POLITICS AND
NEOLIBERALISM: STRUCTURE,
PROCESS AND OUTCOME
RESEARCH IN POLITICAL SOCIOLOGY

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SPECIAL REVIEWERS

The success of Research in Political Sociology depends on the community of scholars in many ways. I am grateful to the advisory editors (p. ix), who reviewed manuscripts and provided advice on editorial decisions. I also owe a special debt of gratitude to the colleagues listed below who served as referees in the peer review process and reviewed one or more manuscripts for Volume 16 of Research in Political Sociology. Thank you.

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Since its inception, the primary objective of Research in Political Sociology (RPS) has been to publish original, high-quality manuscripts to increase our understanding of political structures and processes. RPS and the American Sociological Association’s Section on Political Sociology share this goal, and the publication cooperates with the section to achieve sociological understanding of political phenomena.

RPS is a resource that can be used by political sociologists to strengthen and develop the unique skills and interests they bring to sociology. The articles in RPS are directed toward identifying, understanding, and explaining the various interrelations that exist within and between social and political phenomena. This includes exploring the underlying social roots or origins of politics and power; the organization, management, and process of political power structure; and the effects of political decision-making and power structures on society. The intent of RPS is to facilitate scholarly communication and debate among political sociologists and scholars in other disciplines on the full range of theoretical, methodological, and substantive areas of research in the field. RPS is open to all theoretical, methodological, and scholarly points of view, irrespective of political content, so long as they advance our sociological understanding of political dynamics and social structures.

classes, and other social actors exercise political power to advance their interests in a range of historical and geographic setting. *RPS* is now accepting manuscripts for Volume 17, which will focus on “Politics, Public Policy, and Organizations.”

Harland Prechel
*Editor*
FOREWORD: POLITICS AND NEOLIBERALISM

This volume of *Research in Political Sociology* focuses on a theme that emerged in volumes 14 and 15. The articles in volume 16 employ different theoretical perspectives and methodological approaches to examine the effects of neoliberalism on political and economic change in several societies. Following a theoretical and historical introduction to the relationship between politics and neoliberalism, the volume is divided into the two sections described below.

DECENTRALIZATION UNDER THE NEW FEDERALISM: CONSEQUENCES FOR WORKERS’ HEALTH, HIGHER EDUCATION, AND SOCIAL SERVICES

The articles in this section examine the social consequences of the new federalist policies that emerged in response to neoliberalism on workers’ health, higher education, and the provisioning of social services and economic development assistance.

The article by Heather Scott-Marshall examines the consequences of work-related insecurity on workers’ health in Canada during the late 1990s when policies and social structures that stabilized employment and protected workers were replaced with increasingly exploitative employment relations. The analysis takes into account several conditions including control over employment circumstances that are rooted in social class position.

The author maintains that the increasingly hegemonic power of corporate management facilitated the transformation of employment relations in ways that replaced stability and security as a means to extract labor with relations
that produced insecurity to achieve that same goal. The analysis shows that contemporary workers experience chronic occupation stressors that increased career, income, and work-life balance insecurity. These changes resulted in more diffuse work careers and income trajectories, and increased uncertainty in long-term financial and life planning. These chronic sources of strain have negative affects on workers’ health.

The article by John Harms examines how the neoliberal agenda of tax cuts was manifested as cuts to higher education expenditures by state governments. These cuts were the outcome of policy legacies and the U.S. federalist government structure. Whereas the federal government can finance tax cuts with growing deficits, many states are required to balance their budgets when revenues fall in relationship to expenditures. Higher education is particularly vulnerable because of the way in which budget priorities are established.

The case study provides an in-depth analysis of how tax cuts undermined the capacity of the state of Missouri to provide adequate funding for higher education. These tax cuts are contextualized within broader public policy changes, which included self-imposed legislation that required state managers to balance the budget. The author uses John Kenneth Galbraith’s conception of social imbalance to expose the contradiction between the short-term goal of balancing the budget and the long-term goal of providing a system of higher education capable of ensuring that the workforce is prepared to meet the challenges of an increasingly global economy.

In her article, Linda Lobao examines the consequences of decentralizing the responsibility for social service provision and economic development from the federal government to local governments. This paper tests three competing theoretical perspectives.

The findings provide little support for the neoliberal argument that privatization of public services and less government involvement promotes economic development. Most county governments continue to be actively engaged in both economic development and public service activities. The analysis supports a central dimension of political economy theory, which suggests that neoliberal policies benefitted corporations and wealthy individuals. However, the analysis provides the most support for an institutional perspective, which combines spatial variation, path-dependent development, dimensions of political economy theory, and urban-regime and growth machine theories. The author shows that local actors such as government, business, and labor negotiate public policies and expenditures. Also, whereas rural areas are increasingly marginalized, wealthier urban areas continue to have greater capacity to provide public services.
GLOBALIZATION, NEOLIBERALISM, AND SOCIAL AND ECONOMIC CHANGE

The first article in this section examines the political dimensions of the policy formation process in two racially divided post colonial societies. Erik Larson and Ron Aminzade’s comparative analysis shows how neoliberal economic reforms, domestic politics, party structures, and political dynamics affected racial redress and indigenization policies.

Although Fiji and Tanzania were both former British colonies and their initial policy proposals were similar, political party structures, competition for state power, and the composition of class and race-based preferences varied in important ways that shaped these policy debates. Whereas the political dynamics in Fiji included the use of neoliberal policies to advance the goals of racial redistribution, politicians in Tanzania advanced indigenization policies as a defensive reaction against the distributive consequences of neoliberal policies.

The two remaining articles in this section examine the effects of market-based policies on two of the four BRIC countries (i.e., Brazil, Russia, India, and China), which are projected to be among the largest economies in the global capitalist system.

The article by Lu Zheng and Jean Oi examines the transformation of Chinese state-owned companies to private companies in the 1990s. The authors show that the emergence of the market-based economy in China deviated substantially from the neoliberal model. Specifically, China’s transition included the creation of political institutions to regulate corporations and ensure market stability.

There are three key findings from the quantitative analysis. First, variation in the political-legal arrangements affected the rate of change from state-owned companies to private companies. After the Communist Party openly supported the transition to a market-based economy and local governments subsidized restructuring and imposed deadlines, the rate of corporate restructuring increased substantially. After these incentives declined, the rate of corporate restructuring declined. Second, in contrast to advanced industrial economies, corporate restructuring in China did not result in workforce downsizing. Third, by the end of the 1990s, top managers whose firms failed to lower debt or produce profits were dismissed. As a result, approximately 30 percent of the top managers lost their jobs during the study period.

The article by Shilpa Ranganathan and Harland Prechel examines how the legacies of colonial and post colonial political-legal arrangements and the complex caste and class structure affected economic development in
India. This historical analysis shows that after independence, the family-owned businesses organized politically to retain their position as the dominant power bloc by aligning their interests with transnational corporate interests. This capitalist class fraction redefined corporate property rights in ways that privatized public sector enterprises and permitted greater foreign ownership of Indian firms.

The new political-legal arrangements made it viable for businesses to use a structure that shares important characteristics with the multilayer-subsidiary form where a parent company owns enough stock to retain controlling interests in many legally independent firms. This multilayer-subsidiary form provided the organizational capability to transfer profits from domestic to foreign corporations. The authors conclude that whereas the British imposed their political power to extract capital from India during colonial capitalism, the current political-legal arrangements redefined corporate property rights in ways that benefitted large domestic and transnational corporations. In both historical periods, the political-legal arrangements permitted the transfer of wealth to external political and economic elites.

CONCLUSION

The articles in this volume provide insights into how neoliberal economic policies affect the dynamics and outcomes of the policy formation process in different societies. They show that the implementation of neoliberalism was affected by the prevailing social structures and the political coalitions that emerged in these societies. Several of these articles show that the new organizational and political-legal arrangements redistributed wealth and resources to the dominant classes.

Harland Prechel
Editor
PART I:
INTRODUCTION
ABSTRACT

The fundamental premise of neoliberalism is that government interference with markets is the cause of poor economic performance and that only market-based economies ensure growth and prosperity. In contrast to this claim, the analysis here shows that this is a politically convenient but historically inaccurate account of the relationship between the state and markets. During the previous 130 years, corporations employed neoclassical liberalism and neoliberal conceptions of the relationship between the state and market when it was beneficial to them. The capitalist class also mobilized politically to pressure the state to contain the destructive forces of the market when it undermined their capacity to accumulate capital. The paper concludes that neoliberalism is best understood as an ideology that emerged to legitimate the historically specific policy initiatives to support the capital accumulation agendas of the dominant power bloc.

Neoliberal thinking is grounded in the classical liberal tradition first expressed by Adam Smith (1776) in his treatise, *The Wealth of Nations*. In this work, Smith explained how markets, when unfettered from mercantilist state interventions, would most efficiently coordinate the production and distribution of goods. If individuals were freed from government restrictions
(laissez faire) and allowed to pursue their self-interests, the wealth of nations would be enhanced.

Neoliberalism adopts classical liberalism’s equation of free markets and individual freedom, and its distrust of state intervention in the economy. However, neoliberalism goes beyond classical liberalism by embracing market fundamentalism: “the religious-like certitude of those who believe in the moral superiority of organizing all dimensions of social life according to market principles” (Somers & Block, 2005, pp. 260–261). For classical liberals like Smith, markets were efficient means for producing and distributing goods. In contrast, neoliberals assume that markets are morally good in themselves, and thus should be applied to all aspects of life (e.g., social relationships, identity). Thus, the value of markets is not simply confined to their capacity to efficiently produce and distribute goods; they have inherent value that provides multiple benefits for individuals and society.

Neoliberalism also shares with classical liberalism an emphasis on the role of the entrepreneur. For Smith, entrepreneurs were one of several types of economic actors that engaged in economic activity. They responded to market competition by investing and innovating, thereby increasing productivity and the wealth of nations. While Smith admired entrepreneurs and their economic role, he also recognized the need for other institutions such as governments, churches, and schools. In contrast, neoliberals maintain that since all of society is a market “every human being is an entrepreneur managing their own life, and should act as such” (Treanor, 2005, p. 10). Institutions or programs that interfere with or replace market mechanisms are morally wrong.

Although both liberalism and neoliberalism emphasize individualism, classical liberalism involves individual freedom in market transactions and recognizes other forms of social relations and responsibilities. For neoliberals, however, there should be just markets and freely choosing individuals. This neoliberal idea was captured in Prime Minister Thatcher’s proclamation that “there is no such thing as society...[t]here are individual men and women, and there are families” (Thatcher, 1987). Neoliberalism suggests that individuals are free to choose and must be responsible for the consequences of their choices, just like entrepreneurs are responsible for their investment decisions. The idea of the individual as responsible for the consequences of their choices is captured in the title of the 1996 welfare reform in the United States: Personal Responsibility and Work Opportunities Reconciliation Act.

The acceptance of neoliberalism by many scholars and politicians has been supported by an epistemological infrastructure that renders it immune from historical and empirical criticism (Somers & Block, 2005). Specifically,
neoliberalism relies on social naturalism, which claims “that the laws of nature govern human society” and that nature is “a self-regulating system that when untouched by political intervention will tend towards equilibrium and order” (Somers & Block, 2005, p. 271). This argument involves a conversion narrative that neutralizes and delegitimizes public policies by referring to a more harmonious past characterized by natural order and equilibrium that existed prior to the onset of stagflation and economic crisis in the 1970s and early 1980s. Economic crises such as stagflation are explained as departures from the natural laws of the harmonious past.¹

This social naturalism argument is sustained by the militantly anti-positivistic theory of causality known as theoretical realism where the true causal mechanisms of nature’s self-regulating order are revealed, even though they cannot be observed (Somers & Block, 2005, p. 272). Theoretical realism asserts that unobservable causal mechanisms are more real than the misleading illusions of empirical observation. In this case, the pivotal mechanism of natural order is competition between organisms. In the world of appearances, competition creates losers, and it would seem logical and well intentioned for humans to set up political institutions to help the losers and reduce human suffering. But, neoliberalism suggests that this political intervention violates the underlying natural laws of order and creates the very disorder and suffering it was designed to ameliorate.

In short, a fundamental premise of neoliberalism is that the state’s interference with market mechanisms is the cause of poor economic performance, and that returning to market fundamentalism will restore prosperity. To achieve this goal, neoliberalism advocates several changes in the relationship between societies and states: (1) expand markets by eliminating government policies interfering with markets, (2) cut taxes to simultaneously reduce the resources of inefficient government and channel them to private investors for capital formation, (3) privatize by selling public properties to private economic actors, (4) commodify things that were not originally produced to be exchanged in the market (e.g., health, education, pollution), and (5) eliminate social programs to establish personal responsibility.

**HISTORICAL CONTINGENCIES, POLITICAL-LEGAL ARRANGEMENTS, AND STATE STRUCTURES**

In contrast to the theoretical realism of neoliberalism, classical (e.g., Marx, 1867; Polanyi, 1944) and contemporary (e.g., Poulantzas, 1974; Mizruchi &
Koenig, 1986; Boies, 1989, 1994; Block, 1990; Prechel, 1990, 2000, 2006; Akard, 1992; Grant, 1995; Morris, 2005) political sociologists show that capitalists organize politically in response to economic crisis and attempt to redefine the political-legal arrangements in ways that facilitate capital accumulation. These political sociologists also show that state structures are enacted that are more beneficial to some segments of society than others.

These political and conflictual dimensions of society are captured by social structure of accumulation theory, which maintains that capitalism goes through a cycle that is repeated over time, and that capital accumulation and profitability depends on external institutional arrangements. These institutional arrangements, which include the ideological, political and economic spheres, are designed to ensure conditions favorable to capital accumulation and the reproduction of class relations (Gordon, Edwards, & Reich, 1982; Kotz, McDonough, & Reich, 1994). However, a breakdown in one part of these institutional arrangements undermines capital accumulation.

There are three distinct stages in each social structure of accumulation. The initial exploration phase follows periods of economic decline and profitability crisis. During this exploration stage, state managers and capitalists experiment with restructuring the political-legal arrangements in ways that facilitate capital accumulation. After new institutional arrangements are enacted, consolidation occurs. This constitutes a new social structure of accumulation, which provides the foundation for higher profits. The last stage is decay, which is characterized by incompatibility within the institutional arrangements. Markets weaken during periods of economic decline and instability. Decay and the subsequent capital accumulation crisis results in a new exploration phase and the cycle is repeated.

Research examining the decay-exploration transitions shows that when capital dependence increases, the capitalist class unifies and mobilizes politically to redefine the political-legal arrangements in order to offset destructive market forces. Public policies and state structures are enacted to institutionalize market stability in ways that ensure an acceptable rate of capital accumulation by the dominant power bloc, which is the outcome of political alliances among dominant classes and class fractions (Poulantzas, 1974; Prechel, 2000). Decay-exploration transitions simultaneously entail a shift in the dominant economic sector and the internal composition of the dominant power bloc.

The state played a central role in all three decay-exploration transitions in the previous 130 years in the United States. For example, in the 1870–1890 decay-exploration transition, dominant fractions of the capitalist class mobilized politically to pressure the state to eliminate ‘cutthroat competition’
In response, regional states extended corporate property rights by legalizing the holding company form, which granted corporations a status previously reserved for individuals. Specifically, if a corporate activity was not forbidden by law, it was legal. Among the most important changes was the extension of corporate property rights. After these laws were enacted, corporations could own other corporations, which meant that firms could purchase other firms and incorporate them as subsidiaries of the parent holding company.

The economic crisis in the 1920s–1930s that resulted in the Great Depression was caused, in part, by stock speculation in the unregulated holding company. Again, classes and capitalist class fractions pressured the state to redefine the political-legal arrangements to limit the destructive consequences of individual speculation in an unregulated market.

Similarly, during the 1970s–1990s decay-exploration transition, capitalist class fractions pressured state managers to create new political-legal arrangements in response to prolonged market instability and declining profits. To contain the destructive forces of the market, changes during the early phase of this transition increased protectionism and limited free trade. For example, in the 1980s and early 1990s, the steel industry organized politically and successfully pressured the Reagan and G. H. Bush administrations to pass some of the most powerful protectionist legislation in the 20th century. Also, the manufacturing fraction of the capitalist class succeeded in pressuring state managers to pass the Revenue Tax Act of 1981, which subsidized this capitalist class fraction (Prechel, 1990). Protectionism also increased in other economic sectors in the 1980s; government spending escalated in defense and weapon development and in energy exploration and development (Boies, 1989, 1994). State subsidies were extended to other economic sectors in the 1990s when government spending increased in pharmaceutical, semiconductor, and software research.

WHAT IS NEW ABOUT NEOLIBERALISM?

IDEOLOGY

It is no coincidence that theoretical realism is at the center of the neoliberal epistemological infrastructure. Advocates of neoliberalism must employ theoretical realism to make their case because the empirical history is inconsistent with their claims. During the three historical transitions in the last 130 years, in response to political pressure from the capitalist class, the
federal government intervened in the economy to create new political-legal arrangements to protect capitalist class fractions from destructive market forces.

Despite neoliberal claims, there is no historical record of a previous harmonious society in the United States or elsewhere, and it is impossible to empirically observe or measure the theoretically real natural law of competition. When confronted with data that contradict the claims of neoliberal policy outcomes, supporters respond by advocating policies that further deinstitutionalize political-legal arrangements and claim that this is the appropriate path to a naturally regulated future of order and equilibrium. The result is that the neoliberal regime politically “constructs markets by means of draconian laws and policies, while simultaneously insisting that the process is entirely natural and apolitical” (Somers & Block, 2005, p. 283). Neoliberal ideology justifies a particular set of political and economic institutional arrangements in the name of deregulation that facilitates capitalist growth and development in ways that benefit certain fractions of the capitalist class.

Thus, neoliberalism is a total ideology, which “refers to the ideology of an age or a concrete historical-social group” (Mannheim, 1936, p. 56). Total ideology is best understood as a world view or ideas and categories of thought (i.e., Weltanschauung) that is bound up with existential and historical conditions of a class or epoch (Mannheim, 1936). Total ideology “calls into question the opponent’s Weltanschauung (including his conceptual apparatus), and attempts to understand these concepts as an outgrowth of collective life of which he partakes” (Mannheim, 1936, p. 57; Zeitlin, 1968, pp. 304–305). In this case, neoliberalism emerged in the 1980s and 1990s to delegitimate political-legal arrangements based on the Keynesian model – which suggest that the government had a central role in ensuring capitalist growth and development while providing safeguards for the working classes. Neoliberal ideology attacks these dimensions of the political-legal structure because they interfere with capital accumulation agendas of the dominant power bloc.

By the 1990s, neoliberalism became the term “used to describe the transformations capitalism underwent at the turning point of the 1970s and 1980s” (Dumenil & Levy, 2004, p. 1). As ideology, neoliberalism involves a critique of the previous institutional arrangements and an explanation of why they failed. As a political agenda, neoliberalism involves a set of policies to create new institutional arrangements to facilitate economic growth and development. As during previous historical transitions, these institutional arrangements included political-legal arrangements that benefit
fractions of the capitalist class more than others because public policies
cannot favor all economic sectors equally. Contemporary political-legal
arrangements provide substantial benefits to finance capital, a key
component of the dominant power bloc (Prechel, 2000).

FINANCIALIZATION OF THE CORPORATION AND
THE ECONOMY

By the mid-1980s, capitalist class fractions unified and mobilized politically
to solve the capital shortage problem in corporate America. The solution to
this problem entailed redefining the political-legal arrangements in ways that
facilitated financialization: the influence of finance on corporations and the
economy (Levitt, 2002; Stiglitz, 2003). Capitalists created the Tax Reform
Action Coalition (TRAC), which consisted of 250 large corporations
including more than 100 of the industrial Fortune 500, to pressure state
managers to change corporate tax laws in ways that facilitated capital
formation. The TRAC lobby argued that market forces are the most
efficient incentive to guide business decisions and that corporate taxes
functioned as industrial policy and interfered with market incentives. They
also maintained that policy should allow corporations to use equity (i.e.,
internal) financing instead of debt (i.e., external) financing. However, under
then current tax law, the after-tax cost of debt was lower than the after-tax
cost of equity, which created incentives to use debt financing.

TRAC proposed a policy initiative to allow management to ‘unlock’ the
capital in their corporations and use it to solve their cash flow problems.
However, implementing this agenda required a fundamental change in
corporate tax law. This coalition succeeded when the Tax Reform Act of
1986 (TRA86) and the Revenue Act of 1987 (RA87) included provisions that
repealed the New Deal capital transfer tax between subsidiaries and their
parent companies. By eliminating the capital-transfer tax, this legislation
also reduced the operating costs of this corporate form.

Soon, capital-dependent corporations began to change their divisions
to subsidiaries, incorporating acquired firms as subsidiaries, and issuing
stock in them. By the mid-1990s, 65 of the 100 largest industrial
corporations were organized as a multilayer-subsidiary form. In this
multilayer-subsidiary form, the central office of the multidivisional form is
replaced by a legally independent parent company and the divisions are
replaced by legally independent subsidiary corporations. This transition to
the multilayer-subsidiary form permitted managerial control of legally independent (subsidiary) corporations by owning just over 50 percent of their stock. Because parent companies can raise capital by issuing stock in their subsidiary corporations, the multilayer-subsidiary form created new options to manage capital dependence. This new corporate form permitted management in parent companies to use their subsidiary corporations as internal capital markets. That is, because subsidiary corporations are legally independent companies, they can issue stock. The capital raised by these stock offerings can be transferred tax free to the parent company where it is used, for example, to acquire another corporation or pay down debt (Prechel & Boies, 1998; Prechel, 2000).

The increased financial flexibility of the multilayer-subsidiary form allows management to change corporations’ product lines by simply buying and selling subsidiaries via stock transactions. Together with changes in antitrust laws, this change allowed corporations to rapidly increase their size and control a larger share of the market. Whereas some subsidiaries may have fewer than 10 employees, others are among the largest corporations in the world. For example, the 200 largest industrial corporations listed by Fortune magazine in 1993 contained 29 subsidiary corporations.²

By making it more viable for U.S. transnational corporations to organize their domestic corporate entities as subsidiaries, parent companies could better compare the profitability of their domestic operating units to their foreign subsidiaries. (Foreign operating units must be organized as legally independent subsidiaries because they are embedded in different political-legal arrangements than the parent company.) Also, because subsidiaries are legally independent corporations, the multilayered-subsidiary form creates a liability firewall between the parent company and its subsidiaries. Under certain conditions, these property rights protect parent companies from liability lawsuits caused by, for example, faulty products produced in their subsidiaries. Thus, the property rights associated with this new corporate form provides additional layers of protection for the parent company from product liability lawsuits. Restructuring as a multilayer-subsidiary form simultaneously redefines the legal relationship between individuals and corporations in ways that reduced the responsibility of corporations and increased the responsibility of individuals for their own safety and health. This is consistent with neoliberal ideology that emphasizes personal responsibility.

In addition to creating the political-legal arrangement that provided corporations with a way to raise capital (i.e., stock issuances in subsidiaries) and control markets, corporate America lobbyed for public policy changes
to restructure the banking industry. Two changes in financial corporations’ political-legal environment are particularly relevant. The 1999 repeal of the Glass-Steagall Act permitted firms to sell multiple services and products to a single nonfinancial corporation. Eliminated regulation of the financial sector allowed financial firms to provide a wide range of financial services and products to the same corporation, which includes loans, securities (i.e., stocks, bonds) underwriting, advice on mergers and acquisitions and structured financing.

Financial deregulation also resulted in the increased use of financial instruments such as derivatives, which are contracts between two or more parties whose value is derived from the value of another underlying security. These underlying securities can include anything that represents ownership such as currency, home mortgages, student loans, stocks and bonds, or commodities (Levitt, 2002, p. 311). Derivatives involve creating a market from the performance of another market. Nothing new is produced except more securities and contracts. Historically, market-traded derivatives consisted of futures and options on real commodities such as corn, soybean, wheat, hogs, cattle, and a narrow range of financial products (e.g., stocks, treasury bonds, currencies). After deregulation of corporate financing and accounting practices and the creation of financial and energy derivatives markets, derivatives became a popular means to manage financial risk in corporate America.

