffer and with this outcome some entrepreneurs will start to gravitate towards institutions that provide better incentives.

Rutten found that, in the intermediary phase of the farmer-come-entrepreneur, networks are vitally important. However, he also observed that amongst rural entrepreneurs "it initially appears that caste and religion are central features of business organization, but on closer analysis these can be seen as just one of the ways in which the wealthy business class forms networks to strengthen its economic position…" (Rutten 2003:209) Rutten observes that "It is not so much collectivism or individualism which explains successful or unsuccessful entrepreneurial behaviour; of far greater importance is the flexibility to adjust social and economic forms or organizations to changing circumstances." In some instances where the transition to urbanised entrepreneurship is advanced Rutten also noted that caste and religion no longer dictated behavioural norms. The transition from the village to type two transactions signifies a new institutional environment still governed by social sanctions but also by market forces that encourage increased levels of specialisation and experimentation. Where innovations are nationally or internationally competitive, demand will trigger not only economies of scale but also the need to transact with outsiders on a type three basis.

TYPE THREE

According to North's framework for type three transactions, anonymous, third-party enforcement, by way of legal precedent and/or written contracts enable further economic specialisation and scale. The varieties of entrepreneurship incentivised by this institutional environment includes research and development, brand management and other high value-added activities typically associated with cities in developed economies. North states that for a type-three-transaction environment to thrive the judiciary and government needs to be independent and fair. Where the institutional environment supports type-three transactions, productivity rises because property rights are secure and sophisticated transactions, enforceable by third parties, are made possible. While the relative power of social sanctions diminishes, the threat of legal enforcement increases. However, legal enforcement is expensive but relatively more so for the party at fault so ultimately it is informal constraints – and more limited social sanctions – that guide day-to-day affairs supported at a distance by the legal system.

Urbanisation accompanied by sophisticated type-three systems of exchange also facilitates the formation of economic clusters and specialisation. By establishing markets for knowledge the cost of innovation falls. Entrepreneurs and their firms can access intangible external resources which when combined may provide the firm with a competitive advantage. In the preface of her classic, *The Theory of the Growth of the Firm* (Penrose 1959) [xv], Edith Penrose stressed that "Human resources required for the management of change are tied to the individual firm and so are internally scarce" and that for a firm to grow it must attract resources from outside. Penrose explicitly referred to tangible resources such as physical assets and capital but also intangible resources such as skills and knowledge. Penrose according to Connell presented "a process theory of growth based on the pursuit and coordination of knowledge" (Connell 2009). Middlemen are not part of the social exchange economy of the village and so can demand cash payments or profitable terms of credit. To achieve favourable trades they cultivate and retain knowledge of their suppliers. The middlemen with respect to primary producers are typically in a stronger position in this trading relationship as they have more choice and are better resourced.

Mission critical transaction partners have a major influence on the evolutionary development of the firm's character and capabilities. Customers, especially in monopsony situations, can select for institutional sophistication to reduce transaction costs. For example, rural entrepreneurs that trade commodities with larger international customers are usually obliged to conduct type-three transactions. This kind of relationship may often, as a result of quality standards, oblige rural entrepreneurs to adopt norms and technology that might otherwise not become part of day-to-day business. The quality systems that support type-three transactions take time and hard work to develop but they are vitally important to the entrepreneur's ability to retain and grow accounts. Where the mission critical partner is the customer competition can drive institutional innovation and productivity improvements.

Where the mission-critical transaction partner is the government, the direction of the institutional innovation depends on the incentives established by the government. In other words, the government policy becomes a *selection* mechanism that favours certain types of entrepreneurial fitness. Governments in Korea, Singapore and Japan have successfully cultivated entrepreneurs and new industries but importantly also have a track record of withholding support from firms and industries that do not meet commercial expectations (Booth 1998:136-7). They do not generally allow dependency or undesirable entrepreneurial behaviour such as rent seeking to develop. Another scenario described in the literature is of the 'parasite state' that so disincentives entrepreneurial activity, for example, by way of weak property rights and or prohibitive tax that would-be-entrepreneurs become apathetic. With less entrepreneurial behaviour, the *diversity* of firms suffers and there is a smaller pool to *select* from which in turn makes the challenge of state support for entrepreneurship all the more difficult.

