

LATIN AMERICAN POLITICAL ECONOMY

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DESIGNING INDUSTRIAL POLICY IN LATIN AMERICA

Business-State Relations and the
New Developmentalism

Ben Ross Schneider





Designing Industrial Policy in Latin America

Latin American Political Economy

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Ben Ross Schneider

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Designing Industrial Policy in Latin America: Business-State Relations and the New Developmentalism

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DESIGNING INDUSTRIAL POLICY IN LATIN AMERICA

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Preface and Acknowledgments

This book grew out of a series of papers and projects sponsored by the Inter-American Development Bank and coordinated by Eduardo Fernandez Arias and Ernesto Stein. I was especially interested in participating in these debates because the projects brought state intervention, political organization, and the political economy of policy making back to the fore, with a special emphasis on the role of business. I am very grateful to Eduardo and Ernesto for including me (usually as one of a few political science interlopers) in these projects and for their many insightful comments and suggestions.

In a first cut, these projects provided me with a chance to update Maxfield and Schneider (1998) and try to derive more specific policy implications and applications. Since the publication of that book in the late 1990s, a wave of additional empirical research and some new theorizing offered a strong basis for an extensive aggiornamento. This book uses parts of the overall framework from the earlier book, and its point of departure that effective collaboration between business and government can be good for development. However, the present book concentrates more on issues of information exchange (and less on longer-term trust and credibility). Among economists advocating lately for industrial policies, a clear consensus emerged that government officials need to work closely with business in order to infuse policy making and implementation with information from the private sector. Yet, the consensus on the need for information is not matched by any agreement on how best to achieve the information

exchange or how to keep business from using its privileged position for rent seeking, which is where this book enters the discussion.

The intent of this book is to cover as much recent research as possible on the many experiments in business-government councils in Latin America, as well as to place these experiments in their broader political context. Maxfield and Schneider (1997) incorporated political analysis, but most of those cases and empirical evidence came from authoritarian or weakly democratic contexts. Since then, formal electoral democracy has consolidated in Latin America, and business has established a heavy and active presence in multiple forms of policy debate and decision making ranging from informal networking to think tanks to campaign finance and lobbying. It is at best naive to plan industrial policy without taking this political participation into account. A number of other recent studies—especially from multilateral agencies like the World Bank, Cepal, IDB, and the OECD—have covered a wide range of experiences, but have not embedded the analysis in overall politics. This is a key part of the value I hope this book can add.

Business groups—huge, diversified, usually family-owned conglomerates—were also missing from Maxfield and Schneider (1997) and from most recent scholarship on industrial policy. Most studies of course refer to the chaebol in Korea because they were so dominant. However, it is now clear that business groups dominate the domestic private sectors of nearly all middle income countries (Colpan, Hikino, and Lincoln 2010). It makes little sense therefore to talk about business-government collaboration in industrial policy without explicit consideration of the upgrading capabilities and political power of these business groups.

I benefitted greatly from multiple sources of support for this project. The background working papers for this project went through several iterations and very helpful workshops at the Inter-American Development Bank. Financial support from the IDB at several stages made research trips to Colombia, Mexico, Argentina, Korea, Brazil, and Chile possible. I am grateful to the IDB for permission to reuse two IDB working papers (Schneider 2009a; 2013b). I am also grateful to the Hanse-Wissenschaftskolleg in Delmenhorst for fellowship support for the final revisions.

Several dozen interviewees, most listed in the appendix, provided invaluable insights. I am also grateful for comments and feedback on earlier versions from Eduardo Fernandez-Arias, Marcela Eslava, Alberto Fuentes, Kathryn Hochstetler, Renato Lima-Oliveira, Andrés López, Juan Pablo Luna, Marcela Melendez, Guillermo Perry, and Ernesto Stein, and participants at seminars at the Secretariat of Finance in Mexico, MIT, Repal 2014, and multiple workshops at the Inter-American Development Bank. Andrew Schrank wrote up especially penetrating and useful commentary on several earlier drafts.

1

Introduction: Institutional Dynamics of Industrial Policy

Schneider, Ben Ross. *Designing Industrial Policy in Latin America: Business-State Relations and the New Developmentalism*. New York: Palgrave Macmillan, 2015.
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For a while it appeared that industrial policy had died and been buried along with the 20th century. However, by the mid 2000s, it was, zombie-like, back.¹ Early sporadic debates started among some academics, in a few multilateral agencies in Washington, and in some policy making bodies in Latin America and other developing regions. The reasons for the revival were diverse, ranging from dismay at the results of market reforms in the 1990s, to the surprising success of left-wing parties, to ongoing tinkering and pragmatism among officials in surviving development agencies, and the new developmentalism in the region (Ban 2013). The financial crisis of 2008–10 reinforced statist proclivities across the globe and gave new respectability to the interventionist BRIC model.

Economists who came to advocate, or at least accept, a new role for industrial policy were quick to point out that a key risk (that contributed to its demise in the 1990s) was still that policy makers lacked the information necessary to design effective interventions. This was true in the simpler 20th century and ever more so in the 21st. In Latin America, ongoing development, globalization, and integration into the international economy rendered the challenges of state intervention into the private economy through industrial policy ever more complex, delicate, and information intensive.

The solution proposed by many to managing these informational and other complexities was more intricate, intensive, and continuous contact between government officials and business people.² Rodrik (2007, 100) argued that “the task of industrial policy is as much about eliciting information from the private sector . . . as it is about implementing appropriate policies.” In his analysis of new export activity and self discovery in Latin America, Sabel (2012) argues that the key to success is coordination both among private producers and between public and private actors. In their review of ten successful, late developers outside Latin America, Devlin and Morguillansky (2011, 4) argue that their strategies are “not a creation of the central government alone but instead arise out of public–private

1 For brief histories of the debate, see Stiglitz, Lin, and Monga 2013; Agosin 2013. Industrial policy is commonly understood to be any government intervention designed to favor some sectors or activities over others (in any area of the economy, not just industry).

2 Among other recent studies, including major reports from nearly every development multilateral agency, see Devlin and Morguillansky 2011; Coutinho, Ferraz, et al. 2012; Machinea 2008; Suzigan and Furtado 2006; OECD 2013; Maloney and Perry 2005a, 36; Kuznetsov and Dahlman 2008, 112; Sabel 2009; Crespi, Fernández-Arias, and Stein 2014. Hausmann (2009) in particular emphasizes the need for a “complex policy framework” and “high bandwidth development policy.”

alliances.” Similarly, Ornston (2012) argues that dynamic forms of corporatism (tripartite arrangements among business, labor, and government) explain the recent high tech successes of Ireland, Finland, Denmark, Sweden, and Korea.³

The theoretical and practical implications are that policy analysis should pay more attention to business and that research needs to look beyond the quality of policy and the quality of the agencies of government making policy to examine in greater depth the nature of relations between public and private actors (Rodrik 2007). Hausmann, Rodrik, and Sabel go so far as to define effective industrial policy as process rather than outcome: “we take ‘good’ industrial policy to consist of those institutional arrangements and practices that organize this collaboration [between public and private sectors] effectively” (2007, 4). Yet, while many scholars agree that business-government collaboration is imperative, few delve deeply into the specific institutions best suited to promote it (see Devlin and Moguillansky 2011).

The institutional challenges are formidable. First, governments need to establish appropriate forums or councils for dialogue between representatives of business and government. Moreover, effective dialogue depends on well-organized business interlocutors. For most policy areas, not all businesses can participate in the discussions, so the organization of business, both formal and informal, is crucial for effective representation. And, even if appropriate micro institutions for business representation and business-government dialogue exist, their functioning depends heavily on the overall political environment. If some businesses can bypass associations and business-government forums to change policies, then the associations and councils lose credibility and other businesses are likely to defect (Eslava, Meléndez, and Perry 2012). On this macro level, many institutions and practices matter for business politics, but a minimum list would include parties, legislatures, campaign finance, personal networks, and lobbying.

On the challenge of designing appropriate forums or councils for effective business-government dialogue, a number of authors have put forward lists of institutional and other desiderata. In a practitioners’ guide, Herzberg and Wright focus on “six key factors in setting up and

3 Outside industrial policy, Culpepper (2002) argues that information exchange was a crucial part of business-government (and labor) dialogue over reforms to pensions and vocational education in Europe.

running a competitiveness partnership: ignition, organizing participation, structure, setting and reaching goals, the role of donors, and communications strategy” (2005, 10). Machinea et al., list a dozen “principles” that should guide “public–private alliances” (2008, chapter 6). Devlin and Morguillansky provide a full list of more than a dozen factors that facilitate public–private alliances (2011, 88–90). This book also reviews a fairly long list of optimal institutional features. However, effective business–government collaboration is both simpler to establish—and more complex to sustain—than these lists imply.

To simplify the challenge of facilitating first steps in public–private collaboration, it is useful to think of general functions, three in particular—real information exchange between business and government, allocative authority, and barriers to rent seeking. The actual institutions and organizations used to achieve these three functions are many and can vary from case to case.⁴ The important analytic task—when assessing any particular case—is to sort out which institutional components are really essential to these three general functions. When analyzing dynamics over time, effective collaboration is also more complex than the institutional desiderata imply. That is, collaboration may start with one institutional arrangement but evolve over time into new configurations by adding staff, restricting participation, devolving responsibilities to new forums or working groups, and so forth. Apt metaphors are better drawn from evolving biological systems than from one shot chemical reactions.

For purposes of understanding the institutional challenges of public–private collaboration, it is crucial to distinguish between passive and active industrial policy. Passive policies seek to change the public sector (such as red tape, infrastructural bottlenecks, and other items on the World Bank’s Doing Business survey) to reduce costs for business on the assumption that these changes will improve business performance. Active policies, in contrast, target deeper changes in the private sector, in firm behavior (e.g., exports, upgrading, or technological development) and rely on direct subsidies from the state. In targeting substantive

4 In a sense, councils are designed to correct for what Schrank and Whitford (2011) call network failure. Although they apply the concept mostly to relations among firms and other economic agents, it can also be usefully applied to relations between business and government. For Schrank and Whitford, key issues in network failure are competence and confidence which could map on to the issues here of information and rent seeking. Later chapters bring informal networks in as they affect the functioning of formal councils.

changes in business behavior, active policies establish performance standards and thus require monitoring and sanctioning capacity—a coercive side to industrial policy that is often neglected in the current revival of interest.⁵ These distinctions are developed further later. The point for now is to emphasize that the institutional challenges for passive policy are much less daunting than for active policy. The distinction is also crucial because many recent instances of business-government collaboration in Latin America revolved around competitiveness councils that focus on passive policies.

Many studies and advocates also argue that public-private collaboration requires strong political will and backing from the highest levels (Rodrik 2007, 113; Suzigan and Furtado 2006). This is certainly true if the country is going through major, contentious transitions in the overall development strategy. However, many successful examples of effective business-government collaboration occurred out of the lime light at lower levels, even subnational or in specific sectors, without much top level support. Any transfer of significant allocative authority (such as subsidies or favorable regulation) —one of the three essential functions—requires some measure of political support, but once established, the flow of resources may itself create a sufficient support coalition to keep the dialogue going without recurring infusions of political will from the top.

Appeals to political will and leadership also side step what should be an integral component of any analysis of industrial policy—prospective or retrospective—namely how it fits in the larger political context. Optimally designed policies and associated business-government councils cannot progress much if they do not fit with existing political institutions (electoral, legislative, etc.) and organization of powerful social groups (parties, associations, and networks). Political leadership or political will cannot help much without taking into consideration existing constellations of institutions and organizations. Moreover, given the privileged position of big businesses in most political systems, their structures, preferences, and capabilities merit special attention in any macro-political analysis.

5 Although not concerned with coercion, Crespi et al. (2014, Chapter 2) offer a more nuanced set of conceptual distinctions that contrast vertical/horizontal policies and public inputs/market interventions. Vertical, market interventions are, like active policy, the most risky and prone to rent seeking. However, what is missing in this conception is the fact that policies in this quadrant are intervening in firms (not just markets) and therefore require clear performance standards and monitoring.

The rest of this book takes the following form. Chapter 2 analyzes the main micro, institutional mechanisms of business-government councils concentrating on three key functions: meaningful information exchange, authoritative allocation, and minimized rent seeking. The list of contributing elements of institutional design is longer, including small numbers of participants, off-the-record discussions, frequent meetings, adequate technical staff, transparent decisions, peer monitoring, and so forth. However, these design components can be combined in different and often evolving ways to fulfill the three core functions. Chapter 2 also includes a brief review of the Korean “model” where business-government councils were crucial elements of take-off growth in the 1960s and 1970s and continued to steer technology policy in recent decades.

Chapter 3 covers a range of successful empirical examples in Latin America, organized in part by the scope of business-government collaboration. The goal is to summarize a variety of cases in recent decades that illustrate the wide range of institutional arrangements for promoting collaboration. In contrast to other reviews of broad national strategy (Machinea 2008; Devlin and Moguillansky 2011), Chapter 3 analyzes cases in particular sectors and provinces. Given contemporary complexities in the new developmentalism, many of the most promising opportunities for industrial policy may arise in these narrower, decentralized arenas (Block 2011). The empirical material comes largely from secondary sources, reports, government documents, and periodicals, but also incorporates several dozen personal interviews.

Chapter 4 turns to the macro context, especially the politics and structure of big business. The chapter delves into the formal institutions—electoral and party systems—and informal practices in Latin America that favor policy influence by big business and encourage individual over collective lobbying. From a comparative, historical perspective, contemporary developmental states in Latin America are weaker vis-à-vis business than earlier incarnations in authoritarian regimes with less-developed private sectors (Schränk 2013a). Policy makers in new democracies in Latin America are more constrained, and in this context then the base-line preferences of big business matter more for establishing limits on, and opportunities for, effective collaboration in policy making.

Most recent analyses of industrial policy—even while advocating business-government collaboration—neglect existing firms, especially the diversified business groups and MNCs that dominate big business in

most developing countries. This chapter argues instead that the design of industrial policy needs to take into account patterns of business politics and the strategies and capabilities of large firms. Although both business groups and MNCs may oppose the imposition of active industrial policy, some measures may in principle be able to harness natural strategies of business groups to diversify or push negotiations with MNCs over the kinds of performance standards they accepted in other countries.

What, in summary, does this book add to the recent spate of books on industrial policy listed in the bibliography? In essence, this book fills in the institutional dimension that other studies repeatedly invoke but rarely really analyze. Moreover, the approach here simplifies the institutional analysis of business-government collaboration and grounds it in a wealth of new empirical material from Latin America. Most importantly, the book brings in the politics and actual existing business actors that are almost completely absent from the recent spate. This last lacuna is especially puzzling. Nearly every publication on industrial policy makes extensive reference to business and the private sector, but in the abstract without mention of any specific firms. Yet, the design of industrial policies clearly has to factor in whether the target is small start-ups or huge conglomerates. The contextual analysis should therefore start with the size, structure, capabilities, and politics of existing firms.

2

Principles of Institutional Design in Business- Government Councils



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I Introduction

Outside Latin America, business-government councils are widespread and regularly associated with accelerated development. High growth Asian economies such as Korea, Taiwan, and Singapore were rife with business-government councils (Campos and Root 1996), and section III reports on the continuing centrality of business-government councils in contemporary technology policy in Korea.¹ In Japan, over 200 consultative councils (*shingikai*) “deliberate and report on every conceivable area of public policy” (Schwartz 1992, 218). Some councils dated from the early 20th century, but most, ironically, were imposed by the US occupation that created the framework legislation for councils in order to constrain the bureaucracy and make it more accountable. These councils performed important functions in reconciling divergent interests, coordinating expectations, and facilitating policy implementation (Schwartz 1992, 231–2). In northern Europe, councils are integral elements of “coordinated market economies” (CMEs) (Hall and Soskice 2001; see also Katzenstein 1985). Public–private “alliances” were also central to policy making in a recent diverse set of rapidly developing countries from New Zealand and the Czech Republic to Ireland, Finland, and Malaysia (Devlin and Moguillansky 2011; Ornston 2012). In other countries such as France, some attributed policy failures to the absence of institutions to promote effective collaboration between business and government (Levy 1999).²

Social science theory is of course divided on the wisdom of business-government intimacy. Some see great potential for more effective policy making and implementation (Amsden 1989; Amsden 2001; Campos and Root 1996; Sabel 1994; Evans 1995). Opposing theories claim that close relations between business and government are more likely to end in rent seeking or worse (see Olson 1982; Frieden 1991; Schamis 2002; Etchemendy 2011). Cheap talk is another possibility where meetings mean little to participants and have no impact, positive or negative, on policy and performance. In fact, there are plenty of empirical examples of both negative and positive relations, and hundreds of councils that are irrelevant for policies, learning, or rents. The analytic challenge is to determine the conditions under which one or another outcome is more likely.

1 Analyses of Chinese development occasionally cite the contributions of business-government councils (Murphree and Breznitz 2014).

2 Councils in other policy areas have also been credited with improving policy making. In social policy in Latin America, Garay (forthcoming) credits councils with making policy more inclusive.

This determination requires a close examination of specific institutional arrangements, or councils, for public–private intermediation and the quality of business representation on those councils. Business–government councils are only the most visible and formal features of what are often multifaceted relations between top officials and business people, but they offer the advantage of making the analysis more concrete and specific. Other theories talk more generally about overall relations—as in Evans’ “embedded autonomy” (1995) or Kohli’s “cohesive-capitalist states” (2004)—but do not drill down into specific forms and forums of interaction. For other purposes, the key to the relationship may lie in informal networks, the structure of business groups and MNCs, or political coalitions that are considered in later sections and chapters, but this section concentrates on formal councils. In the absence of long-standing network ties, councils are usually the only means in the short run for policy makers to start the flows of information that are deemed so indispensable to making industrial policy.