Together, the extension of corporate property rights and financialization of the corporation and the economy permitted the reemergence of destructive market forces by making it easier for corporations to hide their financial transactions from the investing public in legally independent subsidiaries and partnerships. With the cooperation or corroboration of managers in investment banks, Enron managers engaged in one of the largest stockholder frauds in the history of capitalism. This massive corporate fraud was viable because of asymmetric information between investors and managers, which was permitted by the political-legal arrangements in which this multilayer-subsidiary form was embedded (Prechel, 2006). Although Enron is the most widely known example of corporate malfeasance, partnerships and subsidiaries were widely used by corporate America to shift unprofitable operations and debt off their balance sheets.

The emergence of private-investment partnerships represents another dimension of neoliberal financialization where profits are made from the secondary financial market by purchasing stock and derivatives and reselling them for a profit (Krier, 2005). Profits are derived from a market that engages solely in the exchange of fictitious capital, which takes the
form of securities and various other financial instruments that represent claims to capital in the money form (Marx, 1894 [1981]; Harvey, 1982). Fictitious capital has a claim on the money capital that is realized from the sale of a physical commodity. Contemporary financialization permits the expansion of economic sectors where profits are derived solely from fictitious capital.

For example, since its inception in 1987, Blackstone Group built a $79 billion portfolio of securities and other financial instruments. In March 2007, Blackstone announced its intent to go public in an initial public offering (IPO) of stock that is projected to raise $4 billion. That is, Blackstone plans to raise this $4 billion in the money form of capital from investors by selling stock (i.e., fictitious capital) whose value is based on the value of another form of fictitious capital (i.e., its portfolio of securities and other financial instruments). As the layers of fictitious capital increase, risk in the economy multiplies because the surplus from an increasing number of transactions is derived from the surplus realized from the sale of physical commodities. Thus, if the sale of the underlying commodity does not produce real capital, it affects all of the levels of fictitious capital that are based on that commodity. This is particularly a problem under the current political-legal arrangements in the United States where corporations are not required to disclose the extent of their use of fictitious capital to investors, as was the case with Enron Corp.

Investment banks benefitted substantially from the multiple forms of corporate restructuring and recapitalization permitted by the political-legal arrangements that redefined corporate property rights and financialized corporate America. Disclosure fees, which are the capital paid to investment bankers for marketing new stocks and bonds, were $9.3 billion in 1996, $8.6 billion in 1997 and $8.8 billion in 1998. Although disclosure fees are only one source of financial firms’ revenue, they were more than the entire 1998 revenue in large industrial corporations such as Dana, Eli Lilly, Honeywell, and Whirlpool. After corporate consolidation occurred in this economic sector, the corporate underwriting market was controlled by very few investment banks. The fees for the top ten investment banks were $6.518 billion (1997) and $7.066 (1998) billion, which represented 80 percent of the total. Moreover, U.S. investment bankers are the major underwriters of global consolidation. In 1998, Goldman Sachs underwrote 38.2% of the worldwide mergers and acquisitions entailing transactions of $960 billion. Many consolidations and virtually all of the largest consolidations occur through stock swaps (e.g., Exxon-Mobil, British Petroleum-Amoco, Daimer-Benz-Chrysler).
By the 1990s, neoliberal ideology was also used to justify deregulation of markets in less developed countries. Neoliberal ideology was also used to critique the protectionist dimensions of the General Agreement on Trade and Tariff (GATT) and legitimate restructuring the transnational trade regulatory arrangements. To advance their free-trade agenda, advocates of neoliberalism succeeded in replacing the GATT with the World Trade Organization and establishing regional trade agreements such as the North American Free Trade Agreement (i.e., NAFTA).

In summary, neoliberal policies, which are guided by limiting government intervention and imposing market regulation on everything that can be commodified, include several interrelated tenet. Deregulation frees businesses from costly rules, privatization sells off public assets to more efficient private entrepreneurs, tax cuts on capital free up money for investment and capital formation, and social programs are dismantled to cut government spending and make individuals more personally responsible. Neoliberal ideology justifies fewer government programs that advance the public good in order to facilitate growth in the economic sphere. This new federalist deregulatory social structure of accumulation which provides a framework to ensure economic stability and growth, created a complex disguise for increased corporate power and restoration of the power of economic elites.

**INCOME AND WEALTH REDISTRIBUTION UNDER THE NEW FEDERALIST REGIME**

The transformation of the state that occurred during this decay-exploration transition in the United States is characterized as the *new federalism*: a reduction of federal government regulatory protections and safeguards for the working classes (Grant, 1995; Prechel, 2000, p. 15). This social structure of accumulation increased workplace discipline and job insecurity for the working class (Marshall Scott herein), and decentralized responsibility to finance and implement social and public services to local government (Harms herein, Labao herein). Like other decay-exploration transitions, the prevailing neoliberal ideology purported to ensure economic growth and restore prosperity for everyone. In actuality, the class structure was altered and created a radical redistribution of resources produced by society.

Financialization of the corporation and the economy was paralleled by one of the largest increases in income and wealth inequality in the history of
the United States. The real (i.e., adjusted for inflation) median family income increased by 20 percent since 1973. However, a detailed examination shows that the majority of this change (i.e., 11 percent) is explained by the increase in the number of two-worker households. A clear picture of the wage issue is represented by the 0 percent change in the real median family income that has one-male worker. The median male worker with a high school diploma earned 14 percent less in 2002 than in 1973 and the real median wages of all men was lower in 2002 than it was in 1973. Moreover, the wages of women, which is the group whose wages grew most rapidly, are still only 80 percent of men’s wages and the typical black family earns approximately 60 percent of their white family counterparts (Mishel, Bernstein, & Allegretto, 2005). During this same time period, the income of the wealthy increased. By the 1980s, the gap between middle and top wage earners increased and continued to widen in the 1990s. Between 1969 and 2002, the middle class shrunk from 71.2 percent to 60.7 percent of the population while the portion of the population that shifted to the lower and upper classes increased (Mishel et al., 2005, p. 90).

The inequality in wealth increased even more dramatically during this regime change. Whereas the political-legal arrangements in the middle decades of the 20th century (i.e., 1930s to mid-1970s) reduced the power of corporations and redistributed wealth more equally in the United States, this trend was reversed in the later decades of the century. The percent of assets owned by the top 1 percent of the population increased from 20.5 percent in 1974 to 38.5 percent in 1990. Although this historic high point in wealth inequality was followed by a slight drop to 33.4 percent in 2001, that change was caused primarily by a decline in stock market growth (Wolff, 2000, 2002). As Mishel et al. (2005, p. 17) point out, “the U.S. economy is capable of generating tremendous wealth, but there is absolutely no guarantee that this wealth will reach the working families responsible for the growth.” Virtually all of the growth that occurred since the mid-1970s, has “flowed to profits, not labor” (Mishel et al., 2005, p. 17).

In addition to the changes described above, there are several additional events that explain why capital, not labor, benefitted from these changes. The anti-labor politics of the Reagan Administration, lax enforcement of labor laws and subsequent decline in union membership and power, undermined the capacity of the working classes to negotiate for higher wages. The key to understanding the redistribution of wealth and income involves changes in the regulatory environment that permitted financialization of the corporation and the subsequent change to the multilayered-subsidiary form. Financialization permitted corporations to create subsidiaries and issue stock in them...
to raise capital, which was followed by a massive growth in the stock market. The Dow Jones Industrial increased from 3,000, an historic record high, on April 17, 1991 to more than 10,000 in 1999 to above 12,000 in the mid-2000s. Moreover, changes in the historical trajectory resulted in an income shift from labor to profits between 1995 and 2000 that intensified in the early 2000s (Mishel et al., 2005, p. 110). Since few families receive capital income, the upper classes, who own most of the corporate securities, were the primary beneficiaries of this increase. The top 1 percent of the population owned 44.9 percent of corporate stock in 2001.

Whereas financialization of the corporation (e.g., increased value from financial transactions such as stock issuances) increased corporate revenues, corporations redistributed this wealth to (1) investors, (2) payment for financial services to investment banks for stock underwriting, consulting on mergers and acquisitions and other forms of corporate restructuring, and (3) wages and bonuses to executives. While nonfinancial corporations redistributed wealth to corporate executives via lucrative stock options and higher salaries, financial corporations redistributed this wealth as high wages and bonuses to investment bankers and other financial managers who underwrote stock issuances and advised corporations. The median wage for chief executive officers, which includes bonuses, grew 79 percent between 1989 and 2000. During that same time period, the median wage for all workers increased by 5.8 percent. If incentive awards, stock options exercised and stock options awarded are included in CEOs pay, it increased by 342 percent from 1989 to 2000. This change represented an increase in the ratio of CEO to average worker pay from 27 in 1973 to 71 in 1989 to 300 in 2000 (Mishel et al., 2005, pp. 212–213).

**CONCLUSION**

Neoliberalism is best understood as an ideology that affects the political process, not as a theory that explains empirical events. Neoliberal ideology is a world view that legitimates policy initiatives in the political sphere to support the capital accumulation agenda of the dominant power bloc.

**NOTES**

1. Harvey (2005) refers to the middle decades of the 20th century as embedded liberalism and the current historical period as neoliberalism. Although Harvey’s
contributions are important, he does not provide a detailed analysis of the political process that transformed the political-legal arrangement during this historical transition.

2. The multilayersubsidiary form shares many characteristics with the late 19th and early 20th century holding company; both have legally independent parent companies that own 50 percent or more of subsidiaries’ stock (Prechel, 2000).

REFERENCES


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PART II:
DECENTRALIZATION UNDER THE NEOLIBERAL NEW FEDERALISM: CONSEQUENCES FOR WORKERS’ HEALTH, HIGHER EDUCATION, AND LOCAL GOVERNMENTS
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WORK-RELATED INSECURITY IN THE NEW ECONOMY: EVALUATING THE CONSEQUENCES FOR HEALTH

Heather Scott-Marshall

ABSTRACT

Structural changes in the economy and labor market, coupled with an ideological climate that reinforces business dominance, have transformed work-related insecurity from a relatively transient experience arising from the threat of job loss to a chronic occupational stressor embedded in the new organization of work. Results from multilevel regression analyses show that exposures to indicators of career and income insecurity have a cumulative adverse effect on individuals’ health trajectories. The findings are discussed in relation to the rise of “post-standard” employment which reveals work-related insecurity as a core property of work relations linked with the distribution of labor market power.

INTRODUCTION

For over three decades, structural changes in the economies of industrialized countries have given rise to fundamental changes in labor markets, work
systems, firm structures and hence, individual work-related experiences. The transition to globalized capitalism has been accompanied by a series of pressures – heightened global competition, quickly changing product and service markets, rapid technological innovation – to which business has tried to adapt. Business’ adaptive response to these pressures derives largely from a new institutional regime that is predicated on neo-liberal philosophy and has involved a fundamental shift away from the equitability motives built into traditional labor market structures and social conventions (Harvey, 2005; Osterman, 1999). Embodied in the rise of the New Economy, contemporary socio-political-economic contingencies have been accompanied by a sea change in employment relations whereby workers are increasingly exposed to market forces. In stark contrast to the emphasis on stability and longevity that characterized the previous labor market regime, current dogma regarding the primacy of markets has given rise to a new set of employment practices that shift a greater proportion of risk onto individual workers (Breen, 1997; Coburn, 2004). A key aspect of this trend is the declining protection against job loss evinced by business’s widespread effort to restructure, streamline and “downsize” operations (Budros, 1997; Rifkin, 1995). Consequently, a large proportion of the workforce has either experienced job loss, or lived with the threat that job loss may be in the offing (Brockner, 1988; Ferrie, Marmot, Griffiths, & Ziglio, 1999; Rifkin, 1995). These trends have given rise to the charge that job insecurity represents a large and growing problem in the contemporary labor market (Heery & Salmon, 2000; Organization for Economic Cooperation and Development, 1997a) with adverse consequences for workers’ health (Ferrie, Shipley, Marmot, Stansfield, & Smith, 1999; Hartley, Jacobson, & van Vuuren, 1991; Isaksson, Hogstedt, Erikson, & Theorell, 2000).

Although career disruption due to layoff represents an important aspect of changing patterns of employment, the exclusive focus on the risk of job loss provides an only “partial picture” of the new work relations (Benach, Amable, Muntaner, & Benavides, 2002, p. 405). Structural changes in the economy and labor market coupled with an ideological climate that has reinforced business dominance have produced a complementary shift in employment relations. These changes are evident in several large-scale trends such as wage stagnation, job deskilling, the reduced availability of full-time permanent employment, and the deterioration of job ladders (Burke & Shields, 1999; Grimshaw, Ward, Rubery, & Beynon, 2001; Livingstone, 1999; Tåhlin, 2001; Vosko, 2003). To date, however, observers concerned about rising insecurity in employment have focused predominantly on the increase in job instability arising from widespread
organizational retrenchment. Moreover, conceptions of the job insecurity “problem” are largely confined to the micro-level where the links to health are understood as arising from acute stress due to the perceived risk of job loss (Scott, 2004; Sverke, Hellgren, & Naswall, 2002). These frameworks lack a comprehensive theorizing of the structural “first causes” of the changes to work relations over the past several decades; consequently, these schemas fail to capture the full range and impact of insecurity in the contemporary labor market. This study uses a political economy approach to examine the problem of work-related insecurity and the consequences for workers’ health. It contributes to the empirical literature on this issue by investigating the prevalence of insecurity in the Canadian labor market, and the effects of exposure to insecurity on workers’ health over time.

**HISTORICAL CONTEXT: THE POSTWAR INSTITUTIONAL FRAMEWORK AND A NEW STANDARD IN WORK-RELATED SECURITY**

Perhaps the most remarkable feature of the North American postwar period (circa 1945-1975) was the unprecedented level of economic expansion. The concentration of large blocs of financial and industrial capital signaled the maturity of a new phase of “monopoly capitalism” (Ross & Trachte, 1990). Monopoly capitalism was distinguished by a particular balance in the set of “strategic social relations” (power and bargaining relations) that underpin the capitalist mode of production i.e., capital–capital, capital–state and capital–labour. Capital–capital relations were characterized by relative market stability and an end to the price wars of the competitive economy of small firms that Marx had studied. Economic competition became limited to a small number of large, primarily domestic corporations (Ross & Trachte, 1990). Consequently, wages were largely “taken out of competition” and a stable wage relationship developed across firms and industries (Osterman, Kochan, Locke, & Piore, 2002). Sharp increases in government expenditures helped to absorb a rising surplus and maintain the expansion of industry, giving rise to new patterns of capital–state relations. Ross and Trachte (1990) have described the conditions of monopoly capitalism as giving capital a new “lever of exploitation” which transformed capital–labor relations. Previously, capital had leveraged its position via a large reserve of underemployed labor; under monopoly capitalism, on the other hand, capital’s leverage centered on exploiting the segmented labor market by appropriating surplus value from the competitive sector (Ross & Trachte, 1990).
Core sector workers were largely sheltered from fluctuations in conditions of supply and demand, allowing wage relationships to remain relatively stable across firms and industries (Osterman et al., 2002). The largesse of this period formed the basis of a new institutional framework, which diversified risk away from individuals and consolidated a range of social securities. First, statist welfare was unveiled in the form of unemployment insurance, hospital insurance (later medicare), and universal old-age pensions. These programs helped to restore citizens' faith in government and the capitalist system, and also dampened labor unrest (Palmer, 1992). Another key development was a new regime of industrial legality that comprised a set of regulations for employment standards and provided workers with a set of institutionalized bargaining rights. The Canadian Industrial Relations and Disputes Investigations Act (IRDIA)\(^2\) of 1948 designated several longstanding employer tactics (e.g., company unionism and overt discrimination against trade unions) unfair labor practices (Palmer, 1992). Following the implementation of the Act, unions grew in size and bargaining strength enabling them to incorporate a range of income security benefits such as health insurance and private pension plans into their agendas (Osterman et al., 2002; Palmer, 1992).

The twinned postwar developments of statist welfare and industrial legality underpinned a new labor-capital accord that manifested in an unprecedented level “class harmony” (Palmer, 1992). Under the pact, workers were able to expect reasonably secure and well-paid jobs in return for loyal and productive service (Rubin, 1996). The fortunes of labor and capital became linked such that workers (at least those in core sectors) achieved a standard of living that grew in tandem with wider economic prosperity (Osterman, 1999; Palmer, 1992). Although the primary goal of the labor-capital accord was to “stabilize class relations and put profit on more predictable ground” (Palmer, 1992, p. 268), the pact is also considered to have given rise to labor’s “Golden Age.” This was a period when collective bargaining rights were won, wages were pushed to new heights of consuming power, and job conditions improved substantially (Palmer, 1992).

To be sure, the main beneficiaries of the accord were English-speaking, male unionists in the trades and mass production, most of whom worked in traditional strongholds of regional and industrial privilege (Palmer, 1992). Many workers remained outside some of the advantages bestowed on the core sectors of the Canadian working class due to a lack of union affiliation, inadequate or unsuitable skills, regional location, gender, ethnicity, or race (Palmer, 1992). However, despite the obvious advantage of workers in the
core, the symbolic importance of the labor-capital accord cannot be discounted. Palmer (1992, p. 336) has described this period in Canadian labor’s history as one of “accomplishment, victory and prosperity” since for the first time ever labor managed to force some semblance of security from capital and the state. Moreover, the institution of an extensive social safety net was key to the development of a predominant worldview involving “social citizenship rights” that encompassed the right to a modicum of economic welfare and security “according to the standards prevailing in the society” (Marshall, 1991, p. 53). Individuals who were excluded from expanding labor market opportunities (e.g., the unemployed or under-employed) were compensated by way of new social programs (Palmer, 1992; Rubin, 1996) signifying a new commitment to diversifying risk away from individuals such that life chances became less dependent on market forces (i.e., the process of “decommodification”) (Coburn, 2000).

The major principles of stability and reciprocity that underpinned the labor-capital accord were reinforced at the firm level. The postwar firm was distinguished by its use of a specific system to augment the stability of the employment relationship, namely the internal labor market (ILM). The ILM was a closed system of employment comprising a set of deferred rewards designed to tie employees to firms over long periods (Cappelli et al., 1997). In particular, employees were granted provisions for long-term job and financial security in return for a longstanding commitment to their employer. Security provisions included: permanent employment contracts, steady career progression from low- to high-skilled posts, transparent and integrated pay structures, and opportunities for skill development through onsite training programs (Grimshaw et al., 2001). Seniority was the principal determinant of increments in wages, income security benefits (particularly employer-sponsored pensions), career-advancement opportunities, and overall job security (Cappelli et al., 1997; Jacoby, 1984; Osterman, 1994; Pinfield, 1995). Consequently, a major byproduct of the closed employment system was that most employees had long service records. In turn, the career provisions of the ILM formed the basis of the modern notion of the “career-job” (Hardy, Hazelrigg, & Quadagno, 1996; Pinfield, 1995).

Although internalized employment practices were never uniform across all sectors of the economy, the advantages to employers of the closed system made it both relatively stable over time and consistent across large sections of industry (Cappelli et al., 1997; Dougherty, 1998; Osterman, 1994). In particular, employers viewed these systems as a highly efficient means of managing the workforce since stable employment relations helped to meet the internal productive requirements of the firm while also protecting its
training investments (Grimshaw et al., 2001). The major byproduct of the internal employment system was the creation of a new standard in employment, which stipulated that stability, longevity, and mutual prosperity were key elements of the employment exchange. This standard is considered “emblematic of the (postwar) era” (Cappelli et al., 1997, p. 48) since it marks the point at which employment relationships were no longer to the same extent mediated by the market.

In turn, the postwar standard in employment profoundly influenced the modern work-life course pattern. Lifelong careers were the fulcrum of the “standardized life cycle” whereby biography unfolded predictably according to pre-work, work and post-work states (Kohli, 1986). The standardized life-course pattern provided individuals with a high degree of certainty in long-term life planning – for example around major investment decisions involving home-ownership, post-secondary education for children, and planning for retirement (Osterman et al., 2002; Rubin, 1996).

GLOBALIZATION AND THE EROSION OF THE POSTWAR STANDARD IN EMPLOYMENT

The accord between workers and employers endured for nearly three decades following WWII. By the mid-1970s, however, the first waves of structural change emerged as recession loomed, global competition intensified, profits diminished, and business sought to extend operations to more profitable low-wage markets (Ross & Trachte, 1990). The world economic crisis that ensued was a major catalyst for restructuring the process of accumulation. The North American economic monopoly that was built on the industrial structures of mass production gave way to a new system of globalized capital based on worldwide networks of information and product exchange (Rifkin, 1995; Ross & Trachte, 1990). These changes were reinforced by the dominance of business rhetoric and ideology at the national level, which insisted that the state should dismantle postwar regulatory structures and replace them with policies that generate market incentives (Prechel, 2003; Ross & Trachte, 1990). This new phase of competition has engendered significant transformations in the structure of the labor market, the nature of state activity, and the mechanisms of surplus extraction (i.e., capital’s lever of exploitation) (Palmer, 1992; Ross & Trachte, 1990).

Global capital–capital relations are distinguished by a heightened level of price competition among firms of different national origin. Market shares
have shifted drastically, and North American firms are far less dominant
in the world economy than during the monopoly phase (Luttwak, 1998;
Ross & Trachte, 1990). Global markets have made the viability of different
businesses highly contingent on their ability to respond to pressures arising
from international competition, rapid technological innovation, and quickly
changing product and service markets (Luttwak, 1998). Hence, the risks of
doing business have increased significantly, and sudden “reversals of
fortune” are increasingly common (Collingwood, 2003).

Capital–labor relations have been profoundly influenced by shifts in the
mechanisms of labor extraction that are available to employers (Ross
& Trachte, 1990). Global capital wields a new lever of exploitation i.e., the
threat of capital flight to more profitable low-wage sectors around the world
(Beck, 2000; Ross & Trachte, 1990). Facilitated by a series of technological
“revolutions” capital can locate most major operations globally (Luttwak,
1998; Ross & Trachte, 1990); as such, the comparative cost of labor has
become “the key to locational competitive advantage” (Storper & Walker,
1984). The threat of capital mobility has also had an impact on capital–state
relations. In particular, governments’ attempt to preserve high levels of
regional investment has spawned a shift in public expenditures toward
investors’ interests and a corresponding reduction in the social wage
(Coburn, 2004; McQuaig, 1998; Ross & Trachte, 1990).

Global capital’s exploitive leverage has produced declines in labor’s
ability to protect its interests in defining the terms and outcomes of labor
market exchanges. Within firms, this shift in the power relations of work is
evincted by specific changes to work organization. These changes involve
the breakdown of traditional methods of structuring the employment exchange.
In particular, the protected career structures that gave rise to the
unprecedented level of employment stability of the postwar period are no
longer considered cost-effective in an increasingly volatile global economic
environment. As such, several of the traditional “pillars” of the ILM have
been dismantled and replaced by new policies for determining wages and
benefits, career progression, internal training, and job security (Grimshaw,
Beynon, Rubery, & Ward, 2002; Grimshaw et al., 2001; Rubery, 1999).

Changes in Wage Determination

The wage systems of postwar firms involved de facto profit sharing whereby
the economic successes of employers were expected to directly benefit the
income security of workers (Osterman, 1999). Market forces were muted
and wage structures were stable and biased toward wage compression (Betcherman, 1999; Osterman, 1999; Rubin, 1996). By contrast, newer wage-setting mechanisms rely increasingly on “pay-for-performance” arrangements that are designed to better align employees’ interests with the profit goals of the firm (Osterman, 1999; Smith, 1997). Changes in wage-setting practices have been implicated in several aggregate-level trends such as stagnating and/or falling wage rates, a rising proportion of workers who are earnings underemployed, and growing income inequality (Burke & Shields, 1999; Jackson, Robinson, Baldwin, & Wiggins, 2000; Katz, 1998; Osterman, 1999; Statistics Canada, 2003).