Interestingly type-two transactions can, when the rule of law is uncertain, prove superior to type three transactions and offer a tactical advantage to castes guilds or ethnic minorities. For example, in the newly independent Papua New Guinea, as Europeans exited manufacturing and financial businesses Chinese minority entrepreneurs sourced financing from their social networks to fund acquisitions. As loans were practically unavailable from the formal banking system they were able to buy these businesses with little outside competition(Wu 1974). However, the weakness of both formal constraints and social sanctions ultimately works against entrepreneurial behaviour and economic development. Dewey's findings suggest where the legal environment is weak and social sanctions function poorly, transactions tend to be less sophisticated[xvi] (Dewey 1962:181).

We shall see that, with lower communication and logistical costs, the informal sector has become a hybrid institutional setting where collective and individual forms of entrepreneurship are becoming more common. By diversifying from farming into regional trading and light industry, the rural entrepreneur gains access to new opportunities and resources not available in his home village and then very quickly is faced with competition on a global basis. Where the government encourages rent seeking forms of entrepreneurship the agility needed to thrive internationally will be missed.

A discussion of the textile industry

The textile industry is often a first step in industrialisation and both Indonesia(Hill 1992) and Pakistan(Zaidi 2005) have significant interests in this sector. Earlier I referred to Gustav Papenek's study (Papanek 2006) of entrepreneurship in the Indonesian textile industry which showed that subsidies in Java encouraged rent seeking. However, in Bali, Papenek describes entrepreneurs that were able to develop textile businesses that became internationally competitive with practically no direct support or attention from government. They adopted what I call "just-enough-technology" entrepreneurship where existing institutions are able accommodate the new approaches, permitting productivity increases which in turn offset the transaction costs of learning.

According to Papenek, textile entrepreneurs in Bali made use of their knowledge of village cottage industry to contract out sewing - the most labour intensive part of clothing production. This enabled them to centralise and focus on scalable activities such as "analysing the market and developing designs; cutting the cloth; inspections and quality control of finished garments; packing, shipping, arranging credit and collecting payments." These entrepreneurs subcontracted labour-intensive activities in much the same way as the early textile industrialists in Europe 'put-out' production to households and workshops (see Rutten 2003:215). By accessing cheap village resources (labour and skills) entrepreneurs were able to limit their investments in infrastructure and management:

> "Having sewing done in the villages had substantial advantages in cost and flexibility. Buildings did not have to be provided to house operations; workers did not have to be supervised; the work was done more cheaply because it could be done during odd hours and on days when there was little other activity; and it was simple to increase or reduce the amount of work without hiring or dismissing workers or paying overtime" (Papenek 2006:88)

A substantial number of the original entrepreneurs in Bali were tourists (turned expatriates) that took advantage of relaxed attitudes towards visa restrictions. By partnering with *Pribumi* that were familiar with local resources and able to apply social sanctions, these tourist entrepreneurs - many of whom had prior knowledge and contacts in the fashion industry - transformed the capabilities of domestic production. With time the *Pribumi* entrepreneurs learned from the tourists and eventually replaced them.[xvii]

Papanek writes "the symbiosis with tourism was crucial for the industry" (Papenek 2006:86) because besides the tourist-entrepreneurs it also provided infrastructure and an on-the-spot retail market which reduced the lines of communication significantly. Once Garuda, the national carrier, lost the monopoly over international flights to Bali, the costs of transport fell. The boom in the tourist and retail industries stimulated both growth and competition driven largely by market forces *governed* by both the industry's and the village's institutions. These *Pribumi* entrepreneurs in Bali "succeeded primarily in the usual way of the market – by enterprise, hard work, risk-taking and saving…seizing the opportunities presented by the rapidly expanding tourism industry; their strong focus on the export market; and their ability to keep costs low by putting out the sewing function to village groups" (Papenek 2006:85).

Meanwhile, Pakistan is one of the world's largest cotton growers and has ample labour that together should represent a tremendous source of competitive advantage for the textile and clothes sector. However, "Pakistan is generally not perceived to be a preferred supplier by buyers in the export markets as it lacks innovation and quality"(Khan 1998). Meanwhile, the competition, from Indonesia and other countries that do not produce cotton, have been able to establish competitive textile and clothes industries by sourcing suitable materials abroad and combining their cheap labour with management systems that can respond to the international market. Pakistani textile entrepreneurs are at a disadvantage to their competitors because the incentives to coordinate production are underdeveloped. Spinners, weavers and garment producers appear incapable of reading and responding in a coherent manner to international market trends and customer needs. According to Naheed Zia Khan it was the unintended consequences of government policy that prevented Pakistan developing a more integrated value chain.

