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The first issue of *Labor Issues in the 1990s* represents another step forward in the activities which the American Institute for Free Labor Development is undertaking today. The changes in the political situation in the international area with the defeat of communist and totalitarian regimes, the realization that regional and worldwide economic integration is a process that is gaining increasing impetus and the impact that those changes are having on workers' standards and rights, led us to reorient our programs and activities for the immediate future. Recently we held our Country Program Directors' Conference at Piney Point, Maryland, where we reached a consensus on a new approach which our organization is taking in view of those new elements, which are indeed affecting trade union activities in our hemisphere.

Our curriculum for AIFLD's Labor Education Program at the George Meany Center, will reflect our new dimensions in an effort to provide our brothers and sisters from Latin America and the Caribbean the tools they will need to face the challenges of a changing world. Naturally, we need to provide information and studies which can be used during our programs, as well as source materials for open and democratic discussions, which are the best ways to better represent the interests of workers and their families. The principles which are guiding us are those established by our parent organization, the AFL-CIO, in a coordinated effort with the international democratic trade union movement represented by the International Confederation of Free Trade Unions and its regional organization, the ORIT.

William C. Doherty, Jr.
Executive Director
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INTRODUCTION

Our Department of Education is publishing its first series on "LABOR ISSUES IN THE 1990s" as part of its continuing efforts in bringing to our graduates at the George Meany Center for Labor Studies Program, our colleagues and experts in the field, the problems which trade unions and workers are facing both in the developed and in the developing world. Our first step was the publication of The Bulletin and now it is followed by this collection of articles and documents related to the new set of problems that characterized the new economic and political world, which is emerging out of the end of the cold war and the globalization of the economy.

These articles reflect the ideas and opinions of their writers, while the documents do represent the position adopted by the sponsoring organization as policy statements. The purpose of putting together a publication of this kind is to provide information, material for analysis and different point of views which can provide a fertile ground for discussion in our educational programs as well as tools for a better understanding of the issues involved.

The publication is divided in five sections covering economics, politics development, labor relations, documents and book reviews. In the first place, we include the entire final document adopted by the International Confederation of Free Trade Unions (ICFTU) and the Organizacion Inter-Americana de Trabajadores (ORIT) during the conference held in San Jose, Costa Rica from October 31 to November 1, 1991. Trade union representatives from 22 countries of North, Central and South America and the Caribbean, joined the representatives of European unions and international trade secretariats to discuss the issues of INTEGRATION, DEVELOPMENT AND DEMOCRACY. The AFL-CIO sent a top level delegation led by Secretary-Treasurer Thomas R. Donahue, Mark Anderson, Assistant Director of the AFL-CIO's...
Research Department and our Executive Director, William C. Doherty, Jr. Working together with the trade union brothers and sisters of the hemisphere they adopted a transcendental resolution on how labor can contribute to the development of a new economic and political order in which democracy and participation with justice and equity become the major goal of the economic policy.

In the first section we include a paper written by Professor Jorge A. Daly on PERU PROFILE where he brings up to date information on the situation of the Peruvian economy which is undergoing major adjustments through new economic policies with far-reaching implications for the bewildered South American nation. Dr. Daly is a professor in Economics at George Washington University and a consultant for the AIFLD.

In the third article, included in the World Bank Observer magazine (January 1991) Joan M. Nelson analyzes the role of ORGANIZED LABOR, POLITICS AND LABOR MARKET FLEXIBILITY IN DEVELOPING COUNTRIES, stressing the fact that the conditions needed to gain workers cooperation in adjustment programs "are analogous to those which encourage business to invest; political stability, a voice in policy that affects their interests, and, arising from these, the confidence that current sacrifices will ultimately yield a fair share of future benefits. Ms. Nelson is a Senior Associate in the Overseas Development Council.

In the second section two articles are included dealing with political problems. One is written by Dr. William a. Douglas, professor at Georgetown University and an AIFLD consultant. Dr. Douglas's article discussed THE ROLE OF TRADE UNIONS IN MODERNIZING POLITICAL PARTIES as a tool to enhance the cause of labor as a major component of a democratic process in Latin America. The other paper is written by Dr. John D. Sullivan, President of the Center for International Private Enterprise which was presented to
the Central and Eastern European Institutes meeting held in Poland last May. Dr. Sullivan discuss the **POLITICAL IMPLICATION OF ECONOMIC TRANSITION**, stressing the importance of considering the participation of unions, business associations, civil groups and other society organizations in building the infrastructure of democracy.

In the area of development I present the first part of a paper on **TRADE UNIONS AND DEVELOPMENT**, focusing the attention in the participation process of unions, management and governments in planning as an integrated force. Particularly important is the presentation on the type of union policies in the area of finance and then absorption of innovation to create new sources of wealth and to develop a safety net to diminish the hardship of economic and social change.

In the section on Labor Relations there are three important papers which discuss specific issues and general cases. Dr. Norman Eiger, professor of Labor Studies at the Institute of Management and Labor Relations at Rutgers University explains **THE CHANGING NATURE OF THE SWEDISH MODEL OF LABOR RELATIONS** which has some unique characteristic and how it is adapting to the new environment with the forthcoming changes in the European Community and the future membership of Sweden in that economic and political block. Professor Stephen R. Sleigh, Deputy Director of the Center for Labor Management Policy Studies of the City University of New York present a concise article on **UNDERSTANDING TECHNOLOGICAL CHANGE** and how important it is to view it as a step forward in the developing process rather than an obstacle or threat to the living standards of workers and their families. The third article is a case study on **EMPLOYEE OWNERSHIP AND GOVERNANCE IN THE SHIPBUILDING AND MARITIME INDUSTRY**. This article was first published in the "Workplace Topics", a publication of the AFL-CIO's Department of
Economic Research. Leonard G. Beauchamps, Director of Research and Collective Bargaining Services of the International Union of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers and Helpers explains how an ESOP scheme was developed to save jobs in a company which went into bankruptcy.

As for the last section, we reproduce the major provisions on employee involvement in labor-management cooperative relations included in the contract signed between Nabisco Brands Company and the Bakery, Confectionery and Tobacco Workers Union. Those provisions promotes cooperation and involvement for the mutual benefit of the company and its organized employees. The book review is on The Other Path, an important book published by Hernando de Soto on the informal sector on the Peruvian economy. The informal sector is becoming a major force in the economic activity of developing nations. Our Executive Director William C. Doherty, Jr., and Dr. William A. Douglas analyzes the book in the context of the relationships with organized labor and how they should combine their efforts to upgrade not lower their living standards.

Ruben Rotondaro
Director of Education
AIFLD
I -- ECONOMICS
INTRODUCTION

1. Meeting in San Jose, Costa Rica, from 31 October-2 November 1991, trade union representatives from 22 countries of North, Central and South America and the Caribbean, joined by representatives of European unions and international trade secretariats, debated the themes of integration, development and democracy. The Conference set up five workshops to discuss the major challenges facing the trade union movement of the region. The conclusions concerning analysis, policy recommendations and trade union action are summarized below.

I. Impact of the Economic Crisis

2. The Americas are characterized by some important problems common to almost all countries. Foremost among these has been the adoption of conservative policies, with their origin in Reaganite and Thatcherite policies now being applied in one form or another throughout the region. Their predominant characteristics are: the promotion of the private sector above the public sector, regardless of any assessment of their respective merits; stringency in public sector expenditure, leading to serious cuts in real levels of social security benefits. retrenchment of many public sector employees and a diminution in the provision and the quality
of services such as education and health (particularly affecting women who often depended on such services) tax reforms leading to a disproportionate shift in tax contributions away from the rich to the poorer sections of society, unemployment and declining incomes; a reorientation from the real to the financial economy; encouragement of big business and multinational corporations; and reforms in labour legislation with the intention of weakening the position of trade unions. Countries where consultative mechanisms exist have in general either ignored them or sought to manipulate them to support the governmental position. Increased poverty and marginalization, the spread of the informal sector and increased social inequality are among the results, affecting all countries on the continent.

3. The indebted non-industrialized countries have faced the additional burden of having to devote a large part of their output to the payment of the service on their external debt. This situation has forced these countries to cut back on investments which are essential for development and has accelerated the adoption of the conservative policies described above, leaving them with few options other than to adopt wholesale such policies as selling off large parts of the public sector to raise revenue and other means of cutting costs. A lack of alternative sources of investment has further encouraged the design of policies to attract foreign investment whatever the conditions, which all too often has included measures such as the weakening of labour legislation in order to provide lower real wages. The adoption of these policies has in many cases been actively promoted by the international financial institutions, which despite some moves towards a more socially responsible approach remain overwhelmingly oriented towards a free-market model of development.
II. Economic Integration

4. Integration at all levels (sub-regional, regional and continental) must be conceived as a process which brings together a wide range of national policies in different areas. Thus integration must include effective inter-regional democratic institutions which involve all sectors of society; it must be based on common agreement of human rights, including trade union rights, and so much contain basic standards in areas of labour and social policy; it must directly address norms in areas such as environmental policy; and it must include strong funds to build integration on the basis of increased investment to raise output and employment in regions which are poorer or which do not benefit from integration. Integration on this basis has the potential to create strong economic and social forces which will result in a genuine prospect of higher living standards for all persons involved, particularly when it takes place between countries at an equivalent level of development.

5. Processes of economic integration have already been underway for a long time on the continent, although these have generally not been taking place in the framework of any formal arrangement. Present moves to set up integration agreements are taking place in the context of the predominance of conservative policies and so have taken a very different form to that described above. Some countries are being forced into integration due to the pressure of their grave economic situation, resulting in agreements which are detrimental to the interest of the majority of their people. In some areas multinational corporation are the main force pressing for integration, with the objective of attaining easier access to markets or taking advantage of a cheaper labour supply. The character of integration agreements has therefore been oriented
to meeting the interests of capital, resulting in an emphasis on establishing a free market to the exclusion of other considerations. Social elements have been left out and here has been no provision for tripartite consultation in the design or implementation of agreements. The US-Canada Free Trade Agreement provides an example of such arrangements as described above.

6. However, the negotiation of economic integration agreements is a reality and trade unions must catch up the lost ground and establish their own agenda for integration. This needs to be conceived in the framework of a long-term strategy to build an alternative approach which would meet the interests of the workers. Central to this is an interventionist governmental role in economic policy, which accepts responsibility for moving towards full employment, eliminating poverty and achieving higher economic growth that brings benefits for all members of society, through an "integrated mixed economy." Trade must meet all the needs of national economic development strategies and should not be random, destabilizing element.

7. The successful implementation of integration depends upon the full involvement of trade unions. It must be based on a "triple democracy" -- political, economic and social which allows trade unions to establish agreements and alliances with the principal sectors of society. Integration agreements and trade agreements will fail to establish a basis for popular support in the long run if they do not contain provisions addressing social, labour and environmental standards and do not include a full role for trade unions, thereby joining the many ambitious integration agreements which have broken down in the past because they were conceived merely to meet the interests of private companies. Trade unions need to build alliances with other social
forces in the integration process. Trade unions from countries involved in integration must establish close international links in order to coordinate their actions and policy demands.

8. Integration agreements must contain social and labour standards through a Social Charter of the fundamental rights of workers. Therefore harmonization is needed of a basic level of labour legislation on the basis of ILO Conventions, including recognition of workers’ rights to strike and to union organization, employment security, social benefits, and collective negotiation. Thereby higher wages and better working conditions, including the advancement of equality for women and for minority groups, can be secured. In the absence of such agreements, the danger is too great that integration will merely result in a loss of jobs in areas where social standards and wages are highest, while increasing the exploitation of workers by multinational corporations in countries where they are unable to call effectively on trade unions to support their interests. Similarly, common environmental standards must be established and enforced to ensure that the practice and the transfer of unsafe environmental practices does not take place.

9. Integration will be more successful to the extent that it takes place in the framework of national socio-economic development strategies, which must be complementary and mutually reinforcing with the integration project. This would ensure the highest generation of employment and production in all areas, including those which are losing out from integration. In this context, measures are needed to establish higher growth worldwide, including above all an end to the debt crisis through reduction and rescheduling of payments. In addition integration
agreements require an interventionist policy to compensate the losers. Agreements should allow the countries to maintain their subsidies to key sectors. At national and international level, funds must be created to stimulate retraining, investment in depressed regions, assistance to disadvantaged regions and groups of the population (the long-term unemployed, women, young people), and so forth. Only thus will it be possible to ensure that integration brings benefits to all members of the agreement and that a basis of popular support for integration is maintained.

10. Integration must recognize the need to safeguard national economic sovereignty in a global economy dominated by transnational corporations (TNCs) and should allow for the management of trade where needed to promote key development issues when these come into conflict with the interests of TNCs. Foreign direct investment, including through the purchase of shares leading to some measure of control of domestic firms, should be carefully scrutinized and must be compatible with national and regional development plans. Multinational corporations must further comply with the basic standards set out in the ILO Tripartite Declaration of Principles on Multinational Enterprises and Social Policy, and in the draft UN Code of Conduct on Transnational Corporations.

11. In the context of the new processes of integration in the region, the government of the United States has announced the so-called initiative for the Americas. The initiative will need a thorough analysis on the part of trade union organizations in U.S. and in the countries of the region which adopt it. However it is cause for concern that the proposal of the North American administration has not been the subject of consultation either with trade union
organizations or other social and political actors. Given the strongly conservative ideological context and the exclusion of trade unions, the initiative could constitute a significant step backwards for social policy and trade unions in the countries of Latin America and the Caribbean, affecting the productive base and worsening the level of unemployment and working conditions.

III. Privatization

12. Privatization policies as presently implemented are too often devoid of any proper evaluation of the proper roles of public and private sector. However, historical experience demonstrates that the most successful economies have been those where public and private sector take complementary roles. Discussion of the public sector must take into account its unique functions. Many services provided by the public sector fulfill roles which the private sector is not motivated to provide, such as assistance to poor groups or distant regions, investments with long-term profitability in areas like transport, or basic services like education and health. Moreover, privatization may entail the loss of domestic control of strategic sectors at the same time as reducing the space for national capital and strengthening the position of transnationals.

13. Efficiency and higher productivity are undeniably worthwhile goals in themselves, and evidently no one would support the unlimited and large scale subsidization of patently inviable public enterprises. There should be an open process of public discussion of the best uses of public resources. However, rather than privatize governments should first examine the options for attaining these objectives in the public sector. The private sector has no monopoly
of efficiency; indeed, where privatization leads to the creation of monopolies and oligopolies, higher prices and increased company profits may be the main result. Social insurance systems have come under particular pressure for privatization in some countries, but constitute a sector which for all the above reasons it is particularly important to maintain in the public sector, while improving the management and without denying the need for efficient restructuring which takes into account social considerations, including through increased trade union participation in decision-taking.

14. Where privatization takes place, provisions should be made to facilitate a process of worker control or part-ownership or individually, including through their trade unions. Controls are needed on the actions of new private sector employers, to prevent exploitation of workers or actions against the interests of consumers. Furthermore, countries must maintain the right of review of purchase of domestic companies by multinational corporations. Resources obtained from privatization should be used for strategic, productive or social goals, including income assistance and retraining of workers made redundant as its result, and should not merely go to financing debt service payments, representing a permanent loss of national resources.

IV. **Trade Union Actions**

15. Trade unions structures require strengthening to deal with these new challenges. Unions need to organize important groups of workers who are generally not unionized, including women, informal sector workers, migrant workers, peasants, cooperative workers, young people and minority groups, and promote their concerns in the processes of integration.
Unions need to improve their abilities to deal with the issues raised by integration through increased training of union officers. Unions need to maintain pressure for legislative reform in those countries where the prevailing labour legislation remains that established by dictatorships, creating a system of industrial relations biased against trade unions. Trade union unity must be sought at national, subregional and continental levels. Trans-frontier trade union cooperation is needed to counter violations of workers' rights in free trade zones and maquiladoras. The safeguard of union rights also depends crucially on actions at continental and global levels. All form of international economic pressure, including trade sanctions, should be used against countries which fail to respect labour rights, and integration agreements should include provisions for trade boycotts in such cases.

16. Trade union participation in sub-regional and regional institutions should be promoted by establishing mechanism for dialogue and social coordination at the national level. Other regions should set up institutions along the lines of the Andean Labour Council. The member countries of the Mercosur agreements should agree to create the proposed tripartite Commission No. 11 to discuss labour and social issues for the sub-region. Genuine trade union representatives should take part in the meetings of the Central American Parliament. At the international level the Additional Protocol to the American Convention on Human Rights in the Area of Economic, Social and Cultural Rights (the San Salvador Protocol) adopted in 1988 by the Organization of American States (OAS) must be ratified by all OAS members. This would form part of a reinvigorated campaign by unions of the region for the ratification and full application of ILO conventions. It is equally vital for the protection of the rights of workers in the Americas that
agreement be reached on the incorporation of a social clause to protect workers’ rights in the GATT.

V. Considerations from the Trade Union Experience of European Integration

17. Integration in the European Community (EC) has always included an important social and consultative component. From its very inception, a tripartite consultative committee has existed with the obligation to submit opinions on draft EC legislation, which has very often had a major effect on the form of the final legislation. Furthermore, structural funds to encourage development in poorer regions of the EC, financed by its more developed countries, have been successful in establishing greater equality between different countries. The Social Charter of the EC adopted in 1989 covers basic rights in the areas of freedom of association and collective bargaining; social protection; improvement of living and working conditions; occupational safety and health; information, consultation and participation; employment and remuneration; equal treatment from men and women; freedom of movement; vocational training; and the protection of children, young workers, the elderly and the disabled. It is not designed to be translated directly into national law but serves as a basis for the elaboration of EC legislation in these areas. Its existence is the result of sustained trade union pressure, and continued union pressure coordinated between different EC countries is essential to ensure its maximum value for the trade union movement. The guarantee of information and consultation rights in multinational companies stands to be one of its most important consequences.
18. The European experience indicates the importance of incorporating social considerations into the economic integration process through redistributive, consultative and legislative means as a fundamental precondition for its success. Full attainment of the goals of the trade union movement for integration in the Americas may be some way off, increasing the urgency for trade unions to take effective actions that work towards these goals. Unions must insist upon the reactivation and strengthening of the tripartite procedures of the Organization of American States (OAS). The OAS should be called upon to adopt and promote the implementation of a Social Charter for the Americas. ORIT/ICFTU should enter into discussions with the ILO concerning an enhanced ILO role in the promotion of social considerations in regional discussions, including through the next ILO Regional Conference for the Americas. International trade secretariats (ITS) should incorporate considerations of integration into their respective activities. Regional trade union coordinating structures should pressurize their inter-governmental authorities, and such regional union bodies within the framework of ORIT/ICFTU should be set up where they do not yet exist. ORIT/ICFTU should maintain and intensify its efforts to promote and coordinate trade union actions by affiliated and friendly union organizations in order to guarantee the participation of workers in integration processes, and a working group of ORIT/ICFTU should be set up to this end.

FINAL CONCLUSIONS

19. Conservative policies, privatization, cuts in public spending and reforms in labour legislation to weaken trade unions are expanding throughout the Americas. In addition, the indebted non-industrialized countries face the additional burden of having to devote a large part
of their output to the payment of the service on their external debt.

20. Economic, social and political integration of countries in the Americas, constructed with labour participation and adequate protection of human rights including trade union rights, contains enormous potential to create a strong economic force which can raise living standards for people throughout the region. However, integration on the basis of conservative policies could destroy the capacity of countries to develop their economies to meet the interests of their people. Integration will only succeed on the basis of consensus in a wide range of areas including: human rights, requiring basic standards in labour and social policy; full tripartite consultation; and strong funds to transfer resources from areas which benefit from integration towards less developed regions. Very few of these elements have been present in the integration accords concluded or presently under negotiation in the Americas.

21. Integration or trade agreements, of whatever form, will in the long run fail to establish a basis for popular support if they do not contain a full role for trade unions. The trade unions of the region conclude, therefore, that any agreements which do not take these elements into account cannot be supported. The European experience indicates the pressing need to incorporate redistributive, consultative and legislative means of addressing social concerns into the integration process. This requires above all the incorporation of a social charter of the Americas of the fundamental rights of workers into any integration agreement to provide a base for improving working and living standards.
22. The greater the growth and employment on a worldwide level, the greater the chances for success in the process of integration, including foremost an end to the debt crisis. Beyond the debt crisis, future loans should be based on the respect of human rights, including trade union rights and genuine democracy. In addition, governments must accept their responsibility to run active economic policies with the objective of attaining full employment, eliminating poverty and achieving higher economic growth that brings benefits for all members of society, through an "integrated mixed economy." Privatization in particular needs to be reassessed. Policies in this regard must aim at increased efficiency and higher productivity in full cognizance of social purposes and strategic functions of the public sector, leading in many cases to a decision not to privatize.

23. Attainment of the above objectives will require increased trade union coordination at international level to further the interests of all workers whether in the formal or the informal sector, through the following actions:

- pressure by regional trade union coordinating structures on their respective intergovernmental authorities, including to elaborate social charters of workers' rights;

- pressure on the Organization of American States (OAS) to ensure that it serves the needs of workers, through reactivation of its tripartite procedures and committees, the implementation of the Additional Protocol to the American Convention of Human Rights in the Area of Economic, Social and Cultural Rights, adopted in 1988 (the San Salvador Protocol), and the elaboration of a Social Charter for the Americas at continental level;

- pressure on the ILO to intensify its actions to promote the respect of human rights, including trade union rights, as well as conditions of the working environment, in processes of integration:
incorporation by ITS of considerations of integration into their activities;

- actions by ORIT/ICFTU: to undertake studies of the effects of integration, organize further trade union meetings to discuss strategy and plan actions to affect the integration process, and intervene at the highest level of the continental institutions to achieve acceptance of the importance of trade union concerns and a social charter. Such actions should be supported by a working group which undertakes technical studies for the formulation of an agenda for a Social Charter and the attainment of other elements on the social agenda;

- continued action by the ICFTU at global level to introduce a social clause into international trade agreements like the GATT, and to achieve a lasting resolution of the debt crisis;

- transfrontier, continental and international trade union actions to counter violations of union rights, including in free trade zones and maquiladoras.

24. These proposed union structures and social charters should be promoted as part of the global strategy of the labor movement, even if integration does not take place.

25. ORIT/ICFTU will maintain and intensify its efforts to further the interests of the workers of the region, including both affiliated and friendly organizations, in ensuring a proper follow-up to the Conference such that the policies of these conclusions are promoted effectively on a continental basis.

26. The main conclusions will be published together with the reports of the working groups of the Conference and will become guidelines for the trade union policies of the ICFTU/ORIT.
PERU PROFILE

by Jorge L. Daly, Ph.D.

This Andean country has not been immune to the sea of economic change that has swept the world in recent years. Not unlike those South American countries traditionally most recalcitrant to welcome the challenge of unhindered foreign trade and investment -- Argentina and Bolivia come to mind -- Peru is also going global.

In the last fifteen months, since President Fujimori took office, sweeping economic reforms have been enacted, marking a sharp departure with the economic policies that sustained the ill-fated state capitalist regime that ruled the country since 1968. To wit:

1. All state company monopolies have been abolished.
2. Tax exemptions of any kind, whether national or regional, have also been eliminated.
3. Stevedoring in ports has been opened up to competition for private companies and shipping rules have been liberalized.
4. An ambitious privatization program has been launched, which seeks the divestiture of 200 companies, out of the 240 state-owned concerns.
5. Land reform has now been reversed. In stipulating that private enterprise can own land, the new regime does away with the principle that "land belongs to those who work it". Furthermore, a market for land is implicitly established, since land can now be mortgaged as a guarantee for private banks which offer credit to farmers.
6. The tariff system has been radically changed. In lieu of the high rates of protection that local producers enjoyed, a three-tier system has been introduced, the highest tier being just 25%.

These and other measures point to an old out embraced by the government of a capitalist road to development. The fact that the government of Mr. Fujimori has chosen laissez-faire type economic reforms sends an unmistakable signal that the economic authorities are committed to
resisting pressures to reactivate the economy through Keynesian policies. In the most recent past heavy government intervention was aimed at designing, implementing, and monitoring the ill-fated egalitarian reforms that were introduced in 1968. President Fujimori’s measures pave the way for the dismantling of those policies.

**Current Political Developments**

In mid-September, President Alberto Fujimori paid a state visit to Washington to confer with President Bush. The visit served to underline the new, close relationship that has emerged between the two countries. In exchange for acquiescing in Washington’s policy on drug trade, Peru is expected to obtain badly needed economic aid and cooperation.

The Washington visit was preceded by a flurry of important events. First, the International Monetary Fund decided to approve the accumulation of "rights" for Peru for up to a maximum of $845 million. Peru cannot draw from IMF’s resources without eliciting the approval and monitoring of the economic program currently under way and without clearing the arrears with this institution. These two conditions cannot be met before the end of 1992. Yet, the IMF’s decision is not devoid of importance since it ends the status of ineligibility to obtain loans that was in effect since October 1985. Second, the government, after intense negotiations, rescheduled the $6.6 billion debt with the Paris Club under conditions that most experts consider favorable for Peru. This sum represents 96% of the total indebtedness with the Paris Club, and has been rescheduled over a period of twenty years. However, the terms that were agreed upon fall well short of the original intention of the government to obtain a debt-reduction deal similar to Poland’s. Finally, in Washington, Peru signed a $425 million loan with the Inter-American
Development Bank.

President Fujimori is also seeking more economic aid from European countries and Japan. As of now, Peru had secured the commitments for financial aid for $1,190 million from the following countries:

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<th>Country</th>
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<td>Switzerland</td>
<td>107</td>
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$1,190

The disbursement of these funds has taken much longer than expected. Some European countries and Japan have been insisting that the conditions for Peru’s servicing of the recently rescheduled Paris Club debt be stipulated and signed prior to any disbursement of the monies. Therefore, some additional delays are likely. Peru has earmarked these funds to comply with servicing the debt to multilateral banks that is due in 1992 and, if possible, to use part of the funds to finance an emergency social program (Programa de Emergencia Social). It should be noted that, contrary to early promises of the government, absolutely nothing has been achieved in this program. The economic stabilization program, for all practical purposes, has been effected without any provision aimed at cushioning the brutal drop of incomes and employment losses that have been incurred since August 1990.
Unfortunately, Peru is plagued by serious problems. One most serious is political violence, which shows no signs of subsiding. All to the contrary, it seems to be increasing. Since President Fujimori assumed highest office, 3,760 people have been killed, an average of 268 a month. In September and October, through, that average had increased to 390 people killed per month. In all, since the conflict started in 1980, a total of 24,000 people have died as a result of violence. Amnesty International constantly reports cases of "disappeared" people, whose fate most likely has been an extrajudicially execution by security forces. The increasing brutality of the army and police is matched by the killings perpetrated by Shining Path and Movimiento Revolucionario Tupac Amaru, the two guerrilla groups which seem to act with impunity. Indians who resist Shining Path's indoctrination are summarily executed. Religious organizations have become new targets. Last August, two Polish priests, Michel Tomaszek and Zbignew Strzalkowski, were assassinated, whereas Alessandro Dorni Negroni, an Italian priest, met the same fate last September in Chimbote, 450 km north of Lima.