Fewer Social (Income) Security Benefits

A key aspect of the traditional employment exchange was the expectation that firms should contribute to workers’ long-term income security by way of generous benefits packages (Osterman, 1999). These institutions were expected to provide, either on their own or through collective bargaining, private reserves for retirement, disability benefits, extended health insurance (i.e., coverage for essential health services excluded from universal medicare such as dental care and prescription drugs), and training and education for workers and their families (Osterman et al., 2002; Palmer, 1992). A strong labor movement was instrumental to extending the range of income security benefits provided not only to unionized employees, but also to employees of non-unionized firms due to “spillover” effects (Osterman, 1999; Palmer, 1992). Macroeconomic change, coupled with declines in the strength of organized labor, has diminished the level of benefits that companies are willing to provide. For example, in Canada the rate of pension coverage has not kept pace with employment growth and an increasing number of firms do not provide any pensions (Statistics Canada, 2004b). More broadly, there is a general perception that employers are no longer responsible for providing a variety of key social-welfare and labor market sources such as health care, disability insurance, and training (Cappelli, 1999; Osterman, 1999).

Eroding Job Ladders

The modern bureaucracy’s “job-for-life” model involved steady career progression from lower- to higher-skilled posts (Grimshaw et al., 2001).
Over the past two decades, widespread organizational restructuring has involved the dismantling of firms’ internal hierarchies (Betcherman, 1999; Grimshaw et al., 2001, 2002; Noyelle, 1987; Osterman, 1999). Several case studies indicate that flattened occupational hierarchies have slowed career progression, increased lateral job moves, reduced promotion opportunities, and contributed to growing intra-firm pay inequality (Ackerman, Goodwin, Dougherty, & Gallagher, 1998; Appelbaum & Batt, 1994; Grimshaw et al., 2002; Hudson, 2002; Osterman, 1994; Scott, O’Shaughnessy, & Cappelli, 1996). Research into the impact on workers of these trends shows that the erosion of opportunities for job and income mobility, particularly when coupled with heightened work demands, has given rise to a new source of career-based insecurity (Grimshaw et al., 2002; Hudson, 2002; Marmot, Ferrie, Newman, & Stansfeld, 2001). The breakdown of job ladders within firms has also been identified as an important determinant of the bifurcation of the labor market. In particular, a growing proportion of workers is trapped in employment arrangements that lack sufficient hours, wages, and/or opportunities for skill-use (Grimshaw et al., 2002; Hudson, 2002; Moen, 2003).

Rising Unpaid Overtime Hours

Workplace reorganization has also been associated with increasing employee workloads (Duxbury & Higgins, 2003; Nolan, 2002; Smith, 1997). Flattened organizational hierarchies often require the expansion of job roles and responsibilities as well as a greater emphasis on “multi-skilling” (Osterman, 1999; Smith, 1997). Studies indicate that many workers in restructured workplaces feel that there are simply too many tasks to complete within their contracted hours (Duxbury & Higgins, 2001; Nolan, 2002; Wheatly, 1992). Other research suggests that longer work hours are linked to an increase in job insecurity and workers’ beliefs that remaining visible to employers reduces the chances of redundancy (Cooper & Williams, 1994; Virtanen, Kivimaki, Elovainio, Vahtera, & Ferrie, 2003). Both trends are credited with the creation of an “overtime culture” in which unpaid work is an expected part of the job (Fried, 1998; Smith, 1997). Unpaid overtime hours have been identified as a major factor in shifting work-time patterns in advanced capitalist societies (Campbell, 2001). In particular, the volume of unpaid overtime hours is increasing in industrialized countries, which has contributed to the slowdown or even the reversal of the long-term historical trend towards working time reduction (Organization for
Economic Cooperation and Development, 1998). In Canada, estimates of working hours indicate that one in five employees works overtime on a regular basis, yet less than half of these individuals are paid for this extra work (Canadian Policy Research Network, 2004b; Statistics Canada, 1998). The new long-hours culture is replacing traditional employment practices that promoted sharp divisions between work and private domains; hence, the boundaries between work and home have become increasingly diffuse (Joyce, 2003; Wharton & Blair-Loy, 2002). Increases in work hours are known to contribute to greater work-life conflict, which is associated with declines in psychological and physical health and impaired family functioning (Akerstedt, Fredlund, Gillberg, & Jansson, 2002; Dex & Bond, 2005; Duxbury & Higgins, 2003; Nolan, 2002).

The Waning Power of Unions

A key determinant of how changes to work affect individual workers is the relative strength of organized labor. In Canada, like several other industrialized nations, the influence of labor unions is in decline. By 2003 Canada’s union density (i.e., the proportion of non-agricultural paid workers who are union members) had fallen to 30 percent, down almost 10 percent since the mid-1980s (Commission for Labor Cooperation, 2003). Factors conspiring against the strength of organized labor include the expansion of service sector jobs, the migration of jobs toward smaller firms, the deregulation of large economic sectors (e.g., transportation, telecommunications), and the increasing proportion of knowledge workers with little or no affinity for unions (Finlayson, 2000). A key consequence of the erosion of labor’s influence is growing income polarization (Burke & Shields, 1999; Osterman, 1999). Previous estimates of the “spillover effects” of unions indicate that these increased the total compensation of workers by an average of 45.5 percent (Renaud, 1998). This stands in contrast to the rising disparity in income levels that is currently observed between unionized and non-unionized employees (Burke & Shields, 1999; Canadian Policy Research Network, 2004a). For example, Canadian workers covered by a union earn an average of $3.03 more per hour than individuals without union coverage (Canadian Policy Research Network, 2004a). Unionized employees are also much more likely to receive income security benefits such as pensions and paid sick leave (Canadian Policy Research Network, 2004a).
Diffuse Career Trajectories

New external pressures on firms mean that market forces increasingly bear on the employment relationship. Market-mediated employment is associated with more diffuse occupational trajectories, where workers can experience both upward and downward mobility in wages, benefits-levels, and job and pay grades (Burchell, Lapido, & Wilkinson, 2002; Cappelli, 1999; Grimshaw et al., 2001, 2002; Osterman et al., 2002). For example, pay-for-performance systems determine which employees receive adequate wages and the amount and frequency of pay raises (Cappelli, 1999; Grimshaw et al., 2002; Osterman, 1999). Restructuring campaigns can result in the assignment of employees to lower job grades. Also, the pressure for long work hours arising from workplace reorganization may not fall equally on employees in different sectors and occupations (Duxbury & Higgins, 2003; Grimshaw et al., 2002; Nolan, 2002). During times of financial crisis, employees can even be at risk of losing fully vested rights to pension benefits since these funds are often among the first cash reserves to be dissolved (Cooper & Ross, 2003; Fonda, 2005). Protection from a union has also become more precarious as the diminishing strength of organized labor has emboldened employers’ attempts to sabotage these coalitions and undermine collective agreements (Downey, 2004; Osterman, 1999).

Hence, unlike the highly structured occupational trajectory of the postwar era that enabled individuals to “orient their plans and actions,” the market-mediated employment relationship offers “no clear apprehension of occupational attainments” (Buchmann, 1989, p. 40). Despite the implications of these developments for several emergent forms of work-related insecurity, to date occupational health researchers have focused on only a single aspect of the experience i.e., the risk of job loss.

RESEARCH ON JOB INSECURITY AND HEALTH

Researchers and practitioners in the field of occupational health have devoted increased attention to job insecurity over the past three decades. The economic recession of the mid-1970s was accompanied by heavy rounds of layoff prompting widespread interest in the effects of job insecurity as a key determinant of work-related stress (Sverke et al., 2002). The health impact of job insecurity is conceived within a socio-epidemiological demand-control framework, where strain arises from the individual’s lack of control over the continuity of employment (Greenhalgh & Rosenblatt,
job insecurity is generally considered a "classic work stressor" (Sverke et al., 2002) that is associated with declines in physical and mental health indicators, as well as increases in ill-health behaviors (Ferrie, Shipley, Stansfeld, & Marmot, 2002; Ferrie et al., 2001; Heaney, Israel, & House, 1994; McDonough, 2000; Vahtera, Kivimaki, & Pentti, 1998). However, despite a substantial body of evidence that indicates that job insecurity poses a significant threat to health (Bohle, Quinlan, & Mayhew, 2001; Ferrie, 2001; Ferrie et al., 2002), the picture is far from uniform (Sverke et al., 2002). A recent meta-analytic review of studies on job insecurity concluded that causal associations between job insecurity and mental health are moderate, while those between job insecurity and physical health are small (Sverke et al., 2002).

One reason that earlier studies have found mixed support for the link between exposure to job insecurity and adverse health is that most of these investigations employ a cross-sectional research design (for an excellent review of this literature see Sverke & Hellgren, 2002). The primary concern with cross-sectional analyses is that these are not able to identify the direction of effects. It could be that poor health gives rise to job insecurity, job insecurity gives rise to poor health, or a third variable may give rise to both poor health and job insecurity. With longitudinal study designs it is possible to control for the temporal sequencing of events, as well as prior year's health. To date, only a handful of studies have attempted to incorporate such temporal elements into their research designs (Dekker & Schaufeli, 1995; Domenighetti, D'Avanzo, & Bisig, 1999; Ferrie et al., 2002; Heaney et al., 1994; Marmot et al., 2001).

Another explanation for the limited effects sizes reported by Sverke et al. (2002) is that job insecurity represents just one aspect of the overall work-related insecurity experience. Indeed, several commentators have argued that the definition and measurement of job insecurity would benefit from encompassing concerns about deteriorated employment conditions and career opportunities in addition to threats of imminent job loss (Ashford, Lee, & Bobko, 1989; Greenhalgh & Rosenblatt, 1984; Scott, 2004; Sverke et al., 2002). The handful of studies that have employed a multidimensional definition of the construct have found that insecurity can arise from several adverse employment experiences such as the loss of income, unpredictable work schedules, the loss of social networks, the assignment of unwanted tasks and responsibilities, and shrinking career development opportunities (Campbell, 1997; De Witte, 1999; Ferrie, Shipley, Stansfeld, Smith, & Marmot, 2003; Marmot et al., 2001; Roskies & Louis-Guerin, 1990). However, even studies that account for multiple aspects of work-related
insecurity fail to transcend the basic demand-control framework. As such, the strain that arises from the threat of job loss, a lack of job mobility prospects, or some other undesirable work event is understood as rooted in the same basic dynamic – i.e., the individual’s lack of control over the continuity of specific aspects of the employment situation. These models do not account for the more basic secular trend in work-based insecurity evinced by the multiple threats to the quality of employment (Burke & Shields, 1999; Chaykowski, 2005; Hudson, 2002; Rifkin, 1995; Rittich, 2004). This includes not only psychosocial aspects of the work environment (such as the subjective threat of being unemployed), but also the impact of several workplace structural determinants including the lack of unionisation, low wages, and the absence of benefits (Benach et al., 2002). Exploring the full range of insecure work experiences and their health impact requires a model that accounts for how shifts in work relations have altered the balance of power inside the employment relationship (Rittich, 2004; Scott, 2004). Such a model would account for the economic, regulatory and social factors that have contributed to declines in employment and income security throughout the labor market (Osterman, 1999; Rittich, 2004), and the effects of the chronic work-related strain to which these insecurities give rise.

THE POLITICAL ECONOMY OF WORK-RELATED INSECURITY AND THE LINKS TO HEALTH

In light of several changes to work that have contributed to fragmented (or, “de-standardized”) career and income trajectories, the nearly exclusive focus on job insecurity in the occupational health literature obfuscates the true scope of work-related insecurity and its effects. These changes have transformed insecurity from a relatively transient experience arising from the threat of job loss to a chronic occupational stressor embedded in the new organization of work. A sociological perspective that accounts for the politico-economic contingencies of the New Economy elucidates the mechanisms underlying key changes to work that affect levels of (in)security. In particular, by foregrounding the exploitive nature of the employment relationship a political economy schema imagines insecurity as a persistent feature of work relations due to capital’s greater structural power. In particular, because workers represent “the class that has no command over the means of production, the labour power of others, or the means of realizing its own labour” (Clement & Myles, 1997, p. 12) they
ultimately lack the ability to define the conditions and outcomes of labor market exchanges on their own terms. A political economy perspective also brings into view how the amount of insecurity in the labor market varies according to conditions in the wider socio-economic environment. During an economic monopoly, for example specific protective institutions (the welfare state, labor unions, and the firm) functioned to redress the power imbalance between workers and owners. Although business retained its structural advantage the largesse of the period fixed the parties in roles of mutual exchange (Coburn, 2004; Palmer, 1992; Ross & Trachte, 1990) modifying the degree of work-related insecurity in the labor market. In turn, recent changes to employment practices that have “disproportionately disadvantaged the working class” through job insecurity, underemployment, casual employment, chronic unemployment, and growing income inequality are fundamentally linked to the “exigencies of the new global economy” and the “adaptive behaviours of the power elite and capitalist-executive” (Scambler & Higgs, 1999, p. 287). Hence, a political economy perspective reveals how adverse labor market experiences represent part of a casually-linked chain or web of risk factors that is rooted in the social organization of work and the relations of class (Scambler & Higgs, 1999; Scott, 2004).

On this view, job insecurity represents only a single manifestation of the more basic work-related insecurity that is derived from the social/power relations of work. A study by Borrell, Muntaner, Benach, and Artazcoz (2004) provides some empirical support for the argument that class position represents the underlying determinant of the health risks posed by various structural features of work. The authors report that aspects of work organization such as job insecurity and physical hazards were the “main explanatory variables of social class inequalities in health” (Borrell et al., 2004, p. 1869). The findings suggest that adverse work experiences like job insecurity represent mediators in the basic relationship between social class position and health status. Hence, studies that merely document an association between job insecurity and adverse health elide the fact that the experience stems from a lack of control over employment circumstances that is more fundamentally rooted in social position. Coupled with the seemingly intractable relationship that exists between socio-economic factors and health inequalities (Bartley, Carpenter, Dunnell, & Fitzpatrick, 1996; Muntaner & Lynch, 1999; Phelan, Link, Diez-Rioux, Kawachi, & Levin, 2004; Scambler & Higgs, 1999; Whitehead & Drever, 1997) data like these seem to confirm the existence of “real class relations hinging on the ownership/control of the means of production” (Scambler & Higgs, 1999, p. 281). As such, the social relations of work represent the “first causes” of
inequalities in labor market power with important consequences for the social distribution of health.

Workers experience capital’s new exploitive power directly as changes to work that have eroded the traditional provisions for long-term career, income and ultimately work-life course security. These changes are key indicators of the extent to which workers lack control over not only the terms of labor market exchanges, but also over the course of increasingly de-standardized work-lives (Wallulis, 1998). Insofar as these changes have constrained workers’ ability to “fulfil salient values or to avoid self-defined noxious states” – particularly with respect to long-term financial and life planning – contemporary employment practices may represent sources of chronic work-based strain (Kaplan, 1996, p. 4).

Hence, the key contribution of the political economy schema is that it reveals work-related insecurity as a core property of work-relations that is modified or magnified according to wider economic conditions. As such, this schema illuminates how employers’ efforts to adapt to new economic contingencies have exacerbated workers’ vulnerability in the labor market. This vulnerability relates to the lack of substantive control over the terms, conditions, and outcomes of labor market exchanges. Workers experience this vulnerability as specific changes to work that have undermined their ability to plan for the future. In particular, the breakdown of workplace structures that were responsible for the postwar standard in employment has contributed to long-term career, income, and work-life balance insecurity, which could give rise to chronic insecurity and strain. These developments have affected all workers to some degree including those who labor under contracts that are nominally secure – i.e., full-time, full-year, non-contractually limited. I refer to these work arrangements as “post-standard” employment. By identifying the key security provisions that are being systematically dismantled at the workplace we can evaluate the impact of work-related insecurity on health. Specific characteristics of post-standard employment that may represent sources of long-term insecurity and strain include: insufficient wages, lack of income security benefits (e.g., employer-sponsored pensions), the absence of reliable job and pay ladders, substantial amounts of unpaid overtime hours, and the lack of job and income security protection from a union or collective agreement. I note that although it would be preferable to compare workers’ experiences of post-standard employment with those of the previous employment standard, available data limits the analysis to the former.

Women. Although the postwar standard in employment developed primarily around the career regime of middle-class men, many observers
maintain that the “career mystique” with which it is associated (i.e., that hard work and continuous employment will pay off in career success and security into retirement) has persisted as a powerful cultural metaphor that has been increasingly adopted by women (Moen & Roehling, 2005; Stebbins, 2001; Yamagata, Kuang, Stewman, & Hiroko, 1997) who now comprise almost half (46 percent) of the Canadian labor force (Social Development Canada, 2005). As such, female labor force participants are likely equally affected by the erosion of the postwar standard in employment security. Hence, it is important to include women in an analysis of contemporary employment experiences on health.

The role of time. An investigation of the health consequences of work-related insecurity requires an explicit recognition of the temporal dimension of the experience as this relates to: (1) the potentially chronic nature of work-related insecurity due to the absence of specific provisions associated with long-term career, income and work-life balance security; and (2) the potential volatility of work-related insecurity due to the loss or gain of specific security provisions (e.g., merit-based pay systems can produce losses or gains in wage security in a particular year and can also affect the frequency and amount of pay raises). Hence, the present study investigates how different patterns of exposure to work-related insecurity impact health.

**HYPOTHESES**

This study has two major objectives: (1) to investigate whether workers who lack specific security provisions associated with the traditional standard in employment have worse health outcomes relative to their counterparts who are granted these provisions; and (2) to investigate whether changes in exposure to work-related insecurity (i.e., due to gains or losses in security provisions) are systematically related to changes in self-rated health. Specific hypotheses are as follows:

**Hypothesis 1.** Longer durations of exposure to work-related insecurity (measured in years) will be predictive of lower levels of self-rated health.

**Hypothesis 2.** Changes in level of exposure to work-related insecurity will be inversely related to changes in level of self-rated health. Of particular interest is whether increases in work-related insecurity are predictive of health declines.
METHOD

Data

Data for the present study were drawn from the Canadian Survey of Labour and Income Dynamics (SLID), a nationally representative longitudinal labor-market survey. The sample frame for the SLID is individuals aged 16 and older who reside in one of the ten Canadian provinces. The SLID is composed of six-year overlapping panels. The first panel began in 1993, a second in 1996, and a third in 1999. The present study draws from the second panel of SLID, which spans the period from 1996 to 2001. In 1996, the response rate for the second panel was 89.8 percent, decreasing slightly to 79.9 percent by the final wave. I note that because two of the major research variables in this study rely on information from the prior wave of data collection, the analyses have been restricted to the period from 1997 to 2001 (this issue is discussed in greater detail in the measures section).

Each panel comprises approximately 15,000 households. Information is collected annually from all household members with one individual selected for a more in-depth labor and income interview. For this individual, detailed information is collected on the characteristics of up to six jobs annually. One of the jobs is identified as the individual’s “main job,” based on the greatest number of hours, or highest earnings in the reference year. Individuals are also asked to provide socio-demographic information, income sources and amounts, and information on their health at the time of the survey.

Because this study investigates the health consequences of insecure employment experiences for individuals who work under contracts that are nominally secure (i.e., “post-standard” employment), a subsample of respondents was selected according to specific criteria at baseline. First, individuals were employed in full-time permanent jobs for the duration of the panel. Also, in an attempt to capture individuals with close ties to their career and/or employer I included only respondents who were not full-time students, were aged 25–54, and who had not held any jobs ancillary to their main job during the observation period. Finally, due to the job enhancements typically associated with management-level positions (e.g., better job security, more generous wages and benefits) it was reasoned that managers might have distinct employment experiences that would warrant separate analyses. Hence, respondents who classified their jobs as managerial in year-1 of the panel were excluded from the sample; however, because the opportunity for career advancement represents a key aspect of
work-related security, employees who were promoted to management during the panel period were included in the analysis.

A final inclusion/exclusion criterion was the selection of individuals who reported good, very good or excellent health in year 1. This “healthy cohort” criterion was used to control for reverse causality, the process whereby unhealthy individuals are selected into insecure employment conditions. The final sample comprised 2,491 individuals.

**Measures**

Self-reports of general health are collected annually in SLID. Self-reported health consists of a single item that is scored on a five-point Likert scale ranging from excellent to poor (1–5, respectively). It is considered a valid and reliable measure of acute and chronic conditions, physical functioning, and to a lesser extent health behaviors and mental health problems (Cott, Gignac, & Badley, 1999; Krause & Jay, 1994).

Six measures of work-related insecurity were constructed using information from the main job: earnings insecurity, job mobility insecurity, earnings mobility insecurity, pension coverage insecurity, union protection insecurity, and work-life balance insecurity. Individuals were categorized as earnings insecure if their hourly wage rate fell below Statistic’s Canada’s “average industrial wage” in the reference year (yes=1; no=0). The average industrial wage is calculated annually as the mean individual earnings across all sectors of the Canadian economy. For the years 1997 through 2001 the average industrial wage rates for full-time permanent employees were as follows: $15.95, $16.21, $16.66, $17.23, and $17.80 (Statistics Canada, 2004a). Earnings mobility insecurity was measured using annual inflation-adjusted earnings information, to determine whether an individual had received a real wage increase in the reference year. To calculate the thresholds, individual earnings information was standardized to 1996 dollars using inflation adjustments provided by the Canadian Consumer Price Index (CPI). Respondents whose current wages did not exceed those of the prior year by an amount greater than that given by annual inflation received a code of 1 for earnings mobility insecurity, and 0 otherwise. Workers were considered exposed to job mobility insecurity in two circumstances: they did not receive a job promotion; or they were demoted during the observation period. Information on job promotions/demotions was based on two survey items that asked respondents whether their job currently involved supervisory or management responsibilities. Job grades, ranging from the lowest
to the highest, were defined as follows: no supervisory or managerial responsibilities, supervisory responsibilities, and managerial responsibilities. Respondents who indicated either no change or a negative change in job grade were coded 1 for job mobility insecurity and 0 otherwise. Pension coverage insecurity was measured by a single item that asked respondents whether their job provided a pension plan (no pension = 1; pension = 0). Respondents were classified as exposed to union protection insecurity if their job was not covered by a union or collective agreement (yes = 1; no = 0). Lastly, respondents were considered exposed to work-life balance insecurity if the number of unpaid overtime hours reported in the reference year exceeded the average for the sample (yes = 1; no = 0).

Three additional variables were included in the model due to their potential role as confounders in the relationship between work-related insecurity and health. Gender was measured using female as the reference category (yes = 1; no = 0). Age bracket was constructed as a dichotomous variable indicating younger or older age status. In accordance with the definition of "older worker" found in the literature (Human Resources and Skills Development Canada, 2005) individuals greater than 45 years of age were considered the older age bracket and used as the reference category (yes = 1; no = 0). An educational attainment measure indicated the level of education achieved by individuals (high school or less = 1; greater than high school = 0).

Analysis

This study investigates the dynamic relationship between work-related insecurity exposures and workers’ health trajectories. A multilevel growth curve model allows for an evaluation of how inter-individual differences in level of exposure to work-related insecurity are systematically related to health change over time. The major distinguishing feature of the multilevel growth model is that random source variance is estimable (i.e., variance that is typically attributed to within-subject error). The random-effects model assumes natural heterogeneity across individuals in their regression coefficients both with respect to time-specific variation and other time-varying covariates (for example work-related insecurity exposures). This heterogeneity is represented by a probability distribution that provides estimates of the magnitude of effects (Diggle, Heagerty, Liang, & Zeger, 2002). The linear multilevel model can be written as:

\[ Y = X\beta + Zu + \Sigma \]  

(1)
where $Y$ is the observed data vector, $X$ is a known design matrix, $\beta$ is a vector of unknown fixed effects, $Z$ is a known random-effects design matrix, $u$ is a vector of unknown random (i.e., individual-level) effects, and $\Sigma$ is a vector of unobserved random errors (Diggle et al., 2002). The model decomposes into two equations at Level 1 and at Level 2 representing change within and between individuals, respectively.