What is a council? In practice, governments use a variety of different labels including councils, boards, forums, and public–private dialogue (PPD), but to simplify the presentation all these are grouped under the general label of council. In principle, business–government councils can be differentiated by formal responsibilities: deliberation, consultation, implementation, and oversight. Deliberative councils discuss policy options and either set policy directly or make recommendations to executive agencies. In consultative forums, government representatives bring policy proposals or decisions to the council for feedback and suggestions. In contrast, executive and implementation councils take broad policy guidelines and decide the specifics of how to implement them. Lastly, oversight councils or boards monitor results and the performance of private firms and government agencies in fulfilling policy goals (that the boards may not have set). In practice, however, many councils are charged with multiple responsibilities, and even in cases of councils with narrow formal mandates, council members may expand their activities informally. In any case, impact assessments need to be attuned to the varying responsibilities and goals of councils in order to compare results with actually intended outcomes.³

3 These conceptual distinctions are important in principle, and should guide initial expectations on what councils may be able to achieve. However, these distinctions are less useful for elaborating a fixed typology to classify councils, because the empirical variation is too complex. Many councils are charged with multiple goals and in others the mix of

Another crucial aspect in the goals of councils is whether the main purpose is to change behavior in the private sector or in the public sector. Some councils seek primarily to change public behavior (red tape, taxes, infrastructure, trade negotiations, etc.). This was the case in most of the “public–private dialogue” (PPD) supported by the World Bank, especially in Africa and transition economies (interview with Benjamin Herzberg, 8 October 2008). This is also the focus of annual surveys like the World Bank’s Doing Business that ranks countries across 11 areas of “regulations that enhance business activity and those that constrain it.” The survey covers areas such as starting a business, dealing with construction permits, getting electricity, registering property, getting credit, paying taxes, and employing workers (World Bank 2013, i). In other instances, especially of industrial policy, the goal is primarily to use public rules and subsidies to alter private behavior—to get SMEs to export more, to get firms to invest more in R&D, to get companies to enter new sectors, and so forth.⁴

The former is *passive* industrial policy where governments take action to reduce the costs of doing business on the assumption that business will respond, versus the latter, *active* policy where governments have expectations on desired shifts in private behavior, use subsidies to induce the shift, and establish performance standards (e.g., increases in exports) which if not met cause the governments to withdraw the subsidies. Both active and passive policies are designed to change conditions in the private sector, but passive policy does it indirectly by lifting constraints on business while active policy does it directly by imposing constraints or performance standards on firms. Active industrial policy, with Amsden’s (1989) core concept of reciprocity (subsidies in exchange for firm performance) was of course crucial to Korea’s big push industrialization of the 1960s and 1970s.⁵ But, coercing firms to comply is not just a policy for early industrialization. It was also central to industrial policy in a

responsibilities changes over time. Some of the most interesting, problem-solving councils combine all responsibilities. For other typologies of scope and function, see Devlin and Moguillansky 2011; OECD 2013.

- 4 Although rarely labeled as such, patent laws are a near universal form of active industrial policy. Patents establish certain performance standards and firms adjust their behavior (invest in R&D). In contrast though to most industrial policies, the subsidy (through patent protection) comes after the change in firm behavior (greater investment in R&D).
- 5 For Amsden (1989; Amsden 2001) and Chibber (2005) developmental states in East Asia succeeded because they “disciplined” business, through what I am calling active industrial policy.

range of later experiences such as Finland's in the 1990s in technology policy (Ornston 2012, 68).

The distinction between active and passive industrial policy is especially relevant to the problems of business-government collaboration. In general, generating effective business-government collaboration in passive policy is far less institutionally challenging than in active policy. In passive policy:

- 1 the costs to business of participation are low (business needs merely to let government know which changes in public infrastructure and regulation would most reduce their costs);
- 2 the benefits to business are high (e.g., lower regulation or transportation costs);
- 3 the risk of rent seeking is low (because most changes in the public sector are horizontal and are closer to public goods, at least for business); and
- 4 government officials need not be concerned with monitoring outcomes or imposing sanctions if firm performance does not improve.

In active policy, in contrast, the institutional costs and challenges are greater on all dimensions:

- 1 the costs to business are high because business has to reveal information about firm capabilities;
- 2 the benefits and subsidies may be substantial, but they come with strings attached;
- 3 the risk of rent seeking is higher because subsidies are firm-specific (as in subsidized credit);
- 4 monitoring costs are high as governments need to determine whether subsidized firms are meeting performance standards (e.g., exports, local content, R&D) (and firms have incentives to distort that information); and
- 5 sanctioning low performing firms is difficult and politically costly.

In practice, of course, governments, or different parts of governments, can do both active and passive industrial policy. In fact, active policy is almost always accompanied by passive policies, though the reverse is not the case. The distinction is essential though when considering institutional requisites.

Recent examples of active policy with explicit targets and sanctions are not widespread in Latin America's new developmentalism. Some of the most prominent examples come from local content policies in Brazil which has the "most ambitious" industrial policies in the region (Devlin and Moguillansky 2013). For example, the BNDES (especially in wind power loans) imposed fines on firms that did not meet local content requirements stipulated in their loan contracts. Similarly, Petrobras imposes penalties on suppliers that do not meet the local content percentages set in their procurement bids (Almeida, Lima-Oliveira, and Schneider 2014). More generally, many regulatory agencies in several contexts have been able to impose fines and sanctions on firms that have not met performance standards (on Argentina, see Post 2014). Moreover, some regulatory agencies are charged with additional developmental functions such as promoting R&D that resemble industrial policy. In this instance, license to operate in the regulated sector constitutes the inducement but already comes with performance requirements (beyond price and quality) like investing specified amounts in R&D (Schrank 2013b).

Councils can also be distinguished by the intensity of interaction between business and government. Many councils may simply serve as forums to exchange information, where public and private participants share information about their plans, preferences, capabilities, and deficiencies. So, for example, in implementation, government participants might just inform business people, or in oversight councils business representatives might just report on progress. Such councils serve in a first sense to decrease dramatically the costs of information. Beyond simple exchange, a more intense and potentially consequential interaction comes in the form of joint problem solving. In this instance, either business or government can raise a problem—congested ports, high energy costs, lack of skilled workers, or absence of pivotal technologies—and then the council seeks to find a remedy through an ongoing process of policy design, implementation, assessment, correction, and so on. This process is similar to what Sabel (1994) emphasized as learning but perhaps shallower, as participants may engage in pragmatic problem-solving without any deeper individual transformation. In any case, the institutional requirements for effective joint problem solving are greater than for other simpler forms of information exchange.

Features of institutional design can foster effective business-government collaboration to the extent they promote three mutually

reinforcing functions: meaningful information exchange; authoritative allocation; and minimal rent seeking.⁶ Factors contributing to information exchange include adequate frequency and duration of interaction, effective representation of business, competent technical staff, and small numbers of participants. These design components matter little though if the councils have no real power to allocate resources, subsidies, or regulations. Then, of course, once significant resources are on the table, effective councils require mechanisms to minimize temptations and opportunities for rent seeking. The next section analyzes a series of institutional design components and their impacts on these three core functions.

II What happens in councils: disaggregating interactions

What are the major alleged benefits of dialogue between representatives of government and business (see also Herzberg and Wright 2005)? For Campos and Root, the benefits are many:

A council serves as a convenient channel for collecting relevant information from, and distributing it to, its participants. It thus improves economic efficiency: it supplements the allocative function of markets by facilitating coordinated responses to changes in economic conditions. A council also helps reduce the opportunities for and welfare losses from rent seeking. Furthermore a council performs a commitment function, binding sovereign authority to a set of rules governing economic policymaking. Hence it helps minimize economic distortions attributable to the nonsimultaneity of the costs and benefits of a policy (1996, 99).

Some of the main hypothesized benefits—information, coordination, and credibility or trust—can be separated out by time frame. In the short run, there is an immediate information benefit for policy makers from talking to business people who know their operations better, as well as a benefit for business people, especially from smaller firms, who may know less than policy makers about the international environment or the domestic macro-economic context. In the medium term, representatives of business and government can work out coordination issues, especially

⁶ In a similar vein, although applied to development challenges, Doner (2009, 68) argues that successful governance requires consultation, credible commitments, and monitoring.

co-dependent investments by government and business or by businesses at various points in the productive chain. Over the longer term, with frequent reiterated interactions, business-government dialogue can promote consensus building, reciprocity, trust, and collective learning (Sabel 1994; Amsden 1989).⁷

A first question in institutional design is who will be at the table.⁸ For example, *smaller numbers* of participants facilitate information exchange. However, keeping numbers small has to be balanced against the need to have all relevant parties at the table. Business associations can help resolve the tension between inclusion and small numbers if one or several representatives from associations can effectively represent larger numbers of business people.⁹ Business associations offer a standard institutional channel for identifying leaders already legitimated by some formal representative selection procedure. However, that selection procedure may favor certain firms, regions, or sectors over others and distort some leaders' legitimacy or ability to speak for the broader interests of business (Schneider 2004). In addition, in some instances, business leaders viewed as broadly legitimate spokespersons may arise informally as in the case of Jorge Gerdauro Johansen in Brazil (Bacoccina and Queiroz 2012) or a series of business leaders in Colombia (Eslava, Meléndez, et al. 2012). These leaders have established reputations that allow them to represent business informally in collaboration with government.¹⁰

Similarly, greater *homogeneity* among business participants makes it easier to come to agreement (Olson 1965). This suggests that in principle adding in non-business stakeholders like labor unions or citizen groups

7 See Schneider and Maxfield (1997) for more extended discussion of longer term evolution of credibility and trust. Here the emphasis is on shorter term questions of institutional design and basic information exchange.

8 For other discussions of institutional design, see Herzberg and Wright (2005, 10), Machinea et al. (2008), Rodrik (2007: 113–7), and Devlin and Morguillansky (2011, 88–90; 2013).

9 For Herzberg and Wright (2005, 13), “the plenary group should contain no more than 20 participants and should include intermediaries such as business associations whenever possible, the aim being to reach out to thousands of businesses without making meetings unwieldy.”

10 Sources of perceived legitimacy and credibility are of course multiple and complex. The simplest source is repeated interactions over time where business people and government officials establish reputations as interlocutors who do not—when the opportunity arises—push particularistic interests. Within the small worlds of economic and political elites, individuals know they are entering long-term networks and relationships where reputations matter.

will complicate deliberations over industrial policy. However, some degree of heterogeneity among business participants can build in peer monitoring and internal incentives against rent seeking (as discussed later), as one sector has incentives to stop firms in other sectors from seeking rents.

Another dimension of heterogeneity that is rarely broached is foreign ownership. In most of Latin America, and many other middle-income countries, a third to a half of the largest firms are MNCs (Schneider 2013). MNCs often come up in recommendations for industrial policy, usually in the sense of using various incentives and horizontal, passive policies to attract more FDI (Devlin and Mogueillansky 2011; Pack and Saggi 2006). When invited to participate in business-government councils, MNCs introduce an important element of heterogeneity, which varies though by issue. On most horizontal and passive policies like subsidies for training or less red tape, MNCs and domestic firms likely differ little in their support.

However, MNCs are mobile (as of course are some more internationalized domestic firms), so may not be as reliable partners as local firms over the longer term and may have more reason to oppose active industrial policies with performance standards that require firms to export more, transfer technology, invest in R&D, and so forth. Yet, in other ways, MNCs may be more amenable to performance standards than domestic firms (and less able politically to oppose them (Chapter 4)). When governments control MNC access to valuable domestic resources—large consumer markets, skilled labor, or natural resources—then governments can bargain over the terms of MNC entry—including performance standards—and MNCs have experience with such negotiations in other countries. But, the main point here is that for the functioning of business-government councils, MNCs pose at least the question of divergent interests, and, as discussed in Chapter 3, policy makers sometimes explicitly excluded MNCs from councils.

The institutional design of councils also regulates what parts of the dialogue are off the record and what parts on. Meaningful sharing of information among participants will in most cases require a *guarantee of confidentiality*. In practice, this guarantee is only in small measure a matter of design and rules. It will only become credible over time as participants build reputations by sharing information in the council that is not subsequently leaked or abused.

Although *time horizons* are generally short in Latin America, and institutional instability common, institutional design can be important at the

outset in signaling likely horizons. Meetings can be called on an ad hoc basis, established by executive order, or legislated into law, in ascending order of the length of expected time horizons of the participants. At the outer extreme, participants may be appointed with fixed mandates, and protected from dismissal, as with regulatory agencies. Statutes or other measures that set a fixed frequency of meetings also establish the more important expectation of reiterated contacts with the same people. Weekly or monthly meetings raise expectations of reiterated interactions with the same set of business and government representatives. Quarterly or yearly meetings, in contrast, raise the probability of turnover among members, and reduce the incentive to invest in personal relationships.¹¹ Significant in this regard, especially in comparison with other regions, is the high number of political appointees in the top ranks of government in Latin America. Virtually all ministry officials in the top 3–4 levels of the executive branch, throughout the Americas (United States as well), are appointed by presidents (see Grindle 2012). Political appointees are more likely to lose their jobs or get appointed to new jobs than are career civil servants.

The *level of the representation* at the council table also affects the dialogue. Some think it is crucial to have the highest level representation from the government, including the President if possible (Rodrik 2007, 113).¹² Such high level representation has the advantage of convincing business participants that the council will take significant decisions on allocation regardless of the formal attributes. For business it is nearly always worthwhile to sit in small meetings with Presidents, both to convey business views in a mostly private setting and to hear what Presidents have to say about policy directions. However, having the President involved can also signal that the council may not last long. In contrast, councils comprised largely of lower level officials and representatives of business associations, with statutory authority to allocate resources have longer time horizons.

In a related vein, reports on industrial policy from multilateral agencies almost always emphasize the necessity of “high level political will”

11 In his review of successful councils outside Latin America, Devlin found they met every month or every two months (2014, 36).

12 For Herzberg and Wright, “government representation must be at the highest possible level for the partnership to have credibility: a consistent feature of competitiveness partnerships is the correlation between the progress achieved and the seniority of government figures involved” (2005, 14).

(OECD 2013, 123) or leadership (Devlin and Moguillansky 2011, 81), sometimes invoking iconic images of President Park Chung Hee chairing monthly meetings of export councils in Korea in the 1960s. Such top-level participation can of course overcome many obstacles. However, more generally, political will and leadership are analytically empty and usually tautological; empty because they are impossible to measure *ex ante* and consequently tautological because their effect is apparent only after the fact. In this view, successful business-government collaboration must have benefited from an infusion of political will, and failed efforts clearly lacked it. Authoritative allocation is a better gauge of government commitment (i.e., actualized political will) because it is based on measurables like subsidies or regulatory jurisdiction.

As noted in the introduction, the institutional design of councils usually sets the varying *responsibilities* (deliberative, consultative, implementation, or oversight). Knowing these responsibilities is crucial for establishing expectations and benchmarks for success. So, for example, a council charged with promoting general discussions between government and business may appear to accomplish little in terms of changing policy or firm behavior, but then that was not the intention. Such general, open ended forums may be more valuable in contexts where there has been little previous contact, as for example in the case of political transitions or the arrival to power of previously excluded parties and politicians (Herzberg and Wright 2005, 8). Otherwise the hypothesis would be that councils are likely to function better if the goals are narrow and measurable (increasing exports or upgrading production in a particular sector, for example) rather than broad and unmeasurable (competitiveness or innovation) (Porter, Emmons, et al. 2002, 15).

Returning to institutional desiderata, for passive, and especially for active, industrial policy, dedicated and *competent technical staff* can be crucial for councils to make progress both at and between meetings (Rodrik 2007, 113).¹³ That is, council members may discuss policy options or reveal areas where they need more information. If the council lacks staff to follow up, then the council is more likely to end up in inconclusive “cheap talk.” Staff may be even more proactive in generating new information or items for discussion or decision. In most cases staff, or

13 The staff, or secretariat, of deliberative councils, usually drawn from participating ministries, was crucial in cases ranging from Japan (Schwartz 1992, 229), to coffee in Oaxaca (Snyder 2001, 89–92), to public–private dialogue generally (Herzberg and Wright 2005, 17).

the council secretariat, is loaned or seconded from participating ministries or government agencies (as in Japan (Schwartz 1992)). In some cases these officials may work closely with staff from business associations in technical working groups.

To overcome the costs of participation, councils must be perceived by business interlocutors to make *authoritative allocations*, to decide on the distribution or redistribution of resources. So, for example, social pacts set prices and wages, trade consultations decide on negotiating positions, and industrial policy councils can distribute subsidies. As noted earlier, the presence of presidents and ministers at council meetings also increases the expectations, absent statutory regulation, that council deliberations will affect government allocations.¹⁴ However, the best long-term mechanism for ensuring some benefit from participating in the council is to set by statute some allocation as in subsidized loans, grants, export quotas, minimum wages, training programs, or infrastructure investment.

Overall, there are no sufficient and only a few necessary institutional conditions—manageable numbers, regular meetings, resources, and some technical support—for serious engagement between business and government. Otherwise, as discussed later, a wide range of different institutional configurations can have, and have had, positive impacts. In thinking about optimal institutional engineering, it is better to use evolving biological rather than mechanical chemical (or alchemy) metaphors. In most successful cases of business-government collaboration, it was not a matter of simply assembling an initial set of institutions and allowing a virtuous process to unfold, but rather a more ad hoc and dynamic evolution where participants came together, sometimes informally to begin with, then cooperated through some initial set of institutions which over time the participants (or exogenous shocks) modified to better suit their evolving functions and political circumstances. Some of the cases in Chapter 3 illustrate these dynamics well.

The third main issue in institutional design is impeding unproductive rent seeking, though this is less of a concern with horizontal and passive policies. Active industrial policies by definition create and distribute

14 Hausmann (2009) emphasizes the importance of rents for motivating business participation. Councils convened under crisis conditions (such as falling export prices, war, inflation) increase the expectation that the council will make allocative decisions (as well as increase the likelihood that participants will accept sacrifices) (see Herzberg and Wright 2005, 12).

rents in order to shift behaviors in business, and even squeaky clean firms will seek them to enhance competitiveness. The worry though is with wasteful or unproductive rent seeking. The near universal remedies proposed are various forms of external policing: transparency, accountability, regular monitoring, and evaluation by outside bodies (Rodrik 2007, 114; OECD 2013). Hausmann puts a lot of stock in transparency: the policy making “system must operate on principles of transparency, which will not only limit the types of requests that the private sector will be willing to make but will also discipline the public response” (2009, 196). Hausmann et al. (2007) further propose outside evaluating teams, including academics and MNC executives. Others emphasize the importance of publishing relevant data and encouraging active and independent media coverage (Coutinho, Ferraz, et al. 2012).¹⁵

The common emphasis on transparency and monitoring is misplaced for three reasons, two practical and one theoretical. On the practical side, transparency is overrated because it can be so easily evaded. If, for instance, council discussions are public record, then rent seekers will rely on side conversations. Monitoring bodies can also be co-opted or defanged. Or, conversely, these bodies may become so strong as to constrain the flexibility and discretion that are indispensable to industrial policy. Some think the new oversight agencies in Brazil have started to have this effect (Almeida, Lima-Oliveira, et al. 2014). The theoretical mistake is to focus exclusively on external deterrence and sanctions. The monitoring approach assumes that council members will collude unless otherwise deterred. The theoretical alternative is to look for incentives internal to the council that could counteract temptations to seek rents.