A significant, major setback was suffered by the Government with the Japanese Government decided to withdraw 36 aid professionals, following the brutal murder in July of three Japanese technicians. Not surprisingly, security has really become one, if not the most important problem that affects the private sector. In a poll recently taken, 39% of the surveyed businessmen indicated that control of terrorism has become the most pressing issue. This concern now is evenly matched with the need to promote economic recovery and has clearly surpassed other goals such as bringing inflation below 50% annually (8% of the surveyed entrepreneurs consider that his should be the primary objective) and eliminating corruption (believed as a priority by 3% of the sample). These signs leave no room for misinterpretation.
just six years ago, in 1985, only 4% of Peruvian entrepreneurs considered terrorism as the top problem. Unfortunately, no decisive solution to this problem is at hand. To the contrary, increasing despair seems to be permeating the fabric of Peruvian society. In another survey that was conducted in Lima, it was revealed that 25% of people believed that Shining Path can be defeated militarily, down from 36% in June 1990 and 44% in May 1987. Significantly, in the shantytowns that surround Lima, whereby the cadres of Shining Path roam almost at will, 40% of the inhabitants believe that a victory of Shining Path is a distant possibility.

Insurgency in Peru can certainly be explained by the long lasting economic crisis. But a more plausible explanation lies in the fact that this brutal crisis is manifested within social and economic structures that are grossly unfair. The grievances of the vast majority cannot be properly addressed because there has been a colossal collapse, if not utter deterioration of social institutions. The prestige of the existing political parties stands at an all time low. President Fujimori, it should be pointed out, capitalized on this discontent, running as an independent. The social vacuum, if any, has become wider. Insurgency is but just one strategy to take advantage of this chaotic situation.

On the political front, the investigations of the BCCI’s operations in Peru, which involved the participation of senior officers of the Central Bank during the past regime, have been centralized under a Congressional Committee. Congress is also investigating corruption charges against five ministers of former President Garcia, who allegedly profited from transactions approved with the grossly overvalued, official exchange rate that was one of the cornerstones of Mr. Garcia’s economic policy. The most dramatic development on this front, however, has been the Congress’ decision in October to lift the former president’s parliamentary immunity.
from prosecution. This act paves the way for a trial as an ordinary citizen which would be conducted only if the Supreme Court finds enough evidence to warrant legal prosecution. After stormy sessions both in the Chamber of Deputies and then in the Senate, the charges have been limited to alleged illicit enrichment, derived from gaps in income and expenditures during fourteen years of public life. These charges, it should be noted, are very minor when compared to the alleged participation of Mr. Garcia in schemes with the BCCI that allowed for the pilfering of approximately $50 million, according to Mr. Garcia’s most fervent accusers. The major charges, apparently, will not be taken into consideration by the Supreme Court. If so, the process may well turn out to be a minor political event, with the strengthening of Mr. Garcia’s political position being a distant possibility.

These events have led to one major consequence: APRA, the most powerful political party has rallied behind former President Garcia and has tacitly declared political war on President Fujimori. APRA’s opposition now is frontal, and it is reasonable to state that President Fujimori will not find cooperation in Congress from this party in the foreseeable future. Increasing cooperation with the parties on the Right, e.g., Libertad, Accion Popular, Partido Popular Cristiano, and also with the Left is expected. Remarkably, President Fujimori seems to be the least concerned, The rescheduling of the Paris Club debt, the end of the status of ineligibility to obtain loans from the IMF, and the signing of the loan with Inter-American Development Bank have served to strengthen his popularity: his approval rating is 54%, and 59% of the population supports the current economic program.
Current Economic Policy

As part of the agreement that was reached with the International Monetary Fund in mid-September, the government has subscribed to a program for 1991-1992 which contemplates the following targets:

a) A 2.5 growth rate by the end of the year and a 3.5% growth rate for 1992.
c) A dollar exchange rate of $1.25 by the end of 1991.
d) Increase of tax collections to 12%-14% of GDP by the end of 1991.

In order to reach these targets, the government is to deepen the economic policies that have been in effect since August 1990. Strict monitoring and supervision by IMF teams of policy implementation has been accepted by the government. In essence, the economic authorities are expected to abide by tight fiscal and monetary policies during the period and to let the exchange rate be determined by market forces. Structural reforms are also expected to be accelerated, including the liberalization of the labor market, further reforms in the tax system and tax administration, removal of restrictions on private domestic and foreign participation in petroleum and mining, reduction of employment in the civil service, and privatization of state-owned concerns.

Of all the targets that the program contemplates, only the exchange rate has a chance of being met. In early November, the exchange rate was already 0.95 soles per one dollar. Two important caveats should be considered, however. The first is that there are compelling reasons to believe that the exchange rate is not being corrected upwards in an orderly way. By late August, the exchange rate would barely move beyond 0.80 soles per dollar. In late September, in a move that was coordinated with the banks, the government intervened to reduce the interest
rates by lowering the bank’s marginal cash reserve requirement for soles to 15% and raising the one for dollars to 60%. As a result of this, interest rates on savings deposits for both soles and dollars declined to 8% a month and 18% a year, respectively. As expected, this arrested the substantial influx of short-term dollars which literally flooded the financial system in the period May-September, in frantic search to reap the 18%-20% interest rates per month that was being offered on sol-deposits during these months. Consequently, the sol started to depreciate at a faster rate. But, quite unfortunately, the lowering of interest rates may turn out to be just a temporary event. There are already visible signs that banks are pressing for higher rates. Both, the expectation that there may be a big jump in the exchange rate on one hand, and the belief that -- in spite of the depth of the current recession -- inflation has yet to be tamed on the other, act to block further reductions in interest rates. In addition to this, lower rates may simply mean bankruptcy for some local commercial banks which, riddled by mismanagement for some years and saddled by a fragile loan portfolio, can barely stay afloat.

The sol has been depreciating faster because of the sharp increase of imports of consumer durables. As these are catered towards meeting the needs of just a small percentage of the population, there are limits to sustained import growth. Another factor, more important in our opinion, is the drop of dollar supply from drug trade, due to seasonal factors. this trend, it should be noted, can be easily reversed in the first quarter of 1992 especially if foreign demand keeps being strong and if the anti-drug campaign proves to be inconsequential.

The second caveat that ought to be considered is that even allowing for a scenario that fosters an orderly upward correction of the exchange rate, the gap that presently exists between the market and the parity rates is so wide that it may be too late for exporters before the two
rates are brought together. The alternative, a decisive, quick devaluation is an option that has been thoroughly dismissed out of consideration by the economic authorities because it will surely rekindle inflation. Consequently, the economy will muddle through in 1992. What this means is that the target of growing at 3.5% in 1992 seems to be out of touch with reality.

It is equally unrealistic to expect that tax collections will raise to 14% of GDP. Some progress is being made, as collections of the sales tax in September was 20% higher than in August. Yet, those improvements -- important as they are -- will not be enough to offset deeper, structural problems. The most important of them is the depth of the recession, which is deleting fiscal revenues.

The economic authorities submitted to Congress the draft of the 1992 budget. A total of 6.3 bn soles have been budgeted, of which 20% will go to defense, another 20% has been earmarked for wages and salaries of public employees and 10% for the regional compensation fund. The budget establishes also that approximately 416 bn soles ($500 million) will be destined for the foreign debt, but this figure is believed to be understated. The budget also contemplates allocating $50 million soles for a school milk program, $92 million for a fund designed to create job opportunities and $46 million for pre-school children.

The problem with the budget draft is that it may be premised once again, on unrealistic economic assumptions. A 33% increase in the collection of the sales tax, and a 23% increase in the collection of income and property taxes have been estimate. The problem resides in the fact that the budget assumes an economic real growth rate of 3.5% for 1992. As noted before, we believe that estimate is overstated.
In the meantime the economic authorities have their hands full in enforcing strict fiscal discipline. Expenditures have been largely brought under control but ad-hoc measures are constantly resorted to bolster sagging fiscal revenues. To wit:

a) An additional once-only 1.5% wealth tax on property was levied in August.  
b) A 15% tax on capital gains earned by banks was created.  
c) A once-only 1% tax on the value of all shares held in Peru-based companies was established.  
d) The sales tax was increased from 14% to 16% in September. This tax now also applies to meats, wheat, maize, salt, tea, coffee, and construction materials which had been previously exonerated.  
e) In early September, telephone charges were increased on average by 30%. Also, electricity rates were increased by an average of 6.2% in September and by 11% in August.  
f) Finally, as expected, the price of gasoline was hiked by an average of 12% in August, from $1.49 per gallon to $1.67 per gallon for 84 octane gasoline. A 10% hike was also effected in September where the price of gasoline went up to $1.83 per gallon. It should be noted that these hikes are higher than the inflation rates that were registered in those months.

On the other hand, the government will certainly accelerate the pace of structural reforms. Politically, it can clearly benefit from the fact that it has practically an "open field", given the extraordinary consensus from all parties on the need to reform the economy. Making the labor regulations more flexible will be, perhaps, the toughest nut to crack but, given the collapse of trade unionism and the utter disarray that still plagues the Left, it is a matter of time before the government decisively reforms the labor market. Labor stability provisions have been already amended, as reasons for dismissals have been extended. Also salary increases are no longer retroactive. Strongest labor opposition to the government has been manifested among teachers and health workers in the civil service and not among industrial workers. Even in mining -- traditionally a sector fraught with labor unrest and stoppages -- 1991 has been relatively peaceful in labor-management relations in comparison with 1990.
Two major reforms have been recently enacted. The first is on foreign investment. It is considered as perhaps the most comprehensive, liberal reform every contemplated in Latin America. The new legal framework on foreign investment marks a sharp, stunning departure from the regulations that were in place until July 1990. The new regime aims at eliminating the restrictions and the lack of guarantees that explain the plummeting of new direct foreign investment in Peru, from a year-average of $50.4 million during the period 1975-1980 to $25.2 million during the period 1985-1990. The reform seeks to reverse this trend by offering the following provisions:

a) Automatic approval of foreign investments.
b) Equal legal treatment for foreign and local investors.
c) Authorized repatriation of total invested capital and freedom for the remittances of profits and dividends.
d) Freedom for investors to use to the exchange rate they consider to be the most advantageous for currency conversion.
e) Enforcement of tax rates at time of investment, foreign exchange regime, and non-discrimination rights.

In addition to these key provisions, this pro-business new foreign regime offers guidelines on debt-equity swaps, reinvestment, technology transfer, investment in goods located in Peruvian territory, and investments in securities, stock and financial paper traded on the stock exchange.

The reaction of foreign investors who are experienced in Peru has been favorable but cautious at the same time due to the lingering memories of how the previous foreign investment regime was arbitrarily interpreted during the administration of President Garcia. Besides, caution from foreign investors is to be the norm in a country that has yet to being inflation under control and which cannot put down an increasingly vicious guerilla insurgency.
The second reform is one the financial sector. The state no longer has any role in the
deterioration of interest rates, and private commercial banks will dominate the process of
financial intermediation. What will be interesting to see is if their reform will lead to heavy
market concentrations and control by a few powerful banks. Another key issue is the
participation of foreign commercial banks. The same rules apply now for both national and
foreign banks, so as to spur competition. This equal treatment will allegedly result in substantial
capital inflows from foreign savers. In addition to this, the foreign exchange market has been
totally liberalized. All restrictions in foreign exchange transactions and on holdings, as well as
on internal or external utilization of funds have been lifted.

In our opinion, the decision to liberalize both the financial sector and the foreign
exchange market is not devoid of great risks. In a highly unstable environment, such as Peru’s,
foreign reserves are subjected to wild fluctuations. Sol-denominated financial assets could easily
and rapidly evaporate in a flight to the dollar, stemming from expectations of devaluation. In
addition to this, the high returns that can be earned in foreign markets pose a constant threat.

State of the Economy

Peru is gripped by a brutal recession. Recent economic indicators point to the fact that
production is below the output levels of 1979.
During the period 1987-1990, GDP declined by 25%. Average incomes have dropped by 3% during the 1980s, but the decline is more visible among wage earners. Since 1988, the drop has been dramatic.

Statistics on employment are appalling. Recent studies point to just 6% of the economically active population as being adequately employed and 86% as being underemployed by the end of 1990. In recent months, since the current stabilization program went into effect, unemployment has been on the rise.
PERU: EMPLOYMENT
(\% change on previous month)

<table>
<thead>
<tr>
<th>SECTOR</th>
<th>SEPT</th>
<th>OCT</th>
<th>NOV</th>
<th>DEC</th>
<th>JAN</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>-4.6</td>
<td>-6.2</td>
<td>-7.9</td>
<td>-7.0</td>
<td>-6.0</td>
</tr>
<tr>
<td>Commerce</td>
<td>-2.8</td>
<td>-3.5</td>
<td>-6.9</td>
<td>-4.8</td>
<td>-6.3</td>
</tr>
<tr>
<td>Services</td>
<td>0.5</td>
<td>-0.8</td>
<td>-1.4</td>
<td>-1.4</td>
<td>-0.4</td>
</tr>
</tbody>
</table>

Not only is this acute recession a curse. Peru has also been beset by hyperinflation.

PERU: CONSUMER PRICE INDEX
(\%)

<table>
<thead>
<tr>
<th>MONTH</th>
<th>YEAR. ACCUMULATED</th>
<th>LAST 12 MONTHS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989</td>
<td>2775.3</td>
<td>2775.3</td>
</tr>
<tr>
<td>1990</td>
<td>7650.0</td>
<td>7650.0</td>
</tr>
<tr>
<td>1991</td>
<td></td>
<td></td>
</tr>
<tr>
<td>January</td>
<td>17.8</td>
<td>17.8</td>
</tr>
<tr>
<td>March</td>
<td>38.9</td>
<td>6932.4</td>
</tr>
<tr>
<td>May</td>
<td>58.2</td>
<td>4688.5</td>
</tr>
<tr>
<td>July</td>
<td>86.5</td>
<td>2891.0</td>
</tr>
<tr>
<td>August</td>
<td>102.1</td>
<td>1431.5</td>
</tr>
</tbody>
</table>

As can be seen, important gains have been obtained in the fight against inflation. But victory cannot be claimed yet. Inflationary expectations are still a factor, since the exchange rate is widely believed to be grossly overvalued. Not surprisingly, price mark-ups in the manufacturing sector are being sustained, even under a free trade regime, since leading industrialists enjoy insularity from competition that is given by their control of import activities. Last but not least, further hikes in the price of gasoline to close the fiscal gap will also smother plans to vanquish inflation once and for all.

The industrial sector is hurting very badly. The principal reason lies in the brutal contraction of aggregate demand for which a reduction in real wages is the main investment.
Extremely high financial costs and an overvalued exchange rate are also two very important factors that are negatively affecting this sector. All this is reflected in disappointing output performances, with production levels that do not match the performances in 1979.

<table>
<thead>
<tr>
<th>PERU: MANUFACTURING OUTPUT, JULY 1991 (1979=100)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fishmeal</td>
</tr>
<tr>
<td>Foodstuffs</td>
</tr>
<tr>
<td>Beverages</td>
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<tr>
<td>Tobacco</td>
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<tr>
<td>Textiles</td>
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<tr>
<td>Leather</td>
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<tr>
<td>Footwear</td>
</tr>
<tr>
<td>Paper</td>
</tr>
<tr>
<td>Chemicals</td>
</tr>
<tr>
<td>Refined oil</td>
</tr>
<tr>
<td>Rubber</td>
</tr>
<tr>
<td>Plastics</td>
</tr>
<tr>
<td>Glass</td>
</tr>
<tr>
<td>Minerals</td>
</tr>
<tr>
<td>Iron-ore</td>
</tr>
<tr>
<td>Metal products</td>
</tr>
<tr>
<td>Machinery</td>
</tr>
<tr>
<td>Electrodomestics</td>
</tr>
<tr>
<td>Vehicles</td>
</tr>
<tr>
<td>TOTAL</td>
</tr>
</tbody>
</table>

The new trade regime will force the sector to become more competitive. The need to modernize cannot be avoided, but it will not be easy, since the road to a modern, competitive industry must cross a minefield of poor economic infrastructure, high energy costs, scarce credit, poor health and educational services and political violence.

An import surge is already in place. A total of $850 million in imports was registered in the period April-June 1991, which, if sustained, could reach $3600 by the end of the year. If so, this should be the highest import level since 1981. Importers are clearly benefitting from the new trade regime. Licenses and costly, time consuming procedures are no longer required.
There is strong evidence, though, that most, if not all of this shopping spree is concentrated in goods that cater to the needs of the well off. Imports of automobiles in the south of Peru have increased fivefold. Likewise, imports of electronic goods and domestic appliances have increased threefold.

Another evidence of this trend is provided by bank loans. Accordingly, short-term dollar credits are being granted to importers and also to the fancy, sophisticated retail stores that are located in the wealthy suburbs of Lima. An expansion of this type of stores is already taking place, offering an array of products that include beef from Argentina, French cheese and wine, Italian sausages, U.S. detergents, etc. This phenomenon is not new in Peru, a country whose income distribution is highly skewed and with a demand profile with high import content. Furthermore, there is no evidence whatsoever that his trade liberalization is playing a significant role in the reduction of the price level.

Local industry is taking a hit, as expected, but the efforts shift production towards foreign markets is not devoid of serious obstacles. Important reforms aimed at facilitating export activities have already been enacted but they have yet to be operational. These include the elimination of export permits, the free disposition to export goods and services, the free convertibility of the currency, the elimination of a union monopoly in stevedoring, and a forthcoming customs reform. But the list of problems that exports face cannot be taken lightly. As mentioned several times, an overvalued exchange rate constitutes perhaps the most important obstacle. Exports complain bitterly but the government is not likely to give in. Compensatory tax rebates are out of the question as well. In addition to this, port costs remain high because a modernization of infrastructure is due.
Consequently, barring windfall commodity prices in the near future, export will, if any, show just slight improvements in the months ahead. The problem is basically one of structure, not of policy. In per capita terms, Peruvian exports are just one-third of what was exported in 1980.

A Look into the Future

Peru’s long isolation from the international financial community is, apparently, over. Yet, one has to wonder about the tangible benefits that this reinsertion represents for the country in the immediate, pressing months ahead. With no fresh money coming in from either the IMF or the World Bank until later 1992, the acute financial tightness that the country has been enduring for the last six years will not be alleviated anytime soon. Moreover, the price that the government has accepted is the continuing adherence to the strict, belt-tightening economic program that is being implemented since August 1990.

Peru’s best chances in the months ahead reside in how well the population at large accepts an unrelenting economic recession as a way of life for the foreseeable future. Once can safely rule out any possibility of economic recovery until well into 1992. This seems to be an accurate prediction. But the depth of the current economic recession suggests that what is at stake is not merely the staying power of the current economic program or even the political legitimacy of President Fujimori’s government, but, rather, the very fabric of Peruvian society. This poor, impoverished nation has for long been under the assault of a dire economic crisis, social unrest, utter institutional decay, and political violence.
In the economy, the recession is now all-too-pervasive to be ignored. Local industry is waging a battle for survival within the context of a shrunk domestic market that now is being flooded with legal and illegal imports, local banks are saddled with receivables of doubtful recovery, and many a mining concern is going belly up. As the economy goes through a painful process of structural adjustment, the social and economic costs are mounting. Both unemployment and underemployment are on the rise with no signs of subsiding in the near future. The ensuing social unrest is not the catalyst of the unfortunate increase in political violence that has been registered in the last months. Terrorism is forcing businesses to spend in security, allocating as much as 10% of operating costs on this item. More importantly, terrorism, in combination with the collapse of the national police -- a law enforcement agency that has for all practical purposes ceased to exist as a reliable, effective, corruption free institution -- has forced businesses to reassess or delay investment decisions.

However, in spite of this grim scenario, the government of Mr. Fujimori can count on a battered, yet resilient population to ride out the worst effects of continuing economic recession provided that the gains that have been obtained in the fight against inflation are consolidated. But this battle is unfortunately far from over. Much will depend on avoiding a big jump of the exchange rate, on reducing interest rates, and on raising quickly fiscal revenues.

Events are rapidly coming to a head in Peru. It is imperative that the government of President Fujimori win the battle against inflation. Failure to do so -- within a context that denies any possibility of recovery in the short-term -- will greatly exacerbate social unrest and chaos. Two forces stand to gain from a nightmarish scenario, e.g. one which allows for another spurt of inflation amid recession. The first is the terrorist groups, both Shining Part and
Movimiento Revolucionario Tupac Amaru (MRTA). As of late, these forces have been gaining in strength, taking advantage of the utter demoralization of the police force and of the disintegration of trade unions. The militarization of the anti-drug campaign currently under way will certainly add to the strength of these groups, as they thrive amid the framework of violence and as they will certainly capitalize from the discontent of coca farmers. At present, it should be stated firmly, these groups have no chance whatsoever of bringing about the collapse of the government, but, since they operate almost at will in 40% of the territory, they have the capability of disrupting any semblance of effective administration and of blunting both foreign and local private investment. The result, therefore, is standoff, but with a gradual increase in the intensity of violence. The second force with the potential to capitalize from the failure of the economic program is the APRA party, especially if its maximum leader, former President Garcia, emerges victorious from his current political ordeal. In spite of the fact that Congress has now paved the way for the legal prosecution of the former President, the chances for turning this process into a political victory for himself cannot be underestimated. All these reasons point to 1992 as a year which will most likely seal the consolidation or the demise of the current economic program, and as the year in which one can confidently assess the viability of Alan Garcia as a presidential candidate in 1995.
ORGANIZED LABOR, POLITICS, AND LABOR MARKET FLEXIBILITY IN DEVELOPING COUNTRIES 1)

Joan M. Nelson

Organized labor is usually viewed as an obstacle to labor market adjustment. But unions' responses to adjustment programs in fact range from militant opposition to acquiescence or even explicit cooperation. Three sets of variables shape these responses: the strength and characteristics of the union movement itself; economic cycles; and political institutions and their ties to unions.

- **Strength of the labor movement**: In industrial democracies, an aggressive stance on wages tends to be associated with moderately strong unions. Small or weak unions are less militant, as might be expected; more surprisingly, large and powerful unions also tend to be more moderate, primarily because of their greater participation in consultation and decisionmaking at the national level. The experience in developing countries is somewhat different: only a few of these have strong labor movements, and among these, militancy is common. The large share of wage labor in the public sector complicates comparisons with industrial nations, since governments as employers clearly behave differently from private employers, particularly in hard times.

- **Economic cycles**: Depression almost invariably reduces militancy in developing as well as industrial nations.

- **Political institutions**: The nature of the political regime -- democratic or authoritarian -- is only roughly associated with how governments handle labor relations, and correspondingly with the options available to unions. More important in shaping unions' behavior are the nature of the political party system and how unions are connected with parties. The conditions needed to gain workers' cooperation are analogous to those which encourage business to invest: political stability, a voice in policy that affects their interests, and, arising from these, the confidence that current sacrifices will ultimately yield a fair share of future benefits.

1) Reprinted from: *The World Bank Research Observer*, vol. 6, no. 1 (Jan. '91), pp. 37-56
In developing as in industrial countries, the probable response of labor unions is crucial to government decisions about wages, prices, and employment. Organized labor is usually seen as a potential obstacle to labor market adjustment, a source of rigidities impeding shifts in relative wages and reallocation of labor among sectors, and a center of resistance to stabilization measures that entail "compression of demand". Yet in some countries, labor confederations have cooperated with the government and private employers to facilitate adjustment. What makes organized labor confront or cooperate, and what empowers it to slow or stall attempts to increase labor market flexibility? What political circumstances and approaches have persuaded organized labor to acquiesce in such attempts in the past?

Both theory and evidence on these questions are fragmentary, and partly because of poor data, much of the literature on organized labor in developing nations is too descriptive and narrowly focused to provide an adequate basis for comparative analysis. Most of the analytic and comparative research appropriate for the purpose is based on experience in industrial democracies. This article therefore reviews key findings from research on industrial countries and considers the extent to which they are relevant to developing nations. The focus is on two categories of variables that affect labor militancy: the size, strength, and structure of the union movement itself, and the economic cycle. The discussion then turns to how political institutions and stability shape union behavior.

Union Structure and Union Militancy

Classic theory assumes that free play of market forces will ensure flexibility in labor markets and that decentralized wage bargaining should restrain wage increases. Conversely, one
expects strong unions and centralized wage bargaining to be associated with comparatively rapid growth of real wages in the organized sectors and with relatively high levels of unemployment. Indeed, one influential line of analysis argues that over time, powerful organized interest groups (including but not confined to labor unions) may lead to such rigidities, such inability to adopt to changing circumstances, as to cause the decline of great powers (see Olson 1982).

Evidence from Industrial Democracies

Recent research on labor movements in advanced industrial democracies poses puzzles for these assumptions. This research finds that during the 1960s and 1970s countries with large, highly centralized union movements tended to experience low wage push, low unemployment, and low inflation. Moreover, strike activity (as a measure of union militancy) was negatively correlated with strong labor movements and highly centralized wage bargaining. Cameron's (1984) findings are an example. He developed five indices of the power of organized labor in eighteen industrial nations, using data from 1965 through the early 1980s. The indices measured union membership relative to total labor force, concentration or fragmentation of union confederations, their power in collective bargaining, the scope of such bargaining, and the extent of arrangements for worker participation in decisions at the firm level (such as work councils and worker representation on company boards). Cameron found that each of these indices correlated negatively with strike activity, levels of unemployment, increases in both nominal and real earnings, and consumer prices between 1965 and 1982. Some of the correlations -- with the organizational unity of labor and workers' participation in decisions in particular -- were strong (Cameron 1984).
More recent studies suggest that the relationship between centralized wage bargaining and militant wage demands may be humpbacked (shaped like an inverted U) rather than monotonic (decreasing steadily). Wage push is least evident where bargaining is highly decentralized (conducted largely at the level of individual firms), and where it is highly centralized; wage pressures seem strongest where bargaining is moderately centralized (at the sector or industry level). Calmfors and Driffill (1988) find a humpbacked relation between centralization -- defined as "the extent of inter-union and inter-employer cooperation in wage bargaining with the other side" -- and several indices of employment and inflation. Freeman (1988) uses the degree of wage dispersion across industries as a strong indicator of market structure and finds that countries with highly centralized or highly decentralized bargaining in their labor markets, have increased employment more rapidly and wages less rapidly than countries with intermediate degrees of centralization.