**Level 1: Within-Person Model**

The first step in constructing the multilevel growth model is to specify the growth trajectory for intra-individual change. Change refers to the underlying growth for an individual as a function of time and a set of growth parameters that define the change function (Collins & Sayer, 2000). This study uses a linear function to describe change in individual health across time following the precedence of previous research that indicates that self-rated health behaves as a latent continuous variable that is normally distributed (Crossley & Kennedy, 2000; McDonough & Berglund, 2003; Wagstaff & Van Doorslaer, 1994). Diagnostic tests to confirm the tenability of the linear assumption were also performed (results available upon request). In its generic format, using a single substantive predictor to represent the effects of work-related insecurity, the Level 1 within-person model used is as follows:

$$Y_{ij} = \beta_{0i} + \beta_{1i}T_{ij} + \beta_{2i}WRI_{ij} + e_{ij} \quad (2)$$

where $i$ is the index for persons, $j$ is the index for occasions, $T$ is an interval measure of time (years in this study), and $WRI$ denotes the six work-related insecurity variables that vary over time for at least some of the respondents. The parameters are interpreted in the following manner: $Y_{ij}$ is the level of self-rated health for individual $i$ measured at time $j$; $\beta_{0i}$ is the intercept (1997 value) of the health trajectory for person $i$; $\beta_{1i}$ is the slope of the health trajectory for person $i$; $T_{ij}$ is time at the $j$th measurement for subject $i$, defined herein as the period in years since 1997 when self-rated health is first assessed (time $1=0$); and, $e_{ij}$ is the time-specific residual (comprising error in both prediction and measurement) for each within-person regression of health on time. Against the backdrop of the basic time trend for each individual, self-rated health also varies as a function of exposure to work-related insecurity (which may increase or decrease at a given point in time for some employees) with $\beta_{2i}$ capturing the magnitude of this relationship.
Level 2: Between-Persons Model
In multilevel growth analysis the parameters from the Level 1 within-person model serve as dependent variables for the between-persons model resulting in a separate equation for each parameter:

\[ \beta_{0i} = \gamma_{00} + u_{0i} \]  
\[ \beta_{1i} = \gamma_{10} + u_{1i} \]  
\[ \beta_{2i} = \gamma_{20} \]

The Level 2 equations describe the inter-individual differences in growth trajectories. The \( \gamma \) parameters reflect the average level of the corresponding within-person parameters. Eqs. (3) and (4) show that the Level 2 model decomposes the individual intercept and slope values for self-rated health (\( \beta_{0i} \) and \( \beta_{1i} \)) into the mean values of the parameters across all individuals (represented as \( \gamma_{00} \) and \( \gamma_{10} \)) plus individual deviations from the mean values (i.e., the random components, \( u_{0i} \) and \( u_{1i} \)). The term \( u_{0i} \) denotes random variation across individuals in average self-rated health in 1997 (the intercept) and \( u_{1i} \) represents unexplained variation in the rate of change in self-rated health over the trajectory period. Eq. (5) captures the effects of differences between individuals in average exposure to work-related insecurity (expressed as \( \gamma_{20} \)). Unlike its counterparts, Eq. (5) does not contain an error term. Early attempts at specifying the work-related insecurity variables as Level 1 random effects led to problems with model convergence. Following the precedence of previous research encountering this issue (McDonough & Berglund, 2003), \( \beta_{2i} \) was fixed at the average value for the sample and the random effect of subjects on the change slope (\( u_{2i} \)) was constrained to zero.

Within-Person Change
The estimate of the impact on health of exposure to work-related insecurity (\( \gamma_{20} \) in Eq. (5)) represents the combined effects of: (1) differences between individuals in average exposure; and, (2) within-person change over time in exposure (Barnett, Raudenbush, Brennan, & Pleck, 1995; Bryk & Raudenbush, 1992; Horney, Osgoode, & Marshall, 1995). To address the research hypotheses, however, we require separate estimates of the effect of total exposure to work-related insecurity, and the effect of change in level of exposure. To obtain separate estimates of the effects, two modifications of the preceding equations were required. First, the values for WRI in Eq. (2) are transformed into deviations from each individual’s mean exposure.
(WRImi) calculated for the five-year observation period:

\[ \text{WRIm}_{ij} = \text{WRIm}_{ij} - \text{WRIm} \]

(6)

The WRIm_{ij} parameter represents the effect of change in exposure to work-related insecurity relative to an individuals’ total exposure averaged over five years. Second, the individual means for exposure to work-related insecurity (WRIm) are included as explanatory variables in Eq. (3) to represent the effect of overall differences in exposure on self-rated health over time:

\[ \beta_{0i} = \gamma_{00} + \gamma_{01} \text{WRIm} + u_{0i} \]

(7)

Each of the time-varying work-related insecurity variables have now been transformed into two estimable components: (1) the individual’s mean level of exposure to the predictor averaged over five time points (average exposure); and, (2) the deviation of the individual’s value on that variable, at a given time point, from the individual’s overall mean (within-person change). For example, measures for a specific work-related insecurity variable for a respondent observed over five years with values of 1, 0, 1, 1, and 0 would be transformed into two variables: (1) WRIm with a constant value of 0.6 for that person (the stable component); and, (2) WRIm \_ which would take on values of 0.4, –0.6, 0.4, 0.4, and –0.6 at each of the five time points (the change component). Using this formulation \( \gamma_{01} \) represents the effects of between-persons differences in average exposures to work-related insecurity. This gives us a sense of the cumulative effects of work-related insecurity and its potential to act as a chronic occupational stressor. On the other hand, \( \gamma_{20} \) (from Eq. (5)) satisfies the need for an estimator that captures the effects of within-person change (Horney et al., 1995). For example, it is expected that the loss of a security provision in a given year would function to depress self-rated health in the same year.

Maximizing the efficiency of the estimation requires construction of a final reduced-form equation by substituting the Level 2 equations into the Level 1 equation as follows:

\[ Y_{ij} = (\gamma_{00} + \gamma_{10} T_{ij} + \gamma_{20} \text{WRIm}) + (u_{0i} + u_{1i} T_{ij} + e_{ij}) \]

(8)

Eq. (8) highlights the composite error term, which resolves the problems of autocorrelation and heteroskedasticity arising from multiple measures of Y for each respondent (Horney et al., 1995; Singer & Willett, 2003; Wolfinger, 1992). Statistical tests of \( u_{0i} \) and \( u_{1i} \) indicate whether the individual intercepts and slopes of self-rated health vary significantly around the mean.
values and the need to add inter-individual predictors (e.g., the work-related insecurity variables) to account for these differences (Diggle et al., 2002).

Following is the specification of the full model:

Level 1 model:

\[ Y_{ij} = \beta_{0i} + \beta_{1i}(\text{time}) + \beta_{2i}(\text{earnings insecurity}) + \beta_{3i}(\text{job mobility insecurity}) + \beta_{4i}(\text{earnings mobility insecurity}) + \beta_{5i}(\text{pension coverage insecurity}) + \beta_{6i}(\text{union protection insecurity}) + \beta_{7i}(\text{work-life balance insecurity}) + e_{ij} \]

Level 2 model:

\[ \beta_{0i} = \gamma_{00} + \gamma_{01}(\text{female}) + \gamma_{02}(\text{aged 45–54 in 1996}) + \gamma_{03}(\text{high school education or less in 1996}) + \gamma_{04}(\text{earnings insecurity average}) + \gamma_{05}(\text{job mobility insecurity average}) + \gamma_{06}(\text{earnings mobility insecurity average}) + \gamma_{07}(\text{pension coverage insecurity average}) + \gamma_{08}(\text{union protection insecurity average}) + \gamma_{09}(\text{work-life balance insecurity average}) + u_{0i} \]

\[ \beta_{1i} = \gamma_{10} + \gamma_{11}(\text{female}) + \gamma_{12}(\text{aged 45–54 in 1996}) + \gamma_{13}(\text{high school education or less in 1996}) + u_{1i} \]

\[ \beta_{2i} = \gamma_{20}(\text{earnings insecurity change}) \]

\[ \beta_{3i} = \gamma_{30}(\text{job mobility change}) \]

\[ \beta_{4i} = \gamma_{40}(\text{earnings mobility change}) \]

\[ \beta_{5i} = \gamma_{50}(\text{pension coverage insecurity change}) \]

\[ \beta_{6i} = \gamma_{60}(\text{union protection insecurity change}) \]

\[ \beta_{7i} = \gamma_{70}(\text{work-life balance insecurity change}) \]

A major advantage of a longitudinal approach to the data is that it minimizes the possibility of reverse causality. In this study, two specific countermeasures were employed. First, a healthy cohort of individuals (reported good, very good, or excellent health) was selected at baseline. Second, temporal
separation between the explanatory variables and the outcome measure was instituted such that the former preceded the latter (i.e., explanatory variables were taken from time $t-1$ and the outcome variable from time $t$).

Growth curve models were estimated using SAS Proc Mixed V9.1. A REPEAT statement adjusted for both correlation and non-identicalness of the residuals across multiple observations on each person (Singer & Willett, 2003). Tests of different specifications of the error matrix indicated that an autoregressive structure best fit the data (results available upon request). Population weights were applied to all descriptive analyses to adjust for survey non-response and unequal probabilities of selection into the survey. Weights were not applied to the multilevel models due to a lack of specific survey design information that is required for precise variance estimates when using this procedure (Shao, Monette, McDonough, & Strohschein, 2004).

RESULTS

Table 1 presents an overview of the socio-demographic characteristics of the employee sample in 1996. A majority (60.8 percent) of the sample was male, and most individuals were aged between 35 and 44 years (41.1 percent). The mean age for the sample was 39.5 years (s.d. = 7.4). Most employees (65.2 percent) had completed some level of post-secondary education.

<table>
<thead>
<tr>
<th></th>
<th>Percent</th>
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<tbody>
<tr>
<td>Gender</td>
<td></td>
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<tr>
<td>Men</td>
<td>60.8</td>
</tr>
<tr>
<td>Women</td>
<td>39.2</td>
</tr>
<tr>
<td>Age (years)</td>
<td></td>
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<tr>
<td>25–34</td>
<td>29.7</td>
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<tr>
<td>35–44</td>
<td>41.1</td>
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<td>45–54</td>
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<tr>
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</tr>
<tr>
<td>Some post-secondary</td>
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<tr>
<td>Post-secondary diploma/degree</td>
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<tr>
<td>Total N</td>
<td>2,491</td>
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</table>

*Weighted percentages.
Table 2 presents five-year averages for exposure to each dimension of work-related insecurity (i.e., “exposure means”) and the proportion of individuals who experience stability or change in level of exposure. Employees reported the longest average exposures to job mobility insecurity (4.11 years), followed by earnings mobility insecurity (2.56 years), union protection insecurity (2.34 years), earnings insecurity (1.75 years), and pension coverage insecurity (1.31 years). Respondents were least exposed to work-life balance insecurity during the five-year observation period: 0.10 years or roughly 37 days (0.10 × 365). A large proportion of respondents were never exposed to work-life balance insecurity, pension coverage insecurity, earnings insecurity, or union protection insecurity. In contrast, more than half (58.6 percent) experienced ongoing exposure to job mobility insecurity. Also, a considerable proportion of respondents consistently lacked protection from a union or was always exposed to earnings insecurity. Few respondents reported ongoing pension coverage insecurity or earnings mobility insecurity, and none were consistently exposed to work-life balance insecurity. Bidirectional change in level of exposure to insecurity (due to experiencing both a gain and a loss of a specific security

<table>
<thead>
<tr>
<th></th>
<th>Earnings Insecurity</th>
<th>Job Mobility Insecurity</th>
<th>Earnings Mobility Insecurity</th>
<th>Pension Coverage Insecurity</th>
<th>Union Protection Insecurity</th>
<th>Work-Family Balance Insecurity</th>
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<tr>
<td>Exposure means</td>
<td>1.75</td>
<td>4.11</td>
<td>2.56</td>
<td>1.31</td>
<td>2.34</td>
<td>0.10</td>
</tr>
<tr>
<td>(years)</td>
<td>(2.12)</td>
<td>(1.35)</td>
<td>(0.99)</td>
<td>(1.90)</td>
<td>(2.35)</td>
<td>(0.37)</td>
</tr>
<tr>
<td>Change proportions</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Always exposed</td>
<td>23.3</td>
<td>58.6</td>
<td>1.4</td>
<td>14.8</td>
<td>38.3</td>
<td>0.0</td>
</tr>
<tr>
<td>Never exposed</td>
<td>52.3</td>
<td>3.1</td>
<td>1.7</td>
<td>60.0</td>
<td>46.8</td>
<td>92.4</td>
</tr>
<tr>
<td>Increase in exposure</td>
<td>5.3</td>
<td>10.5</td>
<td>5.5</td>
<td>3.6</td>
<td>2.3</td>
<td>1.3</td>
</tr>
<tr>
<td>Decrease in exposure</td>
<td>2.5</td>
<td>1.8</td>
<td>6.2</td>
<td>3.0</td>
<td>2.0</td>
<td>0.6</td>
</tr>
<tr>
<td>Both increase and</td>
<td>16.7</td>
<td>25.9</td>
<td>85.1</td>
<td>18.7</td>
<td>10.7</td>
<td>5.7</td>
</tr>
<tr>
<td>and decrease in</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>exposure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total N</td>
<td>2,491</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Weighted means and percentages (standard deviations in parentheses).
provision) was more common than a one-way increase or decrease in exposure. A substantial proportion of respondents reported fluctuations in earnings mobility insecurity and job mobility insecurity indicating uneven income and career trajectories. Fewer respondents experienced bidirectional change in pension coverage, earnings-levels, union coverage, or work-life balance insecurity.

Table 3 presents results from the unconditional growth curve model which includes TIME as the only substantive predictor. The major purpose of fitting this model is to find out whether there is significant inter-individual variation in rates of change in self-rated health. The fixed effects, \( \gamma_0 \) and \( \gamma_1 \), estimate the starting point (4.10) and slope (–0.07) of the population average change trajectory. This means that for the average employee self-rated health declines steadily between 1997 and 2001, from 4.10 to 3.82. The addition of a quadratic term for time did not significantly improve model fit (\( \chi^2(2) = 0.001, p = 0.79; \chi^2(1) = 0.10, p = 0.75 \)), hence the linear model specifying a constant rate of change in self-rated health over time was retained in subsequent analyses. Inspection of the Level 2 variance components \( s_0^2 \) and \( s_1^2 \) shows that there is statistically significant variation in employees’ initial health status and rate of health change that additional Level 2 predictors could explain. These variance components – \( s_0^2 = 0.23 \)
and $\sigma^2 = 0.01$ – act as benchmarks against which we are able to quantify the predictors’ effects (Singer & Willett, 2003).

Table 4 gives results for the conditional growth model including substantive predictors for work-related insecurity and the control variables. The coefficients quantify the effect of work-related insecurity on individuals’ self-rated health trajectories. There are two types of effects depicted in the model. First, estimates for the average exposure variables denote between-employee differences in mean self-rated health due to differences in the total number of years exposed to work-related insecurity. Second, the estimates for change denote the average effect on health status of within-employee change in exposure to work-related insecurity in a given year net of the underlying health trajectory. An increase in insecurity (indicating the loss of a specific security provision) is expected to produce a negative deviation from the individual’s basic health trajectory.

Starting with the control variables, the findings show that both age bracket and level of education are predictive of health differences among employees. Older individuals reported significantly lower health in 1997 relative to their younger counterparts ($\gamma_{02} = -0.08, p=0.01$). Also, consistent with other data on the health advantage provided by education (see for example Lynch (2003)), individuals with low education experienced more rapid declines in self-rated health over time compared to individuals with higher education ($\gamma_{13} = -0.02, p=0.05$). In accordance with Hypothesis 1, we find some significant associations between total average exposure to work-related insecurity and mean self-rated health, though the results are not always in the expected direction. Longer exposure to earnings mobility insecurity depressed self-rated health; expressed in terms of the standard deviation of the outcome (s.d. = 0.74 in 1997), for each additional year of exposure to earnings mobility insecurity self-rated health declined by 16 percent ($[-0.12/0.74] \times 100$). Average earnings insecurity also had a significant adverse effect on self-rated health, which declined an average of 14 percent per year of exposure ($[-0.10/0.74] \times 100$). The effect of work-life balance insecurity is particularly striking with each year of exposure lowering self-rated health by almost a full standard deviation ($[-0.71/0.74] = -0.96 \times 100$). In contrast, longer exposure to union protection insecurity had a protective effect on employees’ health – i.e., the lack of union coverage is associated with better health status on average ($\gamma_{08} = 0.10, p=0.001$). Similar findings have been reported elsewhere (Tompa, Scott, & Dolinschi, 2004) and may be linked to differences in perceptions of self-rated health between unionized and non-unionized employees. For instance, unions tend to encourage workers to be vigilant in attending to issues of
Table 4. Estimated Fixed and Random Effects of Work-Related Insecurity Variables on Self-Rated Health, 1997–2001 ($N = 2,491$).

**Fixed Effect**

<table>
<thead>
<tr>
<th>For Initial Status, $\beta_{0i}$</th>
<th>Intercept, $\gamma_{00}$</th>
<th>4.199 (0.051)**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Female, $\gamma_{01}$</td>
<td>0.029 (0.027)</td>
<td></td>
</tr>
<tr>
<td>Older, $\gamma_{02}$</td>
<td>-0.080 (0.029)**</td>
<td></td>
</tr>
<tr>
<td>High school or less, $\gamma_{03}$</td>
<td>-0.031 (0.029)</td>
<td></td>
</tr>
<tr>
<td>Earnings insecurity average, $\gamma_{04}$</td>
<td>-0.100 (0.031)**</td>
<td></td>
</tr>
<tr>
<td>Job mobility insecurity average, $\gamma_{05}$</td>
<td>0.002 (0.046)</td>
<td></td>
</tr>
<tr>
<td>Earnings mobility insecurity average, $\gamma_{06}$</td>
<td>-0.119 (0.058)*</td>
<td></td>
</tr>
<tr>
<td>Pension coverage insecurity average, $\gamma_{07}$</td>
<td>-0.067 (0.037)</td>
<td></td>
</tr>
<tr>
<td>Union protection insecurity average, $\gamma_{08}$</td>
<td>0.100 (0.029)**</td>
<td></td>
</tr>
<tr>
<td>Work-family balance insecurity average, $\gamma_{09}$</td>
<td>-0.708 (0.145)**</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>For Linear Change, $\beta_{1i}$</th>
<th>Intercept, $\gamma_{10}$</th>
<th>-0.061 (0.007)**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Female, $\gamma_{11}$</td>
<td>0.007 (0.009)</td>
<td></td>
</tr>
<tr>
<td>Older, $\gamma_{12}$</td>
<td>-0.015 (0.010)</td>
<td></td>
</tr>
<tr>
<td>High school or less, $\gamma_{13}$</td>
<td>-0.021 (0.009)*</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>For Change in Average Earnings Insecurity, $\beta_{2i}$</th>
<th>Intercept, $\gamma_{20}$</th>
<th>0.009 (0.027)</th>
</tr>
</thead>
<tbody>
<tr>
<td>For Change in Average Job Mobility Insecurity, $\beta_{3i}$</td>
<td>Intercept, $\gamma_{30}$</td>
<td>0.029 (0.021)</td>
</tr>
<tr>
<td>For Change in Average Earnings Mobility Insecurity, $\beta_{4i}$</td>
<td>Intercept, $\gamma_{40}$</td>
<td>-0.021 (0.012)</td>
</tr>
<tr>
<td>For Change in Average Pension Coverage Insecurity, $\beta_{5i}$</td>
<td>Intercept, $\gamma_{50}$</td>
<td>0.025 (0.027)</td>
</tr>
<tr>
<td>For Change in Average Union Protection Insecurity, $\beta_{6i}$</td>
<td>Intercept, $\gamma_{60}$</td>
<td>0.024 (0.036)</td>
</tr>
<tr>
<td>For Change in Average Work-Family Balance Insecurity, $\beta_{7i}$</td>
<td>Intercept, $\gamma_{70}$</td>
<td>-0.121 (0.046)**</td>
</tr>
</tbody>
</table>

**Random Effect**

| UN(1,1) | Time-specific residual variance 1997 | 0.311 (0.013)**  |
| UN(2,2) | Time-specific residual variance 1998 | 0.402 (0.013)**  |
| UN(3,3) | Time-specific residual variance 1999 | 0.399 (0.013)**  |
| UN(4,4) | Time-specific residual variance 2000 | 0.370 (0.013)**  |
| UN(5,5) | Time-specific residual variance 2001 | 0.349 (0.016)**  |
| Initial Status, $\sigma_{0i}^2$ | 0.224 (0.013)**       |
| Linear Change, $\sigma_{1i}^2$ | 0.013 (0.002)**      |

**Goodness-of-Fit**

| Deviance | 27,371.1 |
| AIC      | 27,387.1 |

**Note:** Numbers in parentheses are standard errors.

*p < 0.05  
**p < 0.01  
***p < 0.001
personal security, health and well-being such that these individuals may be more inclined to perceive health problems. Moreover, the job protection provided to unionized workers could be associated with greater recognition and reporting of health complaints compared to workers who lack such protection.

Only one of the variables for within-individual change was significantly related to self-rated health status, namely change in exposure to work-life balance insecurity. Specifically, an increase in this variable in a given year produces 16 percent decline in self-rated health \((-0.12/0.74 \times 100)\).

The utility of the overall statistical model can be evaluated by calculating the total amount of between-individual variation in self-rated health trajectories that is explained by the Level 2 predictors. This requires that we quantify the proportional reduction in Level 2 residual variance \((\sigma_0^2 \text{ and } \sigma_1^2)\) on the addition of predictors to the model. In multiple regression the proportion of the outcome variation that is explained by the predictors in the model is expressed using the \(R^2\) (or adjusted \(R^2\)) statistic. However, because in the multilevel growth model the total outcome variation is partitioned into different variance components statisticians use the pseudo-\(R^2\) statistic (Singer & Willett, 2003). A linear change model with two Level 2 variance components, \(\sigma_0^2\) and \(\sigma_1^2\), has two pseudo-\(R^2\) statistics. Baseline estimates of these components come from the unconditional growth model (Singer & Willett, 2003). For any subsequent model the pseudo-\(R^2\) statistic is calculated as follows:

\[
Pseudo - R^2 = \frac{\sigma^2(\text{unconditional growth model}) - \sigma^2(\text{subsequent model})}{\sigma^2(\text{unconditional growth model})}
\]

To determine the amount of additional variation in initial health status and rate of health change that is explained by the Level 2 predictors, we compare the Level 2 variance components of the unconditional growth model (Table 3) to those of the fully specified model (Table 4). A comparison of \(\sigma_0^2\) in these models indicates that the Level 2 predictors accounted for roughly 4 percent of the variance in employee health in 1997: \((0.23-0.22)/0.23 \times 100\). A comparison of \(\sigma_1^2\), on the other hand, shows that the predictors did not account for any additional variance in the rate of health change.