Thus, beyond transparency, there is greater reason to put hope in the potential for self-monitoring where some set of participants in the council have strong interests in preventing rent seeking. For example, in the Turkish textile sector, the government delegated to the sector association decisions on how to allocate export quotas. Within the association, a committee made the allocations in an open setting (among association

15 Monitoring is made difficult by both the cost of information and the asymmetry. Information is less costly in policies designed to promote easily measurable outcomes like increased production or exports, but gets far more costly in policies designed to promote upgrading, innovation, or R&D. Moreover, business has the information as well as incentives to use it to their advantage. In principle, councils can vastly reduce the cost and asymmetry problems, but the cost reductions are less likely to result from clever institutional design than from the reiterated exchanges necessary to build credibility and trust.

members) that made it difficult to engage in rent seeking by firms seeking quotas (Biddle and Milor 1997). In Colombia, in the CPC (Consejo Privado de Competitividad), “there are also anecdotes about members of the [CPC] opposing proposals, brought up by other members, considered harmful for the wider interests of the country despite bringing clear benefits to some [CPC] members” (Eslava, Meléndez, et al. 2012, 15) (interview with top staff at CPC, 1 February 2013) (see also Pires, Gomide, and Amaral 2013). In Finland in the 1990s industrial policy,

neo-corporatist networks not only pressured firms to commit resources but relied on peer monitoring to more effectively assess individual efforts. Tekes [Finnish Funding Agency for Technology and Innovation] forced firms to collaborate with public-sector actors and one another. In so doing, it enabled enterprises to monitor one another’s efforts and raise the costs associated with opportunistic behavior (Ornston 2012, 70).

In sum, building in peer monitoring and incentives against rent seeking may be less costly institutionally and more effective than cumbersome, uncertain external monitoring.

The complication for institutional design is that a concern with rent seeking favors a number of features that conflict with those that promote dialogue.¹⁶ So, for instance, expanding the numbers of council members would impede side deals and collusion. More diverse participants from multiple sectors, including representatives from labor unions and other groups in civil society, would encourage opposition within councils to special favors for one sector or firm (Herzberg and Wright 2005, 7–8; Devlin and Moguillansky 2011, 90; OECD 2013). And, more open proceedings with the press in attendance would provide ongoing monitoring. However, most of these monitoring mechanisms would, as noted above, undermine effective dialogue and real information exchange, and thereby reduce the potential benefits. So, the gains of expanding transparency or the numbers and diversity of participants come at a cost to meaningful dialogue.

On the levels of representation, technical personnel from government, especially career professionals (or Weberian bureaucrats) should

16 Campos and Root have a more (overly?) sanguine view of the inherent ability of the council format to impede rent seeking: “In sum, when rules, procedures, and regulations are discussed openly among the relevant parties and input from all parties is encouraged, a more transparent and impartial policy environment emerges. This constricts the possible avenues for seeking or granting special favors and raises the cost and reduces the potential gains from rent seeking” (1996, 102–3).

in principle have more capacity for resisting rent seeking than politicians or political appointees. Peter Evans (1995), in his general theory of embedded autonomy, placed a great deal of weight on the ability of Weberian bureaucracies to impede rent seeking. In a narrower case in Oaxaca (details in Chapter 3), the director and technical staff of the coffee council performed “a disciplinary role that defused the potential for a pork-barrel pattern of project allocation” (Snyder 2001, 89–90). Politicians, in contrast, have short-time horizons and need large campaign contributions and other patronage resources, and so would be more receptive to various political exchanges with business participants. Political appointees in the executive branch are less directly dependent on resources from business, but their current and next appointments can be heavily influenced by business support or opposition. Or, as with many regulatory agencies, they may be considering taking jobs in the private sector after leaving government. Lastly, if business representatives are also drawn from firms’ technical staff, they may be less motivated by rent seeking than business owners (see the next section on technology policy in Korea).

The general point again is to think of ways to resist the temptation to seek rents more through building in contrary incentives rather than by devising rules and procedures against it. So, for example, if government participants and technical staff for councils are drawn from career civil servants in line ministries (Weberian bureaucrats), on secondment, then their long-term interests lie with their ministries, and they gain less by acceding to collusion with business. In contrast, if government representatives are political or confidence appointees, they might see options for later employment with (or campaign contributions from) business participants, and then, as in cases of regulatory capture, incentives for working against rent seeking are diminished. Incentive structures, of course, provide no absolute guarantees, but, if strong and diverse, seem more promising than rules and transparency (especially in weakly institutionalized contexts) in reducing the likelihood of rent seeking.

III The Korean model in export and technology councils

As noted at the beginning of this chapter, business-government forums, or deliberation councils, have been ubiquitous in development

experiences of East Asia and usually credited with improving the design and implementation of industrial policy (Campos and Root 1996; Amsden 1989; Evans 1995). Japan pioneered deliberation councils for a wide range of policy areas, but more recent and relevant experiences for Latin America come from Korea (see also Kuo 1995 on Taiwan). In particular, the Korean export council of the 1960s has become something of a developmentalist touchstone, and recent councils in technology policy illustrate ongoing institutional innovation in designing new forms of deeper integration between business and government. These cases give more concrete examples of most of the more theoretical and deductive points made so far in this chapter.

Historically, the most famous example was the export council inaugurated in the 1960s by Park Chung Hee (Campos and Root 1996, 90–2; Lim 2013). This council met monthly, chaired by the president himself, to monitor the progress of increasing exports and to discuss obstacles to that progress. Participants included top government officials, major business associations, and heads of major business groups or *chaebol* (there were virtually no major MNCs in Korea at the time). This was a prime example of joint problem solving that brought together detailed information from the private sector (that state officials could not have collected) with the mobilization of the state apparatus (Park would instruct ministers to solve specified problems). Moreover, success in increasing exports gave firms access to more subsidies. That is, it was an active industrial policy with clear performance standards. This example illustrates several key arguments made generally about business-government councils:

Reiterated interactions. With meetings scheduled every month in the first years, business participants knew their export performance would be monitored each month with possible public discussion; and ministers knew that they would be called to account for bottle necks not resolved. More abstractly, participants had incentives not to defect (or act opportunistically) in early interactions because they knew they were in long-term relationships.

Private information. The meetings brought massive amounts of private information to government officials that would have otherwise been very costly to collect and sift through. Discovering critical bottlenecks to export expansion allowed government officials to use scarce public resources more efficiently (Westphal 1990).

Allocative authority and resources. The presence of President Park of course meant that the council had full authority to act and sufficient resources (Campos and Root 1996, 90). Business participants had every incentive to attend. However, business also had strong incentives to distort and dissemble in order to gain rents. The next two factors limited distortion and particularistic rent seeking.

Peer monitoring. With all the major exporters and business associations at the meetings, as well as other government and non-government participants, all with different perspectives and access to information, individual sectors or firms would have had a difficult time making a public case for subsidies or policies that would provide particularistic rents. Others in the room would have some idea of the cost structure of particular firms and sectors and thus be able to assess whether a policy would benefit them unduly. This wider knowledge (or at least uncertainty about information available to others) raised the risks and potential costs of rent seeking and dissembling.¹⁷

Measurable goals. The focus of the council was simpler—exports—than many councils such as those convened to discuss diffuse themes like competitiveness or innovation. Measuring exports was relatively easy, and it was hard for firms to manipulate data. In turn, government officials could easily compare the benefits firms received to their export performance (see Lim 2013).

Competitive context. Korean firms were attempting to enter or expand into already competitive international markets which of course gave them incentives to engage in sincere problem solving that would help in international markets. In addition, if firms did manage to extract rents that were not in fact necessary to their export efforts, they still had incentives to use the rents productively.

Technical staff. The council appears to have had ample professional staff drawn from both ministries and well funded business associations (Westphal 1990). In addition, “lower-level meetings between middle managers in private industry, mid-level officials in government, and

¹⁷ With close to 100 people, the meetings could not be considered small and closed, as often recommended. According to an occasional participant in the 1960s, these 100 people included government officials, experts and academics, representatives from business associations, members of the press, and chaebol CEOs. The meetings (lasting around two hours) were monthly in the 1960s, then every two months (interview with Song Byung-Nam, former staffer at the Economic Planning Board and the Korean machinery association, 6 August 2012).

experts and scholars supplemented the monthly export promotion meetings” (Campos and Root 1996, 90).

Korea’s export council is something of an ideal type in the way it combined all the elements deemed necessary for successful public–private collaboration (both in my selective framework (section II) and in approaches with longer lists of contributing factors (Herzberg and Wright 2005; Machinea 2008; Devlin and Mogueillansky 2011)), namely incentives to sustain engagement from the public sector (access to private information) and from the private sector (access to public authority and resources), and mechanisms to discourage rent seeking (peer monitoring, measurable goals, and competitive context).¹⁸ Few councils in other times and countries combine all these elements, but, as a benchmark, other councils can be compared to it to assess the implications of missing or weaker elements. The export policy and council also provide prime examples of active industrial policy and the additional institutional investment required to implement it. That is, the government offered firm-specific subsidies that were intended to change firm behavior (increase exports). The government monitored that performance and rewarded better performers with more subsidies and punished poor performers with fewer subsidies (Westphal 1990).

Democratic governments in Korea in the late 1980s and early 1990s abandoned most of the industrial policies of the previous military regime, in part because the chaebol were increasingly viewed as too big and powerful, as well as successful enough to prosper without government help (a view shared by many chaebol) (see Larson and Park 2014). For left politicians especially, government support for, or capture by, chaebol continued to fuel political controversy and therefore complicated efforts to renew industrial and technology policy.

However, governments maintained, and in the 2000s significantly expanded, active technology policies, an updated name for industrial policy (see Hwang and Choung 2014). By the 2000s, Korea was at the top of the world league tables in spending on R&D (over three percent) and three quarters of that was private.¹⁹ Yet, policy makers felt technology

18 Business associations in Korea were usually core participants in councils. They were generally strong in terms of staff and membership, though often dependent on government for support and legal constraints. See Kim 1993.

19 By 2013, Korea was spending 3.6 percent of GDP on R&D, tied with Finland for second place in the world, behind Israel (Grueber and Studt 2013, 7).

and innovation were keys to Korea's continued growth and competitiveness (especially with China taking over lower technology manufacturing). Public investment in technology is also easier to justify as social benefits generally exceed private benefits, especially if private firms are already investing heavily and governments step in only to complement and accelerate private innovation.

As with many previous policies, the Korean government set up public-private forums to help devise, monitor, and implement technology policy. In fact, various kinds of business-government forums (that often also included academic researchers) were imbricated throughout the policy making structure from the top level NSTC (National Science and Technology Council) through lower level, more specialized working groups, to the advisory boards of government research institutes. The names, structures, staffing, and budgets of successive science and technology bodies varied over the 2000s, but close consultation with business was constant. Significantly, representation from the private sector did not come from chaebol owners or CEOs nor from major business associations, but rather from technical personnel from R&D units in private companies. The NSTC (created in 2011 with ministerial status) had an advisory board of ten members (three from government, one from business, and six from academic and research institutes), and has a staff of 130 (many of whom were hired from business).²⁰ Most of the planning activities of the NSTC happened in seven working groups on areas like green technology, biotech, and IT. Membership in these working groups (15–20 members per group) was divided roughly in thirds among government, public research institutions, and business (again technical experts working in R&D). These working groups met quite frequently, around three times per month (interview with Kim Do Jeon, chairman of NSTC, 6 August 2012). Private sector representation was also common in the numerous other instances of technology policy including the boards of a dozen or so research institutes and in the Ministry of the Knowledge Economy (MKE).²¹

20 Significantly, when the NSTC expanded its staff in the 2000s, government officials sought to recruit half of the new staffers from the private sector. In the end though, they hired more applicants from the public sector because they were more qualified (interview, Kim Do Jeon, chairman National Science and Technology Commission, 6 August 2012).

21 The MKE has a strategic planning unit for R&D. The unit is a semi-public agency, and the staff of around 50 is all hired on short term contracts from the private sector (interview with Chung Yang-ho, MKE, 10 August 2012).

These councils benefited from some of the components of the previous export council such as private information, public resources, and peer monitoring, as well as top-level technical staff. However, the technology councils lacked simple measurable goals—always difficult in R&D where outcomes are uncertain—and a directly competitive environment. R&D is of course crucial to long-term competitiveness, but it is removed from day-to-day market pressures. Several other factors though substituted in reducing opportunities for rent seeking. For one, the representatives from the private sector were lower level technical personnel—scientists and engineers—drawn normally from R&D departments of big businesses. By training at least, their orientation was more towards problem solving on technical issues rather immediate company profitability. Moreover, by the 2000s, three quarters of R&D spending was private, so business, especially the chaebol, was not dependent on public spending and subsidies. Although the government wanted some resources to go to less applied research, most of it was still geared to fostering commercial applications, so private participation was intended to pull spending in applied ways that would benefit private R&D. The risk here is less of rent seeking and more that scarce public investment merely substituted for private investment that would have happened anyway.

Few councils in the world match the Korean export council in intensity nor the technology councils in terms of deep, multi-layered private–public integration. Along with many other investments in technology, Korean policy makers invested heavily in institutional R&D. These council models cannot of course be put forward as templates to be copied as they depended on particular contexts for design and execution. These were also intensely active industrial policies, especially export performance, that imposed major changes in business behavior through targeted and generous subsidies, and so may have less relevance for governments adopting more passive policies. However, they do show the multiple elements that can go into fulfilling the three key functions of information exchange, allocative authority, and constraints on rent seeking.

IV Conclusion

This chapter attempted to distill out—inductively and deductively—core principles of institutional design of business-government councils. This is not the first such attempt; in fact such efforts are proliferating

(Rodrik 2007; Herzberg and Wright 2005; Machinea 2008; Devlin and Moguillansky 2011). Despite important areas of overlap, this chapter is distinctive in several ways. First, while covering a list of institution desiderata, this chapter simplified the analysis by focusing on three core functions—information exchange, allocative authority, and constraints on rent seeking—and analyzed the ways in which different and evolving institutional features have promoted these three functions.

For the most part, this chapter has analyzed these three functions separately. However, they also interact, sometimes in positive ways, sometimes negative. The provision of subsidies through authoritative allocation of course encourages business to share information and at the same time provides incentives to seek rents. Sharing information, at least among participants at the table, in principle makes the allocation of resources transparent, and thereby provides information that helps deter rent seeking, at the same time the allocative authority of the council encourages business to distort the information they share. Lastly, as noted earlier, some of the mechanisms proposed to discourage rent seeking such as public transparency in council deliberations or expanding the diversity of council members to non-business participants also discourages business from providing the detailed, private information that policy makers need. There are no easy solutions to these conflicting incentives, but it bears remembering that they are built into council design from the outset.

This chapter also departs from the emerging conventional wisdom on industrial policy and institutional design in a number of other respects. A crucial distinction elaborated in this chapter is between active and passive industrial policies. This distinction warrants repetition because so many policy proposals for business-government councils are premised on passive policies of reforming government or adding public complements to private investments with no strings attached. This is more a helping hand than a prodding, obliging, or guiding hand. There may be good grounds—due to limitations of political, institutional, and/or bureaucratic capacity—for governments to pursue passive rather than active policy, but passive policies are quite distinct from what are considered successful industrial policies in the 20th century in countries like Korea or Finland that were very active and intervened deeply in private business. Expectations for what passive industrial policy can achieve should therefore be appropriately modest.

Moreover, most other advocates of business-government councils emphasize the importance of top-level political participation, political


will, and leadership. Empirically, these variables are difficult to measure and vulnerable to tautological explanations. The less problematic variable is allocative authority which may require political will at some point, but is thereafter given concrete manifestation in the resources allocated (which can long outlast particular politicians). Another important departure in this chapter is the emphasis on internal versus external monitoring to deter rent seeking. There are both empirical and theoretical reasons to expect that internal monitoring by business peers—often from different sectors—can be simpler to institutionalize and more effective than external monitoring.

Although largely theoretical with occasional empirical references, this chapter also included a brief excursus on export and technology councils in Korea. The idea is that Korea has become a model and common reference point in the recent developmentalist revival, so it is worthwhile taking a closer look at the design of core councils there to establish bench marks that can be useful for comparing councils in Latin America. The Korean experience is also a crucial reference in later discussions (Chapter 4) of industrial policy, business groups, and MNCs (absent in Korea).

In sum, the institutional engineering of councils to maximize the benefits of dialogue while minimizing the risks of rent seeking is delicate, complex, and risky. There are many ways for councils to degenerate, collapse, or vegetate. Some of the causes of dysfunction seem readily apparent, as in forums that are too large, diverse, or politicized, or councils that meet infrequently or suffer high turnover among members. Overall, it is not surprising that so few councils live up to expectations. The next chapter reviews a range of councils in Latin America that have, for the most part, helped improve policy making.

3

Ongoing Experimentation with Business-Government Councils in Latin America



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I Introduction

A fundamental distinction, elaborated in Chapter 2, revolves around the difference between councils designed to change the activities of government (passive policy) and councils intended to alter the behavior of business (active industrial policy). The former are often characterized as competitiveness councils or public–private dialogue (PPD) and generally aim to reduce the cost of doing business by reforming what governments do. These passive policies are easier to negotiate and do not require monitoring or sanctioning of business. The second kind of policy and council aims to change the private sector, the realm of active industrial policy. This conceptual distinction is crucial because the expectations of private–public interaction differ so much. However, in practice some of the specific instruments and measures may look similar (e.g., port reform). This chapter examines councils engaged in both kinds of policy.

Section II selects a range of mostly successful examples of business–government councils from the larger countries of the region (see Table 3.1), especially Brazil where governments have been more engaged in pursuing a range of industrial policies. Table 3.1 comprises a small minority of the hundreds of business–government councils in Latin America, most of which do little or nothing. Several failed cases are also incorporated to highlight vulnerable points in council design and dynamics. The case selection is not random or representative, but rather focuses largely on better known, more successful cases in order to understand better their internal dynamics. With the cases cited in footnotes, this overview tries to be as exhaustive as possible in covering the secondary literature on national councils and better known regional and sectoral councils.¹ The case selection also maximizes variation in the scope, function, and jurisdiction of councils in part to show how wide the empirical variety is—councils can be added to almost any policy area at any level of government—but also to provide something of a “most-different-systems” design. If successful councils with widely different

1 Business–government councils exist in other cases of recent industrial policies, but as yet without sufficient available analysis to know how the councils functioned. On Ecuador, see Andrade 2013, on Argentina, especially software councils, see Gutman, López, and Ubfal 2006; López and Ramos 2008, and on the Dominican Republic, especially export and competitiveness councils, see Cuevas and Lee 2008. On Brazil, see other sectoral cases in Gomide and Pires 2014.