What mechanisms are at work here? Two different explanations are offered for these empirical findings. Calmfors and Driffill see shifts in incentives (rational expectations about gains and losses) as the principal impetus for intransigence in negotiations, depending on the degree to which wage bargaining is centralized. When bargaining is conducted at the firm level, unions have little market power. An increase in wages is likely to bring a large drop in employment, because the isolated firm cannot raise output prices and remain competitive. The market power of unions increases if wage bargaining is conducted at the industry or sector level. But as the centralization of wage bargaining increases, greater power must be balanced against greater risk that wage gains will affect price levels, thus eroding the real value of nominal wage hikes. Increased centralization on the union side of the negotiating table usually goes along with
correspondingly increased centralization on the employer side, and employers also face shifting incentives for resisting or accommodating union demands at different levels of aggregation. The outcome is nonmonotonic or humpbacked relation between increased centralization and labor militancy: unions have the strongest incentives to bargain aggressively at intermediate levels of centralization.

An alternative explanation rests on the theory of "democratic corporatist" arrangements for determining wages and broader social policies developed in the 1970s and 1980s, mainly with reference to Western and North European nations. This use of the term corporatist may call for explanation. The same term often refers to certain kinds of political systems, including some - especially during the 1970s in Latin America -- in which relations between unions and governments are entirely different from those described in the following. Nevertheless, this is the label usually used to refer to the pattern of labor market arrangements discussed here, and I have followed this usage rather than compounding confusion by inventing a new label.

Even when the concept of corporatism is used narrowly with reference to labor market arrangements, definitions and interpretations of its implications vary. But four characteristics are common to most or all of the competing versions: (1) in a corporatist system, each major interest in society is represented by one or a very few central, or peak, associations -- in the case of labor, confederations; (2) these associations include as members most of the relevant groups and individuals; in the case of labor, a high proportion of the labor force is unionized, and most or all unions belong to the peak confederation(s); (3) the peak association(s) have considerable authority or control over their constituent organizations, and these in turn have considerable
authority or influence over their individual members; and (4) peak association officials participate actively in government decisions affecting their constituents' interests. The arrangements for participation vary from country to country but entail discussion and informal or formal bargaining among associations representing various interests and the state.

For labor, such arrangements mean that unions have sufficient economic and political muscle to encourage their incorporation into national decisionmaking circles. (The may have gained this strength historically, by gradual growth of unions and federations, or the government may have directly aided the growth of unions as part of an elite strategy to preempt more radical influences.) Wage restraint and acquiescence in adjustment are a response to generous social security and welfare arrangements that buffer workers against the vicissitudes of adjustment and exchange the immediate advantage of pay increase for employment security and a variety of longer-term benefits.

At the same time, in a strong corporatists system top labor leaders have the authority within the unions to ensure that the rank and file will accept agreements made by the national elite. And discussion and bargaining with other decisionmakers lead labor leaders to recognize national interests that constrain pursuit of labor's narrow or short-term interests. (More radical interpretations would argue that not only rational persuasion, but co-option -- the desire to keep the material benefits and status of associating with the national elite -- is a principal incentive to cooperate in such a case.) Recognition of broader national interests encourages acquiescence in policies of wage restraint, to promote national economic stability and growth and thereby sustained employment and gradually rising real wages. Negotiating wage agreements at the national level also means that individual unions have less scope and need to worry about losses
relative to other unions. 3

In several of the smaller Northern and Western European nations, labor’s cooperation with broader economic policies reflects the clear recognition that nations highly dependent on trade must maintain international competitiveness (Katzenstein 1985). To take one illustration, in Belgium in February to March of 1982, labor agreed to skip an automatic indexed increase in wages following devaluation and to replace later indexed rounds with lower lump-sum wage adjustments to reach an agreed degree of deindexation. Further real wage increases were banned through 1984 and thereafter regulated by a norm of competitiveness taking into account the weighted average of Belgium’s seven more important trade partners (see Theo Peters in Williamson 1985, p. 99).

The following section will argue that virtually no developing country approximates the labor organization and wage negotiation arrangements of the corporatist model. But the principles that make the model work will prove useful in understanding problems of labor relations and labor market reform in developing nations, and they may suggest broad guidelines for improved labor relations. In essence, corporatist institutions affect the range of information and options available to all parties in the negotiations and thereby alter incentive structures. More specifically, they (1) broaden the array of options under negotiation to include a wide range of social policies along with wage and non-wage compensation; (2) lengthen time horizons, largely by increasing confidence both in government economic management and in labor’s continued access to decisions affecting its interests; and (3) increase the sophistication and complexity of economic implications taken into consideration by union, business, and government representatives.
Corporatist labor market arrangements cannot be replicated in most developing nations, in part because the structure of labor markets and the larger economy bear no resemblance to the usually small industrial democracies in which these arrangements have evolved, and in part because the arrangements have grown out of historical features quite unlike those of most developing nations. Moreover, most developing nations cannot afford the employment benefits and other social benefits that are key elements in the corporatist bargain. Indeed, in some developing countries the attempt to provide organized workers -- a relatively small fraction of the labor force -- with generous benefits modeled on those of industrial nations has contributed to both economic difficulties and social tensions.

For all these reasons the corporatist model is not a practical blueprint for emulation, though there may be a few developing countries that could evolve along those lines. Rather, it is a heuristic model that elucidates some of the mechanisms and relations that have helped some nations channel the self-interest of a sizable and well-organized interest group in ways compatible with broader national interests. Where similar arrangements are unlikely to emerge, functional equivalents are needed -- institutions, procedures, and policies that broaden the array of options, lengthen time horizons, and increase the sophistication of all key actors in labor markets.

Applicability of the Evidence to Developing Countries

Virtually no developing country replicates the features of the prototypical strong corporatist system with respect to labor. In many of the countries of Northern and Western Europe, union claim as members two-thirds or more of the work force. Reliable and
comparable data on union membership are missing for most developing countries, but those for which data are available suggest a span ranging downward from about a third of the labor force. In the mid-1980s Argentine and Venezuelan unions claimed about a third of the labor force, Jamaican unions a quarter, Mexican unions roughly a fifth. Outside Latin America, save for Mauritius and Sri Lanka (both with roughly a third of the labor force unionized), union membership is much lower. Some of the most industrialized (and rapidly industrializing) developing countries, above all the East Asian "tigers," have in varying degrees repressed union movements.

Even the comparatively large union movements in some Latin American countries do not usually have the additional characteristics of strong centralized movements. In Brazil and Mexico, for example, rivalries among confederations are strong. The power of Mexico's largest confederation, the Confederation of Mexican Workers, is reduced, quite aside from the effects of aging leadership, by its structure: average union size is small (about 310 members), and less than half of the confederation's members are in powerful industrial unions such as railroads, petroleum, or mining. Nearly half are in enterprise-level unions, which are in turn parts of functionally diverse, regionally based federations. The Confederation of Mexican Workers must often compete with rival confederations active in the same geographic areas, and the government can manipulate these rivalries to undermine the confederation, as the government of Miguel de la Madrid did in 1983. Therefore, it is extremely difficult to coordinate labor action within an industry. Mexican unions rarely have strong representation, such as works councils, at the enterprise level (Middlebrook 1989). Similar weaknesses plague labor movements in many other countries. In short, few if any developing countries have labor movements able to play their
side of the corporatist strategy in labor market policies.

If data were adequate to develop indices of union strength and centralization of wage bargaining for most developing nations, virtually all would fall in the low and moderate segments of a global scale arraying labor movements from weakest and least centralized to strongest and most centralized. (The dimensions do not necessarily covary neatly.) Both classic liberal expectations and the forecasts of recent proponents of a humpbacked relationship based on the experience of industrial nations predict little militancy and wage push at the low end of this scale and greater militancy and wage push toward the center. Evidence from developing countries accords with these expectations.

Walton and Ragan (1988, table 10.3) found a strong correlation between the proportion of the labor force in unions (as of 1975) and the severity of protests against austerity between 1976 and 1987 in twenty-six countries in Latin America, Africa, and Asia. In many developing nations, labor movements are not only a small part of the labor force but are also weak and fragmented. Strikes (especially wildcat strikes) may be quite frequent but are likely to involve few workers and have little effect on broader wage levels. But unions in some developing countries are strong enough to exercise considerable wage push in particular sectors or industries. Unions in strategic sectors may exercise tremendous economic and political leverage, even if the labor movement for the nation as a whole is not strong. Copper miners in Chile and Zambia, tin miners in Bolivia, oil workers in Mexico, Nigeria, Venezuela, and other countries, and, to a lesser degree, bauxite and alumina workers in Jamaica have been in a position to throttle a large fraction of national export earnings and government revenue. They have often used their leverage to maintain wages markedly out of line with the rest of the economy, with
a variety of distorting effects on the industry and the economy as a whole. In Mexico, despite
the pattern of incorporation of Mexican labor confederations, especially the Confederation of
Mexican Workers, their exclusion from economic decisions under the de la Madrid government,
and their inability to block massive drops in real wages, certain Mexican unions were able to
block government reforms. For instance, the powerful petroleum union used threats of sabotage
and massive resistance to force the government to back down on its plans to eliminate the
union's control over subcontracting as part of a rationalization scheme. In a few developing
countries with sizable industrial sectors, including several Latin American nations, Turkey and
Tunisia, not merely unions in strategic industries but labor movements more generally have
periodically been militant, wielding considerable economic and political clout. In the framework
of theories based on industrial democracies, these countries fall somewhere in the central range
of the scale linking centralization to militancy and wage push: their militant behavior conforms
with the hypothesis of a humpbacked relation.

A further characteristic of unions in developing countries may encourage a tendency
toward militancy. Both the corporatist theories and Calmfors and Driffill's theory of union
bargaining strategies implicitly assume unions have considerable analytic capacity to assess the
implications for labor of current economic trends and alternative wage settlements. Few
industry-level unions or national confederations in developing countries have economic staffs
comparable to those in Western European countries. Moreover, available data are often
unreliable, and analysis and forecasting are particularly difficult where inflation and other aspects
of economic performance are highly volatile. The result may be to increase uncertainty and risk
associated with wage restraint and reduce the attractiveness of trading off wage increases for social welfare benefits. 6

One other important aspect of the structure of labor movements in developing countries is that the proportion of the labor force in public service jobs is much higher than in most industrial democracies (see table 1). In several African nations public sector workers made up 60 to 80 percent of nonagricultural workers; in India the figure was 72 percent (Heller and Tait 1984, table 22).

The high proportion of wage labor in the public sector means that the sector's wage and employment policies are important both in their own right and also because of spillover effects into the private sector. Heller and Tait (1984) estimated that "central government decisions on wages and salaries in developing country are likely to affect 5 to 40 percent of employed workers in the urban labor market and therefore have a pervasive 'leverage' effect on domestic unit wage costs."

How do large public sectors affect wage push and employment flexibility? The topic is little studied. Two questions are central: Are public sector unions intrinsically weaker (or stronger) than their private counterparts? And does government, in its role as employer, operate
with different goals and constraints than do private employers? The answer to the first question is ambiguous. The answer to the second is clearly affirmative.

Public sector workers in industrial societies are often assumed to be in a weaker position to exert wage pressure. Historically, they have often been restricted from forming unions.

<table>
<thead>
<tr>
<th>Table 1. Public Sector Workers as a Percentage of Nonagricultural Employment</th>
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<tbody>
<tr>
<td>Category of countries</td>
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<tr>
<td>-----------------------</td>
</tr>
<tr>
<td>OECD</td>
</tr>
<tr>
<td>Developing countries</td>
</tr>
<tr>
<td>Africa</td>
</tr>
<tr>
<td>Asia</td>
</tr>
<tr>
<td>Latin America</td>
</tr>
</tbody>
</table>

OECD, Organisation for Economic Co-operation and Development.  
Note: Data are from 1979 or 1980.  
a. The number of countries shown for each category is that for which data were available on central government employment. Not all countries had data for each category of workers, and the number of observations therefore varies somewhat within each country category for different years.  
b. This category incorporates data for a few countries in the Middle East.  
Source: Adapted from Muller and Taix 1984, table 1.

Even where employees' associations are legal and large, many categories of public sector workers are legally barred from striking and risk dismissal and arrest if they do strike. Their position is weaker still if opportunities for alternative employment in the private sector are extremely limited, as is true in many of the poorest countries.

To balance these handicaps, do public sector workers and their associations have leverage that private workers do not? Freeman (1986) discussing state and local government unions in the United States, argues, "A fundamental difference between public and private sector collective
bargaining is that public sector unions, more so than private sector unions, can influence employer behavior through the political process."

But it is not clear why this should be so. Public sector workers may indeed form voting blocs or lobby or demonstrate for their demands. But so may organized private sector workers. Strikes, work stoppages, or slowdown in vital public services hold the public hostage, generating strong political pressure on the government to hasten a settlement. But the outcome may be repression rather than concessions to the strikers, depending on the political circumstances and particularly on the degree of public sympathy with the strikers.

A more convincing argument is based on patronage ties between politicians and public sector workers. Patronage implies a reciprocal commitment: the exchange of jobs for political support. Many national and local politicians have built up their support bases primarily through this mechanism. Sharp declines in real wages and, even more clearly, large-scale reductions in the work force mean the disintegration of support coalitions. In Africa, moreover, patronage often has tribal overtones and is endorsed, indeed mandated by the strong traditional expectation that a "big man" protects and advances his ethnic brothers. A severe wage squeeze or extensive firings betray that trust.

Comparisons of public and private sector wage levels in developing countries offer ambiguous evidence as to whether public sector workers (and their unions or associations) are handicapped or advantaged. Any such comparisons must be approached with caution. Workers' compensation packages are complex, including base pay, varied bonuses, and non-wage compensation such as subsidized housing, insurance, and other benefits. And it is hard to control across sectors for differences in education and skill composition. There may also be
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<table>
<thead>
<tr>
<th>Category of countries</th>
<th>Number of countries</th>
<th>Total public employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>OECD</td>
<td>16</td>
<td>24.2</td>
</tr>
<tr>
<td>Developing countries</td>
<td>35</td>
<td>43.9</td>
</tr>
<tr>
<td>Africa</td>
<td>16</td>
<td>54.4</td>
</tr>
<tr>
<td>Asia</td>
<td>5</td>
<td>36.0</td>
</tr>
<tr>
<td>Latin America</td>
<td>10</td>
<td>27.4</td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Type of public employment</th>
<th>Central government</th>
<th>State and local</th>
<th>Nonfinancial public enterprises</th>
<th>Total public employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>OECD</td>
<td>8.7</td>
<td>11.6</td>
<td>4.1</td>
<td>24.2</td>
</tr>
<tr>
<td>Developing countries</td>
<td>23.4</td>
<td>4.0</td>
<td>13.9</td>
<td>43.9</td>
</tr>
<tr>
<td>Africa</td>
<td>30.8</td>
<td>2.1</td>
<td>18.7</td>
<td>54.4</td>
</tr>
<tr>
<td>Asia</td>
<td>13.9</td>
<td>8.0</td>
<td>15.7</td>
<td>36.0</td>
</tr>
<tr>
<td>Latin America</td>
<td>20.7</td>
<td>4.2</td>
<td>5.5</td>
<td>27.4</td>
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important contrasts between the wages and security of civil servants and those of workers in state enterprises or local government. Ehrenberg and Schwarz (1986), in their review of U.S. research on the issue, note considerable evidence that the relative wage gap between union and non-union workers is smaller in the public than in the private sector, but they go on to suggest several considerations that cast doubt on the finding. Comparing public to private employees (without considering the union versus non-union dimension), they note that U.S. federal government workers are paid somewhat better than comparable private sector workers; this is particularly clear for women and for non-white males. The finding holds, but less strongly, for state and local employees, except perhaps for male local government workers. Taking into account non-wage compensation (which most studies ignore) would probably strengthen these findings.

For what they are worth, the "styled facts" turn up geographical differences. In some Latin American countries in the mid-1980s, public sector workers seem to have been somewhat less well paid than their private sector counterparts (Lopez and Riveros 1989, Riveros and Sanchez 1990). In Sub-Saharan Africa in the postindependence decades, public sector workers tended to be substantially better paid, but during the 1980s real wages in the public sector fell dramatically, perhaps erasing or even reversing their earlier advantage (Lindauer, Meesook, and Suebsaeng 1988). The regional contrasts are probably attributable more to differences in the relative weight of public and private sector unions than to variation in the militancy of public sector unions. Private sector unions are large and important in a number of Latin American countries, presumably driving up private sector wage levels at least in highly unionized sectors. in African employment and unions in the private sector are much less important relative to their
More broadly, it is surely the behavior of governments as employers more than the behavior of unions that distinguishes wage determination in the public sector from processes in the private sector, above all during hard times. Governments do not have to cope with private and loss sheets but instead are constrained by fiscal and monetary considerations. Recession and fiscal crisis pit pressure from public sector workers to maintain wages and prerequisites against political pressures for other uses of political pressures for other uses of public funds. Trends in personnel costs as a percentage of total public expenditures could be viewed as a rough measure of the political priority accorded to public sector workers. In most of Latin America and Africa in the 1980s, that percentage rose substantially. Under intense fiscal pressure, maintaining public employment has been given very high priority; indeed, especially early in the crisis, governments often tried to hire countercyclically (Lopez and Riveros 1989; Riveros and Sanchez 1990). As the need for long-term reform became inescapable, a few governments laid off large numbers of workers, but most such cases entailed generous compensation. Ghana, for example, paid the equivalent of roughly two years' total compensation to workers stripped from the notoriously overstaffed Cocoa Board. Guyana cut almost a quarter of its civil service and public enterprise workers but awarded severance pay so large that the government had to borrow heavily to cover the costs (Nunberg 1988). Buffering lower paid workers has also been stressed: not only have average real wages in the public sector dropped sharply, but, especially in Africa, differences between the highest- and lowest-paid workers have been cut dramatically. Union pressure obviously played a role in these patterns. But more fundamentally, the patterns reflected the different incentives and constraints motivating governments as employers. In
contrast to those governing the actions of private employers.

**The Economic Context and Labor Militancy**

The most plausible and best-supported proposition about the effects of economic cycles on organized labor is that bargaining power and militancy decline in hard times and increase in prosperity. Strikes vary with economic cycles: when labor markets are slack and protracted unemployment looms, unions often consent to wage regulation; conversely, good times make labor more aggressive (see Lange 1985 and Kennan 1986). Labor militancy is likely to have higher payoffs in right labor markets, and widespread wage drift (induced by workers or employers) and other forms of noncontracted gains are more probable. For instance, in Norway's postwar history of wage regulation, breakdowns were most likely during periods of rapid economic growth. Conversely, Epstein's analysis (1988) of union responses to official austerity programs between 1976 and 1984 in seven Latin American countries with large and important labor movements found fairly strong statistical links between rising unemployment and fewer and smaller strikes.

The rapidity with which workers' priorities shift, during economic crises, from maintaining real wages to protecting their jobs tends to reflect the history of economic growth in the country in question. "The longer the time since the last structural crisis, the more workers are likely to expect that strong economic conditions ... will continue, and that downturns will be only temporary" (Lange 1984). In Costa Rica, for example, the economic tailspin of 1979-82 broke a virtually uninterrupted span of growth from the early 1960s. After Alberto Monge's government's remarkably effective stabilization effort of 1982-83 had clearly
taken hold, popular pressure to restore real incomes to their precrisis peak mounted rapidly.

Lange's discussion of the rational bases of workers' consent to wage regulation adds one modification that is important for our concerns. Although pessimism about short-term economic prospects usually encourages cooperation with wage regulation, the effect is less predictable when labor confronts "structurally bleak prospects."

On the one hand, it might be thought that workers would be strongly inclined to regular wages, for they would think that failing to do so would condemn the national economy to sustained recession or even depression, and their own wages to real decay. On the other hand, the bleak economic prospects might lead workers to think that there is little to be gained by restraint -- things will not get better anyway without major disruptions to their economic lives -- and that it is therefore best to try to get as much as possible while it can still be had. (Lange, 1984).

Lange argues further that, in such situations, a key variable shaping workers' behavior is whether they believe that "the fruits of their restraint will redound to their future economic advantage." This perception, in turn, rests on the credibility of the government's broader recovery program and on implicit or explicit assurances that their interests will be protected during industrial restructuring. In short, when the long-term economic outlook is grim, political relationships and expectations become much more important in determining labor's responses.

**Political Structure, Labor Militancy, and Labor Influence**

Power is relational. The strength of governments, their attitudes and support bases, and their strategies toward labor markets are as important in shaping outcomes as the strength.
autonomy, and orientation of labor movements themselves. And unions adjust their actions to the political context demand consideration: type of regime; the party system and the place of organized labor in that system; and more transitory political circumstances, particularly electoral cycles and changes in regime.

These same factors may also affect governments' commitment to adjustment in general and to labor market flexibility in particular. For this brief survey the discussion is simplified by assuming government commitment to measures (1) to contain wage increases to a significant degree, as an important element in a stabilization package, and (2) to encourage increased labor market flexibility in the medium term. In other words, government commitment to flexible labor markets is taken as a given in this article, and the emphasis is on how varying political contexts shape government tactics and labor responses.

**Regimes and Tactics**

Most of the research reviewed earlier in this article is based on evidence from industrial democracies with governments widely accepted by their citizens as legitimate, with competition among two or more parties that constitute potential governments, and with broad legal and actual protection for civil and political rights. The type of regime, in effect, is held constant. In developing countries, types of regime vary widely.

One would expect the type of regime to be most obviously reflected in the tactics governments choose, one convinced of the necessity of measures organized labor is likely to resist. To cope with that resistance, three basic types of tactics are available: persuasion, partial compensation, and containment. Social pacts combine persuasion and compensation.
compensation need not take the form of immediate wage increases; social pacts often trade short-run wage restraint for social benefits (in effect, deferred improvements in the security and quality of life). Another form of compensation is reform of labor laws to provide labor with assurances of greater freedom to organize or with better access to decisionmakers (in effect, improving prospects of later economic gains). Union pressure can be contained not only by repression (or the threat of repression) but also by co-opting labor leaders or by encouraging internal divisions and the emergence of rival unions or federations.

Broadly, democratic governments rely primarily on persuasion and compensation; authoritarian regimes are less reluctant to use containment in general and repression in particular. So unions in authoritarian systems -- if they are permitted to operate legally at all -- are likely to be more cautious and less militant.

But type of regime is too crude a variable to be a reliable predictor of government's choice of tactics in dealing with labor. Both authoritarian and democratic governments display a wide range of legal and institutional arrangements governing union activity. Some democracies have laws hedging union activity quite tightly, and many democratic governments have been willing to ignore or put down labor protests. In Sri Lanka in 1980 an attempted general strike was broken by dismissing large numbers of public sector strikers. In Bolivia in 1985 the newly elected government of Victor Paz Estenssoro acted promptly and decisively to squelch the miners' union that had repeatedly destroyed earlier stabilization efforts. In Jamaica in the same year Edward Seaga faced down an unprecedented general strike in which both major union confederations (each linked with one of the two major parties) protested his austerity program.
Conversely, some long-established one-party or dominant-party governments grant unions considerable influence, although this may be punctuated with episodes of tension or repression. Examples include the long history of Kenneth Kaunda's relations with the Zambian copper miners; the dominant Institutional Revolutionary Party's long-term management of labor relations and policies in Mexico; Neodestour's relationship with the major Tunisian labor federation; and Juan Velasco's military government's cultivation of support from Peruvian trade unions in the late 1960s and early 1970s.

Electoral cycles clearly do influence not only governments' willingness to launch or maintain unpopular wage and price measures but also organized labor's acquiescence in such measures. This pattern is not exclusive to competitive democracies. Thus Ferdinand Marcos postponed stabilization measures until after the important Philippine legislative elections of May 1984. The De la Madrid government, after five years of ignoring Mexican labor unions' anguished protests, entered into an Economic Solidarity Pact in December 1987, as it became increasingly clear that the elections scheduled for mid-1988 would pose an unprecedented challenge to the Institutional Revolutionary Party's control (Middlebrook 1989).

In sum, the type of regime clearly affects government handling of labor relations and, therefore, the options available to unions. But the more fine-grained features of the relation between organized labor and the government, including the channels and degree of access to decisionmaking circles, count more in how governments manage labor issues. These arrangements are not systematically related to the broad distinction between electorally competitive and noncompetitive regimes.
Party Systems and Labor's Political Role

Party systems and union ties with parties are particularly influential in shaping unions' political roles and their relations with governments. Labor movements occupy positions in party systems ranging from dominance in a ruling coalition to virtual exclusion. The examples that follow demonstrate the range of possible positions.

- Peronist unions in Argentina dominate their party, and they have exercised tremendous power during periods of Peronist control of the government.

- A pattern more commonly found is incorporation of unions or segments of labor as subordinate parts of a ruling coalitions, as in Mexico and Singapore.

- In several Latin American and Caribbean countries, unions have links with both of two centrist parties, which together dominate political processes: Colombia, Costa Rica, Jamaica, and Venezuela are examples. In these cases labor has access to (but does not dominate) the government regardless of the party in power.

- In Peru until quite recently, and in Argentina, labor has been linked to one strong party within a system divided by deep social and political cleavages. In Peru, the result was to exclude the American Popular Revolutionary Alliance (APRA) and its labor allies for many decades. In Argentina, Peronists periodically gained power. In both cases the political system was polarized and destabilized.

- In Uruguay and (less clearly) the Dominican Republic, unions have been linked mainly with weak radical parties: the result is semiexclusion.

- In countries such as the Republic of Korea until quite recently, and Chile under Augusto Pinochet, organized labor has been effectively excluded from rightly limited political arenas.

At any given time, different party systems and links between parties and organized labor strongly influence the options available to unions to defend or promote their interests. Over time, patterns of incorporation into the party system also affect the strength and orientation of the labor movement as a whole.

