

# *The Emergence of the Informal Sector Firms in International Business: The Globally Distributed Indian Diamond Industry\**

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## **Abstract**

This paper highlights and explores the emergence of informal sector firms (ISFs) in international business. Due to the increasing size and significance of informal economy in the global context (particularly emerging markets), we also attempt to understand the characteristics and relevance of these ISFs. The globally distributed diamond industry is one such instance, composed of thousands of informal sector entrepreneurial firms (ISFs) which export cut and polished diamonds (CPD) worth USD 20 billion annually. However, these firms thrive in the atmosphere of secrecy and informality that envelops the diamond trade and has for long been labeled as an unorganized sector in the world economy. Interestingly, the collective output of the ISFs in an emerging economy (India) enjoy a 95 percent market share of net global exports of cut and polished diamonds. This study reveals that networking of the Indian ISFs of the CPD industry resembles a close knit community which works on mutual trust, verbal commitments and familial and personal relationships mostly with informal systems in place. The so called unorganized CPD firms are possibly a different form of organizing which we call the "informal sector firm" and are clearly well-organized and enormously successful in international business despite lack of formal systems and formal education of their people.

## **1. Introduction**

The informal sector offers a wide spectrum for study of firms as it has a wide diversity, constantly evolving structure and it represents a fundamental component of the structure of economies (ICMIE, 2009); the informal sector firms are a key form of organization of production

of goods and services both in rural and urban areas. The pursuit of global business has traditionally evolved from the perspective of the Multinational enterprises (MNE) which is assumed to develop rather predictably from small domestic companies into large, mature, transnational firms (Bartlett & Ghoshal, 1990) over time assuming a likewise organized sector behind the firm's global success. However, literature is less sanguine about such informal organizational forms that do not conform to the theory of the MNEs. There is a renewed interest in informal work arrangements or informal labor markets which stems from the fact that informal work arrangements have not only persisted and expanded but have also emerged in new guises and at unexpected places (WIEGO, 2009). International markets are now being viewed as networks of relationships in which firms are linked to each other in complex, invisible patterns which offer potential for building trust and commitment which are essential for internationalization (Vahlne, 2009). The informal economy has traditionally been the subject of economics and labor-related areas but is generally neglected in the management literature for small economic significance and impact and also for the lack of availability of data. There is high mobility and turnover, seasonality, lack of recognizable features for and reluctance to share information (Asian Development Bank, 2007).

The informal sector contributes significantly to production, consumption, employment and income generation, thus supporting livelihoods as well as output of developing countries and emerging markets. However our knowledge of the sector, its impact and inter-linkages with various economic and social spheres is still rudimentary (CITEE, 2009). According to World Bank estimates, informal economy accounts for 40 percent of the Gross National product (GNP) of low-income

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countries (Farrell, 2004). In India, the unorganized sector accounts for 62 percent of GDP, 50 percent of gross national savings and 40 percent of national exports (ILO Report, 2002 a). The 1999-2000 National Sample Survey organization (NSSO) survey reported that 92 percent of the Indian workforce (370 million workers) was employed in the unorganized sector; more than the total population of the United States. Now that India is an emerging economy, any macro-analysis would find it hard to ignore these figures.

Due to the increasing size and significance of the informal economy in international business (ILO Report, 2011), we conducted a qualitative case study research of the CPD (cutting and polishing of diamonds) firms in the Indian diamond industry. The present study highlights that ISFs have moved up the value chain particularly in emerging markets and created success stories in the global business arena and therefore deserve management research focus. Such informal sector firms are likely to make use of informal relationships which thrive on trust and commitment created through their business networks over several years. The invisible part (Johanson & Vahlne, 2009) may be explained by the influence of societal cultures (Parker, 2011) which support enterprise and networking amongst their entrepreneurs and in turn help ISFs in some locales to become internationally successful.

Specifically, we have two purposes. First, we attempt to highlight and explore the emergence of the informal sector firms in international business and second, we attempt to understand the nature and characteristics of these ISFs. Our interest, indeed what intrigues us, is in these new organizational forms embodied by these globally-distributed ISFs CPD (cutting and polishing of diamonds) firms of the Indian diamond industry, largely resident in the unorganized sector and composed of numerous informal sector firms (ISFs). An in-depth study of small and large ISFs in India is conducted to shed light on their role in international business today.