The yarn and weaving industries are the most dominant elements in the Pakistani cotton value chain and are the largest foreign exchange earners. Together they are also an important part of Pakistan's formal sector and have been a major recipient of government support especially by way of cheap loans. These loans prompted over capacity without incentivising better downstream coordination. Despite an absolute increase in volume, poor quality has led to a weakened bargaining position and mediocre earnings on a per unit basis. Quality issues with yarn and cloth sourced domestically put Pakistan's garment industry at a disadvantage (see Khan 1998).

Khan describes weak supplier and customer relations as well as a poorly developed system of informal and formal constraints reminiscent of Dewey's description of unsophisticated transactions. Pakistan's garment manufacturers do not receive the kind of immediate consumer feedback that their counterparts in Bali have received.

Instead, according to Khan, the industry has become dominated by volume exporters that often "solicit orders by offering lower prices and seem to be interested in 'one shot' business rather than developing long-term relationships with the customers."

This at first glance looks like the lack-of-focus stereotype mentioned in the introduction. However, the theory and literature suggest that these relatively unsophisticated trades are an unintentional by-product of government policy. The dominance of government favour in the formal sector combined with the government's ever present need for foreign exchange may have unintentionally incentivised this pattern of trading.

Conclusion

This paper has argued that the limitation of entrepreneurial performance sits less with structural or cultural shortcomings, but rather with the institutional framework that incentivises entrepreneurial behaviour. We have seen that the expectations of entrepreneurship as a panacea for economic development in Pakistan and Indonesia have exceeded the capacity of the institutional environment to incentivise positive results. Trade protection and import substitution policies implemented by Indonesia and Pakistan, although well intended, created a rent seeking form of entrepreneurship. Meanwhile, rural capitalists in the informal sector have been largely neglected and this has meant that a vast amount of entrepreneurial potential has been overlooked and underexploited. However, from the Balinese example we can see with hindsight that this neglect can be a blessing in disguise. As Papenek demonstrates, the Indonesian government's policy to liberalise the Balinese tourist industry inadvertently provided incentives and resources for entrepreneurs to exploit (Papenek 2006:85) - including for a brief period tourist entrepreneurs who became valuable points of access to international markets and conduits for tacit knowledge to their local counterparts.

For national welfare to improve, it is Pakistan and Indonesia's informal sectors that need to be activated as sources of entrepreneurial activity. To obtain the best results, where participation is high and entrepreneurial activity diverse, each country needs to develop institutional environments that can incentivise more sophisticated forms of transaction. Unfortunately Pakistan and Indonesia's institutional environments have historically made many types of sophisticated transactions prohibitively expensive and this has seriously limited the potential for constructive entrepreneurial activity. Even after considerable economic reform, government tends to favour large-scale enterprises in the formal sector over the interests of the informal sector. Small to medium-size firm access to tangible and intangible resources remains very limited by international standards. However, these limitations are less restrictive than they were. Global infrastructure such as modern telecommunications have helped reduce transaction costs as access to information has become cheaper.

There are companies serving Pakistan's substantial domestic garment market that could evolve into innovative exporters providing institutions emerge that support this form of entrepreneurship. By investing in and learning from their customers, they should develop competitive advantages just as garment producers in Bali have done, providing they can effectively source the tangible and intangible resources needed for their development. Opportunities may have been squandered during plans to incentivise national entrepreneurship but the beauty of Schumpeter's theory of 'creative destruction' is that there are always people looking for new ways to innovate for the better, providing the incentives are right.

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> Transaction cost, property rights, and resource-based approaches to the firm assume that assets, both tangible and intangible, are heterogeneous. Arranging these assets to minimize contractual hazards, to provide efficient investment incentives, or to exploit competitive advantage is conceived as the prime task of economic organization. None of these approaches, however, is based on a systematic theory of capital heterogeneity. In this paper we outline the approach to capital developed by the Austrian school of economics and show how Austrian capital theory provides a natural bridge between theory of entrepreneurship and the theory of the firm. We refine Austrian capital theory by defining capital heterogeneity in terms of subjectively perceived attributes, the functions, characteristics, and uses of capital assets. Such attributes are not given, but have to be created or discovered by means of entrepreneurial action. Conceiving entrepreneurship as the organization of heterogeneous capital provides new insights into the emergence, boundaries, and internal organization of the firm, and suggests testable implications about how entrepreneurship is manifested.