Broadly, it appears that either incorporation into an established dominant party or links...
with parties that alternate in power encourage negotiation and compromise and dampen confrontation. But incentives for the party in power to make concessions to labor differ sharply in the two categories. The dominant party that incorporates major unions may assume that labor has no plausible alternative to cooperation. In more competitive two-party systems access to both major parties assures labor leaders that their interests will get a hearing -- the kind of assurance Lange (1984) suggests is likely to moderate the militancy of desperation in very hard times. In contrast to both systems, the polarized pattern is likely to stimulate militancy, whether or not the party with which labor is affiliated stands a good chance of taking office.

Instability and Transitional Regimes

Just as research on the militancy of labor movements in high-income industrial democracies holds the type of regime constant, it also implicitly focuses on experience in stable political systems. Many developing countries are much less stable and predictable: governments frequently change through coups rather than scheduled elections, and not merely the people in power but the nature of the political system is prone to change. Unpredictable political settings have far-reaching implications for the politics of adjustment, including the politics of labor market adjustment.

In the short run, both elected and "irregular" new governments may have special opportunities to adopt needed economic reforms. The new government is likely to have a honeymoon period during which it can blame the needs for unpopular economic measures on the legacy from its incompetent or dishonest predecessor. The honeymoon effect may be particularly strong both after a long period of political and economic decay and if the new
government enters office with strong popular support. (New governments, of course, vary

tremendously with respect to both their sense of security and the clarity of their economic goals

and program: both factors affect their ability to take advantage of the honeymoon period.) The
effects of governmental turnover on the system as a whole over time are a different mater:
frequent turnover is likely to breed cynicism and to drastically shorten the period of time that
all political players, including labor unions, are willing to take into account as they consider
their strategies and tactics. The result in the realm of labor policy is diminished potential for
trading deferred benefits for current wage moderation.

The current global wave of democratizing reforms and changes in regimes highlights the
special question of interactions between democratization and economic liberalization, including
labor market adjustments. A principal characteristic of democratization is rapid expansion of
popular political participation. Popular demands for improved living conditions may be
temporarily muted by widespread recognition that the country's economic problems require
major reforms and will take time to carry out. That recognition seems to be particularly strong
in some of the Eastern European countries now retreating from state socialism. But popular
demands are likely to be more immediate and insistent in many of the nations of Latin America
and Asia, and in some in Africa now turning or returning to democracy.

In short, new democracies often face considerable wage pressure. If the new government
is viewed as a definitive break with the bad old days, workers are likely to look for speedy
improvement in their situation. But if the new regime is viewed as fragile, labor may well see
to capitalize on the political opening while it lasts. From the government's perspective, too, the
desire to consolidate or broaden popular support encourages wage increases and other populist
measures.

Ups and downs in real wages obviously reflect not only government wage policies but other domestic policies and external trends, but it is striking how many of the new democracies of the past two decades illustrate the tendency to early wage concessions. In Portugal after 1973 real manufacturing wages rose 13.7 percent in 1974 and 10.3 percent in 1975; nominal wages were hiked much more (Schmitt 1981, Stallings 1981). In Spain real wages had been rising rapidly from the 1960's but accelerated after 1974 (Lopez Claros 1988). In Argentina real industrial wages had dropped 11 percent in 1980 and 10 percent in 1981; the departing military government then raised real wages by at least 25 percent. (Diaz-Alejandro, in Williamson 1985, gives the increase as 29 percent. Later data in ECLAC 1989, record the increase as 25.4 percent). Raul Alfonsin, campaigning for the presidency and probably basing his judgment on the 1980-81 data, promised to raise real wages, and in 1984 real average manufacturing wages rose a further 26.4 percent (ECLAC 1989). In Uruguay average real wages jumped 14.1 percent in 1985 with the return of civilian rule, after having fallen more than 30 percent between 1982 and 1984, although the new civilian government was firmly centrist and the unions were not traditionally politically powerful. In Bolivia Herman Siles Zuazo's election in 1982 ended a long period of military rule, but Siles's attempts to gain control over the rapidly disintegrating economy were repeatedly blocked by militant unions. At least four times the government introduced austerity measures only to back off and raise nominal wages after general strikes.

In Turkey Turgut Ozal became head of the economic team when military rule was imposed in 1980 and was later elected prime minister when civilian rule was restored in late 1983. Wage negotiations had become increasingly confrontational in the late 1980s as the
economic and political crisis deepened, and the new military government cracked down on the labor unions. Real wages, already falling steeply in 1978 and 1979, dropped a further 25 percent in 1980. As the stabilization and adjustment program took effect, the rate of decline slowed to 7.4 percent in 1981 and 4 percent in 1982. In 1983, as elections to restore civilian rule approached, wage policy was eased and prices on key staples held in line; real wages increased 5.6 percent. The collective bargaining process was liberalized early in 1985 (this information is based on an internal World Bank report and on Kopits 1987).

Labor pressure on new democratic governments is not surprising. Much more interesting would be a semisystematic explanation for the experience of such governments in trying to bring wages policies back into line and to establish rules of the game to reduce conflict with organized labor while permitting stabilization and adjustment. The 1980s saw a wide array of strategies, including successful pacts (Spain), a variety of tactics to weaken or split labor (as Alfonsin initially tried to do), and straight union-breaking (under Paz Estenssoror in Bolivia). The results of such strategies in winning labor's cooperation with adjustment have ranged from considerable success to total failure. Explaining the results would go well beyond the space available here. But at the core of durable arrangements to encourage moderate labor demands must be a modicum of confidence.

Long-Haul Adjustment, Labor Cooperation, and Equity

Skillful government tactics can make a great difference to the effective or ineffective management of labor demands in the short run. But adjustment is a long-haul proposition, likely to extend over a decade in many countries, perhaps considerably longer in some. Resumed
growth in those countries whose economies have stagnated or worsened in the past decade will facilitate labor's cooperation, but certainly in much of Latin American and Africa it is realistic to expect a long process of painful reorientation.

The crucial element in gaining workers' cooperation is the belief that their sacrifice will contribute to general gains and that those gains will be distributed fairly. That belief requires (1) confident in the government's economic management and at least contingent hope that the government has a plausible game plan -- in countries where external economic trends are very adverse, the plausibility of the government's game plan may hinge in part on the probability of substantial external support; (2) confidence that labor's interests will be fairly represented and that labor representatives will have access to and influence in decisionmaking circles; (3) as a prerequisite, reasonable confidence in political stability, that is, assurance that changes in administration are not likely to bring dramatic change in labor's position or in the rules of the game.

These requirements are strikingly parallel to the conditions needed to get business to start investing again. Labor militancy -- workers' main line of defense against declining incomes -- can be seen as the counterpart to the business caution and capital flight that delayed supply response to partial reforms in many developing countries in the 1980s. Conversely, union acquiescence in wage restraint (to the extent that it is voluntary) is essentially an investment: current income and consumption are forgone in favor of expected greater returns later.

In some countries, cooperation might be encouraged by mechanisms to give labor fuller access to decisionmaking circles, while ways are sought to broaden labor leader's grasp of larger national problems. The corporatist arrangements of Northern and Western Europe are
suggestive but cannot be replicated -- certainly not rapidly or imposed primarily from above. (Schmitter 1981, emphasizes that the ruling elite has very limited ability to remold systems of party and interest intermediation, which are "the product of very lengthy and complex historical forces ... [and] are also subject to strong emergent organizational properties that guide their development and insulate them from ameliorative meddling from above.") But what is widely perceived as a long-term crisis simultaneously increases the importance of political influences on labor relations and opens the possibility of dialogue.

Labor cooperation would also be encouraged if governments -- and those advising them -- placed more emphasis on increased equity to balance insistence labor make sacrifices in the public interest. Recent analysis of the self-destructive "populist cycle" evident over the past forty years in several Latin American nations trace the roots of the cycle to marked and growing income inequalities and the resulting political pressures for redistributive policies to raise the incomes of poorer groups. Sachs (1989) puts great emphasis on this point; it is less prominent but clear in Dornbusch and Edwards (1989). More broadly as the corporatist model suggests, both institutional arrangements and policy outcomes must build up confidence that the benefits of economic reform and recovery will be widely shared. The modest measures likely to be feasible to increase equity in the 1990s -- more progressive taxation (or simply the enforcement of taxes on the books) and reorientation of social services to better serve the working class and the poor -- will not eliminate conflict over which groups bear the costs of adjustment. But such modest measures might reduce anger and distrust and improve the chances for constructive dialogue and bargaining.
Notes

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1. Wage push is inflationary pressure largely generated by a pattern of increases in real wages outstripping increases in productivity.

2. For an excellent brief discussion of democratic corporatism and its contrasts with other meanings of the term corporatism, see Katznein 1985, pp. 30-37.

3. This description of corporatist arrangements for labor policies is, of course, stylized. Institutional arrangements, policies, and economic outcomes vary among the nations usually described as fitting the model, especially the Scandinavian nations, Austria, Belgium, the Netherlands, and Switzerland. Within specific countries, the approach has been more effective at some times than at others. For example, Sweden is often taken as the epitome of effective corporatist arrangements of this kind, yet recent trends in Sweden suggest the model is no longer working very well.

4. The most extensive sets of data on union members as a proportion of the labor force are found in Taylor and Jodice (1983), and in U.S. CIA (1989), but the former is now dated (referring to the mid-1970s) and some of the data from the latter are startlingly out of line with other sources. For example, U.S. CIA (1989) gives Mexican union membership as 35 percent of the work force, compared with Middlebrook's (1989) figure for 1979 of 16.3 percent and George Grayson's estimate (given at a conference on Mexican trade unions at the Overseas Development Council in 1989) for the late 1980s of 20 percent. Recent data for many countries are also available in the periodic U.S. embassy reports for individual countries (U.S. Department of Labor various years); this source is the main basis for the estimates in the text for Argentina, Jamaica, and Venezuela.

5. A literal interpretation of the corporatist approach would not predict this outcome. But the corporatist line of explanation for unions and wage determination has concentrated on what was going on in the industrial democracies with very high degrees of centralization, and it has paid little attention to the range of incentives and strategies guiding union behavior where wage setting is decentralized. Had the focus been more on the decentralized cases (and, even more likely, had it been on developing country cases), the assumed monotonic links among decentralization, labor militancy, and wage push might have been modified. It seems self-evident that very small and scattered unions are not likely to exercise effective wage push, and plausible that they will be only sporadically and briefly militant.

6. This point was suggested by Kevin J. Middlebrook in correspondence with the author.

7. Heller and Tait's comparative study (1984) of public employment and pay is still the most comprehensive analysis available for developing nations, but it gives conflicting information regarding public and parasalarial wage levels compared to private nonagricultural wages. Direct comparisons of wage levels suggested that central government and nonfinancial public enterprise employees tended to be better paid than workers in private manufacturing (table 8, p. 18), but government employment constituted a larger share of total nonagricultural employment than did government wages as a share of total wages (p. 101).
References

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II -- POLITICS
THE ROLE OF TRADE UNIONS
IN MODERNIZING POLITICAL PARTIES

Dr. William A. Douglas

The dramatic shift from military dictatorships to civilian democracies in Latin America during the 1980s has been cause for jubilation among democratic trade unionists. It would be tragic if the region’s democratic efforts should fail in the 1990s. Unfortunately, the new democracies face some serious threats.

One obvious danger is that some Latin American economies might collapse under the strain of trying to service crushing debt burdens while simultaneously undergoing the restructuring required for stability, growth, and competitiveness. When economies flounder, often the incumbent political systems go down with them -- in this case the new democracies.

Another danger, less apparent because of the immediate concern over economic threats, is that a number of Latin America’s democratic political parties lack the characteristics needed to stay in power, govern effectively, and lead their nations out of debt, through restructuring, and into sustained and equitable development. To guide their nations out of crises, political movements need programs, and to develop these programs they need some basic philosophy for analyzing problems and devising solutions for them. Modern political parties are programmatic

- Personalistic vs. Programmatic Parties -

Unfortunately, many Latin American political parties are still personalistic, not programmatic in nature. What holds them together is not mística, that is, common belief -
certain ideological value, but simply a common desire to gain power and thus control the political spoils (el botin politico). They do not offer their nations vision and leadership, but simply practice patronage politics ("prebendalismo").

It is not policies or ideas that dominate the lives of these parties, but patron-client relationships. Often a party of this type is divided into two or more factions ("corrientes") each led by a political boss ("cacique"). A faction is often known by the personal name of its leader ("Fulanistas", "Menganistas"), not by some term indicating a difference in philosophy ("progressives", "developmentalists", etc.) Often there are no discernible differences in program between one faction and another.

The faction's boss and his immediate supporters constitute a clique ("argolla", "cupula", "trenza", "rosca", or "cogollo") which controls the faction in a top-down, authoritarian manner. In each state (departamento) the boss has his political client, who in turn is the patron of his own client at the province level, and so on, down through the municipal and neighborhood (barrio) levels.

The cement bonding this vertical chain of political connections is the patron-client relationship. Clients own loyalty, deference, and support to their patrons. In return, the patrons are obligated to offer services and favors to their clients: not only public employment for the clients themselves, but also jobs for the clients' unemployed relatives, hospital care for their sick children, public works for their neighborhoods, etc. In this kind of party, personal loyalties and obligations dominate, not ideas or programs. and such parties can therefore be accurately characterized as "personalistic".

This old-fashioned, personalistic patronage politics is typical of traditional, rural.
agricultural societies, whether revolving around the "county courthouse" in the rural United States of the last 1800s or around the "coroneles" (Colonels) in Bahia of the early 1900s who are described so well in the novels of Jorge Amado. Patronage machines also often appear during periods of migration into big cities, with the machines helping the migrants to make the transition to urban life -- in return for their political loyalty. Tammany Hall in New York City, and the early Daley machine in Chicago are examples.

Personalistic parties may have been appropriate for those social conditions, but they cannot possibly deal successfully with the present-day, complex crises of population explosion, external debt, economic restructuring, income distribution, and environmental degradation which confront Latin America today. Thus even if the present economic crises can be overcome, the modernization of political parties, changing them from personalistic to programmatic, is an absolute necessity if Latin America is not to regress to dictatorships (be they rightist or leftist) in the 1990s.

- Internal Party Democracy -

Changing political parties from personalistic to programmatic ones will involve many step, but probably the most useful one would be to increase the degree of internal democracy in the parties. If the party officials at each level do not control those at lower levels, then the chains of personal patron-client relationships are broken. It becomes much harder to build party machines or create political bosses, and with no basis on which to distribute the spoils, the practice of spoils-system politics ("prebendalismo") becomes somewhat pointless. With the cement of patron-client ties gone, a personalistic party will usually fall apart. Thus there are
virtually no personalistic parties with internal democracy.

If internal democracy can be introduced into a previously personalistic, machine-ridden party in a developing country, that party will either collapse, or find some new cement in order to survive. The only new cement available is some kind of mystique (mística) which imbues a party philosophy and program. Virtually all political parties in developing countries which have internal democracy are programmatic in nature. Thus increasing the degree of internal democracy is a good way to make a party less personalistic and more programmatic.

Because parties in some developed nations, particularly the United States, do not (for the moment) face such clusters of simultaneous crises as do the developing countries, they still enjoy the luxury of having internal democracy to the point of excess, without being obliged to become programmatic. Lacking either the cement of personalism or of program, U.S. parties survive only by being amorphous. That is not possible in a developing country.

Although most parties with internal democracy in developing countries are programmatic, it is unfortunately not true that all programmatic parties have internal democracy. The most obvious cases in point are the Communist parties, which have been run from the top down for decades, with the party Politburos allowing no independence by lower-level party officials. They have no internal democracy, but they are highly programmatic -- their mística being dogmatic Marxism-Leninism. In addition to the Communists, there are also all-too-many non-Communist programmatic parties in Latin America which are sadly lacking in internal democracy. This is why the best first step in changing a party from personalistic to programmatic is to increase the degree of internal democracy in the party. If we were to somehow make the party programmatic without democratizing it internally, we might end up he
the hapless Dr. Frankenstein — having created a monster.

Space does not permit a full discussion in this chapter of the features of internal party democracy. (That subject will be treated in a forthcoming new chapter for AIFLD's series of Education Manuals.) In summary, two of the most important reforms are:

- the introduction of primary elections to select the party's candidates for public office, rather than continuing to allow the party bosses to designate the nominees (a process often termed "dedocracia").

- the election of party officials at all levels by secret ballot, so that party bosses cannot tell if some of their clients have "disloyally" voted for candidates other than those backed by the party machine.

These types of reforms can produce party structures in which there are independent centers of power at all levels, so that party leaders will actually have to lead in order to win support from the party rank and file. They will no longer be able simply to order that support from their clients, and thus will no longer be able to run the party from the top down. Parties will have leaders instead of bosses ("caciques").

- Labor As a Catalyst for Party Reforms -

Unfortunately, there is little chance that party bosses will voluntarily reform themselves out of business -- the business of operating a political machine on the basis of spoils politics ("prebendalismo") is too lucrative. If the impulse for reform is unlikely to come from inside the party machines, then it must come from outside. The groups which are best-positioned to provide the impetus for the modernization of the parties are the interest groups in society.
especially the trade unions. They have contact with the more progressive parties, influence on them, and access to the party structures, without being part of the party machine and the spoils system ("prebendalismo"). Their access to an influence on the more progressive parties results from the dependency of those parties on the votes of the unions' members. (The more conservative parties need the votes of businessmen, and must therefore pay attention to business associations such as chambers of commerce and industry societies.) The trade unions are thus among the groups well-suited to providing part of the impetus for party modernization -- they have influence on some of the important political parties, but being once-removed from the spoils system they are more interested than can be those who are directly within the party machinery itself.

The past three decades have seen growth in both the number and degree of autonomy of interest groups such as trade unions in Latin American economies, which now have many sectors with many different interests. Manufacturers have different interests from financiers, and firms manufacturing mainly for export have different interests from those producing mainly for the domestic market. Small business and big business have different interests. Workers in the public and private sectors have different interests, as do peasants and urban workers. Each of these varied interests needs representation -- hence the proliferation of interest groups and their increasing assertiveness.

This development provides Latin American society with a new element of pluralism, breaking away from the state-corporatist tradition in which each social sector had a comprehensive guild (gremio) which was in turn controlled by the state. Today we see a wide variety of cooperatives, business associations, trade unions, and community associations in Latin
America that are free from government control. Not only do the autonomous interest groups provide an "infrastructure" for the dispersal of power in a pluralistic democracy, they also provide bases from which to launch campaigns to promote the party modernization which is necessary if the new democracies in Latin America are to succeed.

Trade unions should encourage their members to enter inside the parties of their personal choice and work there to promote two goals. First, the workers involved will want to swing the parties in support of the labor movement's own policy goals in such areas as income redistribution, social reforms, employment generation, and protection of worker rights. The worker activists will soon find that the personalistic parties are not interested in policy and program -- only in the spoils system. Frustration of their initiatives on behalf of progressive policy will lead the trade unionists toward the second goal -- transforming the parties into programmatic organizations. That in turn, they will discover, requires breaking the party machines and democratizing the parties' internal structures so that power passes from personalistic party bosses to the party membership, including the trade unionists active in party work.

As the trade unionists begin working toward greater internal party democracy their slogan should be "Program -- not spoils!" ("Programa -- no prebendas!"). Their initial efforts should be for adoption of primary elections to choose party nominees for public office, and of voting by secret ballot in the election of party officials.

Programs by trade unions to modernize political parties require a number of organizational steps, a full discussion of which is beyond the scope of this chapter. (They are covered in detail in Chapter II of AIFLD's Education Manual #20, Workers Political
Participation). Basically, the first step is for the unions to conduct training programs for their politically-active members covering the need to obtain party advocacy of labor's political program, the weaknesses in the parties' present structures, and how the proposed internal reforms could help remedy them. Then large numbers of the trained volunteers will have to join the party of their choice, working their way up into positions on the party’s neighborhood, municipal, district, departmental, and finally, national committees. Once many members of trade unions obtain such positions, they will have to set up some kind of caucus structure to devise a reform strategy and coordinate their efforts to carry it out.

All this amounts to a complex and time-consuming process for the trade unions and their political volunteers. However, if the labor movement does nothing about the personalistic (an often corrupt) nature of political parties at present -- except sit outside and complain about it -- then many of the new democratic experiments in Latin America will be doomed.

-Avoiding Pitfalls-

Even if the trade unions can be mobilized to make the effort, however, there is a big danger inherent in labor campaigns to modernize the parties. Who will change whom? Will the trade unions modernize the parties, or will the party machines just absorb, and possibly corrupt, the politically-active trade unionists? The political bosses who run the personalistic party machines are past masters at co-opting well-intentioned, but naive, individuals who enter into the parties intending to reform them.

The party bosses will try to gradually include the reformist "insurgents" in the distribution of political spoils. They will offer a favor here, a trip abroad there, and then a
chance to gain more political power by moving up in the party -- as long as the "reformist" forgets about reforms. Little-by-little, the "insurgent" becomes accustomed to the perquisites of power, and eventually he ends up just another party hack, absorbed into the political machine and its spoils system.

In extreme cases, the "insurgent" may be offered a spot on the party's list of candidates for the nation's congress. If he is elected, he then gets a generous salary, use of an official car, and a chance to make lucrative political contacts. The price of all this, of course, is forgetting about reforming the party.

Few people can resist the seductive blandishments offered by the party bosses. The phenomenon of a trade-union officer using the union as a springboard for launching his political career, and then forgetting his labor roots, is all too common in Latin America. (A cynic might argue that in this world the only people who are not opportunists are those who have not yet had the opportunity!) When Ulysses was on his return voyage back to Greece, and his ship had to pass by the island of the sirens, he knew that he would not be able to resist their calls. He ordered his men to tie him to the mast, so he could not succumb. If trade unions are to send their members into personalistic political parties, they must find ways to tie them to the mast of personal rectitude, thus keeping them loyal to the goal of party reform.

There are some practical steps which the trade unions can take to prevent the absorption of their politically-active members by the party machines. The basic condition, however, which is necessary if any of these steps are to succeed, is internal democracy within the union itself. A trade union or agricultural cooperative federation which is itself controlled by a few "bosses" and their clientilistic political machines cannot hope to democratize a political party. Until the
trade unions achieve their own internal democracy, they should not attempt programs of political action on the outside.

Assuming that a union is internally democratic, how can it "tie its members to the mast" when they enter into work with political parties? There is no one formula that can be applied mechanically in every country, but there are some factors which unions should consider when devising ways of dealing with the danger of being co-opted by party machines. For example, the degree of danger is least for workers who do not currently hold an elected position in their trade union. Party bosses have a much greater motive for co-opting union offices -- the party will give them perquisites, favors, and positions in the hope that those offices will then deliver the union’s support for the party in elections. Rank-and-file members are less interesting to the party bosses, because they are not in a position to determine their union’s political alignment. The trade unions should therefore put special stress on encouraging their rank-and-file members to become active in party work.

In those nations where trade-union officers, in addition to the rank-and-file, work at reform within the parties, they may find themselves in a conflict of interest, with their loyalties divided as they try to serve two masters. The job of a trade union is to voice the interests of a particular group of workers. In regard to politics, this means trying to get political parties to adopt policies that those workers need, and support only those parties which do include those policies in their platforms. The job of a party official, on the other hand, is to aggregate the (often-conflicting) demands of various interest groups into a balanced party program. Party leaders also want to win workers' votes for their parties, even when the platform their party adopts is not really very favorable to the workers they are trying to woo. If a person holds
office in both a trade union and a party, it can become unclear in some situations whether his or her primary responsibility is the voicing of the union members’ interests or the balancing of those interests against those of other groups to try to find winning platform for the party. In short, it can be unclear whether he or she is the party’s person in the union, or the union’s person in the party.

One way to deal with this conflict, when a trade union’s elected officers combine party and union positions, would be for the union to clarify that its officers should operate under the discipline of their union when they work in a political party. The crucial point in politics is not who occupies a certain position, but who controls that occupant. The union will often want to make sure that its officer is the union’s man in the party, not vice versa.

For example, suppose that Brother Fulano, who is the Secretary of Organization of a local trade union, also becomes the chairman of a political party’s local municipal organization. Under the model being suggested here for illustrative purposes, if the union is to help modernize the party, Brother Fulano should act under the union’s discipline in his party work. As long he is under union control, he can be a force both for bringing the party to adopt the policy stances labor favors, and for democratizing and thus modernizing the party. Without union control, he is more susceptible to being absorbed by the party machine, promoting policies opposed by this union but favored by the party bosses, so that he can retain the favors these bosses provide to their loyal clients.

One measure which can be suggested as an example of how to keep a union’s elected officers under labor discipline is to require that before they accept or compete for any position in the party, or before they accept the party’s nomination for public office, they would have to
obtain the prior approval of a majority of the union's assembly of delegates. Under this model the union would probably also require that this approval be renewed periodically. For example, if a union leader's term of office as a party official has expired, and he wishes to run again for that or some other party position, he could be required to obtain again the prior approval of his union's assembly of delegates. If he had not supported labor's policy program during this term as a party official the union's assembly of delegates would presumably be reluctant to give its approval.

(A requirement for approval by the full assembly of delegates would be preferable to simply requiring approval by the union's executive committee, because if the union's internal democracy were a bit weak, the members of that executive committee might all be political clients of the leader proposing to enter the party! In that case, the union would not really be able to control its officer in his party work.)

Naturally, even under this suggested procedure, if an officer of the union wishes to compete for a position in a political party, or accept its nomination for public office, even without getting approval from the union's assembly of delegates, like any citizen he would be free to do so, but the union's statutes under this model would require that he resign his union position in such a case. If a person wants to wear two hats, one as an official of his trade union, and another as an official of his political party, a union operating under the model presented here would want to make clear that he should be a trade unionist first, and that his political career must come second.

One of the most common methods by which party bosses succeed in absorbing reformist "insurgents" into their political machines is by offering them places on the party's list of
candidates for public office. Such offices, after all, offer far more prestige, power, and opportunities for personal enrichment than do positions in the party organization. When trade unions are especially fearful about co-optation of their officers who enter into party work, they could encourage them only to enter into the parties' organizations, not to accept party nominations for public office. In such situations the unions' statutes could require that their officers resign their union positions if they wished to accept party nominations for public offices.

Requirements of the types suggested above would allow many members -- and also some officers of trade unions, operating under labor discipline -- to enter the parties, serving on party committees at the municipal, district, departmental, and state levels, and pursuing internal democratization as a useful step towards the goal of changing parties from personalistic to programmatic entities. Again, the precise procedures used to govern this process will vary among countries.