## 2. Literature Review

Organizational forms and types are determined by history and the purpose for which organizations were formed with the socially possible tools at the time of

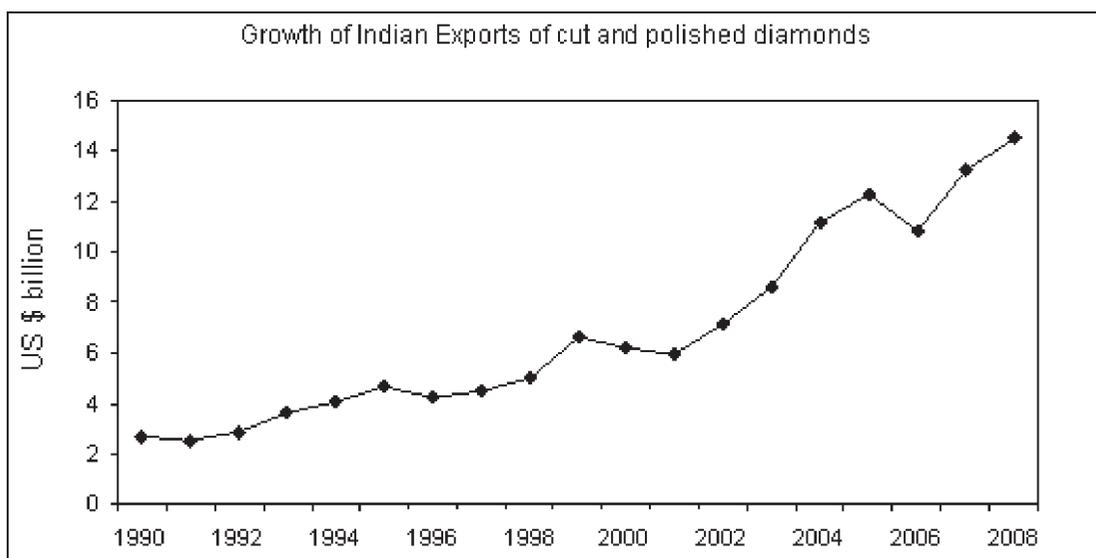
founding and if they work efficiently, such forms remain stable over a period of time (Stinchcombe, 1965) or perhaps until challenged. Thus, if an ISF grows with time in size and global reach, it is likely to retain its character of informality if it were found to work well over time and serve the purpose for which it was established. The organizational imprinting hypothesis suggests that organizations differ from one another because "they are of necessity created out of the specific technological, economic, political, and cultural resources available in the founding context" (Johnson, 2007). In this specific case of informal sector firms, we explore how scholars have tried to explain the existence and nature of the informal sector. The dualist approach (ILO Report, 1972) considered the informal sector as comprising marginal activities, distinct and unrelated to the formal sector. Sethuraman (1976) and Tokman (1978) believed that informal activities emerge due to limited opportunities in the formal sector. The structuralist school describes the informal sector as subordinated economic units (micro-firms) and workers that serve to reduce input and labor costs thereby increasing the competitiveness of large capitalist firms (Moser, 1978). Unlike the dualist model, the structuralist model views the formal and informal sectors as co-existing and inextricably connected and interdependent (Castells & Portes, 1989) and the focus is on the nature of capitalist development rather than a lack of economic growth. The legalist school posits that the informal sector is comprised of micro-entrepreneurs who choose to operate informally to avoid the costs, time and effort of formal registration (de Soto, 1989), and that they will continue to produce informally so long as government procedures are cumbersome and expensive. According to the neo-classical view (Schneider, 2000), the informal economy responds to the economic environment's demand for urban services and small scale manufacturing. It adds a dynamic and entrepreneurial spirit and can lead to more competition and higher efficiencies. The informal sector may also contribute to the creation of markets, increase financial resources, enhance entrepreneurship and transform the legal, social and economic institutions necessary for accumulation (Asea, 1996).

While existing theories throw light on why informal sector may exist in the first place, literature is scarce about how the successful firms in the informal sector organize themselves and traverse their way up the international arena. Our purpose here is to bring to light that the ISF is a different form of organizing even though it has for long been labeled as an unorganized sector and has lacked attention for study. We explore the globally successful ISFs of the Indian diamond industry dominating a lion's share in the \$ 20 billion global exports of cut and polished diamonds.

### 3. Research Design

*The Research Context.* Nearly 11 out of every 12 diamonds sold worldwide are cut and polished in India (Source: GJEPC). By way of context, for our study, raw material is called 'diamond rough', which is mined and procured from different countries around the world: Africa, Russia, Australia and Canada. This rough is imported by different countries where it is cut and polished. Table 2 shows the percentage share of polished diamonds by value for different countries. The finished product is traded mostly in Antwerp, Belgium, and exported to different parts of the world, the major consumer being the USA. Figure 1 shows the rise of the Indian diamond industry over the past two decades. (Figure 1)

The global diamond industry has had a presence in India for almost half a century and is understood to be part of the unorganized sector. While Antwerp, Belgium was the manufacturing hub of cut and polished diamonds in the 1970s; it has shifted to India which is now the world's largest center for cutting and polishing of diamonds, earns significant foreign exchange and has contributed to the country's export-led growth. It is useful to note that the Indian diamond industry is composed of a network of thousands of ISFs of different sizes employing over a million people most of them having little formal education. Further, most of these informal sector firms are concentrated in Gujarat, a western state of India, predominantly in the city of Surat, although industry associates are also in Mumbai. The data for net Indian exports is available from the GJEPC website which functions under the Ministry of Commerce, Government of India. Despite the global nature of the trade (primary consumers are global, not domestic) and the background of the workforce, networking of the ISFs has developed into an industry which enjoys a 95 percent global market share of exports by number of pieces, 82 percent share by carats and 60 percent share by value.



