

Preface to the Spanish Edition of Democracy and Markets

There remains much interest today in the design of political and economic institutions. But, in many ways, the study of institutional design is less imaginative than it was twenty years ago. In the late 1970s and 1980s, one could find in the leading journal of the American Political Science Association, for example, a test of Gramsci's claims about the impact of workplace democracy on political attitudes (Greenberg, 1981) as well as an analysis of the stability of the class compromise (Przeworski and Wallerstein 1982). An Association President, Charles Lindblom, not only issued a call for adopting "Another State of Mind" in the study of political economy, he produced a major book that raised important questions about the "privileged position" business in Western countries (Lindblom 1981 and 1977, respectively; see also Dahl 1985). Today scholars continue to analyze "varieties of capitalism" (Hall and Soskice, 2001). And they worry about the room to maneuver governments have global markets (Garrett 1999, Iversen 1999, Mosley 2000). But the range of institutions they study is narrower; scholars often ignore or investigate only obliquely the problem of achieving popular sovereignty over the economy.¹

To be sure, in some respects, there currently is less variety in the world's political-economic systems. Consider the concept of the mixed economy. While, in recent years, the governments in New Zealand and Spain nationalized some firms, in these and other countries, numerous state-owned enterprises have been privatized. In fact, since the mid-

¹ Hall and Soskice (2001) advocate a shift to the meso level of analysis, making the firm the principal unit of analysis. They generally ignore the larger issue of popular sovereignty. Garrett (1998), Iversen (1999) and Mosley (2000) assume that any room to maneuver achieved through institutional design also achieves popular sovereignty. None of these scholars show that the room to maneuver allows governments to satisfy public preferences for macroeconomic outcomes. Rather, Garrett, Iversen and Mosley posit these preferences rather than establishing them through, say, survey data.

1980s world-wide thousands of firms have been privatized. As regards the four countries that figure prominently in my book, by the late 1980s Britain established itself as a world leader in privatization. By one count, one hundred thirty nine privatization transactions were completed in that country between 1985 and 1999. In the same period, Italy completed eighty-nine such transactions. And Sweden, which originally had few state-owned enterprises, completed twenty one. On the basis of a federal mandate to the OeIAG, Austria completed more than fifty privatization transactions.² Some scholars contend that Austria still is a mixed economy—there is a substantial “backlog” of firms in that country that ought to be privatized (Belke and Schneider 2003). Either way, the fact is that, like the economies in the other three countries, Austria’s economy is less mixed than it was twenty years ago.

Turning to the mode of intermediation, it appears that corporatism is somewhat less prevalent than when I wrote my book. More specifically, corporatist institutions have broken down somewhat in countries like Sweden (Pontusson and Swensen 1996). Even Austria’s producer group politics are, by some accounts, less centralized than in years past (Kenworthy 2000, 2001). Many investigators contend producer group politics now is best studied in terms of wage setting and wage bargaining institutions (Traxler et. al. 2000, 20001). But there remains much agreement that producer group politics in Sweden and Austria are distinct from producer group politics in countries like Britain (Sairoff 1999, Hall and Soskice 2001). So, democratic market systems can still be distinguished in this way.

² The privatization transactions counts come from Brune et. al. 2004. See also OECD 2001. On the Spanish experience see Etchemendy 2004: esp Table 1.

The intermediate variables discussed in Chapter Four of my book also remain useful. For example, differences in the speed and scope of privatization have been traced to the majoritarian versus consensual nature of democracies (Bortolitti and Pinotti 2003) and to the condition (existence) of local capital markets (Jones et. al. 1999). In addition, the interest in central bank design relative to that of other political institutions (Bernhard et. al. 2003, Iversen 1999) is related to the variable I called state administrative style.

In sum, the classification of the world's political economic systems in my book remains useful perhaps most for what it says about the consequences of privatization and about the contrasts between pluralist-private enterprise and corporatist private enterprise political economies.