If trade-union officers work within parties under the discipline of their unions, could that result in union control of the party? Our union's goal in encouraging workers to enter into parties, after all, is to reform those parties, not to win control of them for the union. Gaining such control of them for the union. Gaining such control would be neither desirable nor feasible. Union control of a party would blur the differing functions of the two organizations -- representing a particular interest, and mediating between various interests. A union-controlled party would also probably lose elections, given that the organized workers are only a minority of the electorate in any country. In any event, seldom can any one interest group hope to gain control of a major democratic party. Business associations may be major voices within conservative parties, and trade unions within progressive parties, but the political bases of almost
all major parties consist of amalgams of several interest groups.

- Taking Sides -

As trade unionists become active within democratic political parties with the intent of modernizing them, should the trade unionists, acting as a bloc, take sides in power struggles within the parties? Such leadership struggles are most evident when there are two or more persons competing for party's presidential nomination, but they also take place in less dramatic fashion at the regional and local levels within the party organizations. Whether the trade unionists should stay neutral or get involved in such struggles depends on the situation.

Suppose in a party which has been dominated by two or three factions ("tendencias", "corrientes"), each led by a personalistic boss ("cajique"), one of the bosses competing for the party's presidential nomination offers to support the trade unionists' proposed democratizing reforms in the party in return for labor's support of his candidacy. In such a situation, the trade unionists' proposed democratizing reforms in the party in return for labor's support of his candidacy. In such a situation, the trade unionists could advance their goal of party democratization and modernization by taking sides (assuming they can nail down iron-clad guarantees that the boss will make good on his reform promises if we win). For example, in Argentina at the end of the 1980s the trade unionists active in the Peronista party supported a group within the party called the "New Force", which promised to introduce internal primary elections to select the party's candidates for public office. With labor support, the New Force won, and did indeed institute the promised reforms.

To take another situation, suppose a political party in which many trade unionists are
active has a progressive wing, advocating policies which favor the workers, and a conservative
wing which reflects the interests of the wealthy classes. Clearly, the trade unionists would want
the progressives to win control of the party and its selection of candidates for public office. In
such a situation, the trade unionists will usually want to join in the fray, siding with the
progressives.

Suppose, however, that within a party an intense rivalry develops between two leaders,
both of whom favor the progressive national policies and the internal party reforms desired by
labor. If the labor caucus within the party, acting as a bloc, takes sides, the power struggle
could end up splitting the labor movement, or at least its political component active within the
party. An example of this is provided by the serious frictions within the Trade-Union Bureau
of Venezuela’s Accion Democratica party during the struggle in 1988 between Octavio Lepage
and Carlos Andres Perez for the party’s presidential nomination.

The above examples indicate that whether it is in labor’s interest to take sides in a given
party leadership struggle depends on whether there is some factor, such as concern for internal
party democratization, or for a progressive party platform, which creates a very ample consensus
among the trade unionists in favor of one side in the struggle. If two-thirds or more of the trade
unionists are in agreement on backing a given contender, then labor can often advance its
interests by taking sides, without major damage to the labor movement’s unity. If only a bare
majority within labor favors one side or the other, it will often be best for the trade-union bloc
in the party to remain neutral, freeing each trade unionist as an individual to cheer on whichever
candidate he or she personally favors. In deciding, in any given instance, whether to take sides,
the trade unionists should put a very high priority on maintaining labor unity, because when
weakened by division, labor can do little to advance any of its political goals.

Assuming that the trade unionists show reasonable skill in making such tactical decisions, by working within political parties to promote their internal democratization and modernization into programmatic organizations the labor movement can make a crucial contribution to strengthening many of the new democratic experiments in Latin America.
POLITICAL IMPLICATIONS OF ECONOMIC TRANSITION

John D. Sullivan
Center for International Private Enterprise
May 26, 1991

Paper for the Central & Eastern European Institutes Meeting
International Center for Economic Growth
Poland
INTRODUCTION

One hundred years ago, Pope Leo XIII warned the world about Marxism in his famous encyclical, *Rerum Novarum* (New Things). That encyclical placed the Roman Catholic Church in the center of the ideological struggle that has, in many ways, defined the twentieth century. Pope Leo also lent the Church’s support to the cause of the labor union movement while maintaining the rights of private property. In this way, the Church hoped to indicate the foundations of a just society.

Now, at the close of the century, his successor, Pope John Paul II has once again placed the Catholic Church in the center of debate in his encyclical, *Centesimus Annus* (One Hundred Years). In his reaffirmation of Pope Leo’s work, Pope John Paul pledges the Church’s support for market-based democratic systems and reiterates the dangers of the totalitarian state and the command economy. However, he also believes that market economics alone is not a sufficient basis for the structure of human society. The Pope does not offer yet another model. Instead, he both upholds the role of competitive markets and the necessity for governmental programs to take care of those in need.

Explicit in the Pope’s encyclical is the recognition that economic systems do not exist in a vacuum. Rather they are embedded within and structured by the overall society of which they are a part. One passage from *Centesimus Annus* is worth quoting at length:

*Rerum Novarum* is opposed to state control of the means of production, which would reduce every citizen to being a ‘cog’ in the state machine. It is no less forceful in criticizing a concept of the state which completely excludes the economic sector from the state’s range of interest and action. There is certainly a legitimate sphere of autonomy in economic life which the state should not enter. The state, however, has the task of determining the juridical framework within which economic affairs are to be conducted.
and thus of safeguarding the prerequisites of a free economy, which presumes a certain equality between the parties such that one party would not be so powerful as practically to reduce the other to subservience. (1)

In developing the encyclical, the Pope drew on his own experiences in Cracow, Poland where he served as Bishop during some of the darkest days of the old regime. In addition, the Pope consulted with a large number of economists, philosophers and church leaders. Whatever its source, Centesim Annus resonates with the new institutional approaches to the study of politics, economics, and governance. Central to this school of thought is the idea that the laws, rules and regulations established mainly through governmental processes create the structure of an economic system. Many of reforms currently under debate in Central and Eastern Europe are of an institutional nature including property rights, contract law, financial systems, and company law.

In short, the new institutionalists reject what Ronald Coase so aptly called "blackboard economics": the derivation of policy prescriptions from highly abstract theoretical models that are divorced from every day life in national systems. (2) Like the Pope, institutional scholars point to the necessity of creating rules to create and govern the economic system in any society. The tendency to separate economic, political, and social affairs into individual spheres is dangerous. It is doubly so in the context of the transformation unfolding in Central and Eastern Europe. Only by looking at the intimate linkages between political and the economic subsystems can programs be designed to support the process of system transformation. Unfortunately, this is a message that has yet to be accepted by official policy in many Western assistance agencies.
For some time in the united and in many of the international agencies, there has been an extended debate about the nature of the linkage between democracy and market-based economic systems. One side of the debate pointed to the fact that all of the stable democracies are also market economies. The other side was quick to point that this was an accident of history. They pointed to the newly industrializing countries of Asia and to Chile under General Pinchet as evidence that market-based economics could co-exist with authoritarian governments.

One of the results of the peaceful revolutions in Central and Eastern Europe has been to demonstrate that there are connections between the political and economic spheres. In the words of Hungarian Prime Minister Jozsel Antall:

Freedom and independence in the Eastern region of Europe would never have come about had not the political, social and economic structure of what was once referred to as the Socialist camp collapsed. If 'political' Communism and planned economies had not been shaken and rendered inoperable, then the minds of the reform Communists would not have been 'enlightened', meaning they could not even have voiced what reforms they envisioned. They would not have chosen a relatively peaceful mode of transferring power, since no 'ruling class' or 'elite' in history -- least of all one in a country ruled by a one-party system -- has ever handed over power in a situation where the economy flourished and the political cogs worked efficiently. In our part of the world, political freedom is therefore linked to economic breakdown. (Emphasis added)

Nevertheless, the relationship between politics and economics is not well understood, especially in democratic or transforming economies. One of the purposes of this paper is to explore some of these linkages and to suggest areas where more attention needs to be paid. This is important for both policy formation and programs to build market-based democratic systems. In addition, the paper will also look into the political implications of the economic transitions in the region and their impact on the construction of stable democratic societies.
ATTITUDES TOWARD THE TRANSITION PROCESS

Whatever one's view of Centesimus Annus, the encyclical shows that the debate over the structure of society is far from over, especially in the countries of Central and Eastern Europe. While there is agreement that communism has failed, the question of what the nature of a new society should be is still to be decided. Recent public opinion polling data confirm the politically charged nature of this debate within the emerging democracies of the region. In January of 1991, a poll conducted by Penn & Schoen in collaboration with firms in the Czech and Slovak Federative Republic (CSFR), Hungary, and Poland found that the public was split over the desire for a free market versus a mixed economy. The results show that the publics are split down the middle, as follows:(4)
**Alternative Systems**

Q: In general, do you prefer a socialist economy, a free-market economy, or a mixed socialist and free-market economy?

<table>
<thead>
<tr>
<th>Country</th>
<th>Socialist</th>
<th>Free Market</th>
<th>Mixed</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary</td>
<td>4%</td>
<td>43%</td>
<td>44%</td>
<td>9%</td>
</tr>
<tr>
<td>Poland</td>
<td>3%</td>
<td>47%</td>
<td>39%</td>
<td>11%</td>
</tr>
<tr>
<td>CSFR</td>
<td>4%</td>
<td>48%</td>
<td>36%</td>
<td>12%</td>
</tr>
</tbody>
</table>

Furthermore, while there is strong support for a democratic system, significant percentages still express considerable uncertainty as shown in the following series of questions: (5)

**Democratic Systems and Economics**

Q: Can democracy work in a country with serious economic problems or does it only work in rich countries?

<table>
<thead>
<tr>
<th>Country</th>
<th>Can Work</th>
<th>Only rich countries</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary</td>
<td>43%</td>
<td>42%</td>
<td>15%</td>
</tr>
<tr>
<td>Poland</td>
<td>59%</td>
<td>26%</td>
<td>15%</td>
</tr>
<tr>
<td>CSFR</td>
<td>73%</td>
<td>16%</td>
<td>10%</td>
</tr>
</tbody>
</table>

Q: Right now, would you say that our country's democracy is working or does it have serious problems?

<table>
<thead>
<tr>
<th>Country</th>
<th>Working</th>
<th>Serious Problems</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary</td>
<td>18%</td>
<td>69%</td>
<td>13%</td>
</tr>
<tr>
<td>Poland</td>
<td>15%</td>
<td>60%</td>
<td>25%</td>
</tr>
<tr>
<td>CSFR</td>
<td>8%</td>
<td>83%</td>
<td>10%</td>
</tr>
</tbody>
</table>

Q: Do you think that the present government can work to bring economic prosperity or is a stronger kind of government needed to bring prosperity?

<table>
<thead>
<tr>
<th>Country</th>
<th>Economic Prosperity</th>
<th>Stronger Government</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary</td>
<td>22%</td>
<td>68%</td>
<td>10%</td>
</tr>
<tr>
<td>Poland</td>
<td>40%</td>
<td>33%</td>
<td>27%</td>
</tr>
<tr>
<td>CSFR</td>
<td>40%</td>
<td>37%</td>
<td>23%</td>
</tr>
</tbody>
</table>
Polling data is not available for Bulgaria and Romania. However, the results of recent elections confirm that there are mixed feelings about the transition from the existing system into an uncertain future. In each country, the democratic opposition parties tended to do well among and most highly educated, the youth, and the urban populations. However, the fear of change and the relative unknown nature of the opposition figures appears to have lead the majority of the population to vote for the "reformed" communists (renamed socialists). The situation of Yugoslavia is much more complex as will be discussed below.

The fact that there is little support for the old regime hasn't translated into consensus on the shape of a new system of politics and economy. Hence, there is even more reasons for a clear view of the nature and functioning of a democratic, market-based system.

APPROACHES TO DEMOCRACY AND ECONOMICS

Fundamentally, democracy is a system of government. As such, the design of a democratic system has to consider the rules for structuring economic, judicial, social, and political relations. However, in recent times the formal study of democratic theory has been limit to the study of elections, political processes, and basic freedoms. Typically that has meant looking at democracy in terms of the types of criteria listed below: (6)
Standard Criteria for a Democratic System

1. Freedom to form and join organizations
2. Freedom of expression
3. The right to vote
4. Eligibility for public office
5. The right of political leaders to compete for support
6. Alternative sources of information
7. Free and fair elections
8. Institutions for making government policies depend on votes and other expressions.

Recently, the above criteria were set into the form of a scale to see how various countries would measure up. The results showed that in 1985:

- 41 countries met all of the criteria,
- 10 countries fit nearly all criteria (some limitations on freedom of information with preferential treatment given to official views),
- 9 countries fit most of the criteria (some limitations on freedom of expression and information).
However, of the 60 countries which met all or most of the criteria, 10 had recently gone through a transition from an authoritarian system to a democratic system and one (Colombia) had a very severe internal conflict situation. Clearly, something is missing from an analysis of democracy that does not distinguish between countries like Argentina and Switzerland where one has had frequent bouts of repression and the other has had a long history of continuous democratic rule. Taking the point further, both Brazil and Costa Rica are given the same rating under the standard democracy definition despite Costa Rica’s track record as the only stable democracy within Latin America throughout the last forty years compared to Brazil’s history of military rule. What then accounts for the relative stability of some democratic systems and the frequent suspension of democracy in other countries?

**Independent Associations and Democratic Stability**

Part of the answer to the sources of democratic stability lies in the first criteria, the freedom to form and join organizations. Alexis de Tocqueville, for example, documented the rich associational life in the United States as early as the 1830s. He found that associations played a vital role in limiting the scope of centralized governmental power. Further, based upon their every-day functions, such associations also played a political role. However, it was their non-governmental roles which provided an essential basis for democratic society. (8)

It is surely no accident that totalitarian and, to a lesser extent, authoritarian regimes destroy or subvert independent associations. Nearly all independent organizations and associations were destroyed by Adolph Hitler within a few years of assuming power in Germany. Similarly, the various communist or Marxist regimes throughout the world have
created their own youth organizations, unions, educational societies, political parties, and the like. Needless to say, such regimes don't tolerate the existence of competing organizations not under their direct control. As William Kornhauser pointed over thirty years ago, totalitarian and authoritarian regimes utilize such organizations as a means of mobilizing and controlling the population in support of official policy. (9)

Part of the source of long-term stability in democratic societies is the extent to which voluntary organizations such as private enterprise business associations, churches, unions, civil societies, and other non-governmental organizations have a free and independent existence. One of the most immediate needs in the Central and Eastern European context, is to support the re-emergence of associations and non-governmental organizations as is well recognized within each country. In fact, in Poland, Hungary, and the Czech and Slovak Federative Republic, it was these very groups which negotiated the exit from power of the old order. The task now is to further expand independent groups in both the political and non-political areas of civil society.

**Democracy and Governance**

Another important factor to consider in distinguishing between stabled democratic regimes like Switzerland or Costa Rica and those countries which fail to consolidate democracy is the question of governmental style. If democracy is not simply a question of procedures for choosing leaders what then constitutes democratic governance? A complete answer is yet to be developed. However, some characteristics of the day-to-day process of government commonly employed in stable democracies can be identified as follows:
• Equal access to the legal system for all citizens, including the right to seek redress against the government itself (Many countries prohibit citizens from suing the government).

• A clear division of authority between the legislative and executive powers of government whereby laws and regulations must have the prior authorization of the legislative body. (Many countries allow the executive to issue binding decrees without prior legislative action.)

• The right of citizens to participate in the formation of regulations through comment and notice periods or other open decision making processes. (This limits the ability of agencies of government to make binding regulations without citizen input.)

• Independent local governments, directly elected, with their own formal areas of authority.

Such practices are not always part of the constitutions of democratic societies. Rather, they have been worked out over long periods of time. In fact, the Peruvian scholar, Hernando de Soto, a keen observer of democratic practices in the industrialized democracies has commented that few people in the stable democracies can actually explain how these countries make decisions on a day-to-day basis. He also points out that the lack of procedures like those described above has inhibited the formation of stable democratic systems and is associated with pervasive corruption in many developing countries. As de Soto has said, the result is often the democratic election of a dictator who governs by decree. (10)

Democracy, of course, is not an all or nothing condition. Countries like France have, in recent times, gone back and forth in terms of the degree of civil liberties and have even experienced fundamental changes in their election and governmental systems. The open question at this point is: to what extent are such countries fully democratic in terms of their day-to-day practices of governance? While the four conditions listed above have a certain common sense
appeal, the exact relationship to the consolidation and maintenance of democracy needs to be fully explored.

**Democracy and Economic Systems**

The relationship, or lack thereof, between a democratic society and the type of economic system is a central part of the search for the sources of democratic stability. The former regimes in Central and Eastern Europe were all command economies. In fact, it was the use of economic levers that allowed the regimes to control the bulk of the population, not simply the use of police force. The central question, however, is what type of economic system should replace the old system in order to support a democratic society.

At a minimum, it can be said that the existing stable democracies are based upon economic systems which have a private business base, encourage entrepreneurship, and prevent the emergence of concentrated economic power. Part of the reasons for this relationship is that a private enterprise system is probably essential to sustain the non-governmental associations discussed above. In fact, one area further analysis might be the degree to which civil society organizations (de Tocqueville's associations) require the support of independent private businesses, unions, and other economic groups. In many western societies, especially the United States, it is the private business owner, independent farmer, or labor union leader who provides the financial support and, often, the leadership for such groups.

In addition, there is some degree of relationship between freedom to engage in economic activities and the style of governance described earlier. It is likely that a fully democratic style of day-to-day decision making is compatible with a variety of more or less market-oriented
economic systems. For example, the economic systems of the United States, Germany, and Japan, while having a number of elements in common, are still quite different. A number of the European countries practice a form of corporatist decision making between the government, labor unions, and business associations that isn’t possible under the more laissez-faire systems.

(II) Similarly, United States anti-trust law prevents the formation of many of the cartel arrangements existing in Europe or Japan.

The question of public ownership of large industrial enterprises is a more murky area. In the continental European democracies, many countries have followed a pattern of state-owned firms accounting for as much as 20 percent of gross capital formation. (12) Stable democracies, in comparison to the authoritarian regimes that have followed a state capitalist type of economic system, seem to have worked out mechanisms to prevent the manipulation of public enterprise by political leaders as a means of maintaining power. In short, within a democratic system political leaders must face the same degree of accountability for all areas of economic policy that they face in any other area of public life.

In the context of the transformation of socialist economies, it will be vital to work out the means of regulating and controlling the relation between ministries, parties, and state-firms. One approach that was highly recommended, even in the West, was the Yugoslav system of self-management. In fact, this method is under consideration into the Soviet Union even now. For a number of years there has been a debate over the proposition that the Yugoslav style could support a democratic system. (13) The question was whether the dispersion of economic decision making out of the hands of the central government and one-party political system would be a sufficient basis for democratic governance. In effect, the dispersion of economic power
would prevent the rise of non-democratic state. In practice, it seems that the communist party was able to manipulate self-management through the *nomenklatura* system so that the system was reduced to a form of oligarchy. The results point to the need to work out an open and fully accountable system of corporate governance for both state firms and firms undergoing privatization.

The full implications of issues of the relations between governance practices, civic society groups, the existence of private enterprise firms and business associations, and type of market-based economic system need to be more fully worked out in the context of the transitions in Central and Eastern Europe. As the polling data demonstrates, public opinion in several countries is split in terms of the type of economic system they would like to adopt. The issue that must be faced is to what extent is a mixture of market-oriented system and socialism compatible with the desire to build a democratic society?

**SUPPORTING THE TRANSITION PROCESS**

The transition from communist regimes to democratic, market-based systems will require continuous efforts to gain public support for change and build understanding of the emerging new systems. The public opinion data cited above shows that public support is split and that there are deeply felt concerns about the way their emerging democracies are performing. As the transition process unfolds, other concerns will surface. Some of these can be anticipated but others will be unexpected.
Public Concerns About the Transition Process

In 1989 and early 1990, there was an expectation within the Western governments and multilateral organizations, shared by many private economists, that the transformation to market-based economic system could be effected fairly quickly. Now it appears that there is a growing recognition that it may take several decades for Central and Eastern Europe to approach the per capita income levels and economic structures of the industrialized countries. One of the most telling indicators of shifting official opinion is the reversal in the operating guidelines of the German Treuhandanstalt from pure market driven policies to continuing to support failing firms. (14) This decision may re-ignite the debates over a "big bang" approach to transformation versus the go-slow school of gradualism. (15) In fact, at the recent World Bank annual economic development conference some of these debates appear to have begun.

Not surprisingly, the same issues will play out in Central and Eastern Europe. For example, one of the questions in the January 1991 Penn & Schoen poll found mixed views about the speed of reform. (16)

<table>
<thead>
<tr>
<th>Country</th>
<th>Too Fast</th>
<th>Right Speed</th>
<th>Not Fast Enough</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary</td>
<td>18%</td>
<td>9%</td>
<td>70%</td>
<td>3%</td>
</tr>
<tr>
<td>Poland</td>
<td>8</td>
<td>20</td>
<td>63</td>
<td>8%</td>
</tr>
<tr>
<td>CSFR</td>
<td>40</td>
<td>17</td>
<td>35</td>
<td>9%</td>
</tr>
</tbody>
</table>
The data suggest that public support for radical transformation efforts are greatest in Poland Hungary while the people of the CSFR are more hesitant about taking the plunge all at once. In fact, the Czech people were about twice as likely to support a faster pace of change than those in Slovakia. Comparable data is not available for Bulgaria and Romania but the election results appear to confirm a fear of rapid change. The same pattern is probably behind the results of the recent election in Albania.

Other issues that are like to merge as a result of the transformation process underway include:

• Public support for rapid privatization of large companies may decline as unemployment increases.

Most of the large state-owned firms in the region have at least 30 to 40 percent more employees than can be sustained profitably. At a minimum, significant cutbacks will have to occur in order to survive. However, a significant percentage of the firms won’t be able to survive under a pure market-based regime (i.e. without subsidies or protection). If these firms are close then unemployment may rise further.

• As private entrepreneurs and skilled professionals gain a market-based income, public attitudes toward income differentials may shift.

For more than forty years, income distribution was fairly even as a result of controlled wages. It is an open question as the public’s reaction to the emergence of income differentials for entrepreneurs, doctors, and other professionals.

• Public anger against the former nomenklatura and party officials may increase depending upon their fate.

Given the shortage of skills and experience in management, foreign trade, languages, and other skills in society, the old elite may make out fairly well under a market system. If the benefits of transition appear to be too heavily skewed toward the old elite, populism may increase further.

• The lack of social support for education, housing, and health care may lead to demands for solutions faster than the transition process will allow.
Each country in the region, to some degree faces severe shortages in all of the social services. Housing and health care issues are a particular problem for the younger generation cut off from the subsidies of the past. For the moment, most people are prepared to wait for improvements but the potential for extremist parties to exploit the situation is a danger.

Building Civil Society

Under the old regime, leading public opinion and providing support for policy initiatives was the sole responsibility of the party and state officials. Part of the dilemma of the transition, however, is that the private sector organizations must assume new roles befitting a democratic society before the transition to democracy is consolidated. In short, private business associations, public policy research centers, unions, civil associations, and other non-governmental groups have to begin playing a role as the process of change unfolds.

The magnitude of the challenge faced by the newly constituted private groups is enormous. In order to begin shaping public policy, the new private business associations will need:

- Recruit members from the emerging private business sector.
- Establish mechanisms to identify members’ views on economic issues, formulate potential solutions, mobilize membership support for these positions, and communicate to parliament and the executive.
- Provide services to members and potential members including entrepreneurship training, access to capital, and information on domestic and international markets.
- Identify sources of funding for programs since their members’ ability to support projects will be limited for some years to come.

Similar challenges face the new unions, civil groups, public policy institutes, and other organizations.
In addition, the new private groups will face another challenge as the process of change unfolds. One of the mainstays of a democratic system is the process of socializing or educating the next generation into the ethics, values and beliefs that sustain the system. In the stable democracies, this task is normally undertaken by the family, the educational system, and (often) the religious community. Private organizations such as business associations play a supportive role with programs like youth entrepreneurship or future farmers. In the stable democracies, however, private groups are working with youth that have already been exposed to the basics. In the context of the transition process, both the existing and future generations will have to be reached.

The task of the civic society groups is made both more difficult and more important by the fact that political party structures of each country are only now being formed. The process of party formation is furthest along in Poland and Hungary but even here there are significant challenges. With the emergence of full political freedom, over 60 parties have been created in Poland alone. In Hungary, the governing party, the Hungarian Democratic Forum, is actually a coalition of divergent groups which may or may not split to form alternative coalitions or parties. In this context, private associations take on another role -- helping to form the basis for new political party structures. However, it is vital that the associations not become simply an appendage of a party in order to retain their non-governmental status.

Establishing Democratic Governance

As noted above, the day-to-day process of making decisions in a democratic society is based on the principle of participation. The mechanisms of equal access to justice, regulatory
hearings, legislative processes, and local government are but a few of the procedures that need to be put in place.

At a more fundamental level, the basic concept of law and regulation must be changed and thousands of governmental officials must be re-oriented. To cite one example, Poland’s "Law on Economic Activity of December 23, 1988" contains the following passage:

Within the scope of their economic activity, economic subjects may perform operations and actions which are not forbidden by law.

One raised in a democratic society would find the passage slightly odd. The clear expectation in such societies is that all actions not forbidden by law are allowed. Indeed, that expectation is at the heart of private, individual initiative. Apparently, the converse rule has been applied in Poland and many other command economies. That is, only those actions specifically authorized by law, regulation, or written permission are allowed.(17)

Many regulations from the preceding era can be simply be abolished in order to take the government out of many economic and social areas that are best left to individual initiative. In other cases, however, it will be essential to create a new, market-oriented regime of rules and regulations. Finance, insurance, and accountancy are three institutions that require enabling legislation and regulation to exist. That is, the very establishment of the financial system requires a set of rules that will govern and bind transactions. Other rules that need to be recast include the procedures for contracts, corporate governance, basic business law, and the like.

The key to establishing a fair and workable system is to create the new rules based on feedback from the people. All of the day-to-day decision making procedures described above are based on a simple principle. In formulating rules, it is essential to allow for comment by
all those affected. No government decision maker or academic expert can have enough knowledge or wisdom to design a system in isolation. It is essential to capture the knowledge and experience of those that have to live with the new procedures. Further, it is essential to continuously re-examine the rules to see if they work and, if not, make changes based on experience.

CONCLUSION

Vaclav Klaus, the Finance Minister of the Czech and Slovak Federative Republic, has used the analogy of a chess game when talking about economic transformation. He points out that its not necessary to know all of the moves in detail far in advance. Rather, all that one has to do and, in fact, all that one can do, is to know the rules, the first couple of moves, and what you want to accomplish. As the process unfolds a certain logic will develop that indicates what the next series of moves should be.