TABLE 3.1 *Three functions in councils*

	Information Exchange	Resource Allocation	Rent Seeking	Active Policy
Economy wide				
Foro (Chile 1990s)	No	No	No	N/a
CDES (Brazil 2000s)	Yes	No	No	No
Fundación Chile (since 1980s)	Yes	Yes	No	Yes
CPC (Colombia 2000s)	Yes	Yes	No	No
Coece (Mexico 1990s)	Yes	Yes	Some	No
CNIC (Chile, 2000s)	Some	Yes	No	Yes
Senai (Brazil)/Sena (Colombia)	Yes	Yes	No	No
Sectoral				
Câmaras setoriais (Brazil 1990s)	Yes	Yes	Some	Yes
MEI (Brazil 2010s)	Yes	No	No	No
Prominp (oil supply chain, Brazil)	Yes	Yes	Probably	Yes
Biodiesel (Brazil)	Yes	Yes	?	Yes
Subnational				
Oaxacan coffee (1990s, Mexico)	Yes	Yes	?	No
Mendoza wine (1990s, Argentina)	Yes	Yes	No	Yes

Note: Table constructed from secondary sources cited in this chapter. Assessment of rent seeking is based on these sources and is likely subject to under reporting.

structures and responsibilities operate according to similar internal logics, then it is more reasonable to conclude that the three functions of information exchange, allocative authority, and constraints on rent seeking have more general relevance.

Success here focuses on the immediate activities of the council and the effects on policy making: did council activities somehow improve the process of policy making? The assessment of success relies mostly on external evaluations by other scholars as well as, sometimes, on interviews with participants.² In most success stories in this chapter, researchers look beyond the councils and policy making to credit councils with major performance outcomes like greater auto production in Brazil or major upgrading and export expansion in Argentine wine.

² Ultimately, the metric of success would be whether the council promoted the desired outcome such as more exports, innovation, or productivity. This net impact is of course difficult to measure, because the comparative baseline is a counterfactual, namely what would have happened in the absence of a council (Pack and Saggi 2006). Methodologically, process tracing within councils can probably best show how participants came to recognize and solve particular problems (Schneider 2009a).

Beyond scope and function, councils differ widely in how business is incorporated. Business associations of one sort or another are included in nearly all councils, though policy makers can be selective in deciding which to invite. Some councils, especially in Brazil and Colombia, also privilege direct representation by managers and owners of the largest business groups. Lastly, given the long and extensive presence of MNCs in Latin America, it is intriguing that there is so much variation in whether and how they are included in business-government councils. The goal for this chapter is to analyze variations in representation; Chapter 4 takes a closer look at MNCs and business groups, their politics, and potential contribution to designing and implementing industrial policy.

Section III pans out to cross-national comparisons to ask why some countries of the region have more experimentation with business-government councils and more successful cases. The answer lies partly in ideology and partisan politics, but also in enduring patterns of informal networks. In other words, councils are often embedded in, and benefit from, pre-existing networks. Councils can, over time, change overall business-government relations, but they are also shaped by legacies of past relations.

II Disaggregating councils by scope and function

Economy-wide, broad function. Governments sometimes establish public-private councils with broad mandates to discuss issues affecting the economy as a whole such as systemic competitiveness, overall development planning, infrastructural bottlenecks, or macro stabilization. Economy-wide social pacts are more concerned with macro-economic stabilization than micro productivity and industrial policy, but these experiences can still be instructive.³ For example, social pacts are often initiated in moments of inflationary crisis and with the goal of negotiating significant distribution by setting wage and price increases (allocative authority), so the motivation for participation

3 See, on Chile Weyland 1997, on Mexico Kaufman, Bazdresch, and Heredia 1994; Schneider 2004; Ortega 2002, and on Uruguay and Chile (Fraile 2010). In their study of tripartite councils in eight developing countries, Fraile and Bacarro (2010) found that effective consultation and negotiation in the process of market reform helped to reconcile efficiency and equity (largely through compensatory measures to reduce social dislocation) and in part as a result made the reforms more politically sustainable.

by business and government is high. In addition, pacts often fail due to problems in representation especially the absence of effective, economy-wide business associations (Schneider 2004). Stabilization pacts also resemble active industrial policy in that they establish performance standards for business (wages and price controls), have extensive monitoring capacity, and sanction firms that deviate from the performance standards.

In the 1990s, the Chilean government created one of the early councils on productivity, the *Foro de Desarrollo Productivo*. The Foro held large annual conferences and was coordinated between conferences by a tripartite board with representatives of major business and labor associations, as well as individual labor and business people appointed by the government, with a technical secretariat in the Ministry of the Economy. The results of this Foro were disappointing, even according to its Executive Secretary, Oscar Muñoz. One of the main problems was the continuing antagonism between representatives of business and labor. Relations were so bad that the 1995 Foro had to be canceled when the CUT (*Central Unitaria de Trabajadores*) refused to participate. Other problems included a reluctance to enter binding agreements (in part because the representatives of gremial associations were unsure whether their associations would endorse the agreements), a lack of “peso politico” (political backing), and an absence of resonance in the press and public opinion (Muñoz 2000, 72). Within my framework, the Foro lacked authoritative allocation and made little progress on exchanging information.

In Brazil in 2002 the incoming Lula government created the Council for Economic and Social Development (CDES) (Doctor, M. 2007; Vizeu and Bin 2008; de Toni 2013). The government structured CDES to have representation of business (half of non-government members), labor, government, and civil society, but had different approaches to the invitations to each side. Representatives from the labor side were union leaders, yet nearly two-thirds of the business members were not leaders of business associations, but rather individual business people, many from the largest domestic business groups. Moreover, the government bypassed the national industry confederation whose president was not invited and included the heads of major state-level industry associations as well as sectoral associations in areas like banking, capital goods, and auto production. Over the course of Lula’s two terms (2003–10), CDES had some influence in broad policy debates, but less than its proponents

hoped, or critics feared.⁴ After 2010 CDES was less active; CDES met 4–5 times per year during Lula’s two terms but only once or twice per year in Dilma Rousseff’s first term (2011–14) (Schapiro 2014, 249).⁵ Overall, as a council, CDES was exclusively deliberative and consultative, without authority to allocate resources or make binding agreements.

In Colombia, the competitiveness council has been one of the most active and effective instances of national-level collaboration between business and government.⁶ Created in 2006 by the government of Álvaro Uribe, the council elicited active participation by business through a special organization created by business, the CPC (*Consejo Privado de Competitividad*). The CPC was an innovative organization with a broad membership by both large firms—national and MNCs—and major associations, and directed by a small executive committee that worked closely with government, and whose decisions and strategies were ratified periodically by the larger organization. The council grew out of a presentation by Michael Porter to business people and government officials, including president Uribe. Porter suggested Colombia create a competitiveness council. Uribe agreed and said he would include business representatives in the council if business organized that representation. The key here is that private organization and funding for staff would not have emerged in the absence of government encouragement. As one of the founders of CPC put it, “it would not have been worth the effort if the Government was not willing to recognize the Council as a formal counterpart” (Eslava, Meléndez, et al. 2012, 14).

The CPC achieved intense information exchange, some allocative authority, and, as noted above, avoided policies that might generate rents.⁷ This council was influential and with the government succeeded

4 See Cardoso, dos Santos, and Alencar 2010. During the financial crisis in 2008–09, for example, CDES was an important arena for negotiating the government’s macro policy response (ILO 2011, 45–6).

5 The first Lula government also created another tripartite council, CNDI, focused on industry. Similarly to CDES, CNDI included members from government, labor, and business. Business representatives came both from associations and large domestic firms (MNCs were not included). MDIC minister Luiz Furlan (who came from a long career in business) championed CNDI which met actively during his tenure but rarely after he left in 2007 (de Toni 2013).

6 The analysis of CPC, here and in Chapter 4, draws on Meléndez and Perry 2009; Eslava, Meléndez, et al. 2012; Rojas 2013 and interviews with business and government participants (see appendix).

7 Rents were still available through numerous other policies such as those in the program for World-Class Sectors and other infrastructure programs which may have reduced interest in seeking rents through CPC (Meléndez and Perry 2009, 16).

in a number of passive, horizontal reforms, as well as some sector specific, though still largely passive, policies in areas like cosmetics and palm oil. Councils in Colombia often get revamped or discontinued by incoming presidents, but this competitiveness council survived into the administration of Juan Manuel Santos in part because of private sector support and in part because the top staffer at CPC was nominated to run the National Planning Department. This episode shows both the crucial impact of private sector support as well as the benefits of circulation between public and private sectors—rampant in Colombia—and the strong networks it creates that undergird formal collaboration between business and government (as discussed further in Section III).

Economy-wide, narrow remit. Business-government councils may be most common and prominent in economy-wide (horizontal) policies that have a fairly narrow mandate as in trade negotiations, export promotion, labor market regulation (minimum wage), vocational training, innovation and technology, and R&D. Although most of these areas are not considered standard industrial policies, many of them do bear on the competitiveness of various sectors and have been used by governments to provide special and differentiated incentives, as for example in the many special clauses in trade agreements.⁸

Trade negotiations are where business-government interactions through a variety of formal mechanisms have been ubiquitous (with the conspicuous exception of Mercosur), and perhaps most visible, certainly in academic research. The practice of granting business substantial access and consultation probably started in the 1980s when, on the occasion of the negotiations over a free trade agreement between Canada and the United States, the US government invited business to accompany the negotiations closely. When, in turn, negotiations over Nafta began, Mexico mobilized business to match business representation on the US and Canadian delegations. From the Mexican side, business mobilized into an ad hoc organization, Coece (*Coordinación de Organismos Empresariales de Comercio Exterior*) (Thacker 2000; Shadlen 2004; Kleinberg 1999; Schneider 2004). Through Coece, business, especially

8 Most of these policies are passive in the sense that they revolve around changing government regulation and do not entail performance standards or subsequent monitoring of business. For an innovative re-interpretation of “wage setting institutions as industrial policy,” see Davis and Henrekson (2005) who argue that centralized collective bargaining in Sweden shifted the structure of industry relative to the United States in the 1950s and 1960s.

big business commissioned background studies, met with government negotiators prior to the start of negotiations, coordinated with up and down stream businesses along productive chains, accompanied the actual negotiations in the “room next door” (*cuarto del lado*), and then spearheaded lobbying in Washington for ratification of the agreement.

By all accounts the consultation was useful for giving government negotiators better information on the situation of various sectors, as well as the practical side of US-Mexican trade, and for giving business a better sense of where the agreement was headed, and as a consequence helped turn skeptical businessmen into champions. The government negotiating team had enormous allocative authority in that it was bargaining over tariff levels, phase-in timetables, and other details that had large consequences for business costs. The numerous exceptions and phase-in delays meant of course significant rents for sectors like agriculture and banking. However, built-in peer monitoring reduced rent seeking in other areas. For most industries, the government required business to join working groups organized by productive chain, so that upstream and downstream producers had to come to agreements on negotiating positions, where upstream firms did not want to face import competition if their suppliers were protected (i.e., got rents).

Although not as closely studied, governments made similar arrangements with business in Colombia and Venezuela (Giacalone 1999), Chile (Bull 2008; Schneider 2004), and in the 2000s during the negotiation of the US-Colombia free trade agreement. Most observers and scholarly evaluations had positive views of the interactions. Most of these arrangements were ad hoc, involving only the several years it normally took to negotiate a treaty. Chile, however, became a world leader in negotiating trade agreements, so throughout the 1990s and into the 2000s, governments were negotiating agreements along with private sector representatives. Constant contact made for very close relations between association staffers and government negotiators (Bull 2008). In contrast, negotiations over Mercosur largely excluded business in Argentina and Brazil (Schneider 2001). The result was post hoc lobbying by large businesses and comparatively little business engagement in promoting the trading bloc.

Another potentially revealing economy-wide council is the CNIC (Consejo Nacional de Innovación para la Competitividad) in Chile (Agosin, Larraín, and Grau 2009; Paus 2011, 75). Created in 2006, this council was charged with devising a plan and institutional structure for spending on innovation from a three percent royalty on profits in

mining. The council in the late 2000s included five ministers, at least four representatives from business, one representative from labor, and another seven representatives (academics and experts from outside government) (see <http://www.cnic.cl/>). Through the first government of Michele Bachelet, the CNIC had some successes in getting the process moving, including reaching agreement on priority sectors and activities (mostly related to natural resource exports) in which to promote innovation and in getting some of the funding on its way to innovation projects (interview with José Miguel Benavente, member of CNIC, 10 December 2008). Further public–private collaboration takes place in implementing agencies. For example, some funds flow through the Innova Chile department of Corfo which has a 21-member board comprised of equal groups from business, Corfo, and other parts of government (Agosin, Larraín, et al. 2009, 28). The CNIC budget roughly doubled over the first Bachelet government to 1.4 percent of GDP and was budgeted for \$3.6 billion in 2014 (CNIC 2013, 6). The Piñera government (2010–14) opposed vertical industrial policy and essentially suspended the planning activities of the CNIC and shifted spending from firms to education. Overall, as a business-government council, the CNIC allowed for information exchange and had significant allocative authority (though ministries had to agree to implement their priorities), but its activities were interrupted by government turnover.

Business representatives from associations like Sofofa and CPC took an encompassing view of innovation priorities, and played a crucial role in convincing the scientists and academics to concentrate on funding applied projects.⁹ However, the role of business in the council was more to consult on overall direction than to provide technical details for designing technology policy, and the business representatives did not necessarily have experience with the sectors targeted. The contrast to Korean councils in technology (discussed in Chapter 2) is revealing. Although some CNIC documents cite the Korean technology policy, the CNIC relied more on representatives from broad sectoral associations than, as in Korea, on representatives from R&D departments of large corporations, probably in part because there were fewer large R&D departments in big business groups in Chile compared to the chaebol in Korea.

Also engaged in technology and innovation, the Fundación Chile is a very different forum for business-government interaction. It is a private

9 Interviews with Benavente and Pilar Romaguera, member of CNIC, 16 August 2013.

foundation set up in 1976 by the government and ITT (Agosin, Larraín, et al. 2009). The foundation's public-private board includes representatives from government, ITT, BHP Billiton (after 2005), Sociedad Nacional de Agricultura, and several others. Representatives from private business also participate in many of the foundation's working groups. Its most famous project was the development of salmon farming, now a major industry and export sector (Agosin 1999). The core focus of the foundation is on transferring technologies in sectors related to natural resources; through the 2000s almost 90 percent of investments went to marine, forestry, and agribusiness sectors (Agosin, Larraín, et al. 2009, 30). The foundation operates like a venture capital fund (and hence with active industrial policy), either creating firms of its own (to be sold off later) or, increasingly since the 1990s, entering joint ventures (Maggi 2006). Although subject to some controversy, most assessments of Fundación Chile are favorable. For example, a World Bank study called it "one of the most successful attempts in the Latin America region to establish national 'antennae' for new technologies" (Kuznetsov and Dahlman 2008, 116) (see also Agosin, Larraín, et al. 2009; Maloney and Perry 2005b).

Vocational training. Despite its crucial importance to upgrading, business-government cooperation in training and education has received scant attention (see Ducci 2001). Business-government boards and councils or tripartite councils are since the mid 20th century ubiquitous in government-sponsored training programs in Latin America, especially the systems in many countries that are patterned on the Brazil's Senai (*Serviço Nacional de Aprendizagem Industrial*). Colombia's Servicio Nacional de Aprendizaje (SENA) is a good example (see Meléndez and Perry 2009, 38–9). In 2013, Sena's Consejo Directivo Nacional had four representatives from the government (three ministries and Colciencias), four representatives from business (from associations for industry, commerce, agriculture, and for small business), three representatives from labor, and one additional director (an archbishop). In Brazil, national and state-level councils for Senai have larger majority representation from business associations.¹⁰ These councils exchange information on training needs, allocate significant resources from payroll taxes, but do not usually impose any performance standards on firms. Castro (1998) makes a strong argument that much of the

10 On Sena, see www.sena.edu.co/Portal/Direcci%C3%B3n+General/Consejo+Directivo+Nacional/. On Senai, <http://www.sp.senai.br/Senaisp/institucional/125/o/conselho>.

success of these training systems results from the close involvement of business. As skill shortages become a greater bottleneck to upgrading and overall development, they are more likely to figure prominently in discussions over competitiveness and as corollary policies to other industrial policies (Sabel 2012).¹¹

Industry. Probably the most cited work on the importance of business-government relations in industrial policy is Peter Evans' book on informatics in Brazil, India, and Korea (Evans 1995). Evans stressed the determining role of close business-government collaboration, or "embedded autonomy" in the success of industrial policy, especially evident in Korea. In Brazil, informatics policy suffered both from only a partially Weberian bureaucracy and autonomy, as well as insufficient embeddedness of policy makers in the business community in information technology.¹² Overall, though, Evans book did not delve deeply into the specific institutional arrangements—councils or other mechanisms—to promote embedded autonomy (Schneider 1998).

Since the 1990s, the Brazil government has created a range of new councils to bring business and government together. The *câmaras setoriais* (sectoral chambers) established by the government in the early 1990s offer some revealing lessons about business-government deliberation. In the context of macro instability, the unraveling of an anti-inflation program, and increasing competition from imports, many sectors were having difficulty adjusting. The *câmaras* were designed to be tripartite (government, business, and labor) and negotiate short-term agreements on wages, prices, and in some cases taxes and other sectoral priorities. The *câmara* with the largest impact was in the auto industry where representatives from labor unions, government ministries, and associations of auto assemblers, auto parts producers, and auto dealers met to negotiate agreements over prices, wages, employment, and taxes (Arbix 1995; Toledo 1994; Coutinho, Ferraz, et al. 2012; Doctor, M. 2007). Although criticized as a subsidy to the middle class, most other analyses credit the *câmara* with reducing prices, increasing sales, stabilizing employment, improving labor relations, and fostering a longer term dialogue on productivity. One of the main motivations for all participants was the specter of dramatic decline in the industry.

11 See Culpepper (2002; 2003) on the importance of business-government collaboration (especially information exchange) in skills policy in France and Germany.

12 Business-government relations were also important in IT in Mexico (Gallagher and Zarsky 2007) and Costa Rica (Paus 2005; World Bank 2006).

The auto câmara highlights several aspects of successful business-government collaboration, in this instance with a combination of passive policy (tax reductions) and active policies (wage and price freezes with monitoring and performance standards). First, crisis, or perceptions of crisis, can help participants get quickly into meaningful negotiation. Second, success in an initial area of negotiation can prompt participants to think of other productive conversations they might have (i.e., economies of scope to collaboration) and thereby shift the activities of the council, in this case from wages, prices, and taxes to productivity and quality. The auto câmara also demonstrated the three core functions in that participants exchanged meaningful information on costs, the government offered significant benefits through tax reductions, and participants—especially firms along the supply chain and workers—could monitor one another on rent seeking. In contrast to the Foro in Chile, the inclusion of labor unions was crucial to the success of the câmara.