**Figure 1**  
**Growth of Exports of cut and polished diamonds from India**

Source: gjepcindia.org

**Table 1**  
**Countries exporting Polished Diamond (by value)**

Exporter	Percent
India	60
Israel	12
Belgium	2
Russia/ CIS	6
South Africa	5
U.S.	4
Others	11

Source : ICRA (www.icra.in)

**Sample and Data Collection.** Since precious little can be done about collecting financial and other data sets from informal sector firms, we attempt to explore the intangible aspects of organizing. Culture can be a source of competitive advantage if it is rare, valuable and non-substitutable (Barney, 1986). Although various firm practices in the informal sector may be influenced by culture unique to a firm or its subunits, industries exert influences that cause cultures to develop within defined parameters (Gordon, 1991). Therefore, we collected industry and firm level data using both primary and secondary sources for understanding the ISF of this industry. The industry export-import data were collected from Gems and Jewellery Export Promotion Council (GJEPC), India to assess the size and growth of the industry. This information gave insights about overview of the trade at the global interface, that is, about transactions at the point of exchange between India and other countries, it did not reveal how the industry operates within India nor shed light on the ISFs per say. The two authors travelled extensively over the time period of 2006-2010 across the state of Gujarat to the small, medium and large sized CPD units, mostly ISFs involved in manufacturing of diamonds and Mumbai offices used for trading of these diamonds. Some smaller ISFs were so tiny and existed in locations which did not even have an official address, nobody seemed to know the exact count of all ISFs and estimated the number to be anywhere between tens of thousands to a million, access to these small ISFs was purely via word of mouth.

In-depth interviews were conducted with diamond manufacturers, traders, exporters, workers, artisans, representatives from the related government agencies and at the Indian Diamond Institute (IDI) as well as with others who were knowledgeable of the diamond industry for triangulation. As there were limited records for the distribution of the various CPD units and their location, judgment and convenience sampling technique was adopted for the respondents interviewed. We interviewed respondents from 11 companies, 2 large sized, 3 medium sized and 6 tiny CPD units, and from the office of the GJEPC and the IDI to draw insights about the overall industry.

In order to understand how an ISF traverses its journey from a small local firm which served the purpose of an outsourcing destination to changing the rules of the game and becoming a large global player, we conducted an in-depth analysis of a large-sized successful CPD firm which has existed and grown in this informal sector for the last 40 years. Again, as there is a lack of comparative data to list the more successful firms in this industry, this firm was identified after analysis of inputs obtained from the exploratory study and of those received from responsible actors in the industry for triangulation.

#### 4. Summary of Findings

We present our summary of findings in two parts. First we describe our understanding of how the industry evolved and then we narrate how a successful ISF traversed its way within this industry to emerge successful in international business.

##### 4.1 The Industry Overview:

**A Modest Beginning.** In the 1950s, the processing of diamonds was done mainly in Antwerp in Europe. As more diamond mines were discovered, there was increase in the availability of diamond rough. Also, there were enormous price differentials in the processing of large and small sized diamonds. The diamond manufacturers of Europe were faced with the problems of handling a large chunk of rough diamonds and were willing to share the production of small sized diamonds which gave lower returns on investment (personal

discussion, 2008). At the same time, a newly born Indian democracy (India received independence from the British rule in 1947) was crippled with problems of unemployment and poverty and weak institutions. Our study revealed that a few enterprising Indians who went to Antwerp agreed to bring to India the left-overs of diamond rough for polishing. These were very small pieces of diamonds or 'grains of sand' in diamond terminology. The entrepreneurs from Gujarat in India, utilized this opportunity to develop indigenous methods of cutting and polishing of diamonds in small factories (CPD units). The finished product, the processed diamond was then exported to the globally centralized trading market which existed in Antwerp. This was outsourcing of low-valued diamond rough to an under developed country in those times.

**The Incredible Growth Years.** Between 1970-80, there was an increase in the size of the industry, and in the number of CPD units (ISFs) in India (personal discussion, 2008). The secrets of this business were shared with and restricted to the members of a local community in Gujarat. The community members were largely simple, religious and possessed very little formal education. Personal discussion also revealed that those who were interested in going to school were attracted to the diamond business and dropped out of their studies. Despite the lack of management education, management styles and organizational skills were developed. They tirelessly worked on upgrading the skills of artisans as well as on the techniques of diamond processing. As these informal sector firms (CPD units) increased in size, they moved up the value chain and some even set up their own trading offices in Antwerp in Europe. After creating a niche in the diamond arena with small diamonds, some of these ISFs developed skills and technology for cutting and polishing larger stones and fancy cuts. Improved technology and product quality helped 'in-sourcing' of higher valued raw material, the larger sized diamond rough to India. The larger ISFs eventually developed a worldwide marketing network of global suppliers and clients on their own. The entire process, by the dawn of the 21<sup>st</sup> century, led to a shift in the global production base of diamonds to a country which by now had transformed into an emerging