Minister Klaus is undoubtedly correct. Systematic change is as much of an art as it is a science. However, in the context of Central and Eastern Europe, the transformation has to be thought of as a multi-dimensional game of chess. One level is played according to the logic of economics and others according to the newly adopted logic of democratic politics. Some of the connections that have to be put into place between the levels of the chess game include:

- Creating procedures for democratic decision making on a day-to-day basis such as regulatory hearings and access to lawmakers.
- Establishing and sustaining the "infrastructure of democracy" including private business associations, unions, civil groups and other civil society organizations.
- Building public understanding of and support for the policy and structural changes involved in creating a market system. In effect, creating constituencies supportive of political, economic, and social reform.
NOTES


(4) "Democracy, Economic Reform and Western Assistance in Czechoslovakia, Hungary and Poland," Conducted and Prepared for Freedom House and The American Jewish Committee by Penn + Schoen Associates, Inc. in Cooperation with the Association for Independent Social Analysis (CSFR), Demoskop Research Agency (Poland), and Median, Inc. (Hungary), released April 1. Field work conducted during January 1991. Sample size 3,533 face-to-face interviews. p. 31.

(5) Penn + Schoen, pp. 23-25.


(11) Harmon Ziegler, *Pluralism, Corporatism, and Confucianism*, (Political Association and Conflict Regulation in the United States, Europe, and Taiwan), Philadelphia,


(16) Penn + Schoen, p. 20.

(17) The implications of cultural patterns have not been explored in this paper but are of great importance. Aaron Wildavsky and his associates have recently published an important study on the differences between an individualistic and a hierarchical cultural pattern. See Michael Thompson, Richard Ellis, and Aaron Wildavsky, *Cultural Theory*, Bolder, Co.: Westview Press, 1990.
III -- DEVELOPMENT
TRADE UNIONS AND DEVELOPMENT:

The Challenge of the 1990s

Rubén Rotondaro

INTRODUCTION:

The economic, social and political events that have been taking place since the beginning of the 1980s, have significantly changed the nature and scope of development. Today, development models, in contrast with the past, cannot be designed on ideological grounds, or as part of propaganda efforts to demonstrate the effectiveness of a particular authoritarian or totalitarian regime.

These circumstances have overshadowed the real meaning of development and the true purpose of engaging in economic growth. Another new feature is the increasing awareness of the limits on the utilization of available resources. Before, it was simply a matter of increasing production, the more investment and the more resources utilized, the more products and services were turned out. Increased attention to environmental issues has forced us to reexamine the nature and degree of development and the limits on how far it can go. Pollution of the air, rivers and seas, and the tragic consequences of building thousands of plants and industrial units without any regard to their impact on the human habitat or their threat to the health and well-being on the planet, compel us to reconsider the ways in which we design development projects. However, recognition of these new parameters does not change the fact that the central core of development is the search for more effective and efficient means to achieve a better life for mankind.

The purpose of this article is to bring up to date the old verities and basic concepts related to development. It is not feasible to consider development from a purely political point of
view or from a narrow economic approach rather, development must now be viewed as the essence of any economic system and a participatory experience in which all sectors of the society must become involved. The purpose of development is not just to get high growth rates for a given economy, but to continue trying to construct a social economy, the fabric of which is woven by the combined participation of all sectors of the society. Ideology and development do not go together. Development does not result from ideologues testing out their social hypotheses or trying to justify greed by characterizing it as "a driving force for entrepreneurship". Development should be as a quest to build an economic and social system which embraces the fundamental concepts of a pluralistic society. It requires groups of different kinds acting on behalf of their constituents, but with the understanding that coexistence is the rule, not the exception. Coexistence, in development terms, is a participatory process in which many sectors operate, most importantly government, employers and unions. Lack of participation would lead to exploitation, misery and social disruption as a consequence of strife.

Now the basic question for trade unions is: How can they develop strategies for operating in this kind of environment? How far can their leaders go, as representatives of workers, in reacting to changes in the production system, to the endless process of innovation, and to the complexities of the modern global economy? What sort of policies can they implement to cope with these problems? If we redefine development as a continuous process by which human beings advance in their search for knowledge, and a better life, and as a continuous movement toward new paths of social achievement, we realize that there has to be a rather broad set of alternative means to make development feasible. If it is not possible to
eliminate social pains, at least it is worthwhile alleviating their impact or building defenses to off-set their more serious consequences. In this article we will try to discuss some of these alternatives and new avenues which could make this world a better one in which to live.

DEFINITION OF DEVELOPMENT:

There has been a considerable amount of literature with regard to the definition of development. Development has been considered as part of macroeconomic analysis and studied mainly at the economic departments of various educational institutions. The study has become more a matter of measuring performance, through mathematical synthesis, a sort of mechanistic approach, considering only parts of development’s elements rather all of its ingredients. The schools of economic thought involved in these discussions have grouped themselves like religious sects - engaging in myopic analysis of the phenomena of development as Marxists, monetarists, anti-dependency theoreticians, or neoliberals. They have all spent considerable time and energy illustrating their views and trying to influence the paths that emerging nations follow in building their economies. All of these ideological interpretations lacked an understanding of the complexity of the issues unleashed by the development process. In that respect one of the most interesting and refreshing analyses of the nature of development has been provided by Professor Josef Solterer while he was working in the Economics Department of Georgetown University and later as an instructor for the American Institute for Free Labor Development. Following in the steps of Joseph

Schumpeter, Solterer centered his research in the evolutionary trend that provided a logical explanation of how events flow in modern civilization. It is not a mechanistic course that society obligatorily must follow, as Marx tried to establish in his messianic interpretation of the structures built by the new forms of production, nor the historical sequences arbitrarily outlined by Rostow in his essay on the stages of growth. The Schumpeterian contribution to economic science was precisely the understanding that the circular flow that carries the blood of economic activity is not a permanent one but is subject to change. From time to time, an innovator breaks in, establishing new sources of activities and hence, initiating a new pattern of circular flow. Solterer went further into the analysis of innovation, showing that it is absorbed into economic activity through the creation of new wealth provided by non-monetary finance. Solterer realized that the economy was built upon layers provided by previous economic activities. He saw the process as analogous to the one human knowledge followed, from the beginning of sensation and feeling to the whole process of abstract thought. This process of thinking is instrumental in the search for knowledge and its application as technology. Going further in his analysis, Solterer draws another analogy from physics, which distinguishes between what a particle is and what constitutes a field. A particle is a finite piece of matter of negligible size, though with other attributes, such as

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mass and an electric charge. A field is a substratum, that is to say one of the foundations on which everything lies. It is infinite.5

According to Solterer, there are four elementary economic factors, including two in the short run (value and income), and two in the long run (assets and liquidity). They are the results of the elementary action of interchange (commerce and production), circulation (GNP), innovation (new assets) and absorption (money and finance). Each of these four elementary actions and its result is a necessary part of the social economy and always appearing together with and influencing the others.

Solterer deals with the connection of scientific laws in the economic sciences: Scientific laws - he said - describe a limited set of well defined relations and their connections which are capable of being observed under particular controlled conditions, permitting forecasting. There are three key elements in this definition: 1) limited, 2) observed, and 3) controlled. The term limited confirms that there is not a single scientific law but there are as many as the natural sciences, the law of gravitation, the electrical laws, the chemical laws and others.

The terms observed and controlled imply the possibility of repetition and reversal of actions in order to test the validity of a statement of a law in various directions. These possibilities of repetition and reversal introduce, in turn, various time ranges within which they exist.

Economists - Solterer says - have been aware of this distinction at least since the work of

5 Webster New World Dictionary

6 Solterer, op. cit. From page 8-18 we summarize Solterer’s ideas outlined in his notes and study material quoting him extensively as to present his thoughts in a clearer way.
Marshall in the 19th Century. They distinguished between the short run and the long run within which repetition and reversal are possible.

Solterer goes on tracing an analogy with what happened in the physical sciences. This distinction and implied beginning and end of objects, emerged only with subatomic physics. Classical physics dealt only with existing objects, and not with their creation or destruction. The familiar natural forces, the gravitation force and the electromagnetic force and their laws, are familiar because they have a long time range so we can feel them in everyday life. The more recondite forces, the strong and weak nuclear forces which bind particles together or annihilate them by radiation, have such a short time range that these objects can be observed only in physics laboratories. Beyond these varying objects and their objects, there are indications that there is a substratum with an indefinitely long range which does not take on the form of an object with mass. Physics called it field. It is timeless, existing at a time but not during finite time.

The scientific laws have a common characteristic feature: They must hold if the order of procedure is reversed and repeated. The condition can be expressed more generally by a statement that some things appear to be the same, no matter how you look at them; or in a more limited way, that there are certain different ways you can look at a thing and it will appear the same. This feature of things and their scientific laws is called symmetry.

There are several kinds of symmetries, according to the motion involved: reversal in time or space, or other motions therein called space or time symmetries. Furthermore, symmetries relative to changes of state, called gauge symmetries in nuclear physics, are involved in the absorption of economic innovation.
The substratum in physics, capital in economics, and the other fields in existence, exhibit the highest degree of symmetry. They are only forces, and no more finite particles. As indicated before, there are a number of internal and other symmetries. Everyone of them generates a conservation law. In physics, conservation of mass, energy, momentum and electrical charge. These conservation laws have long since been recognized as fundamental objective knowledge.

One of these is the ethical sphere of economic life: justice in exchange - symmetrical relation in which buyers and sellers, and sellers and buyers of the two - objects trade peacefully.

If each party claimed the knowledge of a true symmetry but different from the other, we will come to the ideological struggle, in which case, there can be no resolution of the strife, short of the annihilation of one party. Marx's theory of class struggle would fall in this category. By the same token, the exploitation of workers in an open and uncontrolled market falls in that category.

The central problem of development: is how are conflicting symmetries reconciled to result in the common increase of assets, including human capital? How are we to arrive at this good? It is not a question of greater efficiency, lesser exploitation and fuller employment of existing resources - the short run symmetries of table B - below but of the creation, not production, of new assets and their liquidities - the long run case - in which the mixture of gain and losses from unpredictable innovation, their braking older symmetries in the future are the determining factors in the appearance of new wealth.
Every symmetry generates a conservation law which is the link between scientific and ethical obligations. What are these symmetries in economics? In the short run they are the assets, exchange (value) and income. In the long run, they are asset creation and liquidity (money).

Naturally, symmetries can conflict. The resolution of this problem is the core of the development theory. Conflicts and diversity of interest can exist within the framework of a consensus that would prevent disruption and annihilation of one group by another.

Soliterer summarizes his theory in the following charts:
<table>
<thead>
<tr>
<th>Basic Economic Action</th>
<th>Result</th>
<th>Results of Non Participation</th>
<th>Union Role</th>
<th>Radio</th>
<th>Science</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interchange</td>
<td>Income Expenditures</td>
<td>Exploitation</td>
<td>Collective Bargaining</td>
<td>Short Run Ceteris Paribus</td>
<td>Micro - Economic Analysis of the Market</td>
</tr>
<tr>
<td>Circulation</td>
<td>Income Expenditures</td>
<td>Unemployment</td>
<td>Concern for Investment</td>
<td>Short Run Fixed Assets</td>
<td>National Income Macro - Economic Analysis</td>
</tr>
<tr>
<td>Innovation</td>
<td>New Assets</td>
<td>Poverty</td>
<td>New Functions</td>
<td>Long Run New Wealth</td>
<td>Capital</td>
</tr>
<tr>
<td>Absorption</td>
<td>Money Liquidity</td>
<td>Crisis Inflation Deflation Stagflation</td>
<td>Union Financing</td>
<td>Long Run Destructive Creation</td>
<td>Finances</td>
</tr>
</tbody>
</table>
# Levels of Basic Scientific Notions

## (Graphic B)

<table>
<thead>
<tr>
<th>Object of Motion</th>
<th>Economy</th>
<th>Physics</th>
<th>Psychology</th>
<th>Learning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particle</td>
<td>Short</td>
<td>Interchange</td>
<td>Gravitation</td>
<td>Feeling</td>
</tr>
<tr>
<td>Limited</td>
<td>Run</td>
<td>Circulation</td>
<td>Electro-Magnetism</td>
<td>Sensation</td>
</tr>
<tr>
<td>Symmetry</td>
<td>Long</td>
<td>Innovation</td>
<td>Motion of prevalent force (chain)</td>
<td>Intuition</td>
</tr>
<tr>
<td></td>
<td>Run</td>
<td>Absorption</td>
<td>Motion of the weak force (radiation)</td>
<td></td>
</tr>
</tbody>
</table>

**Field of Force**

Indeterminate Number of Symmetries

**Capital**

Conscience

**Sources:**

1. *The Nature of the Physical Universe*
2. *The Portable Jung*
3. *The Social Economy Analogue of Piaget's Development of Knowledge*
   - Josef Solterer - Review of Social Economy

**Reflexivity:** Conservation law of volume in exchange

**Transitivity:** National income its measure is the net produce

**Reversibility:** absorbed innovation (assets or capital)

**Parity:** Liquidity (assets are of the same value human, financial physical)
The Tables show how Solterer summarizes those activities within the framework of time and space. The elementary actions are the results of the interchange (commerce and production), circulation (GNP - to measure the goods and services produced in a given period), innovation (creation of new assets) and absorption (money and finance). For Solterer the link between the nature of an economy and the process of knowledge - through the exercise of thought - follows a similar pattern of a creative destruction which characterizes the world of physics. Capital is viewed as a field, not as a tool of exploitation like Marx thought it was. Neither just a factor in the production process as the classical economists consider it. Capital is timeless as the field in physics is. It is not a particle, although it can be considered as such in the production process. If capital is a substratum with an indefinite long range, its creation, destruction and recreation made us believe that it is beyond ideologies but subject to the same conservation laws that singularized the world of physics. These laws contrasts its expansion and its contraction which are beyond the combination of factors that policies can determine. Thus, the problem become not the capital or capitalism but how we could integrate a process of development taking into consideration the question of time, the limits of the environment and the evolutionary process by which societies build their social, political and economic structures. These structures are bound to be affected by moral values, political and social norms which cannot be ignored. To bind a social economy an ethical guideline is needed as the cement that holds the common ground and establish the priorities and goals to be achieved. This cement has to be flexible enough to accommodate disparities in income and standards of living (consequently), but the lack of participation of all sectors of the society will place a great burden on the social system. Inequalities can subsist only in
terms of different rewards for performing different functions on part of individuals and sectors. Social harmony cannot be achieved if the various functions and their retribution are the result of ideological schemes as to interpret the different roles that human beings played in the society.

In other words, the concept suggests that development is a process by which layers of economic foundations are established, not as a concrete or fixed set up, but as the basic ground to further improvement and expansion. Change is the central core of development. Change brings new wealth, expand the horizons of human knowledge and the expectations of people. The cement that holds the process together is the ethical foundation based on justice and solidarity. Consensus become the rule, inequalities and contingencies are faced by the society with fairness and compassion. Innovation as a creative destruction need to be considered within the framework of moral guidelines as not to become a tool for exploitation and misery. The pursuing of personal goals are legitimate aspirations on part of human beings and become essential for the innovation process to take place. But without those moral guidelines, the solidarity links that bound human together are broken and strife becomes the rule of the game. Society, in that case, endures a process in which centripetal forces undoubtedly jeopardize the existence of any democratic structure. Development as a participatory process allows workers, managers and governments to shift the emphasis from the narrow scope of individual aims to a broader social aspiration in which all the segments of the society feel represented. The goals not only include a better material life, but a permanent search for new avenues of learning and knowledge which enrich the human condition in an endless motion of trying to understand the world around us.
Now, how the innovation process is absorbed in the creation of new wealth? What type of mechanisms are utilized? For Solterer the discounting of the present or future gains and their funding is the center of the development process. In the short run aspects of conservation of value and GNP, that is to say employing the given assets and workforce in the most efficient way. In the long run, aspects of funding new streams of future net gains and turning into new available liquid wealth. The essential element in this transformation is the rate of discount turning the future value into a present value. Solterer defines a perpetuity as an endless of infinite series which serves as standard: $C$, to distinguish from $P$ which is the present value of an asset, due to a finite series; $R = i\%$ which is the yearly interest rate paid by a savings bank to a depositor or $P = SR$ will have an asset of $F = R(1+i)$ after one year $F_1 = R(1+i)(1+i)$ after one year $F_n = R(1+i)(1+i)$

$$= R(1+i)^n$$

after

2 years

The present value $P$ or $F$ will be $P = \frac{F}{(1+i)^n}$ or $F = \frac{P}{(1+i)^n}$

$i$ serves here as the rate of discount turning the future value into a present value. The interest payment will always be calculated as $SR = P$

The series of expected future gains or expenses to be discounted and funded will be of different length. For purposes of companies’ assets a standard series, independent of length is needed. An endless or infinite series serves as standard called a perpetuity
1. \[ C = R (1+i) + R (1+i)^2 + R(1+i)^3 + R(1+i)^4 + \ldots \]

Multiply 1) \((1+i)\)

2. \[ \frac{C}{(1+i)} = R (1+i)^2 + R(1+i)^3 + R(1+i)^4 + \ldots \]

Subtract 1) - 2)

3. \[ C-C/(1+i) = R(1+i) \]

Multiply 3) by \((1+i)\)

4. \[ C(1+i) - C = R \]

5. \[ C + Ci - C = R \]

6. \(Ci=R\) Equation gives us the formula used before in the calculation of the yearly interest payment \(SR\), interest rate being \(i\%\) if our initial deposit has been \(SC\) \(SR = SCCi\).

Solterer concludes that money is a perpetuity which is an asset but of a different kind. It comes from many or all possible advantages of those purposes the money has been or will be spent. Such assets are called Capital. Capital in contrast to assets derived from special or particular advantages (land, machines, physical and mental capacity) it is not a particle capable of performing certain functions, but a field of capacities to perform an indefinite number and range of notions, including those yet unknown at present.

What is the origin of future gain? Solterer follows the analysis made by Joseph Schumpeter in his theory of innovation. He considered just a state without economic development - a point of a beginning and end. This would be a complete circular flow without interest or capital and repetitive action or fully occupied factors of production.

These are not freely disposable factors of production, nor funds; anyone coming with a new idea must get new funds from the outside that circular flow and can secure the material for
his project only from bidding it away from its former employment. For Schumpeter it does
not stop on the analysis of development as a short run view of a given economic world to be
described but takes the long run view of an incompletely holding together complex and ask
himself how this heterogenous collection is turned into a homogenous unity, called a social
economy.

In the previous scheme there is no possibility or innovation without money generating
institutions and without the inconvenience from the destruction of former ways of living. All
depends on the existence and the beliefs in future profits and the capacity to live under new
conditions. If so, the short run means of production are turned instantaneously into long run
assets which end, equally abruptly if such faith should vanish. The duration of assets is
measured in terms of timeless capital, as shown before (perpetuity $C=R/i$). Assets are
particles with finite dimensions, capital is a field with more dimensions than any asset. It is
an object at the same time material as mental, sensible and intelligible, existing only if assets
exist, rather than a bank stuff, from which assets are made, so that it could be made by a
particular technology. That is important to recognize to prevent a false conclusion that
development is a technology inherent in a self contained world, all notions of which lead to
combinations of elements of the same world and can be computerized. Development leads to
a new world which cannot be foretold.

To summarize Schumpeter’s approach, innovation is a creative destruction since the
innovation breaks the circular flow. That brings losses for many who will be losing their
jobs and hence their livelihood, that could explain the violent opposition of innovation
throughout history. It is necessary to separate the function of the innovator or the
entrepreneur from the function of the owner or capitalist in order to get to the center of the development process. This means that the entrepreneur must borrow. Where are these funds coming from? These are not available funds in the circular flow. Saving or reduction of consumption and transfer of these funds to the entrepreneur can be of only limited assistance to realize the plan of the innovator in poor countries. Funds are created by commercial banks against the new wealth generated by the innovation. They are the present value of the future net gains. Since the innovation if financed here with newly generated funds, which have become bank deposits on which the innovator draws immediately prices will rise, as the result of the innovation appear only later. Schumpeter used this system as an explanation of the business cycle as an integral part of economic development. But he did not pursue the alternatives to finance development by short-term commercial bank credit. That is to say the varied sector of non-monetary finance. The new financial assets have varying prices, that is they are economic goods and not money whose price is fixed as the monetary unit.

Economies with a large sector of non-monetary finance can absorb innovation with lesser disastrous swings of the force level than those which lack that facility.

To complete Solterer’s analysis of development, as described in the table, it is important to refer to his analysis of the Swiss educator Jean Piaget’s theory of sequential stages in the development of a child’s knowledge.7 Piaget argued that each successive stage in development comes from the preceding one:

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1. Accommodation - determined by the object

2. Assimilation - determined by the subject

3. Adaptation - in the case of several groups in their integration or fusion into a unity

The first two belong to the short run, the third is part of the creative process (long run).

The two groups combined are called development knowledge is the conserved quality in each symmetry group, which we term it an "asset". Mathematical asset of a same kind as a concrete asset for which can be exchanged. Thus comparing Piaget's sequential stages with economic development Solterer finds:

- Reflexivity - conservation law of value in exchange

- Transitivity - national income, its measure is the net product

- Reversibility - absorbed innovation (assets or capital)

- Parity - liquidity (assets are of same value (human, physical, financial)

The symmetry of operations in development of diverse resources of their equal liquidity. All forms of capital must increase at the same rate in parity as well as their incomes in real development. The establishment of such parity is a creative act, not an act of substitution as in the case of justice in exchange. The key to development is liquidity and parity rather than reducing scarcity. Social development depends much less in reducing scarcity and avoiding
exploitation (as it had been concluded in a prior stage of knowledge) and more in
broadening the vista of innovation, accommodating and assimilating all into a new unity of
knowledge and action. Solterer defines development as the increase of participation of
workers in all economic actions and their results in keeping with the common good and in
particular as a valid goal of the efforts of organized labor.\(^8\)

2. DEVELOPMENT, THE GLOBAL ECONOMY AND TRADE UNIONS

The definition of development as a participatory process
lets us focus our discussion on the alternatives opened to the labor movement by the
various strategies offered by those who are designing economic and social policies.

In that respect, both developed and developing countries are faced with similar
problems which pose a threat to their very existence. The globalization of the
economy is making almost obsolete the national-level macroeconomic policies

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\(^8\)A mathematical analysis of Solterer's ideas can be found in Henry W. briefs and J.
"Solterer has developed a paradigm describing persuasively innovative and interactive
economic processes. In this context, all decisions are forward looking; all economic
valuation become asset values, derived by discounting "uncertain" expected net returns from
alternative novel courses of action. Thus all economic "inputs" are assets and exist only
insofar as innovative action takes place. Solterer's key contribution is the formal proof that
such a process of continuous, perssusasive and "uncertain" economic change can persist. He
proceeds by expressing economic development in the form of an incomplete Pfaffian
differential system which has a solution if certain integrability conditions exist" page 652.

Other Solterer's reference works: La Naturaleza del Poder Económico, Facultad de Ciencias
Económicas-Universidad Nacional de La Plata, La Plata, Argentina 1962.
designed to control money and credit, set investment priorities, and influence the
development of sectorial industries and services. National economies are functioning
in an environment whose forces are controlled elsewhere, severely limiting national
governments’ freedom of action. If the financing of the fiscal deficit in the United
States depends on the purchase of treasury notes and bonds by Japanese or European
investors, then perceptions and attitudes of these foreign actors would be much more
important than any policy decision by the Federal Reserve Board. Political events in
Germany leading to the reunification of the two former German states is shifting the
availability of West German funds to the development of former East Germany from
rather the developing countries. Social, political and economic unrest in the former
Soviet Union would increase the demands on Western Europe, North America and
Japan for help. Thus limitations on financial resources are increasing the difficulties
of developing economies in Latin America and Africa who need not only to lessen the
impact of the debt they owe, but also to obtain fresh capital for the development of
their economies. If enough capital is not forthcoming, the situation could become
very dangerous. Vast numbers of people suffering deprivation and facing a gloomy
future would place their social and political institutions under such strain that they
would be close to total collapse. Social disintegration is possible, producing endless
migration to better lands, depredation of natural resources, and unbearable levels of
pollution, as a result of neglect of the developing nations’ needs. Globalization of the
economy is related to the globalization of pollution and threats to the environment. The
collapse of social and political institutions in the developing countries sooner or later would undermine the stability of those similar institutions in the developed world.

Governments are trying to face these crises with various plans calling for shock treatment, privatization of the public sector, elimination of subsidies for basic staples, lowering of real wages, and new rules for business and labor to follow. These plans have created both expectations and anxieties which have raised the social temperature to a very dangerous degree. Recent models for development have stressed export-oriented goals rather than the traditional protection of import substituting industry that prevailed in Latin America in the 1960s and the 1970s. This new strategy is closely related to the structure which underlies the global economy. A factory functioning in the United States or Europe may be removed as a unit to a developing country to take advantage of lower wages and almost non-existent labor controls. Maximization of profits, efficiency and low unit-cost are used as arguments to justify the move, as is the need to create employment in the new location. But the market is still the same - employment is simply redistributed place at both ends of the process. In the developed country, manufacturing workers are displaced, going to work in other areas, mainly service sectors which generally have lower pay, but if all of the human resources available are utilized, the re-distribution can be less painful and less noticeable. In other words, when former housewives enter into paid employment, earnings of the family unit, the total may be the same, or at least not much less, than the family's previous income when there was only one wage-earner. In the developing country, the newly-hired worker is gaining a wage which he did not have before. His income, meager as it might be, puts him in the labor force and increases his capacity to contribute to the movement of the economy.
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Governments are trying to face these crisis with various plans calling for shock treatment, privatization of the public sector, elimination of subsidies for basic staples, lowering of real wages, and new rules for business and labor to follow. These plans have created both expectations and anxieties which have raised the social temperature to a very dangerous degree. Recent models for development have stressed export-oriented goals rather than the traditional protection of import substituting industry that prevailed in Latin America in the 1960s and the 1970s. This new strategy is closely related to the structure which underlies the global economy. A factory functioning in the United States or Europe may be removed as a unit to a developing country to take advantage of lower wages and almost non-existent labor controls. Maximization of profits, efficiency and low unit-cost are used as arguments to justify the move, as is the need to create employment in the new location. But the market is still the same - employment is simply redistributed place at both ends of the process. In the developed country, manufacturing workers are displaced, going to work in other areas, mainly service sectors which generally have lower pay, but if all of the human resources available are utilized, the re-distribution can be less painful and less noticeable. In other words, when former housewives enter into paid employment earnings of the family unit, the total may be the same, or at least not much less, than the family's previous income when there was only one wage-earner. In the developing country, the newly-hired worker is gaining a wage which he did not have before. His income, meager as it might be, puts him in the labor force and increases his capacity to contribute to the movement of the economy.
The shortcoming of this approach is the fact that the factory is not producing for the local market, hence is unable to have a significant impact on the availability of goods and services for the growing population in the developing nation. The results are of the export-led development model are economies divided into segments that are not integrated, creating pockets of wealth and leaving the vast majority of people unable to lift themselves up from extreme poverty. Terms of trade are established in a way that initially benefits mostly the developed country, and not the developing country on the periphery of the global economy. The shifting of jobs and unemployment which used to be regional within a given country, now occurs, due to this globalization process, on an international scale. The new jobs created in the developed country are likely to be in lower pay categories and sooner or later the standard of living will decrease. Those who will benefit most from export-led development are the financial and commercial sectors which will profit as products are imported that previously were produced at home. Both import-substitution and the export-oriented approach are shortsighted and cannot solve the problem of development, the former because it creates inefficiency, and the latter because in the long-run it will distribute poverty rather than wealth. This shifting of jobs decreases the standard of living in the industrialized nations, shrinks their markets and finally the income earned in wages and salaries will be unable to purchase much more than just the elements essential for survival. The economy's benefits will be divided more unevenly than before, increasing poverty for many and wealth for the minority who profit from the global inter-change. The industrialized country will show the same pattern of economic dichotomy which has characterized the developing countries. Viewing this kind of development from a world-wide perspective, it means the
pauperism of most nations, with rising social tensions and severe strains on their institutional frameworks. What can trade unions do about it?