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> This paper explores the tension between two opposite views on how networks create social capital. Network closure (Coleman 1988) stresses the role of cohesive ties in fostering a normative environment that facilitates cooperation. Structural hole theory (Burt 1992) sees cohesive ties as a source of rigidity that hinders the coordination of complex organizational tasks. The two theories lead to opposite predictions on how the structure of an actor's network may affect his ability to adapt that network to a significant change in task environment. Using data from a newly created special unit within the Italian subsidiary of a multinational computer manufacturer, we show that managers with cohesive communication networks were less likely to adapt these networks to the change in coordination requirements prompted by their new assignments, which in turn jeopardized their role as facilitators of horizontal cooperation within a newly created business unit structure. We conclude with a discussion of the trade-off between the safety of cooperation within cohesive networks and the flexibility provided by networks rich in structural holes.

Hill, H. (1992). Indonesia's textile and garment industries : developments in an Asian perspective. Singapore, ASEAN Economic Research Unit, Institute of Southeast Asian Studies.

Hofstede, G. (1980). Culture's consequences : international differences in work-related values. Beverly Hills, Sage Publications.

Jacobs, J. (1992). Systems of survival : a dialogue on the moral foundations of commerce and politics. London, Hodder & Stoughton, 1993.

Khan, M. H. and K. S. Jomo (2000). Rents, rent-seeking and economic development : theory and evidence in Asia. Cambridge, Cambridge University Press.

Khan, N. Z. (1998). "Textiles Sector of Pakistan: The Challenge Beyond 2004." The Pakistan Development Review : **37**(4 Part II): 595-619

Koentjaraningrat (1969). Rintangan p2 s mental alam pembangunan ekonomi di Indonesia. Djakarta,, Bhratara.

Landa, J. T. (1981). "A Theory of the Ethnically Homogeneous Middleman Group - an Institutional Alternative to Contract Law." Journal of Legal Studies **10**(2): 349-362.

Li, Y. (2010). Economic Reform and Development the Chinese Way, Foreign Language Teaching and Research Press.

Lijphart, A. (1971). "Comparative Politics and Comparative Method." American Political Science Review **65**(3): 682-&.

McSweeney, B. (2002). "Hofstede's model of national cultural differences and their consequences: A triumph of faith - a failure of analysis." Human Relations **55**(1): 89-118.

Geert Hofstede's legendary national culture research is critiqued. Crucial assumptions which underlie his claim to have uncovered the secrets of entire national cultures are described and challenged. The plausibility of systematically causal national cultures is questioned.

McVey, R. T. and Cornell University. Southeast Asia Program. (1992). Southeast Asian capitalists. Ithaca, N.Y., Southeast Asia Program, Cornell University.

Naim, M. (1971). Merantau: causes and effects of Minangkabau voluntary migration. Singapore The Institute of Southeast Asian Studies.

North, D. C. (1990). Institutions, institutional change and economic performance. Cambridge, Cambridge University Press.

Papanek, G. F. (2006). "The Pribumi entrepreneurs of Bali and central Java (or how not to help indigenous enterprise)." Bulletin of Indonesian Economic Studies **42**(1): 79-93.

Fostering indigenous (pribumi) entrepreneurs remains a major aim in Indonesia. The history of the Central Javanese batik industry shows, however, that affirmative action programs in pursuit of that aim can be counter-productive if they undermine entrepreneurial skills-innovation in relation to products, markets, technologies and management-and instead encourage cultivation of political and bureaucratic contacts. The batik industry cloth subsidy did this by rewarding well-established and well-connected firms for continuing to do what they had long been doing, while discriminating against new and innovative firms. On the other hand, the emergence and rapid expansion of the Balinese garment industry showed that pribumi are capable of successful entrepreneurship in a favourable environment without any extraordinary government assistance. The challenge for policy makers determined that pribumi play a larger role in business, therefore, is to design policies that encourage the development of pribumi entrepreneurial skills, rather than causing them to atrophy.