**DISCUSSION**

This study employed a political economy perspective to reconceptualize work-related insecurity in a manner that accounts for shifts in the social/power
relations of work since the postwar period. Standard socio-epidemiological models of job insecurity center on the micro-level dynamics of power arising from the perceived threat of job loss. As such, these models fail to account for the structural “first causes” that give rise to the experience and neglect several other employment experiences in the contemporary labor market that can give rise to insecurity and strain. By contrast, a political economy approach foregrounds contingencies in the economic, regulatory, and social environment that have contributed to declines in employment and income security throughout the labor market. In particular, by showing how macroeconomic developments influence the relative presence of institutions that vest workers with leverage against the interests of employers, the political economy of work-related insecurity reveals the phenomenon as a social determinant of health that is linked with the distribution of labor market power. In turn, work-related insecurity is presented as an enduring feature of class relations, though one that is magnified or modified according to conditions in the socio-economic environment. At present, the erosion of key postwar institutions (the paternalistic firm, the welfare state, and strong labor unions) foregrounds workers’ basic inability to exercise control over the terms, conditions, and outcomes of labor market exchanges. This is evinced most directly by the dismantling of workplace structures that were established to protect and augment the stability of the employment relationship. For workers, the net effect of the current changes to work organization is more diffuse career and earnings trajectories and an overall increase in the level of uncertainty surrounding long-term financial and life planning. Hence, a political economy lens reveals how the contingencies of globalized capitalism, including an ideological climate that reinforces employer dominance while holding the structural contingencies of the New Economy in place, have produced shifts in the social relations of production and constituted work-related insecurity as a chronic occupational stressor embedded in the new organization of work. Perhaps the starkest example of this development is the rise of post-standard employment, which denotes work arrangements that are nominally secure though can give rise to various forms of career, income, and work-life balance insecurity. The antithesis of the postwar standard in employment security, post-standard work sheds light on the full extent of the impact of labor market restructuring on work and work relations.

Findings from this study indicate that specific aspects of post-standard employment can represent chronic sources of strain with significant consequences for health. Specifically, there was some support for Hypothesis 1 which postulated that longer periods of exposure to work-related insecurity
would be predictive of poorer health outcomes. Results from the multilevel analysis show that greater exposure to earnings insecurity, earnings mobility insecurity, and work-life balance insecurity (i.e., substantial unpaid overtime hours) are associated with lower levels of self-rated health. The finding that longer exposure to a lack of union protection is predictive of better health ran contrary to Hypothesis 1, though could be explained by differences in the detection and reporting of health problems between unionized and non-unionized employees.

Support for Hypothesis 2, that changes in level of exposure to work-related insecurity will be inversely related to changes in level of self-rated health, was less definitive; the findings indicate that only increases in work-life balance insecurity are predictive of health declines. This finding is consistent with other studies that report the negative health impact of work intensification, long work hours, and increased work-life conflict (Akerstedt et al., 2002; Duxbury & Higgins, 2003; Nolan, 2002). It also underscores that the market-mediated employment relationship can be a key source of work-related strain, particularly with respect to the growing pressure on employees to work more than their contracted hours. In a context of the steady upward trend in work hours that is occurring throughout the industrialized world (Campbell, 2001; Organization for Economic Co-operation and Development, 1998) issues related to work intensification and work-to-family interference will likely be of increasing importance to occupational health research over the next decade.

The strengths of this study’s method lend credibility to the findings. The length of the panel and the detailed nature of inquiry into labor market experiences provided a rich source of information for addressing the research questions. Moreover, the use of multiple methods to control for reverse causality provides greater confidence that the results are not attributable to the selection of unhealthy individuals into work-related insecurity experiences. In particular, the temporal separation of the explanatory variables from the outcome measures in the analyses represents a substantial improvement over other studies that rely on cross-sectional data.

There are three main limitations of this study that may explain the modest evidence found in support of the hypotheses as well as the limited explanatory power of the overall model. One limiting factor is that the measures of work-related insecurity lacked information on individuals’ perceptions of their employment experiences. For instance, some individuals with low wages may not consider themselves exposed to earnings insecurity if they have an alternative source of financial support; others who have limited job mobility prospects may be satisfied with their current level of
responsibility at work. An alternative perspective on the issue, and a major criticism of the literature on stress, is that this literature focuses primarily on subjective measures of stress (Muntaner, 2004) as opposed to labor market position or work circumstances. Furthermore, the concepts of voluntariness and choice in the context of employment arrangements have been questioned by some researchers (Vosko & Zukewich, 2006). Hence, future research on work-related insecurity should consider structural indicators of the phenomenon alongside measures of individuals’ perceptions of their work circumstances. Such an approach provides a fuller picture of the “person-in-context” nature of work experiences – i.e., how the impact of stimuli arising from the conditions of work or an employment experience varies depending on contextual factors (Tompa, Scott-Marshall, Dolinschi, Trevithick, & Bhattacharyya, forthcoming).

A second limiting factor is that the database used for this study lacks measures of mental health and well-being, such as depression, self-esteem, and job satisfaction. These measures have been shown to be more highly, or at least more immediately affected by work experiences than physical health (e.g., Bardasi & Francesconi, 2004; Sverke et al., 2002).

A third limitation of the study is that the variables denoting change in exposure to work-related insecurity treat the health impact of gains and losses in security provisions as equivalent events. This is because both increases and decreases in work-related insecurity were constructed as deviations of identical magnitude from the individual exposure means. However, the impact of change in level of insecurity may be quite different depending on its direction. For example, a loss of work-life balance security (i.e., an increase in unpaid work hours) may have a substantially greater impact on health outcomes than gains in this variable (i.e., years in which unpaid work hours are reduced). In future, elaborating the model to accommodate potential differences in the magnitude of the effects of change would provide further insight into how patterns of exposure to work-related insecurity affect health.

Its shortcomings notwithstanding, this study provides evidence that work-related insecurity presents an occupational health risk to individuals employed in work arrangements that are nominally secure. Findings for average duration of exposure to insecurity suggest that a substantial proportion of such workers face uncertain career and income trajectories. Moreover, there is evidence that exposure to work-related insecurity gives rise to adverse health outcomes. Specifically, after controlling for initial health status and other potential confounders the results show that certain types of work-related insecurity have a cumulative adverse effect on self-reported
health trajectories. These findings provide insight into the full impact of labor market restructuring on the health of the Canadian workforce; to date, studies on the health effects of labor market change have focused on more obviously precarious non-standard work arrangements (Bardasi & Francesconi, 2004; Friedland & Price, 2003; Rodriguez, 2002).

More broadly, fading career structures can introduce a substantial degree of uncertainty into individual financial and life planning which can affect the integrity of social institutions like marriage and family (Rubin, 1996). For example, uncertainty about improvements in living standards complicates individuals’ ability to make long-term life plans – e.g., around home ownership, post-secondary education for children, and for financial security in retirement (Osterman et al., 2002; Rubin, 1996). Such difficulties in the face of workplace change could contribute a brand of existential insecurity that may weaken individuals and societies alike. Indeed, some observers claim that assessing the vulnerability of workers is essential to combating the “social deficit” of globalization (Burke & Shields, 1999; Organization for Economic Cooperation and Development, 1997b; Rittich, 2004) and that the current emphasis on improving efficiency through “working more and harder to ensure labour market success, security, even survival” comes at great cost to “workers, their families, the wider social fabric and the future health of the economy” (Rittich, 2004, p. 52).

Popular neo-liberal rhetoric maintains that the old system of regulated labor markets and generous welfare states inhibits economic efficiency and growth (Harvey, 2005; Jackson, 2000; Somers & Block, 2005). Indeed, we observe the hegemonic power of this ideology in the profound shift away from an institutional structure that had privileged security as a means of extracting labor to another that gives priority to insecurity in this context. However, perhaps the most effective way of ameliorating the insecurity and strain that appears so pervasive is to invest in the laws and institutions that regulate and restrict the market economy. Many researchers and policymakers concerned about the transformations occurring in the labor markets of developed countries have called for the development of a regulatory framework that will help to combat the “over-exploitation” of workers and the “bargaining advantage” of employers (Wilkinson & Lapido, 2002). A reading of the history of Western capitalism highlights the importance of the statutory protection of social rights to the health and well-being of workers and their families (Palmer, 1992; Wilkinson & Lapido, 2002). Only with a thorough understanding of the nature and impact of insecure employment experiences can policy-makers develop an effective regulatory response to prevent resurrection of historical labor-market vulnerabilities.
NOTES

1. The term “New Economy” refers to the full effects on the social, economic and political systems of the information and communication technologies revolution – i.e., the post-industrial society (Lipsey, 2001; Statistics Canada, 2005).
2. Canada’s IRDIA was modeled on American legislation known as the National Labor Relations Act (NLRA). Implemented in 1935, the main purpose of the NRLA as stipulated by Congress was to secure “the equality of bargaining power between employers and employees” (Brand, 1995, p. 383).

ACKNOWLEDGMENTS

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NEOLIBERALISM AND SOCIAL IMBALANCE: HIGHER EDUCATION IN MISSOURI

John B. Harms

ABSTRACT

This manuscript examines neoliberalism as both an ideological system and economic policy shift that emerged as a response to the economic problems of the early 1970s. Galbraith’s idea of social balance and his broader analysis of the changing structure of the economy brought on by the increasing market power of big corporations are contrasted with neoliberalism to illuminate how neoliberalism creates social imbalance between the production of private and public goods. An analysis of higher education policy in Missouri is presented to illuminate the specific dynamics of how neoliberalism creates social imbalance. The major finding is that neoliberalism is primarily a strategy for consolidating private economic power, and not a policy for economic prosperity in the public interest.

INTRODUCTION

In 2004, The Chronicle of Higher Education published the results of a national survey on colleges and universities. According to the survey,
93 percent of Americans agreed or strongly agreed that “colleges and universities are among the most valuable resources to the U.S.” Moreover, 94 percent answered yes to the question: “Do you think every high-school student who wants a four year college degree should have the opportunity to earn one” (Selingo, 2004, p. A1). Clearly, Americans believe in higher education and the U.S. has a long tradition of treating higher education as a public good. Jefferson was instrumental in framing education as a public good, arguing that generally available education would have an equalizing role and promote democracy. In 1785, the founding of the University of Georgia marked the nation’s first state supported institution of higher education. The Morrill Acts\(^1\) of 1862 and 1890 continued the trend towards public higher education by establishing land grant institutions. The GI Bill in the 1940s, the establishment of community colleges in the 1950s, the passage of the Higher Education Act\(^2\) in the 1960s, and the creation of Pell Grants\(^3\) in the 1970s, are further evidence of the development of public higher education in the U.S.

During the neoliberal era of the last quarter century, however, public financial support for higher education has declined. Nationally, public educational appropriations per full time equivalent (FTE) student are at their lowest level ($5,825) in the past 25 years (State Higher Education Executive Officers, 2006, pp. 5–6). As a result, colleges and universities have increased tuition and fees. Nationally, net tuition as a percentage of public higher education total revenues has increased from 21.5 percent in fiscal year (FY)1981 to 36.7 percent in FY2005 (State Higher Education Executive Officers, 2006, p. 6), and tuition and fees have increased 375 percent since 1982 (Measuring Up, 2006a, p. 19). In short, under neoliberal policies, higher education is being transformed from a public to a private good. As a result, students and their families are paying more, and government is paying less.

In this paper I examine higher education in Missouri to illustrate how neoliberalism generates social imbalance and an inadequate provision of public goods and services like education. I first analyze neoliberalism’s market fundamentalism and the public policies associated with it. I then examine how one of neoliberalism’s central policies – changes in tax codes and fiscal policy – impacted higher education in Missouri. I then employ Galbraith’s theory of social balance to identify the four factors causing social imbalance that constitute the infrastructure of neoliberalism. Galbraith’s overall analysis of the modern political economy is presented to provide a critical perspective that reveals neoliberalism and its market fundamentalism to be a disguise for increased private economic power.
NEOLIBERALISM

Neoliberalism is a term used to grasp the regime change in capitalism that began with the crisis of accumulation and profitability of the early 1970s. In the U.S. for example,

In 1965, overall corporate profitability, as measured by the net after-tax rate of return on assets, was a healthy 10 percent. By 1970, it had fallen to 6 percent and by 1974, to about 4.5 percent, less than half of its postwar peak. (Bluestone & Bluestone, 1992, p. 65)

Increasing oil costs, foreign competition, tax bracket creep, rising unemployment and inflation, the demise of Bretton Woods, all contributed to this crisis which was christened stagflation.

Faced with this crisis, economic elites orchestrated a social movement to overthrow the regime of the “Keynesian compromise,” and replace it with a new neoliberal regime.

From World War II to the late 1970s, the decades of the Keynesian compromise, full employment, social welfare protection, and universal access to education and health care had come to be accepted as important features of developed societies. The desire to tackle the challenges of the capitalist order and the fight against communism made development policies urgent necessities. These policies had led to institutional frameworks that were on the margin of the fundamental rules of straight-lace capitalism – more advantageous financing conditions for the nonfinancial economic sector, a high degree of state intervention in industrial policy, and an international monetary framework favorable to development, which placed certain limits on the freedom of decision for the owners of capital. (Dumenil & Levy, 2004, p. 1)

This overthrow involved “moral entrepreneurship” of economic elites or the business community to frame or construct the crisis as a social problem that could be solved by returning to liberal policies that would generate economic prosperity. Following Becker’s analysis of moral entrepreneurs (1963, pp. 120–163), we can see a process involving the factors of “interest,” “enterprise,” and “publicity” at work in the establishment of neoliberalism. The “interest” of economic elites was to restore capital profitability and the revenues they accumulated from it. Their “enterprise” involved harnessing corporate resources to create conservative think tanks like the Heritage Foundation, the Cato Institute, and American Enterprise Institute to promote neoliberal ideas, and to place prominent corporate leaders into positions of political power at the Treasury Department, the Federal Reserve, the President’s Council of Economic Advisors, and the Business Roundtable. This enterprise also involved the mobilization of the National Bureau of Economic Research, and cultivating ties to economic departments...
at universities such as the University of Chicago, to give neoliberal ideas scientific legitimacy. Their “publicity” worked through conservative journals such as *The Public Interest*, and *Commentary*, books published by the think tanks, and academic publications – mostly in economic journals (Hodgson, 1996; Yergin & Stanislaw, 2002; Harvey, 2005).

The moral entrepreneurship of the business community succeeded and neoliberalism has penetrated common sense so that its precepts and policies seem like a natural way to order society (Harvey, 2005, p. 41). In this sense neoliberalism is much more than an economic agenda; it is a hegemonic way of seeing and general philosophy, and it is necessary to identify its distinctive features and how they support the interests of the business community.

Let us examine what is liberal in neoliberalism, and then consider what is neo. First, we must be clear from the start that liberal refers to the philosophy of the late 19th century, and not to those who are on the left and advocate state intervention and social programs to augment market outcomes. This latter signification holds only in the U.S. and is the exact opposite of what classical liberals espouse (see Yergin & Stanislaw, 2002, p. xv, for an explanation of this curious inversion of meaning). Neoliberalism shares with classical liberalism the equation of free markets with individual freedom; *laissez faire*. In this sense neoliberalism embraces “market fundamentalism,” which is the belief that the process of the market mechanism is the best way to order the economy (Treanor, 2005, p. 3; Somers & Block, 2005, pp. 260–261). Grounded in the ideas of Adam Smith’s *The Wealth of Nations*, neoliberals are deeply suspicious of government planning and intervention, which are viewed as threats to individual freedom and “the road to serfdom” (Hayek, 1944). Indeed, market fundamentalism involves a “belief in the moral necessity of market forces in the economy” (Treanor, 2005, p. 4) and that these market forces emerge naturally without any conscious planning. It is important to note the moral element in this position, which functions as a Weberian “ethic of ultimate ends” (Weber, 1958, pp. 120–122); if you let market forces do their work, good ends will inevitably result.

Neoliberalism also shares with liberalism an emphasis on the individual entrepreneur as the prime mover of the economy. It is the entrepreneur who responds to free market forces and risks investing resources to bring innovative processes and products to the market. In Adam Smith’s formulation, the competition between entrepreneurs or undertakers increases the wealth of nations, and without them there could be no economic expansion and creation of additional wealth. Here again we see the connection between individual freedom, freedom of the market, and
economic prosperity that is so central to liberal and neoliberal thinking. In fact, liberalism envisions an individualism where entrepreneurs and the market respond to the demands and preferences of individuals creating consumer sovereignty.

In summary, the business community enlisted the ideas of classical liberalism to explain the economic crises. On the positive side, this meant appealing to the importance of individual freedom and free markets. On the negative side, it meant criticizing the government and state intervention in the economy. As the Reagan administration stated in *America’s New Beginning: A Program for Economic Recovery* (1981, p. 18), “The most important cause of our economic problems has been the government itself”. In constructing this new regime for capitalism, significant modifications of liberal ideas have taken place and justify the signification of neoliberalism. It is time to examine the neo in neoliberalism.

One of the key features of neoliberalism is an extreme faith in markets. We saw in classical liberalism this faith in markets and their moral necessity, but it applied to the regulation of private goods and services. For neoliberals, all of social life should be organized as markets. “The belief in the market, in market forces, has separated from the factual production of goods and services. It has become and end in itself, and this is one reason to speak of neoliberalism and not of liberalism” (Treanor, 2005, p. 6). In short, neoliberalism “holds that the social good will be maximized by maximizing the reach and frequency of market transactions, and it seeks to bring all human action into the domain of the market” (Harvey, 2005, p. 3). For neoliberals, then, it is a moral imperative to commodify everything and create markets for their sale. Thus, health, education, welfare, and pollution, for example, which were not originally produced to be exchanged, have all been transformed into “fictitious commodities” (Polanyi, 2001, pp. 75–76) and regulated by market forces and transactions.

In addition to the neoliberal canonization of the market is its deification of the individual entrepreneur. For classical liberals like Smith, entrepreneurs or undertakers were just one kind of person with a special role to play in the economy. For neoliberals, “every human being is an entrepreneur managing their own life, and should act as such” (Treanor, 2005, p. 10).

This leads to the neoliberal position that individuals, not society, church or state, are responsible for their lives and welfare. Since all of life is a market, individual investment choices determine one’s success and position in society, and for neoliberals this is the way it should be. Neoliberals embrace liberal individualism and are suspect of any institutions or programs that interfere with or replace market mechanisms and the
sovereignty of freely choosing individuals. As Margaret Thatcher once remarked to Women’s Own magazine (October 31, 1987),

I think we’ve been through a period where too many people have been given to understand that if they have a problem, it’s the government’s job to cope with it. ‘I have a problem, I’ll get a grant.’ ‘I’m homeless, the government must house me.’ They’re casting their problem on society. And, you know, there is no such thing as society. There are individual men and women, and there are families. And no government can do anything except through people, and people must look to themselves first. It’s our duty to look after ourselves and then, also to look after our neighbour. People have got the entitlements too much in mind, without the obligations. There’s no such thing as entitlement, unless someone has first met an obligation.

To summarize, economic elites framed the economic crisis of the early 1970s as a result of the “Keynesian compromise” and the idea that government could manage the economy in the public interest. They successfully argued that the crisis was caused by the government and could only be solved by returning to “market fundamentalism” where all dimensions of social life are organized by market principles.

The logic of neoliberal thinking is now clear and its policy decisions are guided by the pivotal idea of limiting and restricting government and returning to market regulation of the economy. Thus deregulation frees businesses from costly rules and promotes economic efficiency, privatization sells off public assets to more efficient private entrepreneurs and commodifies public goods, tax cuts are implemented, especially on capital and for the rich, to free up money for investment and capital formation, and social programs are dismantled to cut inefficient government spending and make individuals more personally responsible. These are the main policy ingredients of the neoliberal recipe for economic prosperity.

HIGHER EDUCATION IN MISSOURI

Following Galbraith’s insight that “investment in education, assessed qualitatively as well as quantitatively, becomes very close to being the basic index of social progress” (Galbraith, 1998, p. 252), we can examine higher education in Missouri and assess the impact of neoliberal policies. According to Grapevine (2006), published at Illinois State University’s College of Education, Missouri’s tax appropriations for higher education declined 10.8 percent or $103.3 million between FY2001 and FY2006, from $959.4 to $856.1 million. Nationally, states averaged an increase of 9.9 percent during this period. In FY2006, Missouri ranked 46th in tax dollars
appropriated for higher education. Looked at from the perspective of appropriations per FTE, the State Higher Education Executive Officers’ State Higher Education Finance report cites a 25.2 percent decline for Missouri between FY2001 and FY2005, while the national average was a 18.2 percent decline (State Higher Education Executive Officers, 2006, p. 30). During this neoliberal era, the percentage of Missouri’s budget that goes to higher education has decreased from 16.8 percent in 1980 to 12 percent in 2007 (Nietzel, 2006, p. 7; see also http://www.missouristate.edu/President/speeches/Report20060920/default.htm). Clearly, relative to most other states, Missouri is providing less public support for public higher education.

While state tax support for higher education declined, The Missouri Budget Project reports that tuition at Missouri’s four year institutions increased 58 percent between FY2001 and FY2006 (Kruckemeyer & Blouin, 2005, p. 2). The result is that in Missouri, net tuition as a percent of total education revenues has risen to 40 percent, while the national average is 36.7 percent (State Higher Education Executive Officers, 2006, p. 31). Overall, the percentage of Missouri college students’ expenses paid by the state fell during the neoliberal era from 81.6 percent in 1980 to 48 percent in 2006 (Zagier, 2006, p. 1B). We see here a clear neoliberal trend of passing the costs of public higher education on to families and students; public education is being privatized and transformed from a public to a private good.

At the same time that families and students are paying an increasing share for their public education, Missouri’s state-funded financial aid is below the national average. In FY2005, Missouri provided $123 for state-funded tuition aid per FTE, or 33 percent of the national average of $374. Need-based aid was $75 per FTE or 27.3 percent of the $275 U.S. average, while non-need–based aid was $48 per FTE or 48.7 percent of the $99 national average (State Higher Education Executive Officers, 2006, pp. 64–65).

To summarize, relative to most other states and national averages, Missouri provides less public support for higher education and financial aid, and requires its students and their families to pay more. As a result, access to public higher education has been compromised, which is reflected in Missouri’s FTE enrollment growth. Between FY2001 and FY2005, FTE enrollment grew a sluggish 7.2 percent, while the national average was 14.4 percent. In this period, Missouri ranked 45th among the states in FTE growth rates (State Higher Education Executive Officers, 2006, p. 29).

It is now necessary to examine how Missouri altered its tax code according to neoliberal principles and created a fiscal environment hostile to funding higher education and providing public goods.
STRUCTURING THE CRISIS IN PUBLIC HIGHER EDUCATION

The source of Missouri’s financial crisis is an imbalance between revenues and spending/appropriations caused by a combination of federal tax policy, and Missouri’s unique Constitution and fiscal policies.

Missouri, like most states, has coupled its tax code to the federal code for reasons of convenience and simplicity. Starting in 1973, Missouri adopted the federal definition of income, and then in 1980, coupled its estate tax to the federal tax (State & Regional Fiscal Studies Unit, 2003, pp. 11–14). What this means practically is that changes in federal tax policy are imported into state tax structures like Missouri’s, and impact state revenues, especially those derived from personal and corporate income taxes, and the estate tax. Missouri’s dismal higher education statistics reported above are thus part of a larger national trend. As Ehrenberg and Rizzo (2004, p. 29) note, during the neoliberal era, “the share of state general funds going to higher education has shrunk by more than one-third over the past twenty-five years.” Part of this trend is explained by changes in federal tax policies that were imported into states and culminated in a “state fiscal crisis” between FY2002 and FY2005 (Lav & Brecher, 2004).

The neoliberal era and regime change started with the election of Ronald Reagan in 1980. Earlier, the Reagan administration’s framing of the economic problem as a governmental problem was discussed. Not surprisingly, one of the first legislative acts for Reagan was the Economic Recovery Tax Act of 1981 (ERTA), which included major tax cuts. The name of this act captures the neoliberal spirit perfectly; the economy will recover when taxes are cut and government stops intruding into the workings of a free market. ERTA reduced marginal tax rates 23 percent over three years, reduced the maximum rate from 70 to 50 percent, and reduced the capital gains rate to 20 percent. It also provided corporations with an “accelerated cost recovery system” (ACRS), which provided generous depreciation allowances for capital expenditures. At the time, the Treasury Department estimated the costs of the individual rate reductions at $162 billion, or 3.7 percent of GDP, and the ACRS at $59 billion, or 1.3 percent of GDP (Steuerle, 2004, p. 82). In FY1990, ERTA’s tax cut cost the government $323 billion or close to 6 percent of GDP (Steuerle, 2004, p. 83).