Trade unions are essentially representative organizations, and as such they have to perform functions which are not always established in a well-organized set of rules and procedures. Corporations have much more flexibility in dealing with the outside world, while government’s can eventually resort to its authority and assert its responsibility to promote the public interest. When workers lose their jobs, or are going through painful periods of adjustment, the top priority of a union official is to represent their interests and concerns. That is why it is so important to deal with the subject of union policies toward development understanding the special framework under which they operate today.

Traditional policies on the part of unions have been focused on the area of collective bargaining, trying to equalize the terms of relations in the labor markets. Social consultations, plus, workers’ participation in development councils and agencies have been experimented within Europe and Latin America, and to a much lesser degree in the United States. Perhaps the areas most neglected and even ignored by unions have been the long-run challenges such as facing innovation and financing new paths of development.

In the following pages we will present as case studies some experiments which illustrate new avenues which may be opened for the trade union movement. In the area of interchange we will study the case of Rohr Industries and the U.A.W. in Rohr’s plant located in Hagerstown, Maryland, as well as an innovative agreement signed by the Bakery, Confectionery, and Tobacco Workers’ Union and Nabisco Brands, Inc. We will also summarize the issue of employee involvement in management decisions, discussing the report
of the Economic Policy Council on The Common Interest of Employees and Employers in the 1990s. It will also be important to discuss the issue of privatization in the economy which is part of general policies of readjustment undertaken by governments in Chile, Mexico, Argentina, Poland and the Soviet Union. We will analyze the consequences and limitations of that approach. Regarding workers’ participation at the shop and industry level, we will compare some European examples like the systems followed by Sweden and Germany.

Not less important is the analysis of the ESOP’s schemes which lately have become a major concern for both management and labor in the United States as well as the new inroads made by the AFL-CIO and its affiliates in the area of finance. Another aspect that is necessary to include in any discussion of development is the analysis of the so-called informal economy with far reaching impact in developing societies. We will discuss the informal sector in Latin America where they have reached a point where has more people employed that the formal one.

These case studies and comparative analyses will allow us to test the concept introduced by Solterer of development as a participatory process. It will also help us in designing a set of policies that unions can adopt in order to cope with the implications of development as an endless process by which human beings are trying to improve their social and economic condition, and at the same time, minimize the burden of hardships related to innovation and liquidity. Last but not least, the relationship with the society as a whole should be considered, particularly if we view a social economy as the fundamental basis for a truly effective democracy.
IV -- LABOR RELATIONS
THE CHANGING SWEDISH MODEL
OF LABOR RELATIONS

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It has been called the Swedish model, the third way, the middle way, the Scandinavian Social Democratic model, but whatever the name, the socio-economic system of Sweden, rooted in the values and traditions of the Swedish labor movement, has achieved world wide renown. Although reviled by neo-classical conservatives and other wings of the right, they have envied Sweden's achievements and have found them puzzling. To those on the democratic left and labor, the Swedish model contradicted that common wisdom that it was not possible to reconcile the values of efficiency and equality. Indeed, it appeared a society was being built in Sweden that did not trade-off efficiency against egalitarianism, unemployment against inflation and universal welfare reforms against democratic values.

However, as a relatively small export dependent economy, Sweden's efforts to build the world's most advanced welfare state on the basis of democracy and solidarity has been subjected since the first oil shock to the global economy in 1974 to immense internal pressures and external pressures from the intensified competition of global markets. As a result, the Swedish model during the last decade has experienced changes. Efforts to expand or even go beyond welfare state capitalism have been halted; centralized bargaining, a hallmark of the Swedish model, is being fragmented; the solidarity wage policy, an important part of the goal of equality, is being eroded by the centrifugal forces of wage drift, employer counter-strategies and union competition; and the stability of relations among the labor market policies has been upset by increasing conflict.

These changes have grown in recent years against a background of the global recessions of 1982 and 1990, stagnant economic growth, inflationary pressures and political change that was
dramatized in September of 1991 by the defeat of the Social Democratic government, which held power since 1981 and for fifty-four out of the last sixty years.

Despite these changes, it would be rash to consign the special character of Sweden's welfare capitalism to the "dust bin of history." The values of the labor movement that inspired the reforms are deeply rooted in Swedish history and culture and even the non-social democratic parties realize that many of the reforms can't be reversed; the labor movement is still the best organized and most powerful in the world and Sweden has exhibited resiliency, adaptability and innovativeness in past crisis periods.

In addition to the universal acceptance of most of the far reaching labor laws and welfare legislation, a major aspect of the Swedish model that remains is that Sweden still has the highest density of unionization across all major occupations in the world. The leading organization among the various movements and institutions that comprise the Swedish labor movement is the Trade Union Confederation (LO), an organization of 23 national union affiliates with 2.2 million members that has succeeded in organizing over 90 percent of Sweden's manual workers.

White collar workers are organized in the Central Organization of Salaried Employees (TCO), a confederation of 20 national affiliates which represents 1.1 million members or 75% of the salaried work force. Professional workers are represented by SACO/SR an organization that has 25 affiliates with 280,000 members or about 60 percent of the professionals with academic degrees.

Traditionally, these strong trade union federations have bargained with the SAF, the powerful employer association, which has 35 affiliated employer industry associations with some 40,000 member firms employing 1.3 million workers. SAF is a highly discipline association of
employers which has as its primary functions the representation of its member firms in negotiations with the trade unions an lobbying for employer supported legislative change. While the SAF has organized almost the entire private sector, three other strong employer associations represent the public sector. Affiliates of these employer organizations employ approximately 1.5 million working in national government agencies, 278 municipalities and 23 county councils.

**From Conflict to Cooperation**

Swedish labor-management relations began to evolve from a period of bitter strikes and lockouts at the turn of the century into the 1920s, toward agreements and cooperative strategies with the election in 1932 of the first Social Democratic government. Although labor no longer had to fear a government tilted toward the interests of the business community, they agreed with the employers that it was a good idea to keep their collective bargaining relations free of state interference and the prospect of imposed settlements. Thus, in 1938 a historic agreement between the labor market parties was concluded at Saltsjobaden that has shaped labor relations, with some amendments, to this day. The agreement laid out the rules and procedures of collective bargaining which became the foundation for cooperation and consultation in the negotiations between the SAF and LO. A number of cooperative agreements followed from the "spirit of Saltsjobaden," in such areas as: layoffs and dismissals, the rationalization of production, work environment health and safety and labor market policies that would not injure "third parties" or the larger society.
The Bargaining Process

The structure of bargaining also evolved after 1939 from decentralized industry and local levels to centralized bargaining in the last 1950s. The first step of the process was the negotiation of a national agreement between the LO and the SAF that constituted a set of framework recommendations to each LO and SAF industry affiliate. Before the agreement became binding it had to been endorsed by the affiliates.

The second stage involved supplementary agreements in each industry on the sectoral implementation of the national framework. Finally, negotiations took place at the company and plant levels before final implementation of individual wage increases. Talks at this level would involve equity adjustments for shift workers, low income and special skilled classifications. At the local level, bargaining varies from one work place to another, but is generally led by representatives of the local union clubs of the LO and the TCO who until the mid 1980s closely coordinated their negotiations. Prior to 1980 little conflict, arose between the blue collar local unions and their white collar counterparts.

Although public sector workers began bargaining collectively after World War II, it wasn’t until 1966 that they obtained equal rights with the private sector symbolized by the granting of the right to strike. Consequently, in the last 1960’s centralized bargaining similar to the private sector, but more highly formalized, emerged among the large unions of civil servants. White collar workers in the private sector grew increasingly powerful in the 1970’s, forming strong centralized bargaining associations or "cartels" within the TCO and similarly in the public sector.
**Solidarity Wage Policy**

Centralized bargaining combined with the high level of unionization, has permitted the labor movement to pursue a wage policy of solidarity as a means to its goal of creating a more equal, fairer welfare society. Solidarity in wage policy aims at narrowing pay differentials between industries and within companies thus leveling out the wage structure.

As defined in 1951 by the LO, the solidarity wage policy means that "work of a similar nature should, to the greatest possible extent, cost the same for all employers." Simply put it means a policy of equal pay for equal work. Unlike bargaining in most other capitalist countries, the changing profitability of firms is not the standard for pay settlements but rather the nature of the work.

The outcomes of such a policy not only focuses labor's resources on bringing up the lower paid groups and narrowing large differentials created by personal power positions and market forces, but it also favors the more efficient companies and encourages greater productivity in the less efficient, lower paid enterprises by forcing them to close if they weren't productive enough to meet the industry standards.

On the other hand, the layoffs arising from the closing of inefficient, marginal firms conflicts with a second central goal of the labor movement -- full employment and employment security. Labor's strategic response to this dilemma was to get the Social Democratic government to pursue an active labor market policy that eases the transfer of laid off workers to the stronger firms, involves programs that encourage new job creation, pays relocation allowances to make workers more mobile, invests heavily in sophisticated retraining programs and uses public works as a final supplier of jobs.
The active labor market policy combined with coordinated government monetary and fiscal policies have maintained for several decades the highest employment levels among the western industrialized countries, (with the possible exception of Switzerland) with relatively low inflation.

In summary, we have described three legs of the Swedish Model: centralized bargaining, equality and full employment.

**Settling Disputes**

Between 1956 and 1979 centralized negotiations on a national level rarely resulted in large scale strikes or lockouts. Often this relative stability is attributed to the power balance between the well organized labor and management sides of the bargaining table and their mutual concern that national protracted conflict would jeopardize Sweden’s economic growth and competitiveness.

Although by tradition and law the Swedish government is rarely called upon to intervene in disputes, the collective bargaining parties are required to take their disputes over interpretations of the contract and of labor laws to adjudication by the Labor Court if they can’t be settled by negotiation or mediation. Approximately 250 cases per year, including rights disputes and individual grievances, are heard on appeal to the National Labor Court.

**The Stage of Workplace Democratization Legislation**

If we can call Stage I the formative period of the Swedish labor movement, from the turn of the century to 1938, as one of conflict, and Stage II the spirit of Saltsjobaden, a period of
cooperation and consultation, the 1970's can be described as Stage III, which was a period of growing tension between labor and employers as union demands for economic and workplace democracy met increasing employer opposition.

When negotiations with the SAF broke down in 1972 over the union demands for employee representation on company boards, the LO and TCO, in concert, turned to the legislature. Thus labor, in order to achieve its new demands for substantive involvement in company decision making, abandoned its strategy of voluntarism, based on avoiding reliance on government intervention in favor of wide ranging legislative reforms. Success followed, for, during the period 1973 to 1978 the labor movement succeeded in getting several new laws through the Social Democratic parliament which limited the decisional prerogatives of management by expanding labor influence in the enterprise and improving the quality of working life:

1) **Law on Board Representation**

A 1973 Act, made permanent in 1976, gave employees in companies employing 25 or more persons the option to appoint a minority of two members on the Board of Directors plus two deputy board members as observers. In the public sector, a 1974 law gave government workers the option of representation on the administrative boards of agencies having at least 100 employees.

2) **Co-determination Law**

A law which took effect on January 1, 1977 provided a framework for unions and employers to negotiate co-determination models in the workplace. Employers were required to inform employees of important plans and changes and to involve
unions in the negotiation of these plans. Although this gave the unions comprehensive information and consultation rights, employers still reserved the final prerogative to decide the issue in most cases.

3) **Trade Union Representation Law**

A 1974 Act strengthened the position of union representatives in the workplace in a number of ways, including: entitlements to negotiated amounts of paid time for shop steward activities, union meetings and expanded educational leave.

4) **The Working Environment**

The Work Environment Act of 1978 supplemented previous health and safety laws by giving union safety representatives increased powers such as the right to stop work considered injurious to worker health and safety and to participate in the planning of changes in the working environment.

5) **Educational Leave**

In 1975 an important act encouraging worker participation in educational activities was passed which allowed employees in public and private sector employment, after appropriate notice, extended amounts of educational leave.

Directly as a result of these and other laws that underscored labor's demands for various steps toward co-determination and industrial democracy, worker education activities sponsored by Unions and the Worker Education Associations underwent a great wave of expansion. Employers sought to balance labor's enlarged educational programming with expanded training programs of their own and also began to counter labor's militancy and public outreach with a public relations and political offensive.
With this as context, our brief discussion will focus on the character of labor relations and collective bargaining under the Swedish model and some of the changes they are experiencing.

The rapidly changing economic and political environmental background against which these legislative reforms took place weakened their impact. Inflationary pressures, generous wage hikes, and the global recession that followed the first of the Arab oil shocks affected Sweden's global competitiveness. This contributed to a coalition of conservative and center parties finally breaking the Social Democratic government's continuous 44 year rule in 1976.

Emboldened by the political changes and made more resistant by the intensification of world-wide competition, employers increased their opposition to labor's agenda. When the LO proposed a radical program of Wage Earner Funds that were aimed at democratizing capital investment funds, the business community fought back with an all out political offensive. At the same time, in 1980, an employee lockout paralyzed Sweden for two weeks in a dispute that kept 80 percent of the workforce off their jobs.

Despite the fact that these developments seriously eroded the "spirit of Saltsjobaden" and caused many commentators to announce the end of the Swedish Model, the ingrained pragmatism of Swedish society prevented the escalation of these no-win conflicts. The 1980 lockout was settled with the aid of government mediation. Subsequent contract settlements were approved in 1981, 1983 and 1984 without disputes that involved government intervention. Although the Wage Earner Fund conflict continued to reverberate to the end of the decade, for all practical purposes it was resolved when the Social Democrats were voted back in 1981 and Parliament
voted a fundamentally diluted revision of the LO's original concept that did not challenge the status quo of capital ownership rights and control.

Where is the Swedish Model Heading?

As labor relations in Sweden in the 1970s and 1980s became destabilized it has raised questions about the future direction of the Swedish model. A brief look at what is currently happening to each of the major components of the Swedish model of collective bargaining may suggest the direction.

The solidarity wage policy of the unions has been subject to a number of centrifugal forces that are causing it to unravel.

1) Wage settlements are increasingly being negotiated on a centralized basis. They no longer follow the lead of the LO-SAF agreement in the industrial export industry.

2) The employers have challenged the system of centralized bargaining claiming it does not give them the flexibility needed to adapt to structural changes in the economy and global market pressures. Since they always wanted to pay employees on the basis of their evaluation of individual performance, they have singled out the solidarity wage policy for particular attack for compressing wage differentials and placing constraints on performance-based wage decisions.

3) Efforts to control wage inflation and price inflation through central bargaining have been undermined at the local company level by wage-drift resulting from locally negotiated compensation agreements.
4) The structural shift in the economy to the service sector and the growth of public sector employment has given rise to powerful white collar union wage demands that are competitive with the demands of production workers. Two large scale strikes in the public sector in the 1980s have been over demands for guaranteeing increases that match the wage drift in the private sector. In turn, private sector workers are critical of the higher taxes needed to pay for these increases.

Will wage negotiations become more conflictual? Will worker solidarity break up as unions break away from centralized bargaining and compete more with each other? If stagnant growth rates remain and inflationary pressures grow, the outlook is toward greater instability, the weakening of the labor movement and increasing intervention by the government to the point of imposing an incomes policy. Various needed government interventions over the last decade point in the opposite direction to the voluntarism of Saltsjobaden.

The recently elected conservative coalition and the emergence of a strengthened new right in Sweden are not grounds for optimism. Since the new government lacks credibility among trade unionists, will it be able to mediate fair settlements and gain acceptance for non-inflationary wage bargains? The near future is not promising in this area. In its first days in office the new government has announced the termination of even the highly diluted Wage Earner Investment Funds, which symbolized a first step toward giving workers a collective stake in ownership and a collective voice in capital decisions. At the same time capital taxes are to be abolished and inheritance taxes relaxed. This appears to be a recipe for escalating labor demands as the government tips toward capital and away from labor’s perception of what is fair on distributive issues.
The coming period will be a great test for the conservative agenda. Can a fragile government coalition tilted toward the interests of the business community, deregulation and privatization succeed in jump starting the economy, overcoming inflationary pressures and moderating labor conflict? Until now the Swedish model was supported by broad labor-management understandings in the context of social and economic policies that favored a balance between efficiency and equality and encouraged the strengthening of labor organizations; this environment no longer exists. Does this mean that the Swedish system built up by the labor movement over decades no longer exists? It is too soon for obituaries. Many of the institutions of the Swedish model remain: a powerful labor movement, a broad range of laws that have opened the door to industrial democracy; a social net of universal welfare programs that are widely envied in the world. The Swedish way was written off several times in the past: in 1969 after the eruption of widespread rank and file strikes; in 1976 after the end of 44 years of social democratic led governments; in 1980 after the general lockout by employers that paralyzed Sweden for two and a half weeks and in the 1980s after two major public sector strikes caused increased dissension in labor's ranks. Nevertheless, each time the Swedish labor market parties rose to the challenge and worked out accommodating agreements and pragmatic adaptive strategies.

Of course, the resolution of crises is not inevitable but past history, although by no means a sure guide to the changed conditions facing the Swedish system today, does suggest there are many underlying strengths in the Swedish culture that encourage the working out of solutions. While the Swedish model is undergoing many changes in adapting to the power of multinational
corporations, the new Europe and the globalization of the economy, the report of its death may yet be greatly exaggerated.
WORKERS AND THE ORGANIZATIONS THAT REPRESENT THEM THROUGHOUT THE WORLD ARE UNDER SIEGE FROM MANY FRONTS. RAPID POLITICAL AND ECONOMIC CHANGE OVER THE LAST TWENTY YEARS HAVE TRANSFORMED RELATIONSHIPS BETWEEN UNIONS AND MANAGERS. RAPID CHANGE IN THE TECHNOLOGY OF WORK IS ANOTHER ASPECT OF THE TRANSFORMATION OF LABOR RELATIONS. THE ADAPTATION OF MICRO-ELECTRONIC TECHNOLOGIES, ESPECIALLY COMPUTERS FOR INFORMATION PROCESSING, HAS HAD A PROFOUNDER EFFECT ON THE WAY WORK IS CARRIED OUT IN FACTORIES, OFFICES, AND GOVERNMENT. AND THE ADVANCEMENTS IN SOPHISTICATED INFORMATION PROCESSING ARE FAR FROM OVER.

HOW CAN WE BETTER UNDERSTAND THE PROCESS OF TECHNOLOGICAL CHANGE AND THE ROLE WORKERS AND UNIONS PLAY IN THIS PROCESS? THIS BRIEF PAPER OUTLINES THREE COMPETING THEORIES THAT SEEK TO EXPLAIN THE PROCESS OF TECHNOLOGICAL CHANGE. OF THE THREE THEORIES (NEO-CLASSICAL, RADICAL, AND EVOLUTIONARY) ONLY ONE (EVOLUTIONARY) ALLOWS FOR A POSITIVE CONTRIBUTION BY LABOR IN SHAPING THE OUTCOME OF CHANGING THE WORK PROCESS.

THREE THEORIES OF TECHNOLOGICAL CHANGE

THE STANDARD WAY OF EXPLAINING TECHNOLOGICAL CHANGE IN MOST MARKET ECONOMY COUNTRIES DERIVES FROM THE WRITINGS OF ADAM SMITH. IN SMITH'S THE WEALTH OF NATIONS A PRODUCTION
model is developed from observing the manufacture of pins. Smith’s pin factory of the mid-
1700’s became a favorite of classical liberal economists and those that refined the model over
the next 200 years. The essence of the neo-classical model is the production function: output
(production) is the result of a combination of discrete factors. These factors include raw
material, energy, capital equipment, and labor. An entrepreneur chooses the combination of
factors that maximizes profit. Technical change, in the neo-classical model, equals the relative
change in total unit costs when all the other factory prices remain equal or the same. In
describing Adam Smith’s pin factory or Henry Ford’s assembly line this static model has a good
deal of explanatory power. When the world of production remains relatively stable over time
the neo-classical version of the production function can be applied effectively by economic policy
makers in business or government. The limit of the neo-classical model is in its strength: while
holding all other factors constant allows for the mathematical manipulation of one variable, the
world however doesn’t always cooperate in remaining stable!

A related model of technical change, developed by Karl Marx in the mid-1800s, stood
Adam Smith’s theory on its head. The radical theory placed technological change at the core
of understanding all of history. "It is not the articles made, but how they are made, and by what
instruments, that enable us to distinguish different economic epochs," wrote Marx. Changes in
production, observed Marx, systematically stripped craft workers of their skills an independence
as the industrial revolution became the dominant production method in the 1800s. The radical
critique elaborated one key aspect of the neo-classical production function: the role of labor.
Workers are different from all the other factors of production, they were less predictable and
given to working against the interests of profit maximization. The entrepreneur thus wants to
maximizes profit by realizing that in order to do this they must control the most difficult and unpredictable factor of production -- labor. To achieve the highest level of control over workers, the radical critique said, capitalists introduced the idea of the division of labor to the production process. By breaking down the control workers exercise over their work, by deskilling the labor process to the greatest extent possible, the owners of capital gain the greatest chance of maximizing profit. The application of Frederick Taylor's "scientific management", time and motion study, in the late 1800s and early part of this century is the clearest example of these ideas being put into practice.

The radical theory of technical change shares the basic premise of the neo-classical model: the choices, or alternatives, that the owners of capital make are relatively static. If at any point in time firm X is making a profit, and competitor firm Y is making a slightly lower profit, why would firm X or Y decide to make significant changes in the production slightly, may make small differences. Where is the incentive to take risks in developing significant changes? What the neo-classical and radical view of technical change share, despite their real differences in emphasis on the role of labor, is the incremental, relatively static view of innovation. In the neo-classical view labor is just one of several variables to be manipulated in finding the most efficient balance of inputs to maximize output; for the radicals the increasing division of labor is an inexorable result of capital's search for profit.

A third view of technical change, an evolutionary theory of innovation in the production process, provides an alternative to the neo-classical and radical theories. Departing from the static theories Joseph Schumpeter developed a dynamic model of economic development that placed innovation as the engine of change. For Schumpeter the static models failed to explain
significant breaks in the history of economic development. "It is the kind of change arising from within the system [of production] which so displaces its equilibrium points that the new one cannot be reached by infinitesimal steps. Add successively as many horse-drawn mail coaches as you please, you will never get a railway thereby," wrote Schumpeter in the early 1900s.

It is the taking of risks, to combine the factors of production in entirely new ways, that creates these breaks with past incremental improvements. In many ways, Schumpeter said, such risk taking is irrational from the point of view of profit maximization. By analogy Schumpeter noted that this same profile of risk taking extends to other creative fields: "We probably would have few novelists, actors or scientists if all potential aspirants to these careers took action based on a probability of success. We also might have few new products, new medical procedures, new political movements, or new scientific theories."

The evolutionary view of technical change shares similarities with the Darwinian theory of biological change. Changes do occur cumulatively over time; preferences are adapted to the existing environment; and occasional discontinuities occur which force a new way of producing. The process of moving from continuity (the horse-drawn mail cart) to discontinuity (the railway) is the key to understanding technical change.

What Does It Mean For Labor?

The implications evolutionary theory of technical change are dynamic, in contrast to the overly deterministic radical model and static neo-classical model. It suggests that breaks in continuity are the key to economic development. Two implications of their theory are especially important for labor: change is inevitable and often destabilizing; and, the direction of technical change, the shape new production processes will take, is difficult to predict.
All around the world dramatic economic, political, social, and technological changes have reshaped traditional relationships between labor and business. The increasing complexity of work, together with competition that no longer recognizes national boundaries, has forced many organizations to reorganize. The old models of hierarchical business structure and precise division of labor are collapsing under the imperative to respond as quickly as possible to changing markets. Businesses are beginning to realize that labor is more than a factor of production. Indeed workers probably know more about the production process than anyone else. Business executives want to tap this knowledge, to use workers skills as a source of competitive advantage -- while paying as little as possible for this knowledge for sure!

The evolutionary theory of technical change suggests that labor can play a key role in developing new innovative forms of production. Unions play an essential role in protecting workers' interests, both at the bargaining table when the proceeds of the enterprises' pie gets sliced and at shop floor where the pie is made. Unions can also play a role in protecting workers who dare to innovate. By protecting some of the downside risk inherent in trying new ways of producing, through such things as contractually agreed upon employment security and training, the union also becomes a positive force in expanding the size of the pie getting sliced! Labor, seen in this way, will play an increasingly important role in developing new ways of working, in economic development, and in increasing the competitiveness of all types of organizations.
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CASE STUDY OF EMPLOYEE OWNERSHIP AND GOVERNANCE IN THE SHIPBUILDING AND MARITIME INDUSTRY

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A few years ago I had a unique opportunity to participate in a project involving a number of critical issues that have confronted the labor movement in 1980s: potential closing of a facility; bankruptcy; concession bargaining; and an Employee Stock Option Plan (ESOP). While I had dealt with each of these issues separately at various times in the past, I had never been faced with a situation where all were present at the same time. In addition, the affected unions were much more proactive, rather than merely reactive, as is often the case when unions are faced with such challenges.