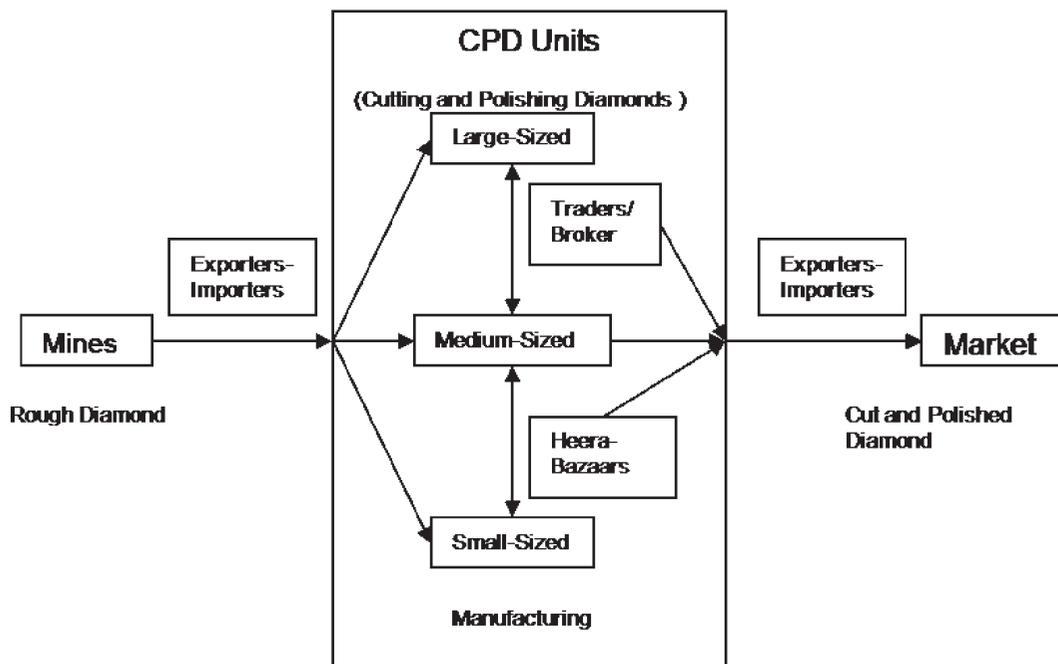
economy. The ISFs were successful in leading the remarkable growth of the CPD industry from USD 0.12 billion in 1975-76 to USD 14 billion in 2008-09 (Source: GJEPC)

**The Industry Structure.** Our visits suggest that even today, there exists a huge network of traders, manufacturers, artisans and brokers engaging perhaps more than a million people. Also, it appears to be difficult for anyone to predict the actual number of diamond manufacturing units or the actual number of people employed, as processing is done in large, medium and small units spread across the state and reaches many villages and even homes for which there are no records. We visited many of these small ISFs, many of whom were family based, with fewer than 10 family members, or extended family members engaged in CPD. The workers worked in humble conditions, some in sweat-shop conditions, nevertheless the families graciously welcomed us into their homes, many of which had no concrete flooring. In some shops, technology required heat fire and temperatures soared to high levels inside the shops as well as outside, while in others, they made use of laser technology and the CPD units were centrally air-conditioned.

As in any other industry, some ISFs performed better and have grown faster. As a result different sizes of units exist which can be categorized as small, medium and large depending on the number of diamond pieces, the size of individual diamond pieces, the quality or grade of diamonds being polished and the number of people employed. The large-sized diamond units are few in number but have risen to be centers of excellence in various aspects of management of resources, human and material, and of doing business, both within and outside the country. Some of these Indian diamond polishing factories are today, on par with the world's best and make use of laser machines, computerized yield planning machines, advanced bruiting lathes, diamond impregnated scaives, etc. and also sell upto 50 percent of their polished diamonds through internet.

**Networking of CPD Units.** Different categories of CPD units are equipped to cater to cutting and polishing of different categories of diamond rough. The large CPD

Figure 2 : Networking of CPD Units



units have subsidiaries and outsource the smaller and lower quality rough to the smaller CPD units. Discussions revealed that the imported diamond could pass through different channels before being exported (Fig 2). It is now possible for a large manufacturer to directly import, process and export diamonds. The medium sized CPD units may depend on the traders and brokers who are involved in the intermediate buying and selling. Smaller units at the lower end of the chain participate in the Heera Bazaars to collect their share of the diamond rough for polishing. These bazaars are (men only) trading markets which buy and sell all forms of small diamonds for subsequent processing. Since we were two female researchers, we had to receive permission to enter the Heera, and needless to say, we caused quite a spectacle.