According to my book, privatization—the creation of economies based more exclusively on private ownership—should produce in the respective countries gains in collective consumption and intergenerational equity and at the same time less intragenerational equity. This will be true especially if privatization occurs in conjunction with fuller development of (links to international) capital markets. Because they might reduce uncertainty about price and wage fluctuations and impart a comparatively long-term orientation to public policy making, strong producer group institutions and strong central banks might enhance performance on the first welfare criterion. Strong labor organizations should continue to reduce intragenerational inequality at least in the short-term. However, independent central banks and high degrees of capital mobility might have the opposite effect on intragenerational equity. So, if the world is composed of more pluralist-private enterprise and corporatist-private enterprise systems, the former should outperform the latter in terms of collective gain and intergenerational equity while the

latter, to some degree, performs better in terms of intragenerational equity.³ If corporatism breaks down still further, the British experience depicted in Figure 12 in the book is indicative of the direction in which blends in distributional equity are headed. In fact, Figure I shows that, during the period of privatization, blends of distributional equity in the U.K. continued to move toward the northwest. The same was true in Sweden. Perhaps because its economy remains somewhat mixed, the decline in intragenerational equity in Austria was less pronounced than the decline in the U.K. Interestingly, the Italian case exhibits no clear pattern.⁴

Figure I About Here

As regards democratic politics, privatization addresses the problems of state manager and worker privilege. In addition, privatization alleviates the need for citizens to manifest what I call in the book, “collective ownership efficacy” (the willingness to monitor and hold accountable the managers of and workers in publicly-owned firms). But privatization leaves intact, if not reinforces, the problem with private ownership: the ability of private asset holders, through disinvestment and capital mobility, to thwart public preferences for more intragenerational equity. Of course, if ownership is widespread as through vouchers and pension funds and (or) capital mobility is limited, this problem is less severe. In general, as I explain in the concluding chapter, the move to pluralist-private enterprise systems can be interpreted as the imposition (choice) of one

³ Rather than “corporatist” I could use “economically integrated” (Sairoff 1999), “socially coordinated” (Hall and Soskice 2001), or “Kenworthy-corporatist” (Kenworthy 2000, 2001). There remains much evidence in these and related works that corporatism creates a more equitable distribution of intragenerational wealth, including of wages. In addition to these works, see Pontusson et al 2002 and Rueda and Pontusson 2000.

⁴The patterns in Figure I are the same if the OECD’s data for Real GDP/Head are used instead of HCFE/Head and the LIS’s 90/10 ratios are employed instead of its Gini indices. On the latter measures of intragenerational equality see Foerster and Vleminckx (2004). Admittedly, the Austrian case continues to be somewhat anomalous. Despite the greater capacity for intragenerational equity, Austria continues to rank below Sweden on this criterion. See Chapter Seven.