Papanek, H. (1972). "Pakistan's Big Businessmen: Muslim Separatism, Entrepreneurship, and Partial Modernization
" Economic Development and Cultural Change, Vol. 21, No. 1 (Oct., 1972), pp. 1-32.

Penrose, E. T. (1959). The theory of the growth of the firm. New York,, Wiley.

Raillon, F. (1991). "How to become a National Entrepreneur. The rise of Indonesian Capitalists
." Archipel **41**: 89-116.

Rutten, M. (2003). Rural capitalists in Asia : a comparative analysis on India, Indonesia, and Malaysia. London ; New York, Routledge.

Schumpeter, J. A. (1942). Capitalism, socialism, and democracy. New York, London,, Harper & Brothers.

Schwarz, A. (1994). A nation in waiting : Indonesia in the 1990s. Boulder San Francisco, Westview Press.

Sidel, J. T. (1998). "Macet Total: Logics of Circulation and Accumulation in the Demise of Indonesia's New Order." Indonesia **66**: 158-195.

Simon, H. A. (1957). Models of man: social and rational; mathematical essays on rational human behavior in a social setting. New York,, Wiley.

Arifin Siregar, "Indonesian Entrepreneurs," Asian Survey 9 (May 1969): 343–58

Streefkerk, H. (1985). Industrial transition in rural India : artisans, traders and tribals in South Gujarat. London, Sangam.

Ul Haque, N. (2007). "Entrepreneurship in Pakistan." PIDE Working Papers Retrieved 2011, from http://www.pide.org.pk/pdf/Working%20Paper/WorkingPaper-29.pdf.

Entrepreneurship is viewed by economists to be a combination of innovation and risk taking. When such activity thrives, high growth rates are achieved as well as opportunities offered to all segments of society, including the poor. The latter benefit form growth and employment as well as through opportunities for entrepreneurship.

In Pakistan innovation and risk taking is severely inhibited by the intrusive role of government in the marketplace. From the early days of planning when protection and subsidy polic ies determined winners in the market place, entrepreneurship has been diverted to seeking government favours.

Government economic policy also seeks to promote growth through a basically 'mercantilist' approach where domestic commerce through seriously neglect is heavily regulated. This sector either employs most of the poor or offers them entrepreneurial opportunities. Hence deregulating this sector could be a priority in and anti-poor strategy.

The paper also argues that land distribution and city zoning and management have also evolved to further reinforce the prevalent rent seeking path to success. The result is that cities are by design not allowed to become clusters of commerce that will be entrepreneur friendly. These clusters of dense urban commerce are magnets of employment and opportunity for the poor.

To develop an entrepreneurship culture in the country, the system of incentives (laws and policies) that promote rent seeking will have to be dismantled. This paper presents an analysis of the state of entrepreneurship/rent seeking prevailing in Pakistan. This analysis allows us to obtain and understanding of the kinds of reforms (including legislative changes) that are required to develop entrepreneurship.

Weber, M. (1968). The religion of China: Confucianism and Taoism. New York,, Free Press.

Weber, M., T. Parsons, et al. (1930). The Protestant Ethic and the Spirit of Capitalism. Translated by Talcott Parsons ... With a foreword by R. H. Tawney, pp. xi. 292. G. Allen & Unwin: London.

Winters, J. A. (1996). Power in motion : capital mobility and the Indonesian state. Ithaca, N.Y., Cornell University Press.

Wu, D. Y. H. (1974). "To Kill Three Birds with One Stone: The Rotating Credit Associations of the Papua New Guinea Chinese." American Ethnologist **1**(3): 565-584.

The author looks at rotating credit associations in the Overseas Chinese community in Papua New Guinea, where complicated financial networks have been built up from simple traditional models, and argues that it is man and not the institution which holds the key to cultural change and economic development; the way in which the economic institution is manipulated by the people determines its adaptability

Yoshihara, K. (1988). The rise of ersatz capitalism in South-East Asia. Singapore ; Oxford, Oxford University Press.

Zaidi, S. A. (2005). Issues in Pakistan's economy. Oxford, Oxford University.