BACKGROUND

The corporation was a privately-held holding company located in the Northwest with a number of operating companies involved in the maritime industry. One of these operating companies was a ship construction and repair facility that built and repaired small ships, tugs, ferries and barges. The Metal Trades Council (MTC), a group of AFL-CIO unions, had a contract with this company. My union, the Boilermakers, had a local affiliated with the MTC as did nine other unions representing employees at the shipyard.

The collective bargaining rights were held by the MTC, not the individual unions. This required cooperation among the unions in the negotiations process -- a difficult task under
normal bargaining conditions and one made more difficult by the issues mentioned above.

Another operating company was engaged in the ocean tug and barge business. Employees of this company were represented by the Master Mates and Pilots (MMP) and the Inland Boatmen's Union (IBU), neither of which was affiliated with the MTC.

These three groups, involving twelve individual unions, were the labor participants. At the request of the MTC, I was assigned by my union to assist the participants. My primary task was to represent the interests of the MTC and not solely the Boilermakers' local. The Boilermakers also had an international representative assigned to the MTC.

The U.S. maritime industry had been experiencing a severe downturn, with many industry sources referring to the downturn as a depression. The Northwest was hit particularly hard during this period, with multiple shipyard closings and severe layoffs in the surviving yards. This corporation was not immune to the general downturn in the industry.

In early 1986, the corporation filed for protection under Chapter 11 of the Bankruptcy Code. This resulted in the closing of some operations and the loss of 1,000 jobs. In 1987, the creditors moved to foreclose on the corporation, threatening the loss of the remaining jobs. During this time, the IBU and MMP approached the MTC about the prospect of an employee-owned company. The MMP and IBU had previously contacted an investment banking firm about an employee buyout. In September of 1987, the family who owned the company agreed to sell it to the employees.
BANKRUPTCY AND THE ESOP

With the corporation in bankruptcy, the Bankruptcy Court became an integral part of the negotiations and, ultimately, in the creation of the employee-owned firm. For example, the labor agreement with the MTC had to be approved by the Court. The corporation was concerned with appearing overly generous toward the union employees by agreeing to wages and benefit levels that might be considered too high when creditors were not being paid. Meanwhile, the unions were concerned with negotiating an economic package as close to area standards for wages and benefits as possible.

In order to accomplish the first major step in bringing the corporation out of bankruptcy, a labor agreement had to be consummated. After a period of intense and difficult negotiations, the parties reached an agreement that neither party wanted to claim as its own. Therefore, the first of many innovative means of accomplishing difficult but necessary objectives was developed. The parties merely let the Bankruptcy Court know that they both would accept that wage and benefits package if proposed. The Court made the proposal, there were no objections, and the agreement was put into effect.

Under Chapter 11 of the Bankruptcy Code, the corporation had a period of time to come forth with its own plan of reorganization while insulated from its creditors. As part of the collective bargaining agreement, it was understood that the corporation's reorganization plan would contain an ESOP. Once the labor agreement was in place, the parties began to earnestly pursue the ESOP and the restructuring of the company.

Another matter complicating the reorganization was the fact that neither the owner, the various unions, or the employees were able to garner any additional capital to invest in the
reorganized company. This required an innovative approach to capital financing. The Bankruptcy Code and the ESOP provided the parties with the vehicle to accomplish this. It was determined that the reorganized company could be created entirely through restructuring of the existing debt with no influx of outside capital. We would create a 100 percent internally leveraged ESOP company!

THE WORK OUT

Unlike most bankruptcies, the unions in this case were involved in negotiating with the creditors and developing the Plan for Reorganization. Union representatives helped determine which assets were to be kept, sold, or foreclosed, and to decide which operations to maintain or close. Representatives of employees not in the bargaining unit also were involved in this process.

The negotiators consisted of the owner, union representatives, representatives of employees not in the bargaining unit, and professional advisors. This group was to spend the next eleven months in what seemed like a never-ending negotiating process. The unions had to develop common positions among themselves, be a part of the consensus-forming process with the parties in the overall group, and provide direction to our professional advisors in the negotiations with creditors.

An investment banking firm headed up a team of bankruptcy advisors which consisted of their own specialists, bankruptcy lawyers, and the owners' in-house attorney. We were also working with advisors knowledgeable about ESOPs. Because we were in the process of developing a plan to reorganize the bankrupt corporation and establishing an employee-owned
firm at the same time, a great deal of interaction was required between the bankruptcy and ESOPs specialists.

The structure of the reorganized company would have a direct bearing on the ESOP. Structure would affect the number and type of continuing operations in the new company which would, in turn, determine the bargaining units that would be involved. While it was decided early that the new business plan would include both shipyard and maritime operations, the specific facilities and equipment of each operation were a part of the work out with the creditors' committee and the Bankruptcy Court. The business plan was to be changed many times during the months of negotiations.

There were a number of large creditors, the largest of which was a U.S. government agency that financed loans to companies in the maritime industry. It had liens against a substantial part of the assets of the former corporation. This agency proved to be one of the most difficult creditors to deal with in the reorganization. Unlike some of the other creditors, the agency was not as susceptible to the pressures of the bankruptcy. Most of the assets they claimed were oceangoing tugs and barges. This became a problem in creating the maritime portion of the reorganized company.

The maritime operation was essential to supply the cash flow necessary to carry the reorganized company until the shipyard could generate sufficient revenue to move the new company forward. A properly structured maritime component was essential to our plans. While not all the existing assets of the maritime operations were necessary, some were considered critical. The negotiations with the agency involving these assets were difficult, thereby prolonging the reorganization process and, on at least two occasions, nearly causing its collapse.
Another major creditor was a locally headquartered bank that held liens against much of the corporation's real estate, including the shipyards and some dry docks. These assets were included in the original reorganization plan. While the bank proved to be difficult at times, it was susceptible to pressures to which the U.S. agency was not. For example, as a local bank, it was vulnerable to community pressures, and these were brought to bear very effectively. The unions, headed by the MTC, picketed the bank's headquarters and generated media coverage favorable to workers' interests. After using these tactics, the negotiations with the bank became an important ally to us in the negotiations with the other creditors. Most were vendors who did business with the bankrupt corporation and, because of their unsecured position, were interested in seeing the new company emerge from bankruptcy. While their claims were unsecured against needed assets, they were represented on the creditors' committee and had a vote on any reorganization plan. They, along with other secured creditors, could neutralize the votes of some of the more troublesome creditors.

Thus the unions became involved in the "politics" of Chapter II. We were engaging in "hardball negotiations" with some of the creditors. At times, it appeared we would never put the deal together. When all else failed, we had to be prepared to utilize the "cram down". That is, if agreement did not appear forthcoming with a creditor, you tried to give them the least amount per dollar of assessed valuation for their secured assets. Hopefully, you could "cram them down" to the point where they would reconsider their position.

The process was both fascinating and ruthless. The "law of the jungle" ruled as the group trying to reorganize the company and the creditors fought over the same piece of meat: namely, the assets of the company. The process certainly offered new perspectives on the
capitalist system. Creating a "new", reorganized company, completely free of debt, was a daunting task. I credit the success of the process to the understanding and desire of all the groups to emerge from bankruptcy with a new, employee-owned and employee-influenced company.

Our goal was not simply to establish an ESOP. Rather, the objective was to have a company owned and governed by the employees. The reorganization provided us with that opportunity. The ESOP, articles of incorporation, and bylaws were the vehicles to accomplish this goal.

Restructuring the company and developing the ESOP occurred simultaneously during most of the eleven months it took to create a new company. On August 23, 1988, the new company officially emerged from bankruptcy.

THE NEW CORPORATION

The new firm was structured as a parent holding company with two operating subsidiaries: a ship building and repair company, and an ocean tug and barge company. Each company had a Chief Operating Officer (COO) who sat on the Board of Directors of the parent corporation.

A unique feature of the firm was that the new Chairman of the Board of Directors was the head of the IBU who had represented employees of the tug and barge company. He had been instrumental in promoting the employee buyout and was a major player in the bankruptcy process. Upon accepting the position as Chairman, he resigned his position with the IBU.
The question of who would head each new operating company became a major topic of conversation among the unions and other parties involved in the bankruptcy, including some of the major creditors. The former owner was available; however, he was "persona non grata" with at least one of the major creditors. While the feeling among the union representatives was that we wanted him as part of the management team, we decided that it was best to offer him the job of COO of the ship building company. He had grown up in the industry and knew it well. However, when some of the creditors learned of our plans, they objected to him having any senior management function, especially related to the shipbuilding company. This became a major dispute between employee representatives and the creditors, one of whom would attempt to challenge our reorganization plan solely because of this matter.

Because we had confronted and surmounted so many problems together, the people involved in the process developed a "team spirit." Consequently, the creditor's attempt to limit for former owner's influence in the new company was viewed as an attack on us all. The saying that "politics makes strange bedfellows" applies equally well to business. I never thought I would be involved in fighting to protect the job of any management representative, much less the owner of a bankrupt company. We were successful in that battle, and he became the COO of the ship building company.

Since this formerly had been a family business, the owner's son had worked in the business for years and was involved with the tug and barge operations. He was a young, intelligent person who knew the business. His only drawback appeared to be his lack of job experience outside of the family business. Nevertheless, the unions supported him as COO of the tug and barge company.
The two COOs had seats on the Board of Directors and, thereby, the opportunity to influence the new corporation. The reorganized corporation was a "bitter sweet" experience for both of them, especially the father. I now believe he initially agreed to the ESOP as a means to buy time and avoid a forced liquidation of the family company. He soon came to realize that the ESOP was the only way to salvage any remnant of the family business. He did not, however, fully come to grips with the fact he no longer ran the company. This results in numerous clashes with the Board of Directors and, ultimately, led to the resignation and departure of both family members.

EMPLOYEE OWNERSHIP AND GOVERNANCE

The first issues that must be addressed in the development of any plan of employee ownership concern the amount of ownership and degree of control which the employees are to have. Employee ownership does not necessarily translate into employee control. This can be a very difficult distinction for employee-owners to comprehend. Many naturally assume that control goes along with ownership. Most ESOP arrangements, regardless of the amount of ownership, provide for little or no employee control.

The unions were determined to have a substantial amount of control in the reorganized corporation. Indeed, there was an agreement in principle on this subject between the unions and the former owner early in the bankruptcy process. The exact amount of ownership and the degree of governance were established as part of the Plan of Reorganization and negotiations with the creditors.

The unions were able to secure an immediate 75 percent ownership of the corporation by the ESOP. The balance of the stock was held by the former owner (5 percent with an
incentive arrangement for an additional 5 percent), the investment banking firm which helped put the deal together (5 percent), the unsecured creditors (7 percent) and a major creditor (5 percent). Also, the unions received 4 seats, and the unrepresented employees 1 seat, on the Board. The other Board seats belonged to the Chairman of the Board, the two COOs, a representative of the unsecured creditors, a major creditor, and a representative of the investment banking firm. The employees held a total of five seats on the 11-member Board, one seat short of a majority. Because the preferred stockholders never filled their seat for the 13 months I served on the Board, for all practical purposes there were only 10 voting members.

The amount of employee ownership was addressed in the ESOP and the Employee Stock Ownership Trust (ESOT). The governance issues had to be addressed in the Articles of Incorporation and the Corporation Bylaws. Because the new company was to be reorganized out of bankruptcy, the ESOP and the corporate structure were parts of the approved Plan of Reorganization.

In addition, the composition of the Board of Directors was specified in the Plan of Reorganization to ensure continuity and to permit the group that prepared the Plan an opportunity to set up the new corporation. After their initial terms representing employees on the Board, union officials were prevented by the Bylaws from being reappointed. Rather, the Bylaws provided that only individuals employed by the corporation in the designated groups could hold those seats. There was a strong feeling that to be truly an employee-owned and employee-run company, the people working there, and not officials of their unions, should eventually hold those Board seats. While this approach may be highly desirable, it was necessary to determine whether there were employees who really wanted to assume the
responsibility of Board membership. The proposal was not without risk, since once procedures were established they would not be easy to change. Consequently, this issue was discussed with employees in the union groups. Most liked the requirement that union Board seats eventually would be filled by employees, and a number expressed interest in seeking the positions.

The union groups had varied opinions about ways to select their representatives. Ultimately, each group decided on a process to choose its own representatives which, in turn, resulted in union members electing their replacements. To ensure an orderly transition, the outgoing Board members attended the next three Board meetings. While we all had concerns, the transition went smoothly. The only problem with the new employee Board members was their desire to discuss "labor management problems" at the Board meetings, and this was resolved after the first few meetings.

THE EMPLOYEE STOCK OPTION PLAN

A subcommittee was created to work with the ESOP advisors to draft the ESOP and the ESOT. The subcommittee had members of the three union groups, the nonbargaining-unit employees, and the former owner.

The ESOP covered all eligible employees of the corporation and its two operating companies. The drafting subcommittee had to develop an ESOP plan that would be accepted by the Bankruptcy Court. Therefore, the ESOP plan was prepared while other issues in the Plan of Reorganization were being finalized.

The ESOP plan had to be appropriate for the varied employee groups it covered. The eligibility of new employees to participate posed some interesting questions. Normally, new employees become eligible after a set period of time (a month, 6 months, or a year). This type
of provision would have worked for the nonbargaining-unit employees who were employed on a steady basis. However, employees in the three union groups worked intermittently, even though many worked a good portion of the year. This issue was resolved by declaring eligibility on the next January 1st or July 1st after working 60 days in any 12 consecutive month period.

Another interesting problem arose concerning the method of allocating shares of stock to employees. In order to utilize some tax advantages available to an ESOP company, it was important to use wages as the method of allocation. If the allocation were to occur on the basis of total gross wages (W-2 compensation), some union groups were concerned that higher-paid management employees would derive a larger amount of stock. However, when a cap of $50,000 was proposed, the MMP representative pointed out that some employees in their bargaining unit could make substantially more in a year. Therefore, allocations were made on the basis of the W-2 wages of the highest-paid employee of a bargaining unit or $50,000, whichever was higher. Many similar circumstances arose as we tried to "balance" the differences between the employee groups covered by the plan.

All employee groups covered by an ESOP should be concerned with who will make determinations of allocations, resolve questions concerning the plan, and direct the Trustee in the voting of the unallocated shares. These and other responsibilities involved in the administration of the Plan were vested in the seven-member Administrative Committee (three members were appointed by the MTC, one by the IBU, one by the MMP, and two by the unrepresented employees). The members of this Committee were not required to be employees or participants. This allowed the unions the flexibility to select union officials, employees, or other individuals for these positions.
THE BOARD OF DIRECTORS

With three exceptions, the initial members of the Board of Directors had been involved from the beginning with the bankruptcy process and the design of the ESOP. This proved to be a wise decision because these individuals had worked with each other for nearly a year. Consequently, previous deliberations which occurred during the reorganization process provided a substantive and emotional context for early decisions concerning the management structure.

All in all, the Board members worked well together. The issues which were brought before them were thoroughly discussed (and at times were hotly debated) before a vote was taken, and the union members did not always vote the same on all issues.

Among the more important decisions on structure was the Board’s creation of subcommittees to deal with various issues, including compensation and labor. The Compensation Committee reviewed compensation guidelines for all employees and supervised benefit plans for corporate officers. As an MTC board member, I was part of that committee. The Labor Committee reviewed and made recommendations to the Board concerning collective bargaining agreements. Union representatives on the Board were required to abstain on votes involving their own collective bargaining agreements.

One of the most difficult decisions we had to make was to cease operations at one of the shipyard facilities. We originally planned to use that facility to build fish processing ships, ferries, and small naval vessels. While we were able to keep it operating for over six months, additional contracts were not large enough to offset the costs incurred by keeping the facility open. The cash drain threatened the solvency of the entire corporation. The leveraged position of the ESOP gave us little margin for error. Even though we explored every possible way to
avoid closing the facility, it was still difficult to accept. Without that yard, we were effectively out of the larger ship construction business, a consequence we had tried desperately to avoid.

It is critical in any highly-leveraged business to maintain an adequate cash flow to meet debt payments. This requires efficient operation. For example, a major project for the new Board entailed revamping the cost accounting system to manage the cash flow efficiently.

These and other challenges faced the new Board. After celebrating our first year in business, the process of turning the Board over to the new employee owner representatives was begun. The company is still in business three years after emerging from bankruptcy, providing jobs to our members and the community. Many more challenges and opportunities will be confronted during the right for survival in the difficult shipbuilding and maritime industries. I look back fondly on my many months of involvement in giving them the opportunity to meet these new challenges.
V -- DOCUMENTS, BOOK REVIEWS
Participative Work Agreement
between NABISCO BRANDS, INC. and
the BAKERY, CONFECTIONERY & TOBACCO WORKERS UNION

The Bakery, Confectionery & Tobacco Workers Union and Nabisco Brands, Inc. mutually agree and pledge themselves to pursue a partnership which promotes cooperation and involvement for the mutual benefit of the company and its employees.

This agreement specifically promotes the continued development of a labor management partnership fostered by maximum communications, trust, and understanding resulting in a work environment which recognizes the full worth and dignity of all employees and facilitates their individual growth and accomplishments toward the continued needs for effective and efficient bakery operations.

This agreement supports the need for local union management partnerships to investigate, consider and test alternate approaches to work assignment, work scheduling, selection, training, development, pay systems, problem solving, process and structure to facilitate both individual & group contribution towards improved quality, efficiency, productivity, and employee satisfaction.

In support of this agreement it is recognized that the union has a legitimate role in assuring appropriate fairness and due process for employees. In addition, it is expected that local union executives will be active and constructive participants in the evaluation of the local union management partnerships. Further, it is recognized that contractual wage rates shall be the base for any new pay systems which may be developed and that seniority rights will prevail.

The Bakery, Confectionery & Tobacco Workers Union and Nabisco Brands, Inc. are strongly committed to this participative work agreement as a means of promoting strong labor/management relations necessary to provide a work place that expands the opportunity for each individual to support the need for and share in the success of the company.

For the Union

John DeFronzo
INTERNATIONAL PRESIDENT
BAKERY, CONFECTIONERY, AND TOBACCO WORKERS INTERNATIONAL UNION

For the Company

[Signature]
SENIOR VICE PRESIDENT, PERSONNEL
NABISCO BRANDS, INC.

[Signature]
[Date]

[Date]
APPENDIX "A1"

1. In the event the Company intends to effect a change covered by Article 28, Section 2 of the current Collective Bargaining Agreement, an appropriate person in the local management of the Company shall communicate such intention to an appropriate official of the Local Union within a reasonable time prior to implementing such a change. Such communication shall indicate the nature of the change to be made.

2. Should the Local Union deem it necessary, it may request a meeting or meetings to discuss the change.

3. The Company may implement the change after the time specified in Paragraph 1 above has elapsed.

4. The Company shall have a reasonable trial period so that all parties may fairly evaluate the change.

5. If, after said reasonable trial period, the Local Union contends that the change requires more than a fair day's work for the affected employees, the Company will restore the method of production in effect immediately prior to the change until an agreement can be reached or an award is rendered by an arbitrator in accordance with the provisions in this Appendix, provided that mechanical changes shall remain until an arbitration award is rendered.

6. If it is mutually agreed by the Local Union and the Company, a meeting may be held to be attended by representatives of the Local Union, the International Union, the Company's headquarters, and the Company's Local Management to attempt to resolve any matters regarding a fair day's work.

7. In the event any matters regarding a fair day's work remain unresolved after the meeting(s) referred to above, the Company and/or the Local Union shall submit the matter to an impartial arbitrator, by serving a notice of intent to arbitrate upon the other party. Simultaneously with the serving of said notice, the moving party shall also request a panel of eleven (11) arbitrators from the American Arbitration Association or the Federal Mediation and Conciliation Service which will be submitted to the Local Union and the Company. This panel shall be a national "Blue Ribbon Panel" consisting of eleven (11) arbitrators of national reputation (i.e. members of the National Academy of Arbitrators) and geographic distribution who are experienced in work measurement and methods. The arbitrator shall be selected and designated from said panel by mutual consent of the parties. In the event the company and the Union are unable to mutually agree upon an arbitrator from said panel, within three (3) days after receipt of the panel, the Company and the Union shall alternately strike five (5) names from said panel. The remaining name shall be designated to hear and determine the matter. It is further understood by the Company and Union that all of the above steps taken and the scheduling of the arbitration shall be accomplished in an expeditious manner.

It is understood that the above arbitrator selection procedure shall not apply or change in any way the arbitration selection methods utilized under Articles 31 and 32 of this Agreement.
ARTICLE 28 - LABOR MANAGEMENT

Section 1 The management of the business of the Company, the direction of its working forces, the schedules and quantities of production and the methods, processes and means of manufacturing, are prerogatives of the Management.

It is understood that no provisions of the Section shall in any way interfere with no abrogate any rights conferred upon the Union or its members by any other clause contained in this Agreement.

Section 2 In cases where changes in methods of manufacturing or increases in production are contemplated by the Management, the Company will submit such changes to the Business Representative and/or top official of the Local Union. Where the Union claims that any such change will result in more than a fair day's work for the employees involved, such change shall be submitted to a person designated by the top official of the parent body of the Local Union and to a person designated by the Management, in an effort to reach an agreement. Where both officials fail to reach an agreement, they shall choose a mutually satisfactory third (3rd) person as arbitrator of the dispute. His decision shall be final and binding on both parties.

Attached hereto and made a part of this Section 2, is the understanding between the Company and the Union signed 12-13-74, as amended 8-24-79. (APPENDIX "A-1")
BOOK REVIEW

THE OTHER PATH TO SOCIAL JUSTICE
IN LATIN AMERICA

William C. Doherty, Jr.
and
William A. Douglas

Since its publication in Spanish two years ago, Hernando de Soto’s blockbuster book The Other Path has done more to destabilize the crony capitalisms of Latin America’s smug, entrenched business elites than the KGB has managed to do in decades. De Soto points out that economic structures in Latin American today resemble those in England in the latter 1700s. England’s economy then was mercantilist -- the government controlled access to the economy and doled out to political favorites the right to produce certain products. Naturally, the number of participating firms was kept limited, creating oligopolies which produced large profits to be divided up among businessmen and politicians living in cozy economic symbiosis.

As de Soto reminds us, population growth, industrialization, and urbanization overwhelmed this mercantilist economy which could not produce enough to sustain the new society. Consequently, thousands of new businesses grew up informally, operating became "socially irrelevant", as de Soto puts it, and the informal firms wanted an end to the closed economy. They challenged and smashed the old mercantilist system, an open, competitive economy resulted, and the industrial revolution was on its way.
In Latin America, says de Soto, mercantilism has persisted to the present day, but now with urbanization and population growth the informal economy has grown larger and more productive than the formal economy composed of legally-licensed and government-favored oligopolistic firms. Conditions are ripe for an end to mercantilism and the creation of open, competitive market economies. Now the Latin American informals want in, and de Soto’s book has provided the intellectual ammunition for their assault on the region’s entrenched elites.

While some may mistake de Soto’s attacks on present government regulation in Latin America as advocacy of a return to Victorian laissez-faire, the thrust of his book is towards the modern and pluralistic form of democratic capitalism which has been successful in the industrialized countries of Western Europe, North America, and the Pacific rim.

De Soto points out frequently and vigorously the vital role government regulation of the economy plays in economic growth -- what he calls "good regulation", not the distorted role government has played under mercantilism of keeping the economy closed and competition checked. De Soto shows us that a legal system providing the economy with secure property rights, equal access to their market for all, the "strict efficient rules of the game" to prevent shady operators from driving responsible firms out of the market, is a key precondition for economic growth. (So, we might add, is full respect for workers' rights to organize, bargain, and strike).

De Soto paints a dismal picture of the kind of regulation now prevailing in Latin America -- the mercantilist oligopolies and their political cronies have indeed built up impressive barriers to market entry and competition. In Lima it takes 289 working days to obtain permission to start a small business. It takes 83 months to get the permits needed to build a housing project.
Formal businesses spend more time buttering up their contacts in the government ministries than they do improving the efficiency of their production or marketing processes, because in a mercantilist system, it is the degree of political "pull", not of efficiency, which determines whether a firm does well or poorly.

The path of the Marxist-Leninist -- left the smashing of Latin America’s mercantilist oligopolies and the creation of economies which serve the people -- has failed, as evidenced by the economic disaster in Cuba and Nicaragua. The Marxist-Leninist path called for violent revolution, totalitarian dictatorship, and fully statist economies. De Soto seeks to smash mercantilism and create social justice by the legal revolution, full political democracy, and an open, competitive, effectively-regulated, market economy. All of these prescriptions fit well with U.S. labor’s ideas on free trade unions as the voices of the workers and as "countervailing forces" to the unbridled power of management. Do Soto’s "other path" is the true road to ending privilege and creating social justice in Latin America. That is why he dedicates his book not only to the workers, but also to "my left-wing friends, whose ideals I share".

As with any social groups, the "informals" and the organized workers in the formal economy have some interests in conflict and some in common. As long as they remain informal, the small firms are outside of minimum-wage, social security, maximum-hour, job-safety, and child-labor regulations, and they tend to under-cut the wages and working conditions of the workers in the formal sector. But as de Soto shows, what the informals want most is formality, because the costs of informality (no property rights, no insurance, no limited liability), no economies of scale, no credit at reasonable interest rates) far outweigh the benefits (no taxes).
Thus all the workers in Latin America, formal and informal, have a pressing common interest -- to break mercantilism, open markets, and let the informals in! In that aspiration, the workers share a common enemy -- the entrenched crony capitalists who want to hang on to their privileges and profitable oligopolies. These same conservative elements also want to keep the workers in the informal sector without the benefits of free trade unions and collective bargaining. The world's nations, through the conventions of the International Labor Organization, have agreed that in a just society these rights should be available to all workers, in whatever "sector" they may labor. If one thing is sure in politics, it is that people with common interest and common enemies will get together. That's why trade unionists all over Latin America, while not necessarily agreeing with all of the author's positions have been reading de Soto's book. So should anyone interested in how economies grow.
NEXT SPRING ISSUE

THE GLOBAL ECONOMY AND THE INTEGRATION PROCESS

- The Global Economy
- The Integration Process in the Caribbean
- Europe 92
- Central America Integration Process
- MERCOSUR
- Workers' Rights in the Integration Process
- Plus Section on Development, Labor Relations Documents and Book Reviews