The Brazilian government has on occasion revived the câmara model. In 2004, the Lula government launched a successful initiative to increase the production of biodiesel (mostly from soy) by both big agribusiness and smaller family farms (Pedroti 2014). In the following years, the government created several councils and related câmaras that brought together representatives from heterogeneous groups including business (especially the mill owners (*usineiros*)), agribusiness, small farmers, and farm workers (through their union Contag). The industrial policy was active in the sense of requiring performance standards for special credits and for the “social seal” for biodiesel produced on family farms. The heterogeneous representation that complicated councils in other cases did not seem to undermine cooperation in biodiesel, and, overall, the public-private collaboration contributed to the rapid expansion of production while extending economic benefits to small farmers and farm workers.

Another recent case from Brazil covers the oil and gas supply chain. Shortly after coming to power, the PT government created Prominp (*Programa de Mobilização da Indústria Nacional de Petróleo e Gás Natural*) in 2003 to establish policy for local content requirements for Petrobras’ equipment purchases.¹³ Prominp provided multiple venues for

13 For more details, see Almeida, Lima-Oliveira, et al. 2014. See also, http://www.prominp.com.br/prominp/pt_br/pagina-inicial.htm. Prominp also coordinated massive investments in education and training, and coordinated programs in scores of different training institutes, schools, and universities. On similarly close business-government dialogue in the shipbuilding industry, see Pires, Gomide, et al. 2013.

information exchange. The top-level steering committee was composed mostly of government representatives from relevant ministries and the BNDES, plus the organization of oil firms, public and private.¹⁴ The executive committee, chaired by Petrobras, included representatives from around a dozen business associations representing major firms that produce equipment for the petroleum industry. Moreover, sectoral and project committees were responsible for elaborating very detailed guidelines on how much of each piece of equipment would have to be produced in Brazil. In short, these multiple councils provided ample opportunity for deep and ongoing information exchange between government and business.

Prominp also had huge allocative authority in that it was setting guidelines for hundreds of billions of dollars of investment. Local content requirements of course raised the cost of Petrobras investment (and were subject to sustained press criticism for the cost increases and delivery delays). These cost increases raised the incentives for business to take advantage of the information asymmetry and seek rents through costs increases beyond that of the naturally higher cost of production in Brazil.¹⁵ This was also a good example in principle of active industrial policy, where the government set performance standards for producers, monitored performance, and assessed fines for non-compliance.

Another very different consultative council for industry emerged in Brazil in 2008, in part due to business frustrations with other councils and ad hoc channels of communication. The Confederação Nacional da Indústria (CNI) took the lead in convening the Mobilização Empresarial pela Inovação (MEI).¹⁶ The substantive focus is innovation, so the CNI invited ministers and agency heads (especially BNDES and Finep) engaged in promoting innovation and around 30 CEOs of the main manufacturing firms, both foreign and Brazilian, but with a substantial

14 On the business side, the steering committee included representatives from the major oil association (IBP, that all major Brazil and foreign firms in oil and gas belong to), from ONIP, another general business-government body in oil comprised of government ministries and agencies and all relevant sectoral associations involved in the oil and gas supply chain.

15 Through late 2014, most of the allegations of corrupt bribe payments by business to Petrobras officials in the Car Wash scandal involved construction firms rather than equipment suppliers, however, the investigation was still unfolding and it was unclear how much might have involved Prominp.

16 MEI keeps a fairly low profile, so the written record on it is sparse. Much of the background here draws on interviews and conversations with Lemos, José Augusto Coelho, and Álvaro Prata. See also, <http://www.inovacaonaindustria.com.br/portal/mei/breve-historico/>.

majority of MNCs. Only CEOs and top-level ministers and officials are members, and they cannot send lower level substitutes. The meetings are well attended and well received on the government side. As a private sector initiative, MEI is purely deliberative with no allocative authority, but it does seem to be an important forum for information exchange, and reportedly contributed to formulating the government's \$30 billion technology program announced in 2013 and to the creation of technology centers affiliated with CNI's training centers (Senai, mentioned earlier) though this required no approval from government.¹⁷

Subnational councils. Industrial policy and business-government councils were also widespread at the subnational level, in both industry and agriculture.¹⁸ Although the range of policy options is more restricted at the local level, as are the resources available for allocation, other factors may facilitate effective public-private dialogue (Sabel 2012; Faguet 2012; Post 2014; Hausmann 2009). The range of participants is narrower and less diverse which facilitates decision making and information exchange, and the complexity of the policy space is less than at the national level. In most cases of provincial elites, personal networks likely pre-exist the convening of a formal council, so participants may enter discussions with a presumption of trust and credibility. Moreover, parallel networks and ongoing elite interactions make it easier to monitor rent seeking. Provincial elites live in an even smaller world with denser connections and more frequent interactions. Perceived threats that encourage participation often derive from competition from other provinces, which makes it easier to analyze and respond to them.

One sector where local councils have been especially important is in the promotion of software clusters. Provincial governments in Mexico (Mexico City, Jalisco, Aguascalientes, and Nuevo Leon) and in Argentina (Rosario and Córdoba) created councils that included representatives from government promotion agencies, software businesses (both local and multinational) and their associations, and local universities that were generally perceived as being effective in promoting the expansion

17 MEI would be a good example of the self-organized groups Hausmann (2009) recommends.

18 Another subnational case of industrial policy guided by business-government councils (with generally positive assessments) is Codech (Council for the Economic Development of Chihuahua) (Ramos 2006). Subnational industrial policy is likely to become more common and consequential in part because of the commodity boom in South America. Countries like Brazil and Chile that tax commodity exports and firms (royalties) transfer part of these royalties to governments of producing regions which in turn can use them for local development policies (OECD 2013, 134–5).

and diversification of local clusters (Ruiz Durán 2006; López and Ramos 2008). Software development seems to thrive on ongoing, face-to-face interactions that business-government (and university) councils are well suited to promoting.

Many subnational councils are in agriculture where the problem with “industrial” policy is less the common difficulty of picking winners, because in many cases government officials do in fact know what types of changes in production (fertilizer, seed variety, crop mixes, etc.) would improve productivity. The problem lies more in getting the information and incentives to many thousands of dispersed farmers. Business-government councils can help solve the credibility gap (that farmers suspect government officials do not know what they are talking about), and business associations can be crucial on the implementation side in getting the word out.

In Mexico, in the wake of the dismantling of the Instituto Mexicano del Café (IMECAFE) and national regulation of coffee, state governments filled the void with various new institutions for sectoral governance (Snyder 2001). In Oaxaca, producer groups and state officials created in 1990 a new business-government council, the *Consejo Estatal del Café del Estado de Oaxaca*, that helped secure “crucial collective goods for the coffee sector, such as a large share of the government’s budget as well as development projects that responded to the producers’ needs and yielded significant advances in productivity and quality” (i.e., mostly passive policies) (Snyder 2001, 88). The statutes established parity on the board between representatives of government and of producer organizations (apparently six of each initially), and provided the council with a director and technical staff. Besides promoting consensus and a united lobbying front for securing resources from the federal and state-level governments, the council also facilitated optimal implementation of decentralized storage and processing facilities that benefited the state’s tens of thousands of small producers.

One of the crucial elements of the story of the creation of the Oaxaca coffee council and its successful functioning was the mobilization of small producers in a new, non-corporatist association, Cepco (Coordinadora Estatal de Productores de Café de Oaxaca). Cepco successfully pressured the state government to create the council and to expand the representation by producer groups. Cepco was also instrumental in helping to implement the programs adopted by the coffee council through the collaboration of its staff with staff from the government, through its

knowledge of local conditions (highly variable through the mountainous terrain of Oaxaca), and through its ability to diffuse information about policies, programs, and new techniques to its dispersed membership.

One of the best researched provincial cases of the benefits of public-private collaboration was in wine making in Mendoza (McDermott 2007; McDermott and Corredoira 2011). Over the course of the late 1990s and early 2000s, Mendoza wine makers rapidly boosted exports by increasing the quantity and especially the quality of production. The provincial government devised a number of novel forums for business and government to interact which were crucial in devising ways to reform the marketing, technology, upgrading practices, and skills in the sector. What helps highlight the net contribution of these business-government councils is the contrast with another, much less successful, wine-producing province, San Juan, where governments also tried to promote wine production using traditional subsidy programs without extensive forms of business-government interaction.

The factors that were important in successful business-government interaction in Mendoza are several. On the government side, the governor had presidential aspirations and therefore wanted to use provincial policy innovation to showcase his leadership and vision. On the side of wine growers, they were facing an immediate crisis, and could see from Chile's earlier success the losses from not exporting more. Lastly, business and government developed over time multiple, overlapping, functionally differentiated forums and councils. The implication of this evolution is that institutional design is not a one shot event but rather part of a longer term process of learning and institutional experimentation. For McDermott and co-authors, the information function was core. There were subsidies (authoritative allocation) and barriers to rent seeking due to the export orientation, but the crucial role of business-government councils and other government support programs was to open up channels for producers to gain new knowledge from government agencies, universities, and other firms. The information function is of course all the more important when upgrading requires coordinated investments by thousands of different firms and other stakeholders.

Overall, these cases first show widespread and continuous experimentation as governments look for new institutional mechanisms for bringing business and government together, whether in long established sectors like wine and coffee or emerging areas like software and salmon farming. In addition, the wide variation of institutional formats shows

that government instigators are not working with a common template but rather adjusting institutional arrangements to the task at hand and the capabilities of the relevant participants. Many of these councils scored significant successes in improving policy making—in both passive and active industrial policy—by building support for new initiatives (Nafta and Coece in Mexico), enhancing information flows and problem solving (CNIC in Chile, CPC in Colombia, and wine in Mendoza), targeting government spending to better effect (coffee in Oaxaca), and facilitating cooperation (business and labor in Brazilian autos or dispersed software firms in Argentina and Mexico).

The examples in this section also support and illustrate the hypotheses in Chapter 2. In terms of internal dynamics, councils seemed to function better when they had small numbers of members, frequent interaction among them, competent technical staff, and less diverse interests represented at the table (with the significant exception of the *câmaras* in Brazil). Fairly immanent threats help participants focus the deliberations (especially in Brazilian autos), and the promise of significant benefits (authoritative allocation) kept business engaged (trade negotiations or wine upgrading). In many other cases, well organized business associations added an encompassing perspective to the deliberations (as in CNIC), yet councils also seemed to work well with a mix of representatives from business associations along with individually appointed business people (CPC). Lastly, explicit or implicit political backing from high authorities seemed important in some cases, especially to convince participants that the councils would have authority and access to resources, however, most worked fine without high-level representation at council meetings by presidents or ministers (or their subnational equivalents).

In most cases, the councils fulfilled the three core functions of significant information exchange, authoritative allocation, and mechanisms to impede rent seeking either through peer monitoring or because policies were horizontal and/or passive (see Table 3.1). These three functions were clearly missing in the productivity Forum in Chile in the 1990s. The Forum was only advisory without resources of its own and had a broad, vague mandate to discuss issues in productivity. Moreover, the heterogeneous and often contentious interests of business and labor politicized discussions within the forum, and neither side had incentives to divulge any meaningful information. The forum did seem to have good support from technical staff, but this was not enough to overcome

the other design problems. Rents though were not a problem because there were none to be had.

III Beyond councils: formal and informal business representation

Business associations are present in nearly all business-government councils, largely of course to have more businesses represented at the table, and to keep associations from challenging and bypassing the councils. Across Latin America, associations vary enormously in their structures and capacities (Schneider 2004) which in turn affects their ability to participate effectively in business-government collaboration. In theory, the best sorts of associations to partner with in councils have high density, professional staffs, and capacity to reconcile divergent member preferences (Doner and Schneider 2000; Schneider 2004). High member density (e.g., member output as a percent of total output of the sector or relevant category) is crucial to give the associations an authoritative voice to speak for the represented group in discussions with the government. The staff is important to the information functions emphasized in Chapter 2.¹⁹ On the dimension of managing divergent member preferences, internal interest aggregation is indispensable if business is to speak with one voice in communicating with government. Moreover, both technical staff and effective interest intermediation may serve to impede rent seeking. If association members meet regularly to reconcile differences, then they are more likely to be attentive, and resistant, to rent seeking by other members.

At first glance, well-organized associations seem a necessary prerequisite for effective business-government collaboration. However, in many instances of effective collaboration, additional less tangible, informal networks and representation can play an important part in how councils function and in some instances substitute for formal representation by associations. Some observers emphasize the importance of leadership or champions, either dynamic, committed, politically well-connected

19 Professional staff in associations, usually long-term employees, can help provide high quality information, long-term relations, and counterpart technical staff to work between meetings with government officials. However, and here time horizons are critical, if associations are invited to participate in a council over the longer run, this invitation itself can convince association leaders that they will need to invest in technical staff (Schneider 2004).

officials from government or informal leaders from the private sector, such as Jorge Johanpeter Gerdau in Brazil, Carlos Villegas in Colombia, or Juan Sánchez Navarro historically in Mexico (Schneider 2004). Such leaders can, at least in the short run, encourage participation and investment by skeptics and stand in for formal representation.

Pre-existing, parallel, or overlapping informal networks can be crucial to dynamics within formal councils (Devlin and Moguillansky 2011, 83). That is, council deliberations can quickly establish trust, credibility, and deep information sharing if members already have prior positive exchanges, expect ongoing exchanges in the future, and know that opportunism in the council could have costs outside it in other business and personal realms. Such parallel networks seem to have been key in upgrading Argentine wine production and may generally be more salient in local and regional councils where economic and political elites are smaller and geographically concentrated (Post 2014).²⁰ The case below of the Consejo Privado de Competitividad (CPC) in Colombia illustrates well these informal factors.

The strength of business associations was crucial in successful councils in distributional issues (stability pacts and trade negotiations) as well as in implementing large-scale outreach programs (such as agricultural upgrading). However, the strength of associations has been less relevant to, and predictive of, the success and failure of many forms of business-government collaboration in industrial and technology policy. For example, in broad, cross-national comparisons, encompassing business associations are better organized in Mexico, Chile, and Colombia than in Brazil (Schneider 2004). But this cross-national variation in organizational strength does not correlate with the prevalence of cases of more successful business-government collaboration and industrial policy. Mexico and Chile have few such cases, while Colombia and Brazil have more, despite the weakness and exclusion of many Brazilian associations from closer dialogue with the government.

These contrasts among Brazil, Chile, Colombia, and Mexico suggest that longer term patterns of successful business-government collaboration depend on a mix of government pragmatism, business organization,

²⁰ In a parallel vein, Katzenstein (1985; 2003) argues that smaller European countries tend to have more consensual ideologies, better organized social groups, and more closely networked elites that engage better in collective learning. Of course, strong informal ties can also increase the risk of rent seeking which may be common in other policy areas (Eslava and Meléndez 2009).

and networks both within business and between business and government. Chile and Mexico may have well-organized business associations, but governments rarely invite them to collaborate. In the first instance, recent governments have, often for ideological reasons, not implemented many industrial policies. In Chile, business-government collaboration foundered either through divisions (again ideological) as in the productivity council in the 1990s or lack of continuity as in the case of CNIC which was downgraded by the Piñera government. Concertación governments (1990–2010) included almost no top officials from business, and often viewed business as part of the right wing opposition (see Fairfield 2015). Government officials consulted frequently, and formally, with leaders of business associations, but were suspicious of informal ties. In addition, Concertación governments maintained much of the neoliberal framework for economic policy and rarely attempted to increase government intervention into the productive sector or promote major industrial policies (Agosin, Larraín, et al. 2009).

The story is similar in Mexico. Business is very well organized and participated in a range of collaborative policies with government through the 1990s, especially in trade and stabilization. However, governments after the 1990s, both PRI and PAN, were liberal in overall orientation and indisposed to adopt industrial policies (Moreno-Brid 2013). Moreover, there were perhaps even greater concerns, in government and in the media, over the domination of associations by large business groups and the stronger resulting orientation by these associations to rent seeking. One of the major associations, one that orchestrates activities of other associations, is the CMHN, a club of 40 or so of the largest business groups (Schneider 2002). In addition, large business groups like Grupo Carso (Carlos Slim) have come to dominate some of the sectoral associations.

In contrast, in Brazil the absence of an economy-wide association and the weakness of corporatist industry associations foreclosed possibilities for meaningful dialogue at more aggregate, and organized levels. However, prevailing pragmatism within the government, especially after 2002, and stronger informal networks across business and government and within government have allowed for important successes in ad hoc policies (as in the auto câmara in the 1990s) or narrower sectoral policies in the 2000s. For example, as noted earlier, since the mid 2000s, the government has tried to leverage the massive new investments in oil and gas to promote domestic industries along the supply chain and created

multiple business-government councils to coordinate policies on local content.

Colombia represents a case where strong organizations, pervasive networks, and abiding pragmatism come together and foster an environment in which multiple, flexible forms of business-government collaboration have long been possible and effective (Thorpe and Durand 1997). From Federacafe (coffee in the 1930s), through Andi (industry, from the 1940s on), and the Consejo Gremial Nacional (economy-wide peak association in the 1990s), Colombian business has been well organized and formally incorporated into multiple councils for policy making in agriculture, exports, training, trade, and other matters (Urrutia 1983; Rettberg 2001). The most intriguing recent examples, noted earlier, are the various competitiveness councils from the 1990s and 2000s.²¹

After 2006, the Colombian government encouraged the formation of the CPC which in turn took a very active role in a range of mostly passive policies designed to reduce business costs and promote exports. In contrast to earlier councils, the major business associations were not prominent in CPC. In an ingenious structure, the small group of business men who initially founded CPC created a small executive committee comprised of individual business men who were strongly associated with the competitiveness agenda and innovation, and who were viewed as more public spirited than self seeking (Eslava, Meléndez, et al. 2012). Yet, the CPC did not entirely exclude the major associations. Instead the CPC has a broader membership for its assembly. This assembly includes the major business associations, plus a range of businesses, domestic and foreign. In practice the executive committee does much of the work, runs the staff, and meets often with government, and then gets together much less frequently with the general assembly to report, consult, and have its strategies ratified. Membership in both bodies is by invitation and surprisingly does not include several of the largest business groups.²²

By excluding associations from the executive committee and some business groups from the CPC, the founders would seem to encourage these excluded parties to bypass council to try to influence policy

21 In a very different policy area, the government created a business-government commission (with some members from academia and civil society) to monitor government spending on defense and internal security derived from a special tax on business and wealthy individuals (Flores-Macías 2013).