**The Heera Bazaar.** Trading across various levels between importers, exporters and manufacturers is carried out through thousands of brokers operating at the same time on open streets in markets called 'Heera Bazaars'. Diamond packets worth millions of dollars continue to exchange hands without formal receipts. There are Heera Bazaars located in different parts of the state of Gujarat which cater to the nearby ISFs. The rough diamonds

as well as the polished ones are traded here. It appears impossible to track and account for the exact number of such transactions or the number of people involved in them, however, they seem to be well-connected to the industry network and are engaged optimally to produce the overall output of the industry. We could discern no real pattern of organization amidst the yelling and shouting (imagine the trading floor of the US Stock Exchange to the uninitiated). How and why two traders came together, agreed on a fair price and exchanged money had no 'handbook of instructions or directions' that we could tell, and no one would address the issue with us.

**A Unique Transaction System.** The transaction of diamonds is carried out through special mechanisms. The transportation of diamond packets, both rough and polished, is largely done through angadias. Angadias are people (couriers), members of a local community of Unja Patels ,who have specialized in carrying diamonds safely within the industry for a period of over four decades and have achieved trustworthiness of the highest order. There are often no written contracts, many transactions occur in cash, and stones worth millions of dollars are transported with virtually no

security. The angadias could also be carrying these diamond packets in their pockets and traveling in the economy class of a train. The whole industry they say, works on trust. One trader showed us what the packets looked like, and they were packets of paper folded around perhaps hundreds of small-sized diamonds, all of which fits into a shirt pocket of the angadia.

**The Industry Glue.** As described, the Indian diamond industry mainly consists of members of a particular community who are often socially/familialy-related to each other. They seem to share an industry culture with few formal systems unlike what we see in the so called organized sector. Most functioning of the industry seems to be nested in psychological contracts and trust which is reinforced through social bonding. It resembles a close-knit community that thrives in the atmosphere of secrecy and informality that envelops the diamond trade. Self-imposed rules, discipline and order is observed and the business dealings carry out smoothly with few formal policies and procedures or documentation. Whereas in the US, when people transport gems and other precious jewelry they must be bonded, and do so with heavy security, in India, there are none of the controls we observe in more advanced economies. Equally stunning, is that despite opportunity, there appears to be little to no theft or heists.

#### **4.2 The Firm Overview**

We now turn to our study of a large-sized CPD unit and include a description of its culture, innovations and practices. We believe that this selected firm has all characteristics of the informal sector firms and the industry as its rise is synonymous with the rise of the industry. Established in 1969 by two brothers with a handful of employees, the second generation of the family joining later, the annual revenues of this unit grew from approximately one million USD in 1988 to 350 million USD in 2008, the employee headcount now stands at 1500. The owners did not seem to remember any financial revenue figures for the time period before and said that it was a very humble beginning with some 20 people in their workshop forty years ago. Today, the firm enjoys the reputation of having revolutionized the domestic and international diamond cutting and

polishing industry, and of redefining the concept of a modern diamond processing unit and its innovative human resource practices.

**The Initial Growth Phase.** Initially, the office and the factory of the CPD unit were separated by a distance of 3-4 km, (the separation of white and blue collars) which resulted in a few misunderstandings and led to worker protests. The founders realized the importance of a regular interaction and communication between the workers and the managing staff. In 1982, they conceptualized a CPD unit with an office and a production facility in the same premise; the concept was later accepted by the management and other CPD units of the Indian diamond industry. Coping with an industry that was booming and manufacturers were roping in workers from other companies, they used their business acumen. Compromising on quality was not acceptable, neither were the employees penalized for doing so, instead, salaries were doubled and a unique quality/incentive-based wage system was established. They resolved to provide good working conditions and better salaries to their employees. Further, methodologies were invented to achieve quality and they were quick to adopt new technology. In less than 10 years after inception, along with routine business activities, the firm also began allocating funds to social and religious welfare activities.

**Defining the Concept of the Workplace.** Far from the sweat shop images that we portrayed earlier (and are still common to some extent in the small and medium-sized CPD units), in June 2002, the company's new US \$ 12 million state-of-the-art manufacturing facility was made operational. It is a centrally air-conditioned 8 floor factory premise of 260,000 sq. ft. area on a 6.5-acre plot in Surat, providing an excellent working environment. There are landscaped gardens, spotless buildings, product line arrangements neatly divided into separate rooms, smartly dressed security guards who welcome visitors with warmth and hospitality and hi-tech automated security systems to guard the place. We were hosted in their ultra modern guest house, where we interviewed the founders and the top three in his management team. More than a thousand workers and skilled artisans work diligently and with discipline

on their respective machines using computerized tracking systems, cutting edge laser technology and the most modern and sophisticated diamond processing equipment.

**The People Structure.** No formal organization structure exists, people are grouped into different work areas; a manufacturing unit exists at Surat and a sales and marketing office in Mumbai. About 86 percent of employees work in manufacturing, 7 percent as support staff including canteen attendants and security watchmen, about 5 percent are employed at the Mumbai sales and marketing office, and the remaining for administration, data processing and audit. It appears that overhead is minimized.