The history of federal tax policy during the neoliberal era is not a monolithic story of tax cutting. There were tax increases, for example the Omnibus Budget Reconciliation Act of 1990, which imposed numerous excise taxes, increased the top individual tax rate from 28 to 31 percent, and
increased the individual alternative minimum tax rate from 21 to 24 percent. Clinton and the New Democrats even managed to erase the deficits generated during the Reagan and Bush administrations, and created a federal surplus by raising taxes and cutting spending (see Steuerle, 2004, especially pp. 273–287 for a summary of changes in federal tax policy).

The tax cuts implemented by George W. Bush in 2001–2003 accelerated the neoliberal trend of reducing taxes and making the tax structure more regressive. These cuts reduced the marginal rates on individuals, provided corporations with bonus depreciation allowances for capital expenditures, gradually reduced the estate tax rate from 55 to 45 percent while raising the exemption, and reduced taxes on capital gains and dividends to 15 percent (Steuerle, 2004, pp. 284–286).

Examining changes in the federal tax from 1980 to the present, it is fair to say that taxes on individuals, corporations, and estates were greatly reduced under the neoliberal claim that taxes and government spending reduced economic growth and individual freedom. Like the name of Reagan’s 1981 tax cut (ERTA), George W. Bush’s 2001 tax cut – the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) – reveals quite clearly neoliberalism’s market fundamentalism and supply side thinking. As President Bush explained in November 4, 2006, “The main reason for our growing economy is that we cut taxes and left more money in the hands of families and workers and small business owners” (quoted in Center on Budget and Policy Priorities, 2007, p. 4).

This brief summary of changes in federal tax policy is presented so that it is possible to examine how federal tax policies are imported into states and impact their revenues. One key difference between federal and state tax and fiscal policies should be noted here. Unlike the federal government that can run deficits, all the states but one (Vermont) must balance their budgets, which means that the importation of federal tax cuts will be more immediately visible at the state level.

As mentioned previously, all states’ tax revenues are impacted by changes in the federal tax code, and by FY2002 all states were confronted with fiscal crises caused in part by imported federal tax cuts. “Federal policies have cost states and localities more than $175 billion over the four-year course of the state fiscal crisis, from state FY2002 through FY2005” (Lav & Brecher, 2004, p. 1). For example, the passage of the federal Job Creation and Worker Assistance Act (JCWAA) in 2002 created bonus depreciation as corporations were allowed to deduct 30 percent of the cost of new assets in the initial year they were placed in service. Then, in 2003, passage of the Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) increased
the bonus depreciation to 50 percent for assets put into service before January 1, 2005. These corporate income tax breaks were imported into Missouri and reduced the General Revenue Fund by $209 million from FY2002 to FY2005 (Johnson, Lav, & Blouin, 2004, p. 5).

Similarly, passage of EGTRRA in 2001 phased out the estate tax and “effectively eliminates state estate taxes in most states” (Lav & Brecher, 2004, p. 6). In FY2001, the estate tax yielded Missouri’s General Revenue Fund $157 million. In FY2007 the yield is de minimus (Kruckemeyer, 2006a, p. 1). Finally, in 2004, another tax reduction for corporations was enacted – the “domestic production deduction” which allows companies to deduct 3 percent of “qualified production activities income” (QPAI). The deduction will double to 6 percent in 2007 and triple to 9 percent in 2010 (Johnson, 2007, p. 1). The projected revenue loss to Missouri by the time of full implementation is estimated to be between $23 and $36 million (Johnson, 2007, p. 4).

A number of states have recognized how federal policies are “passing down the deficit” (Lav & Brecher, 2004) to the states, and have decoupled their taxes from federal policies. Thirty-one states plus the District of Columbia decoupled from the federal bonus depreciation. Another 17 states plus the District of Columbia have decoupled from both the federal changes to the estate tax, and to the “domestic production deduction” (Johnson, 2007, p. 2). Missouri has not decoupled from any of these federal tax cuts and has suffered serious reductions in its General Revenue Fund. According to Lav and Brecher, Missouri has been more affected by these federal tax cuts than most states. Between 2002 and 2005, federal tax cuts cost Missouri $320 million and reduced its General Revenue Fund by 13.4 percent, making Missouri the 3rd most impacted state (Lav & Brecher, 2004).

While federal tax policies imported into Missouri’s tax code significantly reduced the General Revenue Fund that supports public higher education, to fully understand Missouri’s budget crisis requires an analysis of its unique Constitution and fiscal policies. One unique feature of Missouri’s Constitution involves the Hancock Amendment. The Hancock Amendment (Article X section 18 of the Missouri Constitution) is a perfect example of neoliberal policy. Established in 1980 at the beginning of the neoliberal regime change signaled by Reagan’s election, Hancock was designed to limit government by capping state revenues. It did this by limiting total state revenues (TSR) by linking them to personal income. The limit is set by multiplying total state personal income by 5.64 percent (Moody, 2003, p. 4). If state revenues surpass that limit, they must be refunded to personal and corporate income taxpayers. Hancock was first triggered in 1995, and from
1995 to 1999 over $980 million were refunded. In response to these increased state revenues, in the second half of the 1990s, legislators enacted 21 new tax credits and 14 new tax cuts. In the first year of their implementation, FY2000, the tax credits cost the state $170 million, while the tax cuts cost another $648.1 million. In short, changes to Missouri’s tax code resulted in a loss of $818.1 million dollars in FY2000, and have eroded its tax base by 11 percent annually. It is estimated that these tax credits and cuts will amount to more than $1 billion in lost revenues in 2007 (Missouri Budget Project, 2004a, p. 3).

In 1980, following the neoliberal fascination with tax cuts; Missouri enacted three sales tax exclusions that reduced sources for the General Revenue Fund. Prescription drugs and domestic utilities were excluded from sales taxes, while 50 percent of the motor vehicle tax was diverted to the State Motor Fuel Fund. In 1997, in the midst of the tax cuts and credits spawned by Hancock, the state excluded food from the general revenue fund sales tax. All totaled, in 2000, these exclusions or tax expenditures were costing the General Revenue Fund $479.4 million (State & Regional Fiscal Studies Unit, 2003, p. 10). This chipping away at the General Revenue Fund is a notable feature of Missouri’s fiscal policy. For example, in November 2004 Missouri voters passed Amendment 3 which diverted another large share of the motor vehicle sales tax from the General Revenue Fund to a new State Road Bond Fund. Amendment 3 is being phased in over a four year period, further depleting the General Revenue Fund by $73.2 million in FY2006 and escalating to $187 million in FY2009 (Missouri Budget Project, 2004b, p. 1).

The General Revenue Fund is the main source of discretionary spending in the state. Given the neoliberal distrust of government exhibited by passage of the Hancock Amendment, it is not surprising that the General Revenue Fund has been allowed to dwindle. Indeed, with the exception of two temporary tax increases necessitated by fiscal exigency in the late 1980s, legislators have not promoted any new general revenue taxes since 1971, and the great majority of tax increases have been for dedicated purposes and passed by ballot initiatives and constitutional amendments, not legislative action. The use of ballot initiatives and dedicated taxes is a neoliberal policy of limiting the discretion of legislators, and has been common in Missouri. For example, Proposition C (1982) created a 1 cent sales tax for K-12 education and overhauled property tax assessment, and the Parks and Soils Sales Tax (1984) created a one-tenth-of-one-percent sales tax.

A major event in Missouri’s fiscal history was passage of senate bill (SB) 380 in 1993. This legislation was a response to a court ruling that Missouri’s
funding of K-12 education was inadequate and inequitable, and thus in violation of the state Constitution. In response to Judge Kinder’s ruling, SB 380 created the Outstanding Schools Trust Fund and a foundation formula for distributing K-12 dollars. To support the new formula, SB 380 raised taxes by capping the deduction for federal taxes on individual incomes at $5,000 per person, and reduced the deduction for corporations from 100 to 50 percent of income. (Missouri is one of only eight states to have this regressive deduction.) It also raised the corporate income tax rate 25 percent, from 5 to 6.25 percent. This legislation generated an additional $500 million in revenue in FY1994, and was one factor triggering the Hancock refunds in 1995 because SB 380 was passed without voter approval (State & Regional Fiscal Studies Unit, 2003, p. 18).

SB 380 also precipitated a tax revolt and calls for Hancock II legislation that would tighten the definition of TSR so that certain revenues would not be exempted from inclusion in TSR. Given that SB 380’s tax increases were very progressive and affected primarily wealthy individuals and corporations, it is not surprising that these groups mobilized the neoliberal infrastructure. The neoliberal Cato Institute, whose web site banner promotes, “Individual Liberty, Limited Government, Free Markets and Peace,” produced publications explaining how, “legislators – aided by sympathetic court rulings – have discovered ways to avoid the voter-imposed restrictions by exempting certain revenues from the cap” (Stansel, 1994b, p. 1). The main problem, according to neoliberals like Stansel, was that the Missouri Supreme Court had ruled in 1983 that revenues from the voter-approved Proposition C sales tax for education should not be included in TSR. This “evasive” ruling “has allowed Missouri’s state politicians to collect $5 billion more in revenue over FYs 1982–93, than the Hancock amendment would have permitted” (Stansel, 1994b, p. 1). Hancock II would help Missourians “Tame Leviathan” (Stansel, 1994a).

In November 1994, Hancock II was soundly defeated at the polls. Apparently, Missouri voters did not buy the argument that tax increases they approved of by vote should be included in TSR calculations. Responding to the Motor Fuel Tax increase of 1992 and SB 380 tax increases in 1993, both which were passed without voter approval, Missouri voters did accept the neoliberal idea that politicians should not have the discretion to generate revenues, and passed the Carnahan/Farm Bureau Amendment in 1996. This amendment (Article X section 18e of the Missouri Constitution) puts a ceiling on new tax revenues by linking them to an annually adjusted percentage change in personal income. In FY2003 this limit was approximately $74.5 million (Moody, 2003, p. 5).
Any combination of tax or fee increases that exceeds this amount must be approved by voters, even if it falls below the Hancock limitation. The combination of the Hancock and Carnahan/Farm Bureau Amendments put Missouri’s public sector in a precarious position. Missouri, like most states, must balance its budget each year and cannot run deficits. In good economic times like the 1990s when surplus revenues were generated, “Hancock” required refunds and prompted tax cuts and credits. These tax cuts and credits became permanent features of Missouri’s tax code. In bad economic times, like 2001’s recession, revenues fall and create an imbalance between spending commitments (many of which were increased in the good times of the 1990s) and falling revenues. But, because of the Carnahan/Farm Bureau Amendment, taxes and fees cannot be raised to meet the shortfall without a vote of the people. Given the economic difficulties visited on many families during economic downturns, the likelihood of adjusting the imbalance through revenue increasing measures is most unlikely. The result is that the state must cut spending to balance the budget. In a very neoliberal way, Missouri’s tax system is structured so that as the business cycle moves up and down, the public sector gradually shrinks due to decreasing revenues thereby creating social imbalance.

Public higher education in Missouri is funded primarily from the General Revenue Fund. K-12 education, corrections, and Medicaid also draw off this fund, and spending on these programs affects the amount of revenue available for higher education. There are formulae (K-12 foundation formula, Medicaid eligibility rules, and sentencing laws) that mandate appropriations and have increased the spending for K-12 education, Medicaid, and corrections. In 1981, Missouri replaced its FTE-based funding formula for higher education with a base-budget formula. Practically, this means there is no formula guiding funding for public higher education. It is a math problem of determining what is left over after the other programs have drawn from the fund.

The recession of 2001 precipitated a state fiscal crisis as mandated spending exceeded tax revenues. In order to balance its budget, Missouri cut appropriations for higher education, which explains the decline of $103.3 million reported in Grapevine (2006) between FY2001 and FY2006. In response to the cuts in public funding, colleges and universities raised tuition and fees, which explains the 58 percent increase in tuition reported by the Missouri Budget Project earlier.

Missouri has created a structural budget crisis. “The central policy issue confronting the State of Missouri is the resolution of the structural deficit between essential general revenue expenditures and available revenue...
receipts” (Fajen, 2004, p. 3). A central element of this structure is the erosion of the tax base created by tax cuts and credits (both federal and state) and constitutional revenue limits. Examining net general revenues as a percentage of Missouri’s total income reveals the net general revenue tax burden (Table 1).

In FY1997 (Hancock is triggered) the tax burden peaked at 4.517 percent of personal income, and has steadily declined to an estimated 3.717 percent in FY2007. During this same period personal income grew from $126.2 billion in FY1997 to an estimated $197.9 billion in FY2007. Had the FY1997 tax burden of 4.517 percent been applied to the estimated $197.9 billion of personal income in FY2007, Missouri’s tax revenues would be more than $1.5 billion greater than the estimated $7.3 billion in FY2007.

Table 1. Net General Revenue Tax Burden.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>MO Net Gen. Revenue ($ millions)</th>
<th>MO Personal Income ($)</th>
<th>Revenue as a % of MO Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>1985</td>
<td>2,535.9</td>
<td>67,744</td>
<td>3.743</td>
</tr>
<tr>
<td>1986</td>
<td>2,649.1</td>
<td>71,593</td>
<td>3.700</td>
</tr>
<tr>
<td>1987</td>
<td>2,870.2</td>
<td>75,118</td>
<td>3.821</td>
</tr>
<tr>
<td>1988</td>
<td>3,215.0</td>
<td>79,078</td>
<td>4.066</td>
</tr>
<tr>
<td>1989</td>
<td>3,461.9</td>
<td>84,086</td>
<td>4.117</td>
</tr>
<tr>
<td>1990</td>
<td>3,720.6</td>
<td>88,483</td>
<td>4.205</td>
</tr>
<tr>
<td>1991</td>
<td>3,795.9</td>
<td>92,541</td>
<td>4.102</td>
</tr>
<tr>
<td>1992</td>
<td>3,792.9</td>
<td>97,761</td>
<td>3.880</td>
</tr>
<tr>
<td>1993</td>
<td>3,938.9</td>
<td>103,009</td>
<td>3.824</td>
</tr>
<tr>
<td>1994</td>
<td>4,244.7</td>
<td>107,411</td>
<td>3.952</td>
</tr>
<tr>
<td>1995</td>
<td>4,953.6</td>
<td>114,023</td>
<td>4.344</td>
</tr>
<tr>
<td>1996</td>
<td>5,301.0</td>
<td>118,857</td>
<td>4.460</td>
</tr>
<tr>
<td>1997</td>
<td>5,701.1</td>
<td>126,225</td>
<td>4.517</td>
</tr>
<tr>
<td>1998</td>
<td>5,947.7</td>
<td>133,648</td>
<td>4.450</td>
</tr>
<tr>
<td>1999</td>
<td>6,127.7</td>
<td>140,486</td>
<td>4.362</td>
</tr>
<tr>
<td>2000</td>
<td>6,133.1</td>
<td>147,811</td>
<td>4.149</td>
</tr>
<tr>
<td>2001</td>
<td>6,389.9</td>
<td>155,275</td>
<td>4.115</td>
</tr>
<tr>
<td>2002</td>
<td>6,210.9</td>
<td>158,966</td>
<td>3.907</td>
</tr>
<tr>
<td>2003</td>
<td>5,926.3</td>
<td>163,742</td>
<td>3.619</td>
</tr>
<tr>
<td>2004</td>
<td>6,345.8</td>
<td>170,653</td>
<td>3.719</td>
</tr>
<tr>
<td>2005</td>
<td>6,711.4</td>
<td>180,407</td>
<td>3.720</td>
</tr>
<tr>
<td>2006</td>
<td>7,332.4</td>
<td>189,427</td>
<td>3.871</td>
</tr>
<tr>
<td>2007</td>
<td>7,358.3</td>
<td>197,952</td>
<td>3.717</td>
</tr>
</tbody>
</table>

*Source:* Kruckemeyer (2006a)
A second facet of this structural crisis involves how the state calculates its essential general revenue expenditures. This involves primarily the K-12 foundation formula and Medicaid eligibility criteria, which have mandated increased appropriations for K-12 education and Medicaid (Moody, 2003). Consistent with neoliberalism, Missouri’s legislature has framed the deficit as a spending problem of an overzealous government. As a result, by FY2005 the K-12 funding formula was under-funded by at least $610 million (Fajen, 2004, p. 8) and school districts were once again suing the state for not providing adequate and equitable funding, as mandated by the State Constitution. Similarly, in the 2005 legislative session, Medicaid eligibility criteria were drastically cut and provisions were provided to eliminate Medicaid altogether by 2008 (McBride, 2006).

In response to the revenue shortages and the problems facing public higher education, in 2006, Governor, Blunt, proposed selling part of the Missouri Higher Education Loan Authority (MOHELA) to provide funds for capital improvements. This privatization would provide a one-time influx of revenues for much-needed capital improvements, but at the long-term cost of further reducing the base for future state revenues.

ANALYSIS

This case study reveals how Missouri has structured its fiscal policies so that public higher education is being transformed from a public good provided by government, to a private commodity exchanged in markets. What is revealing to note here is the specific mechanism by which this privatization is taking place. Usually privatization is accomplished by the outright sale of public goods to private parties. Governor Blunt’s current proposal to sell MOHELA is a perfect example of this privatization process.

The privatization of public higher education in Missouri, however, has occurred through a much less visible process that merits the label stealth privatization. This has involved a steady erosion of the tax base of the General Revenue Fund by numerous tax cuts, tax credits, and tax exemptions. These, combined with the Hancock and Carnahan/Farm Bureau Amendments, have created a ratcheting effect that shrinks the General Revenue Fund along with the ups and downs of the business cycle. In times of economic expansion, like the mid- to late 1990s, refunds and tax cuts are legislated to meet the requirements of Hancock. Then, when the
economy retracts, as in 2001, revenues fall and cannot be replaced without voter approval. Faced with a fiscal crisis, the state is forced to cut spending to balance the budget. One of the few areas where such discretionary legislation is possible is higher education, which was cut $99.6 million in FY2003. Despite a growing economy, by FY2007, state appropriations of $878.3 million were still $96.3 million below FY2002s $974.6 million. Of all the states, Missouri registered the largest percentage change in appropriations between FY2002 and FY2007 at -1.9 percent. The national average was +2.9 percent in nominal, not real (inflation-adjusted), dollars (Grapevine, 2007, table 4).

Confronted with these shortfalls, Missouri’s public universities and colleges had few options but to raise tuition and fees, and pass the costs of education onto students and their families. In this way, public higher education was involved in stealth privatization. If politicians had announced in FY2002 that they were passing legislation to raise tuition and fees by 58 percent over five years, there would have been massive resistance. Instead they offered tax relief from oppressive and inefficient government in the form of tax cuts, credits, and exemptions. When there were insufficient funds for public higher education and tuitions increased, the blame was focused on Missouri’s inefficient and greedy public institutions of higher education.

Once again the neoliberal infrastructure mobilized to explain how we are “Going Broke By Degree” and “Why College Costs Too Much” (Vedder, 2004). Economist, Richard Vedder, a member of the Spelling Commission on Higher Education whose work is promoted and published by the neoliberal American Enterprise Institute, explains why college costs too much. “[T]here are four major reasons for rising costs: third-party providers, the lack of market discipline, ineffective price competition, and government regulation” (2004, p. 24). His solution: privatize higher education and let market forces make education more efficient and affordable.

As Vedder’s work clearly demonstrates, one central problem with neoliberal thinking is that it does not recognize market failure to provide public goods. Even Adam Smith, who neoliberals constantly refer to, recognized the need for government to produce public goods. In The Wealth of Nations, Smith spells out the role of the sovereign and its duty of erecting and maintaining certain public works and certain public institutions, which it never can be for the interest of any individual, or small number of individuals, to erect and maintain; because the profit could never repay the expense to any individual or small number of individuals, though it may frequently do more than repay it to a great society. (quoted in Sackrey, Schneider, & Knoedler, 2005, p. 37)
Among the public institutions that Smith identified were “those for the instruction of the people” (quoted in Sackrey et al., 2005, p. 38). In short, Smith recognized that it was not profitable to produce the necessary levels of education, and that the state would have to augment the market mechanism. Moreover, for Smith, education was essential for creating the wealth of nations and promoting economic growth (Sackrey et al., 2005, pp. 39–41).

Current empirical research confirms that education is a main driver of economic growth. “In a review of literature on returns to education across 44 countries, World Bank economist George Psacharopoulos calculates internal rates of return to education of 14% and 12% for secondary and higher education, respectively, in developed countries” (Schweke, 2004, p. 7). According to Vedder, however, “the more state governments support higher education, the lower the rate of economic growth in the state” (2004, p. xviii, emphasis in the original). This case study of Missouri’s higher education system in the neoliberal era reveals that the money freed-up by tax cuts and credits did not find its way into the market of higher education as neoliberal thinking would suggest. The privatization of higher education has not created greater prosperity in Missouri, and instead has propelled social imbalance and disinvestment in public higher education.

**SOCIAL IMBALANCE**

Between 1952 and 1978, John Kenneth Galbraith published four books that, taken together, attempted to explain the changing contours of the modern economy and the implications these changing contours had for the discipline of economics and public policy. These four books: *American Capitalism: The Concept of Countervailing Power* (1952); *The Affluent Society* (1958); *The New Industrial State* (1967, significantly revised in Galbraith, 1978); and, *Economics and the Public Purpose* (1973), span the period when the Keynesian compromise developed and began to be challenged by what we now call neoliberalism. Central to Galbraith’s contribution was his recognition of how the emergence of big corporations and the interventionist state altered the workings of the modern economy and rendered “the conventional wisdom” (Galbraith, 1998) of classical and neoclassical economics obsolete. Perhaps the single most important contribution of Galbraith was his focus on “the problem of power” (Galbraith, 1993[1952], pp. 23–31) and how it was elided both in economics and the discourse of business. By the time Galbraith had published the revised third edition of *The New Industrial State* in 1978, the economic crisis that mobilized...
neoliberalism – stagflation – was firmly entrenched and Galbraith explained it by how power was woven through the institutional structures of the modern corporation, the interventionist state, and labor unions.

Galbraith’s analysis is historical and empirical and places power and interests at the center of his explanations. It also offers contrasting policy implications and provides a much-needed critical foundation for analyzing neoliberal policies. For purposes here I will use a major idea from his overall oeuvre, Galbraith’s (1998) notion of “social balance,” to illuminate how neoliberal ideas and policies result in the inadequate provision of public goods like higher education. In short, Galbraith’s analysis and critique of social imbalance highlights the infrastructure of neoliberalism and its contradictions.

In 1958, John Kenneth Galbraith published *The Affluent Society* where he advanced “The Theory of Social Balance.” Basically, for Galbraith, there must be “a satisfactory relationship between the supply of privately produced goods and services and those of the state;” “every increase in the consumption of private goods will normally mean some facilitating or protective step by the state” (Galbraith, 1998, p. 189). If you produce private automobiles, you need public highways. The problem, as Galbraith reiterated in his introduction to the 40th anniversary edition in 1998, was social imbalance,

Forty years ago I stressed the compelling difference between public and private living standards. We had expensive radio and television and poor schools, clean houses and filthy streets, weak public services combined with a deep concern for what the government spent. Public outlays were a bad and burdensome thing; affluent private expenditure was an economically constructive force. (1998:x)

In *The Affluent Society* (and later in *The New Industrial State* [1967], and *Economics and the Public Purpose* [1973]), Galbraith provided an explanation for why an affluent society has social imbalance.

According to Galbraith, we have imbalance because of a public policy that stresses the urgency of private production and economic growth while actively discriminating against investment in the public domain. There are four facets to the “conventional wisdom” driving the public policy of imbalance:

3. The “persuasion” of advertising and the media system that promotes private commodities (Galbraith, 1998, p. 194) and the vested interests of business.

Space constraints do not permit a full presentation of Galbraith’s insightful analysis here. It is enough, however, to note briefly how analysts like Vedder and Stansel have harnessed economics to justify privatization of higher education for neoliberal institutes that promote the vested interests of business in low taxes and private production. It is also quite clear that the mass media and advertising invest heavily in “persuading” consumers about the benefits of private commodities, and say little to nothing about public goods. Finally, much of what is privately produced is functionally frivolous, but necessary to provide jobs and income for economic security, which has become quite problematic in the neoliberal era.