22 The CPC is one of the bodies that comes closest to being self-organized, which Hausmann (Hausmann 2009, 195) argues is crucial to effective business-government interaction.

through other means. To some extent this happens as the business associations in particular have strong relations with political parties and Congress. However, to the extent it does not, it seems to be due partly to the reputation of members of the executive committee as non-rent seeking, forward thinking business leaders who can be trusted, informally, not to use their privileged positions to seek rents. So, if rents are not to be had in the CPC, then other groups have less to fear. CPC leaders have also taken pains to avoid policies that might give the appearance of favoring particular sectors or firms, and even supported tariff reductions that angered agricultural associations (Eslava, Meléndez, et al. 2012). As such, the CPC focused on passive policy and would not be up to the challenges of active industrial policy. The success of CPC can be partly attributed to clever design and ongoing reputation management. However, it is also dependent on a context in which myriad and multiple networks permeate business and government elites and generate a wide distribution of information, both about reputations as well as about what actually goes on in closed meetings.²³

These brief comparisons of national contexts suggest a number of conclusions. First, as seen in Mexico and Chile, well-organized business associations are not sufficient to promote effective business-government collaboration in the absence of government disposition to undertake industrial policies and/or solicit business cooperation. Second, in countries without well-organized business associations, as in Brazil, business-government collaboration can still thrive when governments (or business in the case of MEI) devise ad hoc arrangements, particularly sectoral. Third, even where associations are well organized, as in Colombia, governments and business may bypass these associations in order to reduce opportunities for, or perception of, rent seeking. Fourth, in both the Brazilian and Colombian cases, greater pragmatism, and closer networks between business and government facilitated the success of more ad hoc representation by business. Lastly, considering the subnational cases discussed earlier, even within politicized or disorganized contexts at

23 For example, in a 2008 survey of business, 30 percent of respondents said they participated in the design of policies that affected them. Of these, 64 percent participated through associations and 55 percent through direct contacts (respondents could identify both means) (Eslava and Meléndez 2009, 17–18). More specifically, in the case of CPC, President Uribe's brother was the second in command at Corona, a big building materials and retail group, and could keep Uribe informed on what CPC was doing and how it was viewed within the business community (interview with former member of CPC executive committee).

the national level, subnational governments can have greater success in public–private collaboration because geography makes business organization easier, networks form more naturally, and governments tend to be less ideological and more pragmatic (see Post 2014).

IV Conclusions

As noted earlier, existing studies of business-government collaboration are often too vague and voluntaristic in emphasizing political will, high-level support, and consensus, as well as too detailed in the lists of institutional desiderata. Chapter 2 provided another list though somewhat shorter, of components like small numbers of participants, technical staff, and frequent meetings, but with connections to the three basic functions of information exchange, authoritative allocation, and barriers to rent seeking. The empirical cases in this chapter then provided some illustrations of how the institutional components might be variably and dynamically arrayed to fulfill these three main functions.

As with most recent general studies of industrial policy (cited in Chapter 1), the secondary literature covered in this chapter does not systematically evaluate the roles of big business—MNCs and business groups. However, designers of industrial policies and business-government councils varied a great deal in how they managed representation by business associations or by direct inclusion of managers of MNCs and business groups. For example, trade negotiations relied mostly on associations. In contrast, the more spontaneous innovation and competitiveness councils—MEI and CPC—largely bypassed associations and explicitly included CEOs from foreign companies, yet differed starkly on the inclusion of business groups (that were excluded in CPC and invited into MEI). Other economy-wide councils like CNIC and CDES mostly excluded MNCs, though CDES had direct representation by owners of many large business groups. These differences, as the next chapter argues in greater detail, are consequential for how industrial policies are conceived and implemented.

In closing this discussion of contemporary forms, it is important to remember that business-government councils in Latin America have a long pedigree. From the beginnings of industrial policy in the 1930s and 1940s, governments in Latin America created various forums to give business representation in formulating, implementing, and or


monitoring policies. In Brazil in the 1930s, Vargas put representatives of the new corporatist industrial associations on various *conselhos* charged with setting tariff protections (Diniz 1978). In Chile, the government created a development bank, Corfo, and put representatives of the industry association Sofofa on the bank's board (Cavarozzi 1975). In Colombia, the newly powerful federation of coffee growers, Federacafe, gained seats on a variety of boards, including the central bank, over the 1930s and 1940s (Urrutia 1983).

Business-government councils also show no signs of disappearing. Although patterns of business representation vary across countries, over time, and across policy areas, governments continue to create councils and appoint business people to them. Recent cases from the 2000s and 2010s include new councils for competitiveness in Colombia, for innovation in Chile and Brazil, and for trade negotiations in a number of countries. The proliferation of councils also continued on a subnational level, both provincial and municipal. Given this long tradition, and ongoing experimentation, it is surprising that there is so little systematic research or evidence of institutionalized learning on what sorts of councils work best and for what purposes.

So the scope for future research is wide. One extension in analyzing institutional design would be to look beyond individual councils to consider as well the interactions of particular councils with other agencies, forums, and informal networks. It may be that the key to business-government collaboration is less in finding the optimal institution or council, in the singular, but rather the optimum matrix of interconnected councils, agencies, associations, and networks. This seems to be one of the main implications of the success of wine exporters in Mendoza. A network of councils allows an evolving division of labor, gives more specific and concrete tasks to particular forums, permits a cross fertilization and sharing of experiences of successful interaction, and speeds the process of building wider range trust.

4

Putting Councils and Industrial Policy into Context: Political Systems and Big Business



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I Introduction

Even if governments design optimal venues and councils for interacting with business, and find, on the side of business, well-functioning business associations and supportive informal networks, the potential for business-government collaboration still depends on the larger political economic context in two fundamental ways. First, business and government do not meet in a vacuum, and businesses are simultaneously investing in many other avenues for influencing politics and government policy (Eslava, Meléndez, et al. 2012; Schneider 2010a). If the outcome of council deliberations and the resulting industrial policies do not suit powerful businesses, then they can use alternative channels to lobby to get them changed.

Second, business-government councils and policy outcomes also depend on the structure and capabilities—and the preferences that arise from them—of the main business interlocutors. For many policy areas, the dominant corporate participants in Latin America will be MNCs or huge, diversified, family-owned, business groups, so careful consideration of the structures and strategies of big business is essential to understand the kinds of preferences they are likely to push when collaborating with governments. Too many discussions of industrial policy refer to partnerships with a vague and generic “private sector” that is presumably therefore amorphous and malleable. In fact, as policy makers in any middle-income country know well, they face big businesses with well-entrenched structures, capabilities, and preferences. Industrial policy is about creating businesses of the future, but in the immediate run it also means tailoring policies and mechanisms for business-government collaboration to actual existing firms.¹

In the overall political context, formal institutional features like the common combination in Latin America of majoritarian presidentialism with PR legislatures (MP/PRL) and informal practices like appointive bureaucracies favored business groups in distinctive ways.

1 See Amsden (2001; 1989) for earlier analyses of industrial policy that—exceptionally—took full account of structure and capabilities of large business groups and MNCs (on Colombia, see Eslava and Meléndez 2009). Government collaboration with incumbent firms can create several dilemmas that merit separate analysis. If the policy goal is to upgrade an existing industry, then preferences among policy makers and business people are easier to align. If however, policy is intended to create new firms or new sectors, then it may run into opposition from incumbent firms that prefer more support for their existing activities (on Brazil, see Almeida and Schneider forthcoming).

Democratization in Latin America in the late 20th century broke up a lot of close, opaque relations between business groups and authoritarian governments. However, business groups in democratizing polities learned quickly to avail themselves of new venues such as parties, elections, courts, and the media (Schneider 2010b; Yadav 2011; Bull, Castellacci, and Kasahara 2014).

Nearly all studies of, and recommendations for, industrial policy note the perils of rent seeking, and many provide some thoughts on how industrial policy might be shielded from it. However, none of these studies, to my knowledge, takes the next step and asks what specific features of the political system and of large existing business might make rent seeking more or less likely.² Nor do advocates of industrial policy contemplate adjusting policies and their institutions of formulation and implementation in order to accommodate peculiar features of politics (think of them as soft spots or points of vulnerability) by either building in more protection or more countervailing pressures. Such a complete plan of institutional engineering is beyond the scope of this book, but it would need to start with the sort of political diagnosis that follows.

A main goal of this chapter is to fill the large gaps in studies of industrial policy by multilateral agencies that almost never mention specifics of political systems or of big business.³ Some recent scholarship on the developmental state focused more on politics though primarily in authoritarian contexts or in terms of broad social coalitions without getting into specific institutions of the political system (Doner, Ritchie, and Slater 2005; Haggard forthcoming). This chapter, in contrast, delves into specifics of emerging democratic systems and into details of the structures, strategies, and preferences of big businesses in Latin America, mostly diversified business groups and MNCs.

Section II starts with the features of political systems, formal and informal, that give big business privileged access—and alternative channels—to policy making. Section III provides some brief background

2 Some argue that the US political system is ill suited to conducting industrial policy both due to problems of institutional fragmentation (three branches of government and federalism) and consequent policy instability (see Schrank and Whitford 2011, 526) and to institutional openings for rent seeking (Krauss and Pierre 1993).

3 For example, the OECD book on industrial policy has very little on politics until a brief concluding chapter that opens with the claim that, “politics are important if industrial policy is to be successful” (2013, 240). The chapter then mentions several key issues like legitimacy, inclusion, and bureaucratic autonomy but without reference to specific political institutions or business communities.

on distinctive structures of diversified business groups in Latin America and how these structures affect their preferences across a range of policies. Section IV assesses how the structures and preferences of both business groups and MNCs affect their potential for collaboration in industrial policies.

II Political institutions and privileged access for big business⁴

Formal political systems in Latin America stand out in comparison to other regions in their combination of two core features: majoritarian presidentialism and proportional representation (PR) elections for the legislature. This MP/PRL system has distinctive dynamics that can be very briefly summarized as follows (for details, see Schneider and Soskice 2009; Schneider 2013a). First, as elsewhere, PR elections tend to fragment parties. The median number of effective parties was about three for all countries of Latin America and above four for larger countries (Stein, Tommasi, et al. 2005, 37). Second, party fragmentation means that presidents usually lack legislative majorities (Martínez-Gallardo 2010, 127). Third, therefore, presidents have to negotiate with other parties or individual legislators in order to pass legislation. In exchange for votes, legislators can in turn ask for executive decisions to favor their constituents or campaign contributors.

In essence, the MP/PRL system opens up many opportunities for legislators to intervene in the executive, and business is well positioned to take advantage of this leverage. So the best way for business and other groups to lobby the executive is often indirectly through the legislature. Investment in individual legislators as well as in parties thus has potentially high rates of return for businesses whose profitability depends in part on government regulations.⁵ In Brazil, for example, two recent studies document direct individual connections between campaign contributions and government payments. Musacchio and Lazarrini (2014) find that firms making campaign donations are more likely to receive loans from the BNDES. In another study, firms that

⁴ Sections II and III draw on Schneider (2013a) which provides more empirical detail.

⁵ Chang, Kayser, et al. 2010 argue that PR systems elsewhere favor producer groups over consumers. See also Iversen and Soskice 2009.

donate to PT candidates receive more federal contracts (Boas, Hidalgo, and Richardson 2014). Both studies fit the theoretical expectation that, in MP/PRL systems, business can gain leverage over executive agencies by working with individual legislators (especially in an open list system like Brazil's).

By way of contrast, a political system on the far, non-porous end of the continuum would be a majoritarian two-party system with closed lists and financial contributions prohibited or restricted to parties, and consequently disciplined, encompassing parties focused on the median voter. In this sort of system, business has fewer points of access to press individual interests. In practice, Britain's polity is on the less porous end of the continuum, as is Chile's on the spectrum in Latin America. India, with a majoritarian electoral system and stronger parties offers a stark contrast with fragmented parties and PR in Brazil. When asked where they preferred to lobby, 52 percent of Indian business people responded party leaders (versus 11 percent in Brazil) while 52 percent of Brazil business respondents preferred to lobby individual legislators (versus 3 percent in India) (Yadav 2011, Table 4–10, 96–101). The basic point is that a fragmented party system in a PR legislature offers business people easy opportunities for individual influence.⁶

Germany offers an apposite counter example of how institutions can squeeze individual business influence out of electoral politics. Despite the lack of any limit on donations to parties and elections, very few firms, even among the largest make political contributions (McMenamin 2013; Goerres and Höpner 2014). Individual and corporate donations account for only about a third of campaign spending which in total is more than an order of magnitude less than campaign spending in the United States (Khazan 2013). Parties are richly funded but primarily by the government and membership dues. Corporate donations usually add up to less than five percent of party funding.⁷ Contributions to individual candidates do not seem to work to buy later access. There is little lobbying by individual firms; lobbying is instead dominated by business associations (McMenamin 2013, 103).

6 Moreover, in Mexico, the constitutional provision against immediate re-election meant that legislators had little need to pay attention to voters who elected them, especially compared to the need they had for resources for their next electoral campaign (in some other jurisdiction) (see Elizondo 2011).

7 Library of Congress online, <http://www.loc.gov/law/help/campaign-finance/germany.php>, accessed 1 December 2013.

In sum, the German political system does not offer individual business access, and businesses therefore rationally abstain from investing in it.⁸ Individual legislators are primarily dependent on parties that choose electoral lists, finance campaigns, and maintain strict party discipline. So, individual legislators have little reason to court potential business donors or to cater to the needs of individual businesses because most party funding comes from elsewhere. Lastly, business associations are well incorporated through various formal consultative roles in policy making, and conservative pro-business parties have since World War II almost always participated in governing coalitions. Overall, business in Germany has less to fear from politics than in other political systems, and less to gain individually from politics, so rationally invests little in politics.

In addition to formal institutions, other informal practices and networks also enhance business influence. Colombia is renowned for close business-government networks. As noted in Chapter 3, of businesses participating in the design of policies that affected them, over half participated directly while around two thirds participated indirectly through a business association (some did both) (Eslava and Meléndez 2009, 16). In most countries of Latin America, the owners of the largest firms can talk directly to presidents and ministers. However, some politicians make an explicit point not to take individual meetings, including Jaime Serra (minister responsible for Nafta negotiations in the 1990s (Schneider 2004)) and finance ministers in Concertación governments in Chile 1990–2010 (interview Andrés Velasco, former minister of finance) (as well as president Park in Korea (Campos and Root 1996, 91)). These cases stand out as exceptions to the rule.

Bureaucracies in Latin America are porous and staffed at top levels by political appointees rather than career officials. Appointees in top economic positions are sometimes suggested or vetted by business groups (and are sometimes ex-employees) and most consult regularly with business groups (Schneider 2004). In many cases, presidents appoint

8 The distinction between individual versus collective business influence is also crucial in other contexts. In the politics and lobbying for bank bailouts following the financial crisis of 2008–09, individualized business-government relations led to unbalanced bailout packages while collective negotiations led to greater burden sharing across private firms (Grossman and Woll 2014). More generally, see Krauss and Pierre (1993) on how fragmentation in the US political system favors individualized business politics in contrast to more centralized parliamentary systems.

business people directly to the cabinet. The practice varies over time and across countries from few or none in leftists governments of Argentina and Brazil since 2000 to nearly half in the Uribe and Piñera governments to around a quarter for the Fox and Toledo administrations (Schneider 2013a, 146, table 7.1). Business appointees were also common in Argentina prior to 2000. But even countries where the practice was historically uncommon—Chile under Concertación governments (1990–2010) and Mexico under the PRI (1930s–2000)—had recent governments with many business people in the cabinet.⁹

A number of other factors increase the structural and instrumental power of business groups (Fairfield 2015; Schneider 2013a, chapter 7).¹⁰ Think tanks often provided business groups with additional avenues to participate in shaping policy debates, especially in Colombia, Chile, Argentina, and Mexico (on Chile see Cociña and Toro 2009). Last, but hardly least, the media, especially television, were sometimes bought up by business groups or were mostly aligned with them on major policy issues. Some major television channels grew into important groups in their own right as in Televisa in Mexico and Globo in Brazil. In other cases, business groups have bought into TV and radio (especially in Central America (Segovia 2005, 31)). Media control thus gives business groups another potential means for pressuring politicians.

The great majority of business groups are owned by families, and business owning families have additional advantages in politics. Families have several trusted members they can send into politics to engage on behalf of the whole family. Most importantly, families can make longer term commitments to support politicians and can also bear an extended grudge if crossed.¹¹ CEOs and other salaried managers tend to rotate through firms, especially in MNCs, and so lack comparable long-term credibility. Families also have stronger interests in defending their firms

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- 9 In contrast, in Korea, at the end of the authoritarian regime none of the ministers or vice ministers came from big business. However, as in Japan, many close networks between business and government were formed by the movement of retiring bureaucrats into big business. In addition, in Korea, many chaebol families were linked by marriage to top politicians (Suh 1989, 134–5).
 - 10 The relative absence of MNCs from politics also magnifies the power of the largest domestic groups. For example, 13 of 18 countries in Latin America proscribe campaign contributions by foreigners (Griner and Zovatto 2005, 31).
 - 11 See Shleifer & Summers (1988) generally on the advantages of family business in maintaining credibility in implicit long-term contracts. A number of suggestive studies correlate the prevalence of large family firms with a range of negative outcomes in growth, inequality, and social welfare (Fogel 2006; Morck, Wolfenzon, and Yeung 2005).

where the family wealth is primarily tied to this single corporate asset.¹² Professional managers can move on to other high paying jobs if their firms go under. The majority of family members in a business group, especially in later inheritor generations, are unlikely to find equivalent incomes elsewhere.

In sum, political systems and practices in Latin America are remarkably accommodating for business interests, especially narrow or individual interests of big business. Large business groups also have general advantages over others in politics, starting with more money. Steady acquisitions at home and abroad augmented the size advantage and added to their structural leverage (Fairfield 2015). As with traditional MNCs, more internationalized business groups can threaten governments that they will shift investment abroad. In comparative terms, from formal institutions like MP/PRL to informal practices like appointments and media control, big business in Latin America has more options for political influence than are available to big business in other countries.

These differences in political context are crucial to bear in mind when assessing the relevance for Latin America of experiences outside the region of industrial policy making and business-government collaboration. There is a historical correlation between successful developmental states and authoritarian rule and more specifically between performance standards imposed on firms (through active industrial policy) and authoritarianism (Amsden 2001; Schrank 2013a). Even in more democratic contexts, developmental states in Asia counted on powerful insulated bureaucracies with strong backing from ruling parties, as in post-war Japan (Johnson 1982). These political and bureaucratic conditions of course do not exist in contemporary Latin America. Moreover, business groups in Latin America are larger, more internationalized, and more diversified in political investments (media, think tanks, business associations, campaign finance, etc.) than were business groups in the early days of developmental states in Asia, as in Korea in the 1960s and 1970s.