Marketing and Sales. Expenses on conventional marketing are kept to a minimum. The logic here is that if you offer transparency in the attributes of the product, it translates into customer confidence which goes on to build more customers through word of mouth. And yet, talk of buying -selling norms, there exists a law of non-negotiable price. Take it or leave it, the first offer is the final offer and is determined by a computerized system, based upon a long list of parameters which 'do not' emphasize the fluctuating prices and the profitability of the company. No lengthy credits of up to 9 months to customers at this CPD unit, the average receivables in 2008 were just 10 days. Initially, customers were angry and the sales went down, but the company adhered to its policies, refined the grading systems and ensured that the stones were exceptionally well cut. Over time, they developed a strong client base that was ready to buy their diamonds online without physical inspection of the diamond. This has cascaded into a strong global customer base that has spread across USA, Europe, Japan, Asia, the Middle East, Australia, Canada, New Zealand and South Africa to an extent that they are willing to pay a premium.

**Achieving Quality in Production.** No two diamonds are alike just as no two humans are, and achieving quality in polishing diamonds is not an easy task. The rough diamonds are sorted and valued depending on shape, quality, color and size. In this unit, some 1270 skilled artisans, assorters, graders make use of their traditional knowledge as well as the high tech laser

technology and machines to convert the rough stone into polished diamonds through a well designed manufacturing scheme. There is no QC department in the set-up, but a unique system of individual accountability and responsibility has been designed for every action/decision, which inherently ensures the best possible quality control. We were allowed to watch this process of quality control, and unlike other ISO standards, their grading system is transparent and comprehensive.

**People Management Practices.** It doesn't end with the diamonds and their manufacturing and selling, at lunch time all employees including the owner eat together in their company canteen facility with the unit's own kitchen staff serving vegetarian food free of cost. The CEO notes, "It is not free lunch, because it is only for those who work here. If the workers are happy, they perform better, if they perform better, our clients are happy, if my clients are happy, so am I." Annually, every employee has two vacations (Diwali and summer) which are three weeks long. Everyone works eight hours per day; they have pension plans, and workers self-supervise. Closed circuit cameras monitor many parts of the factory, particularly the assembly line.

Negative thinking or "acting out" has no place, according to the founder. People are encouraged to think and act positively, as well as to not shout or even raise their voice during discussions. Before vacation begins, the founder addresses all employees through the public address system, or in a town meeting, and advises them on various issues related to their personal safety and family welfare, advising them to drive carefully, and to not indulge in bad habits like tobacco. He explains to his workers that their life also belongs to their family members and therefore they should take care of it. It was common for employees to confess that their behavior at home had improved since they started working at this CPD company. In turn, the families of these workers have also developed deep regards for the founder.

Generally, the company prefers to promote from within. It recruits experienced workers who have a proven track record of honesty, diligence and dedication in their area of work. The founders believe that people

need to be made aware of the immense unused potential lying within them. In addition, they never ask a person to perform a task below the level of his/her potential. This is perhaps how they make optimal use of their human resources. Safety of the valuable diamond pieces in CPD units is important, hence fingerprints as well as palm-prints of new recruits are taken, nevertheless they still utilize the angadia system of transporting gems and cut diamonds.

In order to keep people motivated, an innovative quality/incentive-linked wage system and unique methods of resolving disputes have been devised. State of the art safety standards and welfare measures take care of the employees. Since inception, the founders have stressed effective communication and any lapse is not accepted on any employee's part irrespective of rank, job or position in the company. "People have a tendency to send selective messages, we have meticulously tried to nullify them. If any worker or artisan tries to approach me, I listen to him with utmost priority " claimed the founder.

**Major Innovations at the CPD Unit.** Surprisingly, unlike the reputation of the industry, a unique IT-driven business model is in place which seamlessly merges manufacturing, grading, pricing, sales and marketing aspects of the business. The CPD unit started computerizing in 1987. A Grading system was invented in 1996 at this CPD unit for a diamond piece which became the standard for the global diamond industry. Beyond what we normally think of as the 4 "C's"-color, cut, clarity and caratage, they have evolved a criteria of 17 grading attributes, 17 C's sets standard in the industry, and this means world-wide. 'On-line Sales' was launched in 1997, a first for any manufacturer in the global diamond industry. For a product such as a diamond, it calls for a great deal of credibility of a company to give the confidence to its buyers to purchase online without physical inspection. In 2005, the company hosted an in-house web server, providing the entire inventory on real time basis for their online buyers. Later, besides the grading details, digital images of diamonds were also made available. Sales through the website totaled about 37 percent of total sales in 2006

which, is an amazing reflection of customer trust and confidence given the nature of the product.

In 2003, the company introduced Confirmed Order Requirement (COR), a revolutionary system of buying diamonds on specification without personal inspection. Apart from boosting consumer confidence in the business integrity of the company, the system alone contributed to 12.31 percent of sales in less than six months. Sales crossed the US \$150 million mark in the year 2003. Exports crossed US \$100 million in 2002 on year-to-date basis. Sales grew from US\$ 67.09 million to US\$ 174.80 million in a period of 3 years between 2001 and 2004.