Galbraith’s larger analysis of how the American economy had changed provides critical insight into neoliberalism and its market fundamentalism. For Galbraith, a “bi-modal” economy developed consisting of a competitive sector regulated by supply, demand, and price competition, and an oligopolistic “planning system” managed by a “technostructure” that manipulated supply, demand, and prices to generate earnings and corporate growth. Central to this transformation was “bureaucratic symbiosis” where the State collaborates with corporations to assure adequate earnings and growth. For Galbraith the “new industrial state” implemented policies that generated social imbalance and necessitated an “economics for the public purpose.”

What Galbraith’s analysis suggests is that neoliberalism and its market fundamentalism is less a plan for general prosperity, and more a strategy for consolidating the interests of big corporations and their wealthy investors. Examining the tax changes that are central to the stealth privatization of public higher education in Missouri supports Galbraith’s analysis.

In Missouri, the Federal tax cuts of 2001–2003 dramatically benefited the wealthy. In 2004, the top 1 percent of Missouri residents received an average benefit of $47,976, while the average benefit for the poorest 60 percent of households was $458 (Johnson et al., 2004, p. 3). Similarly, corporate taxes in Missouri have decreased in the neoliberal era. In FY1985, corporate taxes as a percentage of net general revenue were 7.5 percent and fell to 5.5 percent in FY2006 (Kruckemeyer, 2006b). “According to US Census data released in December 2005, Missouri Corporate Income tax Per Capita was $38, well below the national average of $131. Missouri’s rank was 46th out of 46 states that levy this tax” (Kruckemeyer, 2006b, p. 1). Galbraith was
CONCLUSION

This case study of public higher education in Missouri reveals how one facet of neoliberal policy – tax cuts – leads to *stealth privatization* and social imbalance. The neoliberal claim that returning to market fundamentalism will generate prosperity is clearly contradicted by Missouri’s experience with higher education. The National Center for Public Policy and Higher Education succinctly summarizes the condition of Missouri’s public higher education:

> Missouri’s underperformance in educating its young population could limit the state’s access to a competitive workforce and weaken its economy over time … . Since the early 1990s, colleges and universities in Missouri have become less affordable for students and their families. If these trends are not addressed, they could undermine the state’s ability to compete successfully in a global economy. ([Measuring Up, 2006b](#), Missouri, p. 3)

Instead of greater economic prosperity, the effect of Missouri’s neoliberal changes to its Constitution and fiscal policies has been to consolidate private economic wealth and further propel social imbalance.

This state-level case study is important because it reveals more clearly the impact of neoliberal policies and how they create social imbalance. Unlike the federal government, which can finance tax cuts through growing deficits and thus hide the real impact of social imbalance, states like Missouri must balance their budgets to take account of falling revenues and align them with appropriations. As Missouri’s experience illustrates, social imbalance is manifested by the inability of state government to provide essential public goods and services. The analysis here has focused on how higher education has been adversely impacted by neoliberal policy, but it should be emphasized that neoliberal imbalance has also led the state into a crisis of providing K-12 education, and health care for the needy. Certainly, eliminating Medicaid is a drastic manifestation of social imbalance. Indeed, one of the central conclusions of this analysis is that most of the public goods and services that citizens depend on today are provided by state and local governments, and it is at the state and local levels that the problem of social imbalance is most severe.

Another important finding of this case study involves how federal tax changes are imported into state tax codes, and in the neoliberal era, have contributed to social imbalance. Thus, while neoliberal politicians in
Washington can promote market fundamentalist ideology and legislate tax cuts, they do not have to confront the consequences of social imbalance; these are passed down to the state and local level. Moreover, as the federal government has delegated responsibility to the states for managing Medicaid, and Temporary Assistance to Needy Families (TANF), the problems of social imbalance are increasing.

Ultimately, what this case study reveals is how pivotal state fiscal policy – and especially its tax code – is for the provision of public goods and services. The dismal statistics about Missouri’s public higher education are largely the result of its unique constitution and tax code, which have been altered in the neoliberal era to reduce the ability of its elected officials to generate revenues for the provision of essential public goods and services. It is no surprise that Missouri ranks 46th in appropriations for higher education, ranks 45th in FTE enrollment growth, and ranks 46th in taxes per capita (Vock, 2006, p. 1). While the neoliberal discourse takes place at the national level, its policy impact is primarily at the state and local level.

The analysis here has described how neoliberalism generates social imbalance. It also generates a self-fulfilling prophecy. Starved for resources, the government becomes “hobbled” and does a poor job of providing public services. This reinforces the neoliberal vilification of the government, and prepares fertile ground for additional neoliberal policies, which generate further social imbalance. The only way to break this vicious cycle is to understand the mechanisms of social imbalance, and identify the interests they serve. This research is offered in the spirit of understanding social imbalance, and the development of an institutional structure that can express the public interest. Our future prosperity depends on the provision of essential public goods like higher education.

**NOTES**

1. The Morrill Acts involved the federal government granting federal land to states for the purpose of establishing colleges.
2. The Higher Education Act of 1965 increased federal money given to universities, created scholarships and low-interest loans for students, and established a National Teachers Corps.
3. The Pell Grant program is a type of post-secondary education federal aid, and is the largest need-based grant aid program in the country.
4. The Bretton Woods Agreement established an international monetary system and rules for commercial and financial relations among industrial nations after World War II.
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Neoliberalism and Social Imbalance: Higher Education in Missouri


THE LOCAL STATE,
DECENTRALIZATION, AND
NEOLIBERAL ROLL-OUT:
A COMPARATIVE, SUBNATIONAL
ANALYSIS OF GROWTH AND
REDISTRIBUTION RESPONSES

Linda Lobao

ABSTRACT

This paper examines decentralization of economic growth and redistribution functions in light of the neoliberal development model. While cross-national literature explores this topic, relatively little research centers on the subnational scale. I focus on county governments and address two questions. Do counties’ economic development and public service activities correspond with theories about a neoliberal drift? Are counties
racing to the bottom in social service provisioning and well-being? I ground these questions within three contrasting perspectives, neoliberal, radical political economy, and a more spatially sensitive, institutionally oriented approach. Data are from a county government survey and secondary sources. I found little evidence of trade-off course between redistribution and growth policy activities. While counties are not racing to the bottom, localized social services and economic development activities reinforce past spatial disparities, with poorer, rural localities tending to fare worse.

INTRODUCTION

A large literature argues that the U.S. has undergone fundamental shifts in the state institutions regulating economic growth and redistribution. The state itself is more subject to market influences, the scope of the federal government is reduced, and greater authority is devolved to lower governmental units. Most sociological research addressing these shifts is macro-oriented, centered on nation-states as a whole (Leicht & Jenkins, 2007). Here I examine institutional arrangements forged by the local state with citizens and business and how they work out across subnational space, including both urban and rural areas. I examine two dimensions of institutional arrangements, how the local state allocates resources toward service provision (policy relationships with citizens) and toward economic development (policy relationships mainly with capital). In the first case, local governments are coping with changes in public services and entitlement programs, brought about by devolution (Kodras, 1997, p. 83). In the second case, local governments have expanded their role in economic development over the past two decades (Wolman, 1996). While each of these changes is treated in independent literatures, recent political economic theories see them as a package of policy shifts reflecting the “roll-out of neoliberalism” (Peck & Tickell, 2002), whereby decentralization of responsibilities for economic growth and redistribution to local governments is intended to undermine past Keynesian state-society relationships.1

Brenner (2004) argues neoliberalism as an assault against the Keynesian scale of regulation, a project designed to change the state’s division of labor by making key functions less centralized and more localized. Neoliberalism encourages market entrepreneurship, inducing subnational governments to assume greater responsibility for economic growth and increasing territorial competition between places. Although local government engagement in
economic development is longstanding, in the U.S. case, this combines with other state projects such as 1996 welfare reform legislation and continued devolution of services to lower levels of government. The result is a package of state changes that subordinates the needs of citizens to those of business and undermines past Keynesian growth and redistribution strategies (Peck & Tickell, 2002).

Analysts note that a major gap in research on the neoliberal roll-out is how it works out at the subnational scale (Brenner, 2004; Lobao & Hooks, 2003; Ruben, 2001). When localities become engines of market growth and sites of administrating services, there is the potential for greater inequality between places, an “increasing divergence of social welfare standards and an enhanced differentiation of development pathways among local economies within each national territory” (Brenner, 2004, p. 214). However, empirical research tends to treat decentralization and other institutional shifts advocated by neoliberal policy as relatively uniform within nations.

To analyze how these recent institutional shifts unfold for the local state across the U.S., I focus on county governments, now the fastest-growing general purpose governments, due in part to devolution (Lobao & Kraybill, 2005). Counties are particularly relevant to assessing inequality across subnational territory since they cover large metropolitan as well as small unincorporated areas. I address two questions. (1) How do counties’ economic development and public service policy responses correspond with theoretical views of the changing role of governments? That is, to what extent are there evidence of decentralization and other attributes of the neoliberal drift? (2) To what extent do county governments’ economic development and social service policy responses affect local well-being? Analysts put forth various answers to these questions which roughly correspond to assertions that decentralized growth, and redistribution policy has beneficial, detrimental, or mixed effects on localities. To ground these answers theoretically, I situate them within three contrasting frameworks: neoliberal, radical political economic, and a more spatially sensitive, institutionally oriented approach.

The neoliberal and radical political economy frameworks are contrasted mainly in cross-national analyses (Lavalette & Pratt, 1997; O’Brien & Penna, 1998; Tornquist, 1999), but researchers stress the importance of testing their claims across U.S. localities (Lobao & Hooks, 2003). First, neoliberal justifications for market-oriented government are precise because American communities and families are asserted to benefit. Second, both theories inform social science and policy debates about local government.
A leaner, meaner, decentralized state is a tenet of neoliberal thinking, while radical political economists are among foremost scholars against such efforts (Lobao & Hooks, 2003). The political economy perspective provides a rationale for viewing localized social services and economic development activities as creating “race to the bottom” across the nations’ localities, while the neoliberal perspective would see it as a “race-to-the top.”

Contrasted with the outcomes expected from both these macro-level perspectives is an intermediate view. Unlike the two previous perspectives which tend to see either generically positive or negative outcomes of decentralization, this perspective stresses the unique qualities of local areas that produce contingent outcomes, not fully captured by theory. Encompassing a large literature, this view emphasizes path-dependent development and each localities’ distinct institutional and other attributes that modify outcomes expected by macro-level theory (Brenner, 2004; Lauria, 1997; Lobao, Rulli, & Brown, 1999; Peck, 1996). I briefly summarize the three perspectives, outlining their expectations for the local state’s response to decentralization and how it affects local well-being. In examining policy responses, I follow other recent studies by focusing on the scope of activities undertaken by governments in economic development and public service arenas (Basolo & Huang, 2001; Clingermayer & Feiock, 2001; Jenkins, Leicht, & Wendt, 2006).

THREE CONTRASTING FRAMEWORKS ON THE LOCAL STATE

Localized Government and a Race to the Top: The Neoliberal School

Contemporary neoliberalism is the product of four sources: the Chicago School of Milton Friedman; the “new classical liberalism” in economics which argues for a return to classical Smithian principles; public-choice theory of politics and its critique of government services; and right-wing policy organizations (O’Brien & Penna, 1998, p. 81; Peet, 1999, p. 49). Much neoliberal thinking is directed to a criticism of the federal state and social welfare programs (Hayek, 1960; Mitchell & Simmons, 1994). However, within the general neoliberal critique of the state, there is recognition that some attributes of government are more beneficial or less harmful than others. The decentralized state is preferable to the federal state. The inherent trade-off between growth and distribution (Okun, 1975)
as well as taxpayer resistance puts greater pressure on local officials to reduce government size and scope of services (Peterson & Rom, 1990). Certain state functions also are more preferable than others. Expansion of the state beyond providing true public goods to education, health, and related social services is “the hallmark of the interventionist state” that deters growth (Pratt, 1997, p. 36). By contrast, programs, policies, and other activities aimed at creating a more business friendly environment are a preferable function (Buchanan, 1986; Tiebout, 1956). Smaller government is beneficial (Buchanan, 1986). Larger government crowds out businesses performing similar public services – and providing these services through the private sector is more efficient, yielding greater benefit to the masses.

To sum, the neoliberal perspective sees a trade-off between growth and redistributive activities. It indicates that well-being should improve where local government offers minimal public, particularly social services, but engages in private-sector business development.

Localized Government and a Race to the Bottom: Radical Political Economy

Radical political economy is a family of traditions that challenges the neoliberal attack on the welfare state (Albelda, Drago, & Shulman, 2001; Block, 1987; Lo, 1998; Peck, 2001). Political economists have observed fundamental changes in state institutions regulating economic growth and redistribution, a transition from “a Keynesian welfare state” to a neoliberal “workfare state” that promotes market competitiveness and directs social policy to the needs of employers (Jessop, 1994). Decentralized public service and economic development activities are a part of this shift, whereby the central state becomes less willing to act on behalf of labor and citizens and encourages territorial competition among subnational governments (Brenner, 2004).

Recent political economy perspectives do not necessarily see a decline in the state under neoliberal governance. Rather, there is a shift in the division of labor to lower governmental units and towards activities catering to business needs over those of the general public and poor (Peck & Tickell, 2002). Changing governance patterns where localities assume greater responsibility are seen as engineered by capitalist interests. This contrasts with other views that see decentralization as a citizen-driven response to improve government by making policy more flexibly tailored to local needs.
Further, according to political economists, decentralization regardless of its origins, has evolved to become a cornerstone of the neoliberal development model (Brenner, 2004). As state functions become decentralized, detrimental consequences for communities are likely. Decentralization places greater pressures on local governments to become more atomistic in behavior, and to engage in competitive economic development activities at the expense of public service activities (Kantor, 1995; McGuire, 1991).

The political economy approach like the neoliberal approach sees a trade-off between local governments’ economic growth and redistribution policy activities. However, political economists stress the negative outcomes of this trade-off, particularly for the poor. This suggests that counties highly engaged in economic development activities may provide fewer public services, particularly social services. A large literature on welfare reform addresses the potential for a race-to-bottom, whereby localities seek to reduce services for the poor (Schram, 1999).

In addition to detrimental impacts owing to service cuts, the political economy approach argues that general public and social welfare services are part of broader systems of regulation which can be a source of competitive advantage (Amin, 1999). In contrast to neoliberals’ views, such state services can enhance human capital and business, promoting local well-being.

In sum, the political economy approach stresses the problems with decentralized government: the potential for service cutbacks, trade-offs between growth and redistribution activities, and dismantling of previous advantageous systems of regulation. Communities are thus expected to fare worse as decentralization and other attributes of the neoliberal development model unfold.

The Mixed Effects of Localized Government and Potential for Subnational Disparities

In contrast to generic outcomes of decentralization expected from the previous perspectives, an intermediate view can be developed from literatures that stress place-specific, institutional processes and path-dependent development. A broad group of frameworks fall under this banner. While theoretically diverse, they serve as point of contrast with both the more conventional, neoliberal and radical political economy perspectives above – they see subnational variations in response to decentralization. Under this banner, I place two bodies of work: one is concerned with
revising macro-level political economy theory, to take account of local and regional differences in the state’s operation (Amin, 1999; Brenner, 2004; Jenkins et al., 2006; Lobao et al., 1999; Peck, 1996); the second, a local institutional literature centers on local development processes, as seen in urban-regime theory (Dowding, 2001; Lauria, 1997), growth machine perspectives (Logan & Molotch, 1987), and related approaches (Holupka & Shlay, 1993). Both bodies of work argue that place-based processes intervene in state-society policy shifts, so that conventional perspectives yield overgeneralized accounts of these shifts.

This diverse literature makes several points relevant to how a potential national drift toward neoliberalism affects localities. The first is that national shifts – and theories purporting to explain them – play out differently in different spatial settings. Macro-level theories thus may not work out isomorphically at the subnational scale (Jenkins et al., 2006; Lobao et al., 1999).

A second commonality is recognition that localities’ distinct internal attributes mediate state-society shifts. Of these attributes, researchers stress the importance of institutional arrangements among social actors, government capacity to engage in development and service activities, economic structure, and demographic composition (Jenkins et al., 2006; Lobao & Hooks, 2003; Stoker & Mossberger, 1995). Institutional arrangements reflect established patterns of relationships and relative bargaining power between key social actors, such as the state, business, citizens, and labor. These arrangements are embodied in practices, programs, and policies guiding economic development (Jenkins et al. 2006) and redistribution (Amenta & Halfmann, 2000). For example, local institutional literature has long documented that business sectors standing to gain from economic development programs such as manufacturing (Reese & Rosenfeld, 2002), and place-bound sectors such as real estate (Lauria, 1997; Logan & Molotch, 1987) tend to influence local officials’ growth policy agendas (Lauria, 1997; Logan & Molotch, 1987). Local governments that are larger and more prosperous have greater capacity to engage in economic development activities, and those less dependent on state/federal funding have greater incentive to do so (Reese & Rosenfeld, 2002). Similarly, larger, more prosperous governments have greater capacity to directly provide general public and social services and to avoid service cutbacks (Kodras, 1997). Economic structure also contributes to state responses. For example, localities more dependent on manufacturing employment can be expected to engage in more industrial recruitment activities (Jenkins et al., 2006).
Finally, localities vary in demographic attributes which affects the need and demand for public services. All these internal factors can foster subnational variation in responses to changes such as decentralization.

A third commonality involves recognition that external position or geographic location in the broader political economy mediates state-society shifts. For example, rural locations tend to remain the nation’s repository for poorer quality jobs such as in nondurable manufacturing and agriculture, and distance from metropolitan centers hinders the ability to attract higher quality employment. These factors, in turn, limit the ability of rural localities to adapt to social policy shifts such as welfare reform that hinge on the quality and quantity of employment (Gibbs, 2002).

Finally, this literature stresses path dependency in regional processes. Past institutional arrangements, economic structure, and other distinct features of localities are seen to have cumulative and lasting effects on public well-being (Jenkins et al., 2006; Molotch, Freudenburg, & Paulsen, 2000).

Taken as a whole, this set of literature suggests subnational variability in response to decentralization. The capacities and willingness of local governments to take on increased responsibilities are unevenly distributed. This literature suggests a spatial marginalization hypothesis: poorer localities, including much of rural America, are likely to fare worse as they face greater competitive pressures to capture mobile business resources and as they address new or expanding public service mandates (Kantor, 1995, p. 196). A related point is that pursuit of economic growth policy agendas may not dampen pursuit of social and other public service agendas. Path-dependent development suggests that places which in the past offered greater support for citizens’ well-being may continue to do so, even as federal government itself becomes more neoliberal in character (Brenner, 2004). Further, if decentralization in fact leads to more localized governance and to distinct local modes of regulation, then local governments may act more autonomously and potentially increase all types of activities, those pertaining to growth as well as redistribution. This too is likely to stress some localities more than others.

In sum, three different outcomes are possible as decentralization unfolds. The neoliberal and radical political economy frameworks suggest local governments will pursue a trade-off course between growth and redistribution policy activities, with the neoliberal framework seeing potentially beneficial outcomes and the radical economy framework, detrimental outcomes. By contrast, a third set of literature sees no necessary trade-offs between pursuit of growth and redistribution activities and spatially variant outcomes for well-being.
COUNTY GOVERNMENTS AND RESPONSES TO DECENTRALIZATION

Compared to cities and states, counties have been given little attention as governmental units. Yet they are important for understanding the local state under decentralization. Counties have more than 230 million residents, covering more people than any other substate unit of general purpose government. Of the contiguous U.S. states, 46 (including Louisiana parishes) have functional county governments. Counties also are the major government for unincorporated, predominantly rural areas. They are the fastest growing general purpose local governments (Gold, 1996, p. 282). From 1980 to 1997, government employment, a common indicator of size, grew by 31% for county governments, by 26% for states, and by 8% for municipalities, while federal employment declined by 3% (Lobao & Kraybill, 2005, p. 246). Counties are a significant administrative unit where new federal and state mandates are being devolved and implemented. Almost half of Americans live in the 13 states where county governments are responsible for directly administrating TANF (Temporary Assistance to Needy Families), the nation’s social welfare program (Lobao & Kraybill, 2005, p. 246). The political importance of counties was seen in the last two presidential elections, where counties’ decisions about counting absentee ballots, operation of polling places, and selection of voting machines drew national concern. In sum, counties’ growth relative to other governmental units, role in devolution and management of contested political issues makes them a fertile site for studying the neoliberal roll-out.

Research on Local Economic Development and Public Service Activities

Extant literature suggests that counties have expanded the scope of their activities compared to the past. Clarke and Gaile (1992) conclude cutbacks in federal intergovernmental aid in the 1980s led U.S. cities to engage in greater economic development activity as they were forced to depend more on own-source revenues. Similar changes appear to have occurred in small, rural communities in response to federal cutbacks in the next decade (Johnson & Scott, 1997). Analysts have noted increased economic development activity by county governments in different states since the 1980s (Reese, 1994). Local responsibilities for public services also have been increasing since the 1980s (Watson & Gold, 1997, p. 2). This shift intensified in the 1990s as some social programs, such as Aid to Families with
Dependent Children (AFDC), were changed from open-ended, matching grants to block grants with greater local operating flexibility.

Subnational differences in governments’ ability to assume increased responsibilities have been noted (Rodriguez-Pose & Gill, 2003), in accordance with the third perspective on the neoliberal roll-out. Difficulty in implementing devolved services and likelihood of dismantling public services is expected to be greater in counties that are poorer and more rural and where government support for citizen well-being has been weak historically. As noted, such localities have less resources and capacity to administer economic development and social service programs. Fiscal stress is thus likely to be spatially uneven as government becomes more decentralized (Brenner, 2004; Wildasin, 1997). A prime line along which subnational disparities in responses to decentralization should be expected is between metropolitan and nonmetropolitan (rural) governments. Nonmetro areas tend to be disadvantaged by: poorer economic structure; population size, density, and composition (such as a larger elderly population); and higher poverty rates, with these disadvantages greatest for more remote nonmetro counties (Brady, Sprague, Gey, & Wiseman, 2002; Goetz & Freshwater, 1997; Lichter & Jensen, 2002). Local capacity to respond to macro-level change also is weaker in rural areas (Johnson, Pelissero, Holian, & Maly, 1995; Lobao & Kraybill, 2005).

Empirical research on county government activities is limited. The vast majority of studies using counties as units of analysis draw from data on populations as opposed to governments. Extant research provides some evidence of nonmetropolitan disadvantage when government functions are localized in counties. A study of block grant programs found that nonmetro governments experience greater difficulty in obtaining and implementing grants than metro governments, indicating serious weaknesses as local fortunes increasingly depend on the capacity to secure and manage external funding (Rural Policy Research Institute (RUPRI), 1995). Using data from county officials collected in the mid-1990s, Warner and Hefetz (2002) found that nonmetro counties provided fewer public services than metro counties. In a survey of county officials in six manufacturing belt states, Dewees, Lobao, and Swanson (2003) found that most counties undertook major development activities, but little urban–rural variation in the types of activities undertaken. Using a national sample, Lobao and Kraybill (2005) found that nonmetro counties were less likely than metro counties to engage in economic growth promotion and they provided fewer public services. While some research exists on urban–rural differences, researchers have attended little to other factors that might account for disparities in county
governments’ activities and whether observed rural–urban variations are in fact a function of other local attributes.

Most county-based research uses secondary data on county populations (not governments) and focuses on social services, particularly welfare reform. This research further suggests that nonmetro populations, particularly those in the most remote counties (non-adjacent to metro areas) fare worse as government functions are decentralized. Changes in social programs tend to have greater effects on remote, nonmetro populations owing to their higher poverty rates (Economic Research Service (ERS), 1997, p. 46). Welfare benefits per recipient have been historically lower in more rural states (Nord, 1998). A number of studies document a spatial mismatch of workers and jobs in poorer and more rural counties, which reduces the probability of successful employment of welfare recipients (Gibbs, 2002; Goetz & Freshwater, 1997; Henry, Reinschmiedt, Lewis, & Hudson, 2002; Lichter & Jensen, 2002).