These power asymmetries do not in principle compromise business-government collaboration in passive industrial policy, but they do make active industrial policy and associated performance standards more difficult and risky. Intervening to change behavior in large businesses and imposing sanctions for underperformance—active industrial policy—is much more

12 In Germany, for example, family owned firms are more likely to make campaign contributions (and mostly to right wing parties) (Goerres and Höpner 2014).

daunting when firms have many alternative avenues to pressure politicians and bureaucrats to attenuate performance standards and penalties for non-compliance. The ability of huge firms to evade or stymie performance standards imposed by regulatory and competition agencies gives one indication of the likely difficulties that active industrial policies face (see for example Elizondo (2011) on Mexico). Therefore, business-government councils in active industrial policy operate at least in the shadow of this broader context where the participants know that business has outside alternatives if dissatisfied with the outcome of council deliberations and decisions. Overall then, this “shadow” could encourage policy makers to favor passive industrial policy, that is, make the focus of policy changes in government behavior and rules rather than trying to change firm behavior. However, presumably there are areas where both business and government would share interests in problem solving, even if it meant that business had to bear some of the costs of government intrusion. To find out what those areas might be requires an examination of business preferences.

III Structures and preferences of business groups

Understanding likely policy consequences of business lobbying requires an analysis of both how business groups engage in politics and what it is that business groups want from policy. As Culpepper (2011) argues with respect to corporate governance in developed countries, policy making varies across countries not so much in terms of business influence—big business usually gets what it wants—but rather in business preferences. To understand what policies business groups will push or oppose requires a brief consideration of their overall strategies and sources of competitive advantage (Schneider 2013a, chapter 3). This section focuses on large, diversified business groups that dominate private business across Latin America. Any industrial policy seeking to upgrade a large portion of the private sector will need to work with (or find a way around) these huge business groups.¹³

¹³ The focus in this section is on business groups mostly due to their dominance, but similar analyses of structure, strategy, and preferences could be conducted for MNCs, SMEs, or other groups of firms. Also, largely in the interests of space, this section does not consider much cross national variation in business groups such as their greater size and internationalization in Brazil and Mexico or their greater specialization in Brazil and Chile (Schneider 2008; Schneider 2009b). These variations are sometimes important, but

Many business groups have strengths in commodity and other production that involves the organization of large numbers of unskilled and semi-skilled workers (see Table 4.1). Business groups are diversified but also have a lot of core assets in naturally low risk sectors where they have inherent advantages in international markets (natural resources, especially mining, agroindustry, and food processing), sectors where they are shielded from international competition (as in non-tradable service sectors like banking, telecoms, and other utilities), or oligopolistic or favorably regulated sectors that provide them with a reliable cash flow (e.g., cement, beverages, media). Very few business groups have most of their assets in highly competitive manufacturing activities. Embraer, the Brazilian aircraft maker, is the exception that proves the rule. The reasons for this pattern of sectoral distribution are part of long-term path dependent series of development strategies which welcomed MNCs through most of the 20th century that came to dominate manufacturing. These development strategies also relied on natural resource exports where many business groups thrived.

The Angelini, Matte, and Luksic groups in Chile are emblematic. Angelini started in paint, but expanded over the 20th century into oil (Copeco, now the flagship), retail, and pulp and paper (Bucheli 2010). Matte grew out of paper and diversified into electricity, construction,

TABLE 4.1 *Selected diversified business groups in Latin America*¹⁴

Group	Country	Sectors
Techint	Argentina	Steel, tubing, engineering, oil exploration, health care
Votorantim	Brazil	Aluminum, cellulose, banking, cement, orange juice
Luksic	Chile	Mining, beverages, food, banking
Ardilla Lulle	Colombia	Beverages, banking, media, agroindustry
Slim	Mexico	Telecoms, retail, construction materials
Cisneros	Venezuela	Media, telecoms, tourism

Sources: Schneider (2008), *Wikipedia*, and company websites

what is more remarkable is the great similarities in business groups across countries, large and small, in Latin America. For more details on history, strategy, structure, and political activities of business groups in Latin America, see also the chapters in Colpan, Hikino, et al. 2010; Bull, Castellacci, et al. 2014.

- 14 These are among the largest and more traditional family owned business groups in the region. Some of the newer entrants in the ranks of the largest firms are more specialized (Chilean retail firms like Fallabella and Cencosud) or not family owned (Brazil's Vale), but most of the business groups are diversified and family owned.

forestry, telecoms, and banking. Luksic began in mining but then acquired firms in banking, beverages, and basic manufacturing. By the 2000s, all three business groups were widely diversified into unrelated activities with major holdings in commodity exports and non-tradable utilities and services.

For policy analysis, the distinctive structures and strategies of business groups help to explain the surprising lack of opposition by big business to trade liberalization, and market-oriented reform overall, in the 1990s (Naim 1993; Kingstone 1999). Through diversification, business groups can have subsidiaries in non-tradable, export, and import competing sectors, and thus shift investments among these sectors in response to policy shifts. In addition, privatization programs in the 1990s opened up attractive new opportunities to business groups that wanted to get out of manufacturing. Similarly, diversified business groups are fairly well insulated from, or hedged against, currency fluctuations, and may have weak or mixed preferences on exchanges rates (see Steinberg 2015).

Where business groups have stronger interests is in the “quiet politics” of maintaining the regulatory environment that gives them competitive advantages over local startups and potential MNC entrants. Many business groups sought out regulated sectors in the wake of market reforms in the 1990s. A top financial executive at the Grupo Matte in Chile said the group strategy was to be big in four or five regulated sectors which were therefore “low risk and capital intensive” (*Qué Pasa*, 5 November 2005, p. 22). Many regulations are technically complex and low visibility, and politicians and voters lack the expertise and interest to engage them. Such areas of low salience politics give big business an advantage in pressing their preferences into policy (Culpepper 2011). Stock markets are another area where business groups want to maintain favorable regulation. Stock markets grant business groups access to additional capital and sophisticated means for extending business group control over more corporate assets especially through mechanisms like non-voting shares and pyramidal structures. Lastly, business groups share an abiding interest in weak and passive anti-trust regulators, largely because many of them have market power in some segments of their operations that allows them to generate the steady cash flow needed to expand and sustain other firms in the group.¹⁵

¹⁵ Mexico provides the clearest examples such as Telmex’ monopoly of fixed line telephony (that allowed it to charge some of the highest rates in Latin America) and Cemex’ control of two thirds of the Mexican cement market (with prices in Mexico twice those in the United States) (Schrang 2005, 109; World Bank 2007, 40).

IV Business groups, MNCs, and possibilities for industrial policy

However, in terms of industrial policy, the structure of business groups can open up significant opportunities for collaboration. For example, Rodrik and others argue that a core goal of industrial policy should be to promote export diversification (Imbs and Wacziarg 2003; Rodrik 2007). Public and private interests are well aligned in a fundamental sense that business groups are, prior to any policy initiative, already diversified and usually actively seeking out new opportunities for further diversification. This activity is what policy makers could in principle harness to the goals of industrial policy. Moreover, in the complex process of searching for new areas of optimal national diversification (self-discovery), business groups can potentially be ideal partners because they know the “product space” around them and can easily identify the next best sector to move into (they would be, in Hausmann’s metaphor, adept monkeys) (Hausmann and Klinger 2006). In addition, business groups have the resources—financial and human—to allow them to move rapidly into new activities. In Amsden’s terms (2001), business groups benefit from economies of scope, as in the Korean chaebol that had project teams that worked to establish a series of ventures in new sectors. More generally, business groups have advantages in recruiting top managers, in processing information (as in consulting firms), and using trusted brand names to move into new activities (Khanna and Yafeh 2007).

As noted at the beginning of this book, a flood of recent publications on industrial policy, especially by multilateral development agencies such as the World Bank, the IDB, Cepal, and the OECD all recommend, some at great length, measures to promote dialogue between business and government. Curiously, given this interest in the private sector, none of these publications delve into the existing distribution of firms by ownership (foreign, state, or domestic private), by size, by sector, or mention the fact that the largest private domestic players—the business elite—are mostly family owned, diversified business groups (for an exception, see Devlin and Moguillansky 2013). Similarly, many proponents of industrial policy recommend adjusting policies to their contexts, but the discussion rarely gets into the details of the firms comprising the context (Moreno-Brid 2013; Rodrik 2007; Hausmann 2009). This neglect might make sense if countries were starting out on development or if industrial policy were targeting only low-tech sectors with masses of tiny, undifferentiated

firms. This though is hardly the case in middle-income countries—the focus of most analyses—with long histories of development and well-structured, institutionalized, and politically powerful sets of huge (and rapidly growing) business groups.

Moreover, most of the reference cases in these reports—Japan, Korea, Taiwan, and Finland (though not Ireland)—used industrial policies that explicitly targeted domestic business groups. The history of Nokia is both emblematic of Finland's economic transformation over the past century and illustrates how intertwined and mutually supportive industrial policy and corporate strategies of huge business groups can be (Vartiainen 1999; Sabel 2009; Ornston 2012). Over the course of the 20th century, Nokia, like many multi-sectoral business groups, grew and diversified into new sectors moving progressively from forestry products into energy, electronics, mobile telephony, and finally software, often by acquiring other firms (as is also common practice among business groups elsewhere). Along the way, Nokia was in constant contact and dialogue with government agencies over a series of government policies on technology, R&D, corporate governance, and of course telecommunications regulation (Ali-Yrkkö and Hermans 2002). At times, observers often note, lines between government and business blurred, and it was difficult to establish whether it was business or government that pushed the other to take the next step in advancing technological capabilities. Nonetheless, nearly all agree that neither Nokia (nor other business groups) nor Finland's version of a developmental state could have succeeded without the other.

Similar stories of symbiosis between specific business groups—not some generic private sector—and developmental states are well known also in Japan, Taiwan, and Korea (Johnson 1982; Amsden 1989; Lim 2013; Amsden and Chu 2003). In these countries, policy makers targeted particular business groups and worked closely with them, and the flow of influence and information went both ways with business groups pushing policies to benefit them, but—importantly for the contrast with contemporary Latin America—government officials also had strong direct influence on company strategies. For example, when in the 1970s the Park regime in Korea embarked on the drive in Heavy and Chemical Industries (HCI), planners called on existing chaebol to develop new sectors. The government “chose Hyundai and Daewoo to develop power plant facilities and Hyundai, Samsung, and Daewoo to build ships” (Chang 2003, 54).

In Latin America, the earlier histories of developmental states and business groups were also intertwined during ISI. Household names of the 20th century such as Matarazzo, Techint, and the groups of Monterrey and Medellín all invested heavily in import substituting industries. Then, as later, policy makers did not, however, impose performance standards. In its simplest form, ISI was a set of tariffs and restrictions on trade that any firm could take advantage of as it wanted (i.e., passive policy) (for history, see Agosin 2013). Similarly, during market reforms of the 1990s, governments also structured privatization programs to favor business groups, and the success of both privatization and business groups in the 1990s was closely entwined, sometimes incestuously so (Etchemendy 2011; Schamis 1999). Privatization policies again rarely carried explicit performance standards, though of course many privatized utilities were subject to sectoral regulation (Post 2014). In Rodrik's (2007, 106) summary, policy makers in Latin America used "too much carrot, and too little stick."

After privatization and into the 21st century, the close link between government policy and business groups dissipated, in large part because many governments reduced or abandoned active intervention in the economy. When various ad hoc industrial policies returned in the 2000s, they rarely engaged existing business groups, except tangentially as business groups might have subsidiaries in sectors targeted for promotion.¹⁶ In Brazil, the BNDES continued to finance nearly all large firms, but without much discrimination among firms nor terms of reciprocity. The push in the late 2000s by the BNDES to help particular business groups expand abroad through acquisitions is the best recent example of development policy designed to harness business groups to development goals—the creation of national champions—and to use policy to shift the strategies of individual business groups (Almeida, Lima-Oliveira, et al. 2014). However, beyond the requirement to expand abroad, the BNDES demanded little in subsequent performance standards.

16 The regulation of privatized utilities often became an area of quasi-industrial policy since regulatory agencies were not just interested in reasonable prices and quality, but rather with transforming and rapidly expanding the provision of water, sewerage, electricity, telecommunications, and internet access. In a revealing study of water in Argentina, Post (2014) found that diversified business groups were better partners for provincial regulators than were foreign MNCs, in large part precisely because business groups were diversified with multiple business relationships with governments which could be managed more flexibly compared to specialized and rigid foreign firms.

One recent explicit example where the Brazilian government leveraged the propensity of business groups to diversify and their built-in project execution capacity (Amsden 2001) was shipbuilding. When the Lula government decided in the early 2000s to revive the shipbuilding industry, it encouraged large, diversified construction firms like Odebrecht, Camargo Corrêa, Queiroz Galvão, and others to enter the sector (Pires, Gomide, et al. 2013).¹⁷ This was a natural step because shipbuilding draws on many capabilities already existing in large construction firms, because Korea provided a clear precedent as the government in the 1970s had pushed diversified chaebol into shipbuilding (chaebol which later came to dominate the international shipbuilding market), and because the Brazilian government had decades of experience drawing large construction conglomerates into new ventures, from building Brasília, to damming rivers, to all sorts of other infrastructure, and even for Odebrecht into petrochemicals. The shipbuilding case stands out as one of the few in Brazil and in Latin America, where the government leveraged business group diversification to implement a new industrial policy.¹⁸

On the start-up and technology front, there are very few recent cases of policies specifically designed to harness the diversification capacities of business groups.¹⁹ One revealing case is Votorantim Novos Negócios (VNN). In the early 2000s, Votorantim, one of the largest traditional business groups in Brazil, created this venture capital subsidiary with \$300 million to invest. VNN invested in 12 new projects (interview with Fernando Reinach, one of the top executives at VNN, 5 July 2011). Eight of these 12 did not pan out; the other four took off (some supported with public funds from existing industrial and technology policies). Votorantim sold these four to MNCs and other investors, but by 2010 Votorantim had closed VNN despite impressive returns from its successful investments. When thinking about industry policy to promote R&D, innovation, diversification, and self-discovery, the VNN example offers

17 In contrast, during the first development of shipbuilding in the 1970s, the government promoted more specialized entrants.

18 Many of these same construction companies were the most deeply implicated in the Car Wash scandal and allegedly paid huge bribes and kickbacks to Petrobras. As of late 2014, it was still unclear how much the bribery scheme affected shipbuilding and performance standards there.

19 In the 1970s, the government pushed some business groups into the computer industry (e.g., Villares, see Schneider 2004), and others into joint ventures in new sectors with MNCs and SOEs, using the tripod model (Evans 1979).

several clear lessons. First, large, diversified business groups can easily and successfully raise venture capital to enter risky, high-tech startups. But, second, business groups almost never do so on their own.

MNCs account for a half to a third of the largest companies in most countries of Latin America and are, besides business groups and SOEs, the other natural targets for industrial policy.²⁰ As noted in Chapter 2, MNCs resemble domestic firms when it comes to passive industrial policy and likely favor, and would respond favorably to, a range of horizontal measures like streamlining regulation and improving infrastructure to reduce costs. However—and here structure and strategy, and preferences derived from them matter—MNCs are less likely to respond to crucial horizontal incentives to train workers or invest in R&D and technology. The global reach of MNCs mean that they have already decided on where to concentrate R&D activities as well as distribute their production according to existing skill pools in the countries where they operate. MNCs do little R&D outside developed countries (with some in China, India, and Brazil) and horizontal tax deductions are unlikely to alter this pattern much (Schneider 2013a, chapter 4).

What about MNCs and active industrial policy? At first glance, the global structure of MNCs, and their easy ability to shift investment from country to country would seem to make them better able than domestic business groups to resist policies (by exiting or threatening exit) designed to change their behavior and meet performance standards. However, under certain conditions, MNCs may make better partners in active policy in part because MNCs are accustomed to negotiating the terms of their operations with host governments elsewhere (see Cohen 2007). In theory, MNCs are more open to negotiations if host governments control access to something they want: large domestic markets, low wage/high skill labor, or natural resources.²¹ Brazil, for example, has been successful in forcing MNCs to meet performance standards on technology transfer, local content, and R&D in exchange for access to markets, government procurement, and/or subsidized credit from BNDES (Almeida, Lima-Oliveira, et al. 2014). What makes implementation of these policies easier

20 Among others, Pack and Saggi (2006), Alfaro and Charlton (2013), and Devlin and Moguillansky (2011) recommend that industrial policy target FDI.

21 Where MNCs locate primarily to take advantage of low labor costs, they may be less willing to participate in industrial policies. For example, Andrew Schrank (2011) finds that domestic firms in the Dominican Republic upgraded more quickly in partnership with government agencies than did foreign firms.

is that MNCs are entering these reciprocal agreements voluntarily (as opposed to domestic firms that may feel governments are changing the rules and increasing their intervention). Lastly, MNCs are generally less politically active, and less able therefore to bypass councils and policy makers (as noted in section II).

Beyond devising industrial policies to affect the strategies and performance of MNCs already operating in a country—since the late 20th century a large share of the biggest firms in Latin America, especially manufacturing (e.g., autos) and services (e.g., banking and telecoms)—policies could also be used to push the future composition of the FDI stock towards higher quality FDI. More than 160 governments have agencies to promote FDI and more than two-thirds of these target “quality” FDI (Alfaro and Charlton 2013, 164). Definitions of quality of course vary by country, but much targeting goes after FDI that is intensive in technology, skills, innovation, and exports. Empirically, at least in a sample of OECD countries, FDI was positively associated with growth for industries with higher skill requirements, more reliant on external financing, and with higher quality (as defined by host governments) (Alfaro and Charlton 2013, 193).

Many industrial policies target small firms and start ups (OECD 2013, 128–31).²² However, countries that escaped the middle income trap like Finland and Korea did so by also transforming their biggest firms—their domestic business groups. Designing possible industrial policies for business groups requires finding out first what these business groups look like, how they are structured, and what their strategies, capabilities, and preferences are. Similarly, for MNCs policy making requires an examination of the willingness of foreign firms to bargain over performance standards. Scholars of 20th century development like Alice Amsden considered MNCs poor partners for industrial policy and warned governments to limit their entry (Amsden 2009). That view is now moot as most middle income countries already have significant FDI. So the task now is to find out what types of policy work best with MNCs.