**Social Responsibility.** The importance of CSR as we know today was practiced by these Indian entrepreneurs for the last three decades. Besides developing industry best practices as mentioned above, they contributed to other aspects of diamond trade and industry like suggesting government policy decisions. This CPD unit has made numerous and significant contributions towards religious, social, educational and disaster management needs of society.

## 5. Discussion

"Firms did not exist at the dawn of economic history" (Weber, 1929) and all economic action then, was apparently informal in nature. As industry and capitalist structures got more organized, formalization came into effect with smaller firms first, which later grew into larger domestic firms and thereafter into multinational companies. The growth of the firms and their trajectory of transition from domestic to international is well documented and explained by scholars (Penrose, 1957; Hymer, 1960; Dunning, 1982; Rugman, 1973; Ghoshal, 1983; Mcdougall, 1990 ). However, most frameworks assume formal sector firms and formal transactions, and more often than not, begin by dissecting the large multinational firm from the perspective of the developed countries. We now present our understanding drawn from the industry and firm level exploratory field study conducted in the informal sector firms.

There is evidence from this study that informal sector firms are not just local firms but can also have global reach. The analysis of the findings from the exploratory

study of the Indian diamond industry and that of the case study of a large CPD unit leads to useful insights. The Informal Sector Firms which have made it big on the global front have flourished like a close-knit community with entrepreneurs like the one we have described above leading at the forefront. As the volume of business increased, they passed on the business to others connected to the same community. Despite little formal education, professionalism exists where verbal commitments are honored and met, and a high order of integrity is exhibited, and it is all a part of their societal culture. Culture is a shared pattern of values, beliefs and assumptions (Schien, 1996). The networking of ISFs as observed in the diamond industry ISFs, works on a culture of trust and mutual respect. The people involved take pride in their work and in what they have achieved. A sense of belonging to the community is a big motivating factor and people try their best to be known and respected by adhering to the norms as established by their culture. A display of simplicity, sincerity to work, diligence and discipline was observed down the line from the large to medium and small sized CPD units.

It appeared that the smaller units were not underpinned by the larger ones, and were happy to be operating from their native places, the location of their respective villages where they shared their life with the members of the family and kith and kin. However, the mention of the big company names did evoke a sense of respect and motivation to grow. It was observed that in the broader context of the Indian diamond industry, there is lack of formal systems like documentation of the diamond packets exchanged and of the financial transactions or that of the recording of employee details or number of units etc. However, it appears this made them feel proud of their ability to conduct a business of a huge global dimension based on mutual trust within their community. Not delivering on the verbal commitments or any symptoms of dishonesty and they would be dispelled from the community. The community or clan feeling appeared so strong that the mere thought of being ousted from the group and from the diamond business engaging the community motivated them to behave as per norms.

Also, it was uniform across the sizes of the CPD units that the unit owners were sensitive to the family concerns of their employees which in turn helped employees to be loyal and devoted to their work. Another interesting observation at least in the smaller units, was that after the workers and the artisans learned the art of cutting and polishing a diamond, they were likely to start their own CPD unit and employ others known to them through personal references. A culture of individual responsibility which goes in line with entrepreneurial spirit as is demonstrated by these ISFs, drives them to start their own units. The ISFs would like to have their cultures more attuned to their societal cultures which they are passionate about. If the ISF is non-compliant it means it cannot expect any help from the institutions and the informal sector by default makes the entrepreneur responsible.

It is not that some societies are completely impervious to commercial incentives or international influences such as trade, investment, technology. It is just that some cultures accept these ideas more readily than others, and that different cultures often promote commerce and enterprise differently (Samuelson, 2001). Close personal relations and family ties there helped foster economic development, created the very same security and trust needed for trade relationships that law and judiciary had fostered in the West. In the postwar era, the reliance on family-dominated firms meant that many Asian nations did not have to wait until they had a well-developed commercial legal system before growth could accelerate (Samuelson, 2001).

An enterprising spirit was omnipresent and everyone understood the importance of what they were doing irrespective of the place they were operating in on the value chain. The huge network of these thousands of ISFs was held together by a common goal of doing and improving the business of diamond cutting and polishing and they understood exactly the informal systems in place. Most large sized unit owners mentioned that they had a dream of making Surat the world's largest diamond cutting and polishing center, which they achieved and it gives them a sense of fulfillment. And they contributed to the society by getting involved in social, religious and other pro-social human endeavors.

Due to lack of formal systems, we suggest that an ISF's behavior is largely influenced by the dominant values and beliefs which result as an interaction of societal culture, industry culture as well as values and beliefs held by the founders of the firms and of those with influence within the ISF. The firm's behavior is guided by the complex interactions of these three different cultures and is therefore more flexible and adaptive to dynamic external circumstances. The culturally-sensitive and culturally-strengthened ISF is perhaps what explains the resilience of such firms during the recent global crisis. Economies which are dominated by the informal sectors as in emerging economies have also exhibited the first signs of revival as demonstrated in the case of the diamond industry.