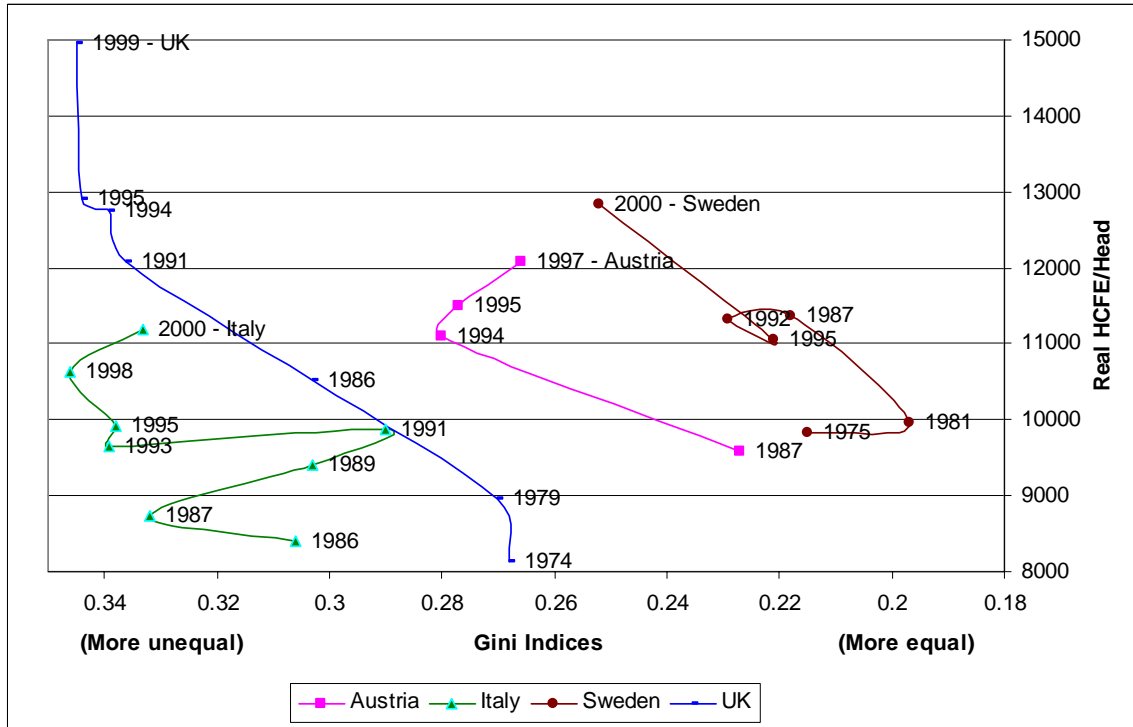


Figure I - Income Inequality and Household Final Consumption Expenditure Per Head (US\$, 2000 prices and exchange rates).

Sources: The Gini Indices are from The Luxemburg Income Studies Project at www.lisproject.org. The range of the bootstrap standard errors for each country are as follows: Austria, 0.0026(1987)-0.0061(1994); Italy, 0.0043(1989,1991)-0.0070(1998); Sweden, 0.0021(1975)-0.0025(2000); UK, 0.0024(1994)-0.0043(1995). The Real HCFE/Head (Real Household Final Consumption Expenditure/Head) figures are from The OECD Annual National Accounts, Comparative Tables, OECD Statistics at www.oecd.org.

set of tyrannies over another. Perhaps it is the realization of this fact, that explains the “backlog” of privatization in Austria—the desire of Austrians and their elected representatives not only to retain some capacity to achieve blends of distributional equity in the northeast of Figure I but also to strike a balance between the tyrannies that exist in corporatist-private enterprise and corporatist-mixed political economies.⁵

Several ancillary arguments appear in the book. One is that political-business cycles in government and state-owned business investment are unlikely. If these cycles occur at all, they occur in pluralist-mixed political economies. With James Alt, I tested for the existence of such cycles in Britain in the period in which that country’s economy was most mixed and dissensus about nationalization was at its peak. Alt and I (1994) found no evidence that electoral politics affected public investment patterns. Rather we found that public investment, consistent with the Morrisonian ideal, was motivated by certain macroeconomic variables. However, public investment had little impact on these same variables.⁶ Also, in the book I repeatedly analyze the values and behavior of the managers of firms. I stress the potential for managerial tyrannies of various kinds, especially in centralist systems where there is a tradition of deference to the state. In a recent article (2002) I raise similar concerns about monetary technocracy. Technocratic control over monetary policy—central bank independence—is prevalent increasingly in all political-

⁵For instance, in his account of privatization in Austria in the 1980s, Mueller (1988) alludes to the growing public concern over the subsidies paid to Austrian nationalized industries. But neither he nor Belke and Schneider (2003) mention the privilege that exists in the alternative political economy (corporatist-private enterprise).

Because the book emphasizes the importance of mixed economies, the comparisons in Chapter Eleven are between pluralist-private enterprise and pluralist-mixed and corporatist-mixed political economies. As regards the arguments in this Chapter, in addition to analyses of the scale and mobility of private firms, a comparison of pluralist-private enterprise and corporatist-private enterprise political economies should include an evaluation of the channels of accountability within peak organizations in the latter.

⁶ Belke and Schneider (2003) argue such cycles exist in Austria. Unfortunately, I was not able to obtain finely grained data to test this claim with the same methods used in Freeman and Alt (1994).

economic systems, even those with noncentralist administrative traditions. I argue that some of the institutional innovations political scientists are advocating to ensure central bank independence may be incompatible with democracy.

What does the book contribute to the current debates about democracy and markets?

First, it demonstrates the importance of employing a complete set of welfare criteria in evaluations of institutions. It is remarkable that so much literature continues to employ a single criterion. The literatures on the impact of wage bargaining (setting) systems on wage inequality and on the impact of central bank independence on inflation are illustrative.⁷ Works that employ a fuller set of criteria often ignore issues of intergenerational and intragenerational justice. They often assume that macro unemployment performance is indicative of intragenerational equity and(or) that citizens in all countries ascribe to some market-oriented conception of justice. The book shows that both assumptions are unreasonable.⁸

A second contribution is the illumination of capital market's dual nature. One of the key points in my book is that, by disciplining private managers, capital markets promote efficiency and, in turn, collective gain for living and future generations. At the same time, by providing opportunities for disinvestment and exit by private asset holders, capital markets diminish popular sovereignty over the economy. Much of the literature on privatization ignores this second effect. This leads scholars to paper over such things as "golden share mechanisms." These mechanisms are motivated by concerns about the

⁷ Econometrically, it is unreasonable to treat key variables as endogenous in one study and then exogenous in another. It also is unreasonable to pool data from countries, the economies of which clearly are causally connected. I recommend comparative case studies using reduced form multivariate time series analysis (Freeman and Alt 1994) and also computational approaches (Freeman and Houser 1998, Houser and Freeman 2001).