Careful analysis of large existing businesses is also indispensable for passive industrial policy. Many passive policies focus on the sorts of obstacles in the World Bank’s “Doing Business” index and other costs

22 Start Up Chile was one of the most visible in Latin America (Crespi, Fernández-Arias, et al. 2014). The program offered competitive grants of \$40,000 to start-up proposals from around the world.

in the public sector. However, the quest for lower costs to level the playing field and help business compete abroad will in most countries in Latin America ultimately run up against private oligopolies and monopolies. As noted at the beginning of this section, many business groups prefer to have some subsidiaries in basic inputs like cement, steel, and other metals, in utilities like telecoms, electricity, and water, and in non-tradable goods generally (Schneider 2008). Given natural monopolistic tendencies and generally high returns to concentration, many countries now have oligopolistic price problems in these sectors. So, once competitiveness councils have dealt with lower hanging fruit in passive policies to lower costs in the public sector, the next major “doing business” costs to tackle come from the private sector.²³ For example, in Mexico in the 2000s, business respondents thought the two biggest obstacles to business development were public and private monopolies (World Bank 2007, 35). The point is that pushing passive policies of cost reduction and competitiveness at some point is going to run into private oligopoly in large business groups, and at this point policy progress will require the sort of enhanced institutional capacity associated with active industrial policy, namely the ability to intervene coercively to change private behavior, to establish performance standards, to monitor firm behavior, and to impose costly sanctions on firms that do not comply. So, while it may be appropriate to advise states with low institutional capacity to start on passive industrial policy, when these states confront private oligopoly they will have to develop the institutional capacity to coerce the private sector even to pursue a passive cost-cutting agenda.

V Conclusions

Everyone agrees that getting business and government to collaborate is a challenge and that it is difficult to get business to share information, to help with implementing policies, and to refrain from exploiting politics and information asymmetries to get rents. However, most analyses leave the discussion at an abstract level with generic references to business and the private sector. This chapter sought instead to bring in actual existing businesses—the diversified business groups and MNCs—that dominate

23 The CPC had run into some opposition from other business groups for its criticism of oligopoly and high prices (interview, Rosario Córdoba, 31 January 2013).

the private sector and the real avenues of lobbying available to them. For any particular country, the analysis would need to get further into specific firms and sectors. Despite striking continuities in the overall dominance of MNCs and business groups, the business world constantly churns with new entrants and exits, so that some target activities, say software or service exports, might be dominated by smaller, nimbler firms. However, the general take-away for discussions of industrial policy is to avoid whenever possible generalities and talk instead of specific kinds of firms.

The “bad news” of this chapter was the political vulnerability of the policy process. Compared to other regions, the MP/PRL political systems of Latin America, along with other formal and informal practices, gave business groups enormous leverage in politics. Worse, that leverage was more individual than collective and reached beyond the legislature deep into the executive. Business in new democracies has multiple avenues to influence policies from campaign finance, to media, to friends in high places. This vulnerability should be a key consideration in designing context appropriate policies and business-government councils. At a minimum, political systems in Latin America create new risks for industrial policy in the 21st century.

The “good news” of the chapter relates to the fact that business groups and MNCs might be more amenable to industrial policy than the abstract, unspecified private sectors in other analyses. Because business groups are diversified and diversifying, policy makers can potentially harness these business practices to policy goals. And, because MNCs are accustomed to bargaining in exchange for access to markets, workers, and resources, they too may be more open to active industrial policy. And, to the extent business groups and MNCs buy into, or can be convinced to buy into, industrial policy from the beginning, the political vulnerabilities may be less worrisome.

The conventional wisdom now has it that one size does not fit all (in contrast to the Washington consensus), and that industrial policy should be customized for varying contexts and capabilities (Rodrik 2007). The analysis of that context should include—from the outset—large firms and their place in the political system. On the political side, policy makers might, for example, look to avoid agencies subject to high turnover among top officials. Policy instead might be run through agencies long reputed to be “pockets of efficiency.” Speculating, some of the new regulatory agencies might be mobilized, especially those with stronger

bureaucratic capacity. Technical personnel from regulatory agencies are already tasked with monitoring their sectors (and have deep knowledge of it), have experience with setting and enforcing performance standards, talk with business regularly, and have some statutory protections from rent seeking (e.g., fixed mandates). Efforts to customize policies to context could also look further to areas where they might harness existing business interest. For example, many commodity producers consume a lot of energy and naturally worry about securing stable, cheap, long-term supplies, so these firms (often parts of business groups) might be especially engaged in industrial policies in energy. Alternatively, policy makers might research their main MNCs to see what performance agreements they have entered into in other countries that might be replicated. The general point is to look first for particular areas where business might be more amenable to collaboration rather than trying to set priorities in a vacuum for a generic private sector.

5

Conclusions

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Comparative scholarship on business-government relations and development now constitutes a rich and diverse field. Much of this literature focuses on macro political issues of pro-growth alliances and coalitions, usually forged under conditions of threat and vulnerability (Doner, Ritchie, et al. 2005; Kohli 2004). This book has not engaged much these broader theories in part because the issues in Latin America are less visible chronic afflictions of slow growth, low investment, and laggard productivity rather than severe crisis and threat. However, it is important to remember how effective crises were in motivating business and government to work together in a range of success cases from Japan to Korea to Denmark and Finland (Ornston 2012). The challenge in the new developmentalist policies in Latin America is to encourage business-government collaboration in relatively good times (though no longer the great times of the 2000s).

This book also focused on a narrower set of institutional issues related to business-government councils. This focus arose in part from the near universal consensus in analyses of industrial policy in the 21st century that governments have to work with business in order to formulate and implement effective industrial policies. Given this consensus, the crucial institutional question becomes how to get business and government together in countries without traditions of such collaboration. In the immediate run business-government councils are among the first best options for engaging initial dialogue.

In thinking about the institutional engineering for such councils, the goal was to distill out of the myriad forms of collaboration encountered elsewhere the core functions these councils fulfill. Other studies have proposed longer lists of institutional desiderata, but these lists are often unattainable and utopian in the short run. More importantly, these lists do not identify which elements are really necessary and sufficient, nor are they sensitive to the fact that idiosyncratic mixes or constellations of institutional elements have worked well in different contexts. The three functions—information exchange, authoritative allocation, and impediments to rent seeking—are jointly necessary and sufficient for effective policy making (though not necessarily for policy success which depends on a range of other exogenous factors). And, the specific institutions to achieve them can vary.

The other thing missing in nearly all studies and recommendations on industrial policy is attention to the distinctive ways existing political systems channel business influence into politics and the particular

preferences and capabilities that existing big businesses—business groups and MNCs—bring to industrial policy. Both the political system and business preferences are crucial elements for designing both the range of policies—vertical/horizontal, passive/active—and the type of councils needed to make and implement them. Claiming that big business has disproportionate political influence is hardly news. What is more interesting is the particular and variable ways this influence is channeled. Business in coordinated capitalism in Northern Europe, for example, has enormous influence on some issues that is facilitated by access to PR legislatures (Iversen and Soskice 2009). However, that influence comes through encompassing associations and goes into institutionalized parties. This is very different from the sorts of direct, individualized, personalized links between individual business people (or business families) and individual politicians that characterize business politics in Latin America.

Returning to the institutional design issues in Chapter 2, the analysis of business access in Chapter 4 should give some indication of where and how business could bypass business-government councils and thereby undermine agreements and longer term negotiation in councils. If, for example, a large business is excluded from a subsidy program adopted in a council, the business can use connections in congress and parties (and their influence in the executive) to have their firms included. If successful, such bypass lobbying can signal to council participants that the real action is no longer in the council, and this realization can lead to a downward spiral where participants lose interest in the council which subsequently achieves less, confirming participants skepticism. Anticipating these reactions and probable bypass tactics, policy makers can attempt *a priori* to insulate the council or vulnerable parts of the policy process. These insulation investments require clear prior political and institutional analysis of the likely ways business can get around the council.

The analysis of the privileged access of business may also be useful for weighing the costs and benefits of active versus passive industrial policies. Many horizontal and passive policies (that improve public sector procedures to lower business costs) are public or near public goods and should not therefore provoke business lobbying to skew or undermine them. In contrast, active industrial policies that seek to use public subsidies to change firm behavior using performance standards (exports, R&D, etc.) may be more likely to run into difficulty as firms

avail themselves of alternative political channels to resist or dilute the sanctions imposed for failing to meet performance targets. This does not mean that active industrial policy is hopeless, but it does suggest more limited and targeted use, again informed by prior political analysis to try to anticipate possible business reactions.

Some of the implications of the analysis of preferences in business groups work in the opposite direction, namely favoring active over passive industrial policies. As noted in the discussion of diversification in business groups, active industrial policies—with subsidies and performance standards designed to promote new sectors and self discovery—may find willing partners in diversified business groups that are already structured and designed to seek out new opportunities. The resistance here may arise less from political resources that business groups can mobilize than from the range of very profitable alternative diversification projects that emerge for business groups abroad or during commodity booms that are less risky than high-tech activities likely to be targeted by active industrial policies. On the flip side, passive industrial policy designed to lower the costs of business are likely at some point to run up against private oligopolies that often dominate basic inputs (e.g., steel and cement) and utilities. Policies to lower these costs could be a boon to business generally (well beyond cutting red tape in government), but the political obstacles to tackling the intense interests of the largest business groups can be daunting to insurmountable.

The analysis of active and passive policy—and potential business opposition—shades into a broader conceptual distinction between state coercion and state enabling. The latter, helping hand state is the common denominator in the recent spate of research on industrial policy. Much of the conceptual language from consensus building, to self discovery, to coordination failures, suggests a spontaneous, bottom up approach to industrial policy. Hausmann (2009) perhaps goes the furthest in advocating what he calls the invisible hand of government: a decentralized, co-financed process where the government does little more than provide the rents necessary to motivate business to participate. Economists and others who worry about the inevitable ignorance of policy makers (information asymmetry) and the ineluctable rent seeking that accompanies any government action have difficulty getting to a point where they would favor government coercion to force firms to do things they oppose. However, any full consideration of successful industrial policy in the 20th century would have a hard time ignoring the coercive

features. Park Chung Hee, for example, initially locked up and publicly humiliated many of the chaebol owners that were later his partners in forced-march development (Lim 2013). Additionally, many other new forms of government intervention in the economy are openly coercive, especially regulations in utility oligopolies, competition and anti-trust policy, labor markets, and environmental protection. But, few consider this coercive side of regulation when recommending mechanisms for industrial policy.

In development studies, the liberal, market focused Washington consensus of the 1990s gave way in the 2000s to a broader interdisciplinary consensus that institutions matter for development. Debate continues on which institutions matter most, and the new developmentalism and the revival of industrial policy has helped reinvigorate that debate. However, much of this discussion has lacked a deeper appreciation—both theoretical and empirical—of what precisely institutions are and how they work on the ground. Institutions and concepts as diverse as property rights (Acemoglu, Johnson, and Robinson 2002) and embedded autonomy (Evans 1995) are now part of the standard lexicon on institutions and development. Yet, scratching just below the surface often reveals little substance to these institutions, leaving major questions on the who, what, where, when of the actual actors and organizations doing the causal work. A crucial task for our understanding of these and other institutions is to thicken and deepen the research on them. This book is intended as a small step in that direction.

In a general discussion of institutions, business-government councils stand out as hybrids—simultaneously public and private—a special class of linkage institutions. Given the emphasis on incorporating the private sector, these councils might be viewed alongside other initiatives to bring private practices into the public sector as in NPM (new public management), outsourcing, and quasi markets (see Gingrich 2011). These administrative reforms though are intended fundamentally to introduce greater flexibility and competition into organizations that are still public. Business-government councils in contrast bring private information (not competition) into public decision making. As such, and especially in intense joint problem solving and public-private collaboration, the public sphere cedes some ground to private actors.

This ceding of some public authority raises crucial issues of legitimacy in democratic contexts, and complicates longer term processes of consolidation and institutionalization. Chapter 3 noted a wide range

of councils that governments created to manage short-term transitions (as in negotiating trade treaties) where the council was not designed to outlive the transition. On the other extreme, councils on vocational education were written into labor codes in the mid 20th century and have been thoroughly institutionalized ever since (labor codes are some of the longest lived and most resilient institutions in Latin America (Carnes 2014)). In the middle range are councils with indefinite charges to foster development, local content, innovation, or competitiveness. The longer-term institutionalization of these councils depends first on the coming and going of governments. Generally speaking, these councils are always vulnerable to government turnover because of their partisan origins (and association with opposition parties) but also more generally because incoming governments may want to reclaim the public authority ceded by previous governments to the council. On the private side, though, business—especially in cases of more spontaneous, bottom-up organization (as in MEI and CPC)—may push for longer-term institutionalization, precisely to try to maintain a foothold in the state.

Appendices

A: Interviews

Consuelo Arbelaez Bernal, administrative director,
Consejo Gremial Nacional, Bogotá, 8 August 2011.

Carlos Julio Ardila Gaviria, son and heir of founder of
Organización Ardilla Lülle, Bogotá, 10 August 2011.

José Miguel Benavente, council member of CNIC,
Santiago, 10 December 2008.

Priscila Branquinho das Dores, oil and gas department,
BNDES, Rio de Janeiro, 28 March 2014.

Jaime Campos, executive director, AEA (Asociación
Empresarial Argentina), Buenos Aires, 12 December 2008.

Gabriel Castañeda, anti-trust lawyer, Mexico City, 16
February 2011.

Renata Cavalcanti, former head of engineering in explora-
tion at Petrobras, former subsecretary of development for
state of Rio de Janeiro, 27 March 2014.

José Augusto Coelho, former executive director,
Confederação Nacional da Indústria, Brasília, 10 June
2013.

Rosario Córdoba, president, CPC, Bogotá, 31 January
2013.

Hernando José Gómez, former president of CPC, former
head of Departamento Nacional de Planeación, Bogotá, 1
February 2013.

Jaime Gutierrez, president of Ptesa and member of steering council of CPC, 1 February 2013.

Benjamin Herzberg, World Bank, Washington, DC, 8 October 2008.

Roberto Junguito, former minister of finance, former minister of agriculture, former head of several business associations, Bogotá, 8 August 2011.

Mauro Borges Lemos, former president, Agência Brasileira de Desenvolvimento Industrial (ABDI), Brasília, 17 January 2014.

Andrés López, Cenit, Buenos Aires, 11 December 2008.

João Fernando Oliveira, president, Embrapii, Brasília, 5 November 2014.

Juan Pardinas, executive director, Instituto Mexicano para la Competitividad (IMCO), Mexico City, 15 February 2011.

Andrés Pesce, Fundación Chile, Santiago, 10 December 2008.

Álvaro Prata, secretary for technological development, Ministry of Science, Technology, and Innovation, Brasília, 17 July 2013.

Fernando Reinach, former head of Votorantim Novos Negocios, 5 July 2011.

Pilar Romaguera, council member of CNIC, Santiago, 16 August 2013.

Mateus Simões de Freitas, manager for innovation and technology, Senai, Brasília, 17 January 2014.

Álvaro Teixeira, former executive secretary, Instituto Brasileiro de Petróleo, Rio de Janeiro, 27 March 2014.

Andrés Velasco, former minister of finance (2006–10), phone interview, 26 January 2012.

Luiz Carlos Villegas, former president of Andi and of Consejo Nacional Gremial, Geneva, 5 September 2011.

Korea Interviews (Seoul)

Choi Youngrak, professor of technology management, University of Korea, 7 August 2012.

Chung Yang-ho, Director General, Energy and Environment, Ministry of Knowledge Economy, 10 August 2012.

Kim Do Jeon, chairman National Science and Technology Commission, 6 August 2012.

Lee Yeonho, professor, Yonsei University, 7 August 2012.

Park Chung-woong, former secretary to the chairman and head of international relations at Federation of Korean Industry, 7 August 2012.

Song Byung-Nam, ex staff at Economic Planning Board and Korean Association of Machine Industry, ex-CEO of Kia motors, 6 August 2012.

B: Glossary

AEA – Asociación Empresaria Argentina (Argentine Business Association)

Andi – Asociación Nacional de Empresarios de Colombia (National Business Association of Colombia)

BNDES – Banco de Desenvolvimento Econômico e Social (Bank for Economic and Social Development, Brazil)

CDES – Conselho de Desenvolvimento Econômico e Social (Council on Economic and Social Development, Brazil)

Cepco – Coordinadora Estatal de Productores de Café de Oaxaca (State Coordination for Coffee Producers of Oaxaca, Mexico)

CNDI – Conselho Nacional de Desenvolvimento Industrial (National Council for Industrial Development, Brazil)

CNI – Confederação Nacional da Indústria (National Confederation of Industry, Brazil)

CNIC – Consejo Nacional de Innovación para la Competitividad (National Council for Innovation for Competitiveness, Chile)

Coece – Coordinación de Organismos Empresariales de Comercio Exterior (Coordination for Business Associations in International Trade, Mexico)

Contag – Confederação Nacional dos Trabalhadores na Agricultura (National Confederation of Farm Workers, Brazil)

Corfo – Corporación de Fomento de la Producción (Production Development Corporation, Chile)

CPC – Confederación de la Producción y el Comercio (Confederation for Production and Commerce, Chile)

CPC – Consejo Privado de Competividad (Private Council for Competitiveness, Colombia)

CUT – Central Unitaria de Trabajadores (Workers' Unitary Central, Chile)

FDI – foreign direct investment

Finep – Financiadora de Estudos e Projetos (Fund for Research and Projects, Brazil)

IBP – Instituto Brasileiro de Petróleo, Gás e Biocombustíveis (Brazilian Institute for Oil, Gas, and Biofuels)

IDB – InterAmerican Development Bank

ITT – International Telephone & Telegraph

MDIC – Ministério do Desenvolvimento, Indústria e Comércio Exterior (Ministry for Development, Industry, and International Trade, Brazil)

MEI – Mobilização Empresarial pela Inovação (Business Mobilization for Innovation, Brazil)

MKE – Ministry of the Knowledge Economy, Korea

MNC – multinational corporation

MP/PRL – majoritarian presidency/proportional representation legislature

NSTC – National Science and Technology Commission, Korea

OECD – Organization for Economic Cooperation and Development

ONIP – Organização Nacional da Indústria e Petróleo (National Organization for Industry and Oil, Brazil)

PR – proportional representation

PRI – Partido Revolucionario Institucional (Institutional Revolutionary Party, Mexico)

Prominp – Programa de Mobilização da Indústria Nacional de Petróleo e Gás Natural (Program for Mobilizing National Industry in Petroleum and Natural Gas, Brazil)

PT – Partido dos Trabalhadores (Workers' Party, Brazil)

Sena – Servicio Nacional de Aprendizaje (National Training Service, Colombia)

Senai – Serviço Nacional de Aprendizagem Industrial (National Industrial Training Service, Brazil)

VNN – Votorantim Novos Negócios (Votorantim New Businesses, Brazil)

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