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[i] For Max Weber's best known book see Weber, M., T. Parsons, et al. (1930). The Protestant Ethic and the Spirit of Capitalism. Translated by Talcott Parsons ... With a foreword by R. H. Tawney, pp. xi. 292. G. Allen & Unwin: London.

ii Weber and the best known contemporary proponent of the cultural approach Hofstede have been described as both orientalist and essentialist. See also McSweeney, who found Hofstede's global framework "anorexic and mechanistic." Hofstede, G. (1980). Culture's consequences : international differences in work-related values. Beverly Hills, Sage Publications.

, McSweeney, B. (2002). "Hofstede's model of national cultural differences and their consequences: A triumph of faith - a failure of analysis." Human Relations **55**(1): 89-118.

Geert Hofstede's legendary national culture research is critiqued. Crucial assumptions which underlie his claim to have uncovered the secrets of entire national cultures are described and challenged. The plausibility of systematically causal national cultures is questioned.

[iii] An example is David Cameron's recent appeal to the British entrepreneurial spirit to find the economic salvation.

[iv] Booth 1988 see pages 312-318

[v]From 1965 to 1967 Suharto was essentially in control of Indonesia but Sukarno retained the title of President

[vi] Select members of the politically neutered Chinese Indonesian business community -the *Cukong*- were awarded monopolies by way of joint ventures. The *Cukong* dominated the economy, influencing not only the formulation of law but also the behaviour of other organisations in the political and economic sphere. Rents from these joint ventures were fed back into foundations (*yayasan*), political parties and 'security' organisations, including paramilitary "youth" groups, under Suharto's control.

[vii] See also Winters, J. A. (1996). Power in motion : capital mobility and the Indonesian state. Ithaca, N.Y., Cornell University Press.

[viii] Significant progress was made in terms of health, education and infrastructure Schwarz, A. (1994). A nation in waiting : Indonesia in the 1990s. Boulder San Francisco, Westview Press.

but the regime did not leverage, as well as it might, Indonesia's potential as a low-cost exporter. Instead Suharto retained tariffs and monopolies, focusing instead on import substitution and a redistributive approach to Indonesia's political economy see p67-68 of McVey, R. T. and Cornell University. Southeast Asia Program. (1992). Southeast Asian capitalists. Ithaca, N.Y., Southeast Asia Program, Cornell University.

See also Booth 1988

[ix] During the Asian financial crisis the IMF imposed institutional reforms on Indonesia's government as part of its rescue package. A letter of intent, setting out the conditions for the IMF's support, was jointly signed by the government and the IMF on 15th January 1998. This agreement and three supporting memorandums (April 9th, June 25th, and November 15th) set in motion a tectonic round of institutional change that it was hoped would remedy the New Order's institutional legacies. They stipulated that subsidies be wound back, barriers to international trade reduced and monopolies dissolved. These agreements were also aimed at restructuring corporate debt, reforming the banking system, improving governance and ensuring economic stability. Central to the IMF's strategy was a belief that these signals of reform would encourage the return of foreign investors but disappointingly little debate was focused on the plight of domestic entrepreneurs beyond the usual calls for state intervention.

[x]Dana, L. P. (2009). Handbook of research on Asian entrepreneurship. Cheltenham, UK ; Northampton, MA, Edward Elgar.

Khurrum, S.Bhutta and Adnan, Omar Pakistan p230 "According to the 2005 economic census of Pakistan, there are 3.2 million business enterprises nation-wide and SMEs constitute over 99% of them. They employ 78 percent of the industrial employment and by value contribute nearly 35 percent. Pakistan exports are estimated to be US$16.1 billion primarily in textile, rice, leather goods, sports goods, chemicals manufactures, carpets and rugs.(Government of Pakistan 2005. 96 percent of firms are owned and managed by an individual as a sole proprietary concern. 98 percent employ fewer than 5 people and 99 percent employ fewer than 10 people. ... These characteristics of the SME sector suggest that most of the businesses are in a low-growth trap, dealing in traditional products and unable to climb up the technology ladder."

See Latif, Adam p 97 "In 2005, 99.9% of all enterprises were SMEs. They produced approximately 60% of Indonesia's GDP and absorbed more than 99 % of Indonesia's labour force ... and play an important role in the efforts to produce non oil exports."