Earlier, ISFs served as outsourcing and off-shoring units of production of goods and services, but have gradually moved up the value chain and networked with both formal and informal sector firms in different countries thus giving rise to an informal industry culture as evidenced in the global diamond industry. This industry culture is influenced by societal cultures in places where ISFs are geographically concentrated. In globally distributed industries and supply chains, different cultures merge to give rise to specific industry cultures which then influence cross-border behavior of firms.

Most existing approaches to ISFs make an implicit economic assumption that human nature is universal: confronted with the same incentives, people everywhere will respond similarly. However, human behavior is shaped by history, geography, religion, climate and tradition related influences that create culture and hence is not uniform (Samuelson, 2001). People across the globe have different values, beliefs and customs; they behave differently and create societies with different legal and political systems (de soto, 1989). Some societies may be more culturally-friendly to economic growth than others and these forces may also affect enterprise, invention and material accumulation (de Soto, 2001). This may explain why ISFs in some regions perform better globally than others. Even within countries, different regions and different groups have different experiences.

## 6. Conclusion

Although we have chosen one large CPD as our focal case, the authors visited dozens of small and medium sized ISFs and interviewed hundreds of respondents associated with the diamond cutting and polishing industry during the data collection phase. We think it fair to say that the informal economy thrives on an enterprise culture which cultivates entrepreneurship and facilitates its growth while contributing significantly to the economy. Informal sector firms are growing large and that more such firms can emerge from anywhere across the world in any industry because they have certain advantages of both local and global knowledge. As the world's borders become more porous and open to international trade and development, there is space for both the formal and informal sector firms to become global players. However, the societal cultures like the one we see in the Indian diamond industry is likely to play a significant role in internationalization of the ISFs. The countries with more of such ISFs will draw higher FDI as they provide for the structural support to the firms which have moved up from the lower band to the upper band as well as a cost structure to the industries of which they are a part. While many in the corporate business and the world economy in general continue to struggle with the aftermath of the recession, the ISFs we studied have shown sufficient resilience to bounce back. A possible outcome of this study is that industries and firms of the informal sector possess close knit community culture which helps them to survive the difficult times.

*The Significance of ISFs to IB.* The study of the informal sector firms in the diamond industry provide useful insights. First, the ISFs organize as networks in specific industries and the firms benefit from competition, complementarities and common resources of the clusters, providing efficient production systems and processes. Second, these ISFs are embedded in networked communities with shared cultures which provide for solidarity and mutual trust, providing employment and entrepreneurship opportunities and livelihood to community members. Third, the ISFs provide for parts of the global value chains in sourcing of raw materials, processing, and in distribution networks. Fourth, the

ISFs which traditionally catered to the industry and to larger firms to provide for outsourcing of certain parts and processes but with advent of ICT, have moved up the global value chains and established contacts with end consumers and suppliers alike. Fifth, the ISFs work with minimum overheads and transactional costs which are characteristic of their organizational form, possess flexible specialization skills and agglomerate to export products and services.

Thus, governments are incentivized to support the networks of ISFs and even create special export zones and benefits for them. The trade is documented at the country borders but not so much monitored at the firm level in the case of ISFs; the collective benefits for society, government and global value chains make way for institutions to allow the ISF clusters to organize and monitor themselves. However, given the growing significance of ISFs, it is important for both managers of formal sector firms as well as policy makers to gain further insights into the organizational forms of firms of the informal sector.

## 7. Directions for Future Research

This preliminary study on the multifaceted diamond industry opens significant new directions for future research. The ISFs, so called due to the absence of traditional corporate structures, strategies and statistics, remain under-researched and empirically undocumented. That these unorganized, globally-dispersed companies appear to gel or 'fit' into a more 'organized' framework later in the value creation chain challenges our current thinking on organizing and managing for competitive advantage. Neither theorists nor empiricists have studied these unorganized organizational forms, nor charted any so-called best practices despite this dominant global market share. Hence, this is a first such attempt to study these new organizational forms, as represented by the ISFs of the Indian diamond industry in India. We believe this study will have significant implications for theory as it explores new forms of organizing as displayed by the ISFs of the Indian diamond industry. There exists a large scope to learn from their innovative operations and value systems.

It is evident that some unique leadership styles, management skills and culture exist within the ISFs as in the Indian diamond industry and its contribution to the growth of economy as well as to the study of organizations cannot be ignored. Study of the unique people management practices is likely to add to the body of literature on human resource management. It is therefore suggested that more empirical research be conducted to unearth the unexplored dimensions. Clearly there are implications for practice for SMEs in all developing countries. Given the cultural and social diversity, the informal sector is also differentiated and heterogeneous; nevertheless, a first step in analyzing globally distributed work here is to recognize it as an existing and potentially powerful driver of the economy.

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