⁸ On the idea of a market-oriented conception of justice see such works as Lane (1986).

identity of private asset holders, more specifically, the belief that governments will be able to exercise greater influence over welfare outcomes in an economy populated primarily by firms owned by natives rather than by foreigners.⁹

The dual nature of capital markets is related to what is currently called the “room to maneuver debate.” From the perspective of my book, this debate is about how much capacity governments have to create certain kinds of welfare outcomes in pluralist-private enterprise vs. corporatist-private enterprises political economies. Illustrative is Iversen’s (1999) case for “decentralized monetarism”--his argument that the best combination of growth, employment, and prices is achieved in a (private enterprise) system with intermediate wage bargaining and a strong, insulated central bank. Suppose Iversen could show more explicitly that decentralized monetarism also produced more intragenerational equity than other forms of such political economies. The question of whether the blends of welfare produced by decentralized monetarism is consistent with popular preferences in the respective countries would remain. It is possible that citizens in decentralized monetarist systems desire an alternative combination of welfare outcomes.¹⁰ Observers like Rodrik (2000) suggest that national institutions like those Iversen calls decentralized monetarist simply aren’t able to achieve such outcomes. In a

⁹ Interestingly, economists and business scholars view inequity as a barrier to (share issue) privatization. They argue that the shares in state owned enterprises must be underpriced severely when income is maldistributed in order that median voters can buy them. Share ownership by median voters is needed to ensure support for conservative (market-oriented) governments who are trying to create private enterprise systems. It is only in this way that these scholars address intragenerational equity (Biais and Perotti 2002, Jones et al. 1999).

While the same works acknowledge efforts to ensure “domestic” ownership and prevent quick sales to foreigners, they fail to see how concerns about intragenerational equity motivate these features of privatization programs. The government in Austria aims to create an Austrian core shareholding structure in its economy. Also, a proposal to privatize Voest by selling it to Canadians led to a uproar and, in turn, to a plan to keep the firm in the hands of Upper Austrians (Belke and Schneider 2003: esp. p. 37 and fn. 24). On the golden share mechanism used in Spain see Etchemendy 2004: esp. pps. 638-9 and 646).

¹⁰ Once more, Iversen (1999) does not attempt to show with survey or other data that citizens are satisfied with the welfare outcomes of decentralized monetarism.

world of increasingly global markets for goods and capital, nation-states find themselves in “golden-straight jackets.” World federalism is the only way to restore meaningful popular sovereignty over the economy according to Rodrik. The challenge then for students of democracy and markets is to imagine collections of supranational, regional or even global democratic institutions that can be combined with ownership structures within and across nation-states to produce more publicly preferred blends of distributional equity. I hope that somehow my book contributes to this project, if at least alerting scholars to the different, potential tyrannies that could exist in such systems.¹¹ Publication of this new edition of my book would not have been possible without the hard work of Dr. Juan Jesus Mora Molina. It has been a pleasure to work with Dr. Molina. I sincerely thank him for the many hours he has spent on the translation. I also thank Ms. Tonya Cook and the staff at Cornell University Press for arranging to have the book published by Editorial Almuzara. This edition is dedicated to my son Thomas, a true friend, great athlete, and, most important, student of the Spanish language.

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Minneapolis, Minnesota
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¹¹ Rodrik (2000) that because of increasing international economic integration we must choose between nation-states bound in “golden straight-jackets” or mass politics. The former connotes limited room to maneuver in terms of policy and hence welfare outcomes. The latter—which, according to Rodrik, is possible only through world federalism—seems to imply some degree of popular sovereignty over economies. Unfortunately, Rodrik does not show that citizens comprehend the straight-jacket, let alone that they consider the straight-jacket “golden.” He does not develop his conceptions of world federalism or mass politics in any sustained way.

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