[xi] (Ul Haque 2007 :12) "Today almost 40 percent of business takes place in the informal sector and still as compared to the large scale industry, the small scale enterprise and industry continues to face unfavourable policies. Neglect of the sector on part of the government is evident from the fact that even today actual growth rate of the sector is not computed, (the way it is done for large scale sector), and instead it is merely imputed. The small scale and the informal sector may be much more dynamic and productive than what government figures have continued to show till today. It is also important to note that the small scale sector is the breeding ground for innovation but continues to attract little research."

[xii] Scholars such as Dobb, M. (1947). Studies in the development of capitalism. New York,, International Publishers.

(1976 p277-278) have argued that the entrepreneurs of the industrial revolution in Britain were not from the established and elite merchant class but were largely craftsmen and yeomen farmers dissatisfied with the status quo. This embryonic middleclass had no reason to support the privilege (or rents) historically granted by the crown (from feudal times) to guilds and other vested interests. Instead they innovated with the resources, tangible and intangible that they had at their disposal with little or no government support apart from a robust legal system that guaranteed property rights and reduced transaction costs.

[xiii] Papanek, H. (1972). "Pakistan's Big Businessmen: Muslim Separatism, Entrepreneurship, and Partial Modernization
" Economic Development and Cultural Change, Vol. 21, No. 1 (Oct., 1972), pp. 1-32.

The business elite or the "Twenty-two Families" that came to dominate Pakistan's post independence economy were migrants from India and appear to have actively developed social-commercial networks such as chambers of commerce that facilitated type two transactions See p11-13 See also P19 "Group loyalties play an extremely important role in hiring and employment in commercial enterprises (though not in the case of factory labor). Potential entrepreneurs can come from various class levels within the community, which retains its strong emphasis on self-employment in business as the most desirable occupation, thus assuring a continuing supply of both manpower and entrepreneurial replacements. Within the business communities, there is also a well functioning information network, producing not only intense rivalries among competitors, but also diffusion of information and a system for assessing credit worthiness, and much better access to credit facilities than would be available to unaffiliated individuals. Rivalry, information, and access to capital produced a tendency toward more innovative entrepreneurial behaviour, especially in a situation with as many opportunities for business profit as existed in the early years of the new state." The parallels between this migrant elite and Chinese mainland capitalists that settled in Taiwan after the war would make an interesting study.

[xiv] When institutional innovations such as harvest rights, eventually emerged in China, in the late 1970s and early 1980s it prompted an explosion in rural entrepreneurship (p245-257). Li, Y. (2010). Economic Reform and Development the Chinese Way, Foreign Language Teaching and Research Press.

[xv] In some instances the Penrosian view is referred to as the knowledge-based view (see Foss, K., N. J. Foss, et al. (2007). "The entrepreneurial organization of heterogeneous capital." Journal of Management Studies **44**(7): 1165-1186.

Transaction cost, property rights, and resource-based approaches to the firm assume that assets, both tangible and intangible, are heterogeneous. Arranging these assets to minimize contractual hazards, to provide efficient investment incentives, or to exploit competitive advantage is conceived as the prime task of economic organization. None of these approaches, however, is based on a systematic theory of capital heterogeneity. In this paper we outline the approach to capital developed by the Austrian school of economics and show how Austrian capital theory provides a natural bridge between theory of entrepreneurship and the theory of the firm. We refine Austrian capital theory by defining capital heterogeneity in terms of subjectively perceived attributes, the functions, characteristics, and uses of capital assets. Such attributes are not given, but have to be created or discovered by means of entrepreneurial action. Conceiving entrepreneurship as the organization of heterogeneous capital provides new insights into the emergence, boundaries, and internal organization of the firm, and suggests testable implications about how entrepreneurship is manifested.)

[xvi] Dewey 1962: 181 Considers the case of "… a professional urban trader who does not belong to any sort of cohesive social unit. This means that there is no way in which either party can bring informal sanctions to bear on the other. Since legal action is too troublesome and expensive there is no way in which any contract can be enforced unless it is made and completed within the scope of the immediate face to face relationship. As a result the seller hardly ever gives credit, and the buyer does not attempt to assure his future supply by trying to establish a long term contract with the seller. This inhibits planning except on a day to day basis."

[xvii] This is essentially a short term form of foreign direct investment (FDI) Like long term FDI - especially in capital intensive industries – it offers technological and management sophistication (institutions and organisations) that might not otherwise appear or take a long time to do so.