DATA FOR THIS STUDY: A NATIONWIDE SURVEY OF COUNTY GOVERNMENTS

Systematic examination of county governments is hampered by existing data. The major source of data on these governments is the Census of Governments but it contains little information about economic development and public services directly provided by counties. National data is produced by International City/County Management Association (ICMA), also using surveys of county officials. However, ICMA surveys focus on counties with populations of 25,000 or more, excluding over half of all counties. Response rates to ICMA surveys are about 30–35%, so that even for sampled counties, about two-thirds are missing.

To understand the activities of county governments across the U.S., I use data from a survey conducted in 2001 in collaboration with the National Association of Counties (NACo). The survey’s purpose was to examine how county governments respond to decentralization and it was designed to produce the first nationally representative information about counties’ economic development policy, social service, and general public service activities. Using the list of officials (county commissioners or their equivalent) provided by NACo, we mailed questionnaires to approximately 2,700 counties in the 46 contiguous states in which counties are functional units of government. Dillman’s (1978) methodology was followed. A total of
1,678 counties responded to the survey, a response rate of 62%. Twenty-six percent of these counties are metropolitan; 24% are nonmetropolitan counties adjacent to metropolitan areas; and the remaining 50% are nonmetropolitan, nonadjacent to metropolitan areas. These percentages are nearly identical to the proportion of all U.S. counties in each metro-status category.

Surveys using government officials as key informants are the most common way of gathering local government data unavailable through secondary sources. This methodology is used in the surveys conducted by ICMA, the National Governors’ Association, and the U.S. Conference of Mayors, and independent researchers (e.g., Basolo & Huang, 2001; Reese & Rosenfeld, 2002; Sullivan, 2002). Primary surveys of officials have limitations. Detailed financial data usually cannot be collected, as it is too labor intensive for most officials to provide. Wolman (1996) notes that much data collected allow construction only of dichotomous variables, such as use or non-use of an economic development policy tool or government activity. Wolman (1996) indicates that key informant surveys ideally should aim for a range of responses, such as the degree of use of an economic development tool or activity. To capture a range of responses and to tap changes, informants were asked to rate the degree to which certain government activities changed compared to the past. Retroactive questions about change are used in the government surveys noted above. These questions may introduce perceptual and other response biases that cannot be readily avoided or corrected. However, the only way to assess national trends in counties’ (and other local governments’) economic development and service activities is to ask key informants: no generalizable, longitudinal studies exist that capture the presence of these activities or spending on them (Reese & Rosenfeld, 2002; Wolman, 1996). In the analyses below, I tested for two types of systematic bias: non-response bias and bias due to informant officials’ characteristics. Both yielded no significant evidence of systematic bias.

I present findings for the sample as a whole and by three geographic categories: metro, nonmetro adjacent, and nonmetro nonadjacent. To condense terminology, I refer to these counties as metro, adjacent, and remote.

The empirical analysis centers on three questions. (1) To what extent are there reported changes in economic development and public service activities, in accordance with frameworks on the neoliberal drift? (2) How do these activities vary subnationally across metro, adjacent, and remote governments? (3) Is decentralization affecting the well-being of county
governments and their populations? I provide a descriptive as well as multivariate analysis. Descriptive findings for metro, adjacent, and remote rural counties are statistically significant unless noted otherwise.

**FINDINGS**

*Economic Development, Public Service Activities, and Financial Well-Being*

**Economic Development**
Almost three-quarters of counties engage in economic development. Eighty percent of metro, 75% of adjacent, and 67% of remote county officials report that their county engages in economic development planning and policy implementation. Moreover, for 51% of counties (55% of adjacent compared to both 51% of remote and metro counties), county government is one of the two most important economic development players in the county. With regard to specific economic development activities, for a menu of 12 policy tools, the following proportions of counties report using these tools: collaborative planning for economic development with other local governments (68%), economic development assistance to small communities (51%), tax abatements (50%), workforce development for low-income workers (50%), worker training assistance for local business (41%), national advertising of the county as a place to do business (36%), travel to other parts of the U.S. to recruit new business (32%), tax increment financing of infrastructure (30%), subsidized loans to business (29%), assistance in transfer of new technologies (25%), travel to other parts of the world to recruit new business (14%), and loans or grants for exporters (12%).

The spatial marginalization hypothesis suggests that nonmetro governments will be less active in economic development. Nonmetro counties, especially remote ones, are indeed less likely than metro counties to use the policy tools above. These urban–rural differences are further reflected in lower budget allocations and staff. For example, while 61% of metro governments have least one economic development professional on staff, only 31% of remote governments do.

Consistent with the literature on the expansion of local growth initiatives, for a menu of 12 economic development policy tools, officials were much more likely to report that use had increased rather than decreased in the past five years. Officials were asked “to what extent does your county undertake the following activities today as compared to the past five years?” The five
most frequently reported increases are in collaborative planning (35% of governments), workforce development (26%), assistance to small communities (21%), national advertising (16%) and tax abatements (16%). For any of the 12 activities, a maximum of only 3–4% of counties reported decreases in the activity.

Past research tends to assume local governments pursue mutually exclusive approaches to economic development: traditional, less sustainable first-wave business attraction activities (such as tax abatements or tax credits for specific businesses); second-wave “demand-side” activities (such as increasing local productivity through providing infrastructure); and third-wave activities (such as subsidizing research and development) (Eisinger, 1988). By contrast, I find all three approaches tend to be undertaken jointly and have increased as a bundle. This suggests territorial competition is increasing and that local governments hedge their bets by pursuing a mix of strategies. This finding corresponds with a recent study of U.S. states which documents a similar increase in use of all three types of activities (Brace, 2002).

There are also urban–rural differences in shifts in the portfolio of economic development activities. In remote counties, a higher proportion of officials reported greater focus in the past five years on business attraction activities that tend to be fiscally less sustainable. By contrast, urban and adjacent county officials reported their focus was shifting to local business retention and expansion and small business development.7

Social and other Public Services

Counties provide a variety of services which they operate directly and in cooperation with other public or private partners. Out of a menu of 21 services that counties provide, 7 are provided (almost all entirely directly) by more than half of county governments. The most ubiquitous service is law enforcement, provided by 84% of all counties. Other widely provided services are 911 service (82%), senior citizen programs (57%), mental health services (53%), health clinic services (52%), emergency medical services (51%), and solid waste removal (51%). For 16 of the 21 government services, there are statistically significant urban–rural differences, with nonmetro counties providing fewer services than metro counties and remote nonmetro counties providing fewer services than adjacent counties. The greatest urban–rural gaps are found across social services.

Both the neoliberal and political economy frameworks anticipate that increases in economic development activities will be accompanied by reduction of public service activities. In contrast to these expectations,
Officials report public service activities were much more likely to have increased rather than decreased. Officials were asked to report whether there “have been any changes (increases, cutbacks, no change) in the services your county government provides” over the past five years. For most services, from 15 to 30% reported increases in county activity. The major service increase was in law enforcement, with 63% of counties reporting increases. For most services, metro counties were significantly more likely to report increases relative to nonmetro counties, while remote counties were significantly less likely than other counties to report increases. Service cutbacks were rare. Only 1–2% of counties reported cutbacks in any of the 21 services. There was little urban–rural variation in cutbacks.

Officials were asked whether their governments faced funding shortages for social services. The most frequently reported funding shortages were in services to the aging (47%), childcare (41%), transportation (25%), and housing assistance (30%). Metro counties are more likely to report funding shortages, unexpected from the spatial marginalization hypothesis noted earlier.

The role of county governments in welfare reform varies by state. States devolving welfare directly to counties tend to be more urbanized. Twenty-two percent of surveyed counties, 33% of metro, 21% of adjacent, and 16% of remote governments administer TANF directly. Of these counties, metro counties report greater success in placing welfare recipients in jobs than nonmetro counties, a finding expected from the spatial marginalization hypothesis. Thirty percent of remote counties with TANF-related jobs programs report placing 20% or less of their welfare recipients in jobs. In contrast, only 11% of metro and 17% of adjacent counties with jobs programs report job placement at 20% or under.

In sum, the spatial marginalization hypothesis suggests that nonmetro counties will face greater problems in social service delivery under decentralization. There is support for this view in terms of welfare-recipient job placements, which are far less successful in remote counties. However, descriptive findings here also indicate that while most counties report funding shortages, metro counties are more likely to report these problems. Because the scope of social services is greater in metro counties, new mandates may increase funding pressures relative to nonmetro counties where social services have always been more limited.

Financial Well-Being

The political economy perspective emphasizes that decentralization creates fiscal stress as localities become dependent on own-source funds and as the
federal government abdicates its role in redistribution (Kodras, 1997). Fiscal stress is reported as an important problem by more than two-thirds of counties. Compared to metro counties, nonmetro counties report greater fiscal stress due to federal and state revenue sharing. Thirty-eight percent of remote, 31% of adjacent, and 24% of metro governments report that loss of federal revenue is a “very important” problem. Forty-eight percent of remote, 45% of adjacent, and 38% of metro governments report decline in state revenue is a very important problem. Sixty-two percent of counties, with no difference between metro and nonmetro governments, report mandated costs from higher levels of government are a very important problem.

In nonmetro counties, fiscal stress is exacerbated by taxpayer resistance, funding capacity, and general tax base. These counties face greater pressures to reduce local taxes: 37% of remote, 33% of adjacent, and 24% of metro counties report that pressures from local taxpayers to reduce taxes are a very important problem. Nonmetro counties have less capacity to seek external grant funds. Fifty-one percent of metro counties but only 30% of adjacent and 28% of remote counties a grant writer on staff. A much higher proportion of remote (40%) compared to adjacent (31%) and metro counties (12%) report that a declining tax base is a very important problem.

Multivariate Analyses

Survey findings point to an increased role of county governments in promoting economic growth and public services, and to subnational variations in these trends. Multivariate analyses are conducted to address the extent to which increases in the scope of economic development and social service activity are related to other local attributes. In turn, I also address whether economic development and social service activity affects county well-being, using two measures: an index of reported county government funding shortages; and median family income – a common measure of economic well-being (Lobao & Hooks, 2003; Nielsen & Alderson, 1997). As discussed, the neoliberal and radical political economy perspectives suggest two divergent outcomes for well-being as economic development and social service activities are undertaken by localized government. I analyzed social services as opposed to all public services because for both perspectives, a social service is the greatest point of contention. Again, my focus is the scope of county activities, a focus that
follows other studies assessing the scope of state/local governments’ economic development and service activities (Basolo & Huang, 2001; Clingermayer & Feiock, 2001; Jenkins et al., 2006).8

Measures
Descriptive statistics for variables used in the multivariate analyses are shown in Table 1. To assess changes in the scope of activity, I use two summary variables, one for economic development and the other for social services. Additive indexes of changes in 12 economic development policy activities and 10 social services activities were constructed. The same coding format was used in both indexes: county increased activity in past five years county provided activity at similar levels over past five years county did not provide activity or activity was cutback (less than 4% of counties reported any cutbacks). Other methods of coding these variables yield similar results as those reported below.9 The scope of economic development activity, measured by the number of different policy tools used, is an indicator of local government competitiveness (Basolo & Huang, 2001; Clingermayer & Feiock, 2001; Reese & Rosenfeld, 2002). As such, this index combines policy tools that have been seen as conceptually varying in quality. Tax abatements, for example, are considered lower quality attraction methods while strategies to retain local business by upgrading human capital are higher quality (Eisinger, 1988). However, recent studies find that although different in principle, use of high-low quality tools now tends to coincide empirically (Brace, 2002), as I find here also. Tax abatements are ubiquitous today, with activist governments using them in concert with other tools. To condense discussion, avoid multiple measures, and because empirically, counties’ uses of economic development tools are interrelated so that different combinations of them yield similar results, I use a single measure (see Note 9). Cronbach’s alpha coefficient is 0.85 for the economic development index and 0.84 for the social service index. The two indexes correlate significantly at r = 0.301. Thus, in contrast to a trade-off between growth promotion and social service activities, the same counties report expanded involvement in both.

The third perspective on the local state and past empirical work (Lobao et al., 1999) indicate that subnational variations in both government policy responses and general well-being are related to five factors: (1) institutional arrangements among the state, citizens, and capital; (2) economic structure; (3) internal attributes specific to each locality such as population composition; (4) external, geographic location; and (5) past history. These factors reflect local needs and capacity to engage in economic development and
Table 1. Descriptive Statistics for all Variables$^a$.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Economic development activity</td>
<td>5.838</td>
<td>(5.048)</td>
</tr>
<tr>
<td>Social service activity</td>
<td>5.641</td>
<td>(4.821)</td>
</tr>
<tr>
<td>Reported funding shortages</td>
<td>2.145</td>
<td>(3.166)</td>
</tr>
<tr>
<td>Median family income, 2000 Census</td>
<td>$42,228.34</td>
<td>(9,519.31)</td>
</tr>
<tr>
<td><strong>Institutional Arrangements</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Per capita federal income transfers</td>
<td>3.774</td>
<td>(0.825)</td>
</tr>
<tr>
<td>Local government revenues/expenditures</td>
<td>1.002</td>
<td>(0.110)</td>
</tr>
<tr>
<td>Per capita federal funding changes</td>
<td>$1,232.38</td>
<td>(1,349.80)</td>
</tr>
<tr>
<td>Revenue state and federal sources/total</td>
<td>0.756</td>
<td>(0.314)</td>
</tr>
<tr>
<td>Service demand pressures</td>
<td>2.222</td>
<td>(0.743)</td>
</tr>
<tr>
<td>Service privatization</td>
<td>0.243</td>
<td>(0.429)</td>
</tr>
<tr>
<td>Welfare devolved to county$^b$</td>
<td>26.75</td>
<td></td>
</tr>
<tr>
<td>Devolution-related pressures</td>
<td>8.397</td>
<td>(2.448)</td>
</tr>
<tr>
<td>% Budget for business attraction</td>
<td>21.37</td>
<td>12.86</td>
</tr>
<tr>
<td><strong>Interest group involvement</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>NGOs</td>
<td>1.589</td>
<td>(0.848)</td>
</tr>
<tr>
<td>Real estate business</td>
<td>2.131</td>
<td>(0.975)</td>
</tr>
<tr>
<td>General business</td>
<td>1.899</td>
<td>(0.768)</td>
</tr>
<tr>
<td><strong>County government capacity</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government size</td>
<td>344.184</td>
<td>439.863</td>
</tr>
<tr>
<td>Grant writer on staff$^b$</td>
<td>33.92</td>
<td></td>
</tr>
<tr>
<td>Industrial park$^b$</td>
<td>36.71</td>
<td></td>
</tr>
<tr>
<td><strong>Economic Structure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>% Extractive employment</td>
<td>11.04</td>
<td>(9.90)</td>
</tr>
<tr>
<td>% Nondurable manufacturing</td>
<td>8.01</td>
<td>(7.32)</td>
</tr>
<tr>
<td>% Durable manufacturing</td>
<td>9.91</td>
<td>(6.63)</td>
</tr>
<tr>
<td>% Unemployed</td>
<td>5.78</td>
<td>(3.02)</td>
</tr>
<tr>
<td><strong>Population Characteristics</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>% College graduates</td>
<td>13.49</td>
<td>(6.33)</td>
</tr>
<tr>
<td>% Population &gt; age 65</td>
<td>15.17</td>
<td>(4.64)</td>
</tr>
<tr>
<td>% Population change</td>
<td>7.48</td>
<td>(11.03)</td>
</tr>
<tr>
<td>% Latino</td>
<td>5.49</td>
<td>(11.83)</td>
</tr>
<tr>
<td>% Black</td>
<td>7.71</td>
<td>(13.03)</td>
</tr>
<tr>
<td>Population size</td>
<td>84,109.623</td>
<td>(304,677.124)</td>
</tr>
<tr>
<td><strong>Geographic Location$^b$</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>25.74</td>
<td></td>
</tr>
<tr>
<td>Nonmetro adjacent</td>
<td>24.02</td>
<td></td>
</tr>
<tr>
<td>Nonmetro nonadjacent</td>
<td>50.24</td>
<td></td>
</tr>
<tr>
<td>Major highway</td>
<td>48.39</td>
<td></td>
</tr>
</tbody>
</table>

$^a$ Values are rounded to two decimal places.

$^b$ Values are rounded to one decimal place.
social service activities (Reese & Rosenfeld, 2002), and they are long-standing correlates of measures of local well-being (Lobao et al., 1999). Independent variables tapping each of these five components were used. Because the dependent variables, economic development and social service activity, measure change over the past five years (e.g., 2001–1997) independent variables were selected to be causally prior. This constrains the time period for which key independent variables can be drawn. In addition to survey data, I draw from the U.S. counties (U.S. Bureau of the Census, 1999) which compiles federal data for demographic and economic variables for inter-census years and the Census of Governments. Each independent variable is selected to be closest in time period to 1997.

Institutional arrangements are measured by variables tapping aspects of state-citizen-business relationships, particularly variables related to decentralization. Variables constructed from secondary data are: per capita income transfers (total from federal sources/population, a measure of government dependence); the ratio of local government revenues to expenditures; change in per capita federal funding over 1997–1990; and proportion of local government revenue from state/federal sources. Variables constructed from the survey data include a summated index of officials’ reports of four types of pressures related to devolution over the past five years (loss of federal revenue, loss of state revenue, mandated costs from federal and state government, and state tax and expenditure limits), with each of these coded 3 (very important problem), 2 (somewhat important) and 1 (not important). Officials were also asked about problems due to rising citizen service demands over past five years, with this variable coded 3 (very important problem), 2 (somewhat important) and 1 (not important). Privatization, long considered an indicator the neoliberal roll-out (Kodras, 1997), was assessed by asking officials whether or not any county public service was privatized in the past five years (24% of officials responded affirmatively). The county’s location in a state that devolves

<table>
<thead>
<tr>
<th>Historical Factors</th>
<th>Mean</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Past AFDC per capita, 1990</td>
<td>$177.24</td>
<td>(61.14)</td>
</tr>
<tr>
<td>Median family income, 1990 Census</td>
<td>$43,647.00</td>
<td>(10,303.75)</td>
</tr>
</tbody>
</table>

aStatistics shown are for county-government units unweighted by population size.
bCategorical variables, percent of counties reporting.
welfare to the county level and the proportion of its economic development budget devoted to external business attraction were included. As the local institutional literature notes the importance of local actors in economic development, included are officials’ reports about involvement of three groups in the “county’s economic development agenda”: nongovernmental organizations; commercial and industrial real estate; and general business, specifically, manufacturing and services. These were measured on a scale from 1 (little or none) to 4 (high) involvement. Local government resources/capacity variables are collected from the survey and include: county government size; presence of a grant writer on staff; and presence of an industrial park.

Economic structural attributes include: local economic base, measured by the proportion of employment in the extractive sector and non-durable manufacturing (both generally producing lower earnings) and durable manufacturing (generally producing higher earnings), with remaining services as the excluded category; and percent unemployed.

Population characteristics include: percent college graduates, population over age 65, population size (logged), percent change in population from 1990 to 1997, percent Latino, and percent black population.

Geographic location in the national political economy is measured by metro, nonmetro adjacent, and remote nonmetro location. While past studies anticipate metro–nonmetro differences, whether these differences will remain in multivariate models is unclear. To further address location, I add a variable designating whether the county is located on a major highway.

Past history of social welfare policy is measured by using AFDC per capita, a generosity measure of the former social welfare program. Past economic well-being is measured by median family income. Both are from 1990 sources.

Multivariate Models
Ordinary least squares regression is used for the models presented in Table 2. Use of counties raises certain methodological issues, which I considered. Among these is potential heteroskedasticity, which affects the size of the standard errors of coefficients. The significance levels in Table 2 are based on using the robust standard errors as a correction.

Rural–Urban Differences in Models
For all four models in Table 2, I first ran preliminary models (not shown) regressing the dependent variables on metro–nonmetro status variables
Table 2. County Governments’ Economic Development and Social Service Activities and Local Well-Beinga.

<table>
<thead>
<tr>
<th>Institutional Arrangements</th>
<th>Economic Development Activity</th>
<th>Social Service Activity</th>
<th>Reported Funding Shortages</th>
<th>Median Family Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Per capita federal income transfers</td>
<td>0.560*</td>
<td>0.043</td>
<td>0.014</td>
<td>−1112.66***</td>
</tr>
<tr>
<td>Local government revenues/ expenditures</td>
<td>0.306</td>
<td>0.741</td>
<td>−0.550</td>
<td>−1860.23**</td>
</tr>
<tr>
<td>Federal funding changes</td>
<td>0.026</td>
<td>0.077</td>
<td>0.009</td>
<td>0.03</td>
</tr>
<tr>
<td>Revenue from state/federal sources</td>
<td>0.294</td>
<td>−0.032</td>
<td>0.540</td>
<td>71.85</td>
</tr>
<tr>
<td>Service demand pressures</td>
<td>0.300</td>
<td>0.680***</td>
<td>0.362***</td>
<td>−25.20</td>
</tr>
<tr>
<td>Service privatization</td>
<td>0.641*</td>
<td>0.988***</td>
<td>0.211</td>
<td>−132.47</td>
</tr>
<tr>
<td>Welfare devolved to county</td>
<td>1.277***</td>
<td>1.207***</td>
<td>0.823***</td>
<td>268.23</td>
</tr>
<tr>
<td>Devolution-related pressures</td>
<td>0.066</td>
<td>0.176**</td>
<td>0.210***</td>
<td>1.46</td>
</tr>
<tr>
<td>Budget for business attraction</td>
<td>1.019***</td>
<td>0.037</td>
<td>0.137</td>
<td>28.20</td>
</tr>
<tr>
<td>Interest group involvement</td>
<td>NGOS</td>
<td>0.224</td>
<td>0.315*</td>
<td>0.117</td>
</tr>
<tr>
<td>Real estate business</td>
<td>0.229</td>
<td>−0.010</td>
<td>0.355***</td>
<td>−92.64</td>
</tr>
<tr>
<td>General business</td>
<td>0.885***</td>
<td>0.390*</td>
<td>−0.106</td>
<td>125.67</td>
</tr>
<tr>
<td>County government capacity</td>
<td>Government size</td>
<td>0.228</td>
<td>1.520**</td>
<td>−0.141</td>
</tr>
<tr>
<td>Grant writer on staff</td>
<td>0.881***</td>
<td>0.812***</td>
<td>0.194</td>
<td>88.54</td>
</tr>
<tr>
<td>Industrial park</td>
<td>1.936***</td>
<td>1.055***</td>
<td>−0.028</td>
<td>−26.05</td>
</tr>
<tr>
<td>Economic Structure</td>
<td>% Extractive employment</td>
<td>−0.005</td>
<td>−0.042</td>
<td>−0.003</td>
</tr>
<tr>
<td>% Nondurable manufacturing</td>
<td>0.021</td>
<td>0.010</td>
<td>0.005</td>
<td>−23.04*</td>
</tr>
<tr>
<td>% Durable manufacturing</td>
<td>0.048</td>
<td>0.015</td>
<td>0.003</td>
<td>64.75***</td>
</tr>
<tr>
<td>% Unemployed</td>
<td>0.023</td>
<td>0.015</td>
<td>0.064*</td>
<td>−115.80***</td>
</tr>
<tr>
<td>Population Characteristics</td>
<td>% College graduates</td>
<td>−0.039</td>
<td>−0.040</td>
<td>0.035</td>
</tr>
<tr>
<td>% Population &gt; age 65</td>
<td>−0.062</td>
<td>−0.021</td>
<td>0.025</td>
<td>192.21***</td>
</tr>
<tr>
<td>Population change</td>
<td>−0.050***</td>
<td>−0.012</td>
<td>0.011</td>
<td>98.02***</td>
</tr>
<tr>
<td>% Latino</td>
<td>0.008</td>
<td>0.021</td>
<td>0.025**</td>
<td>−19.34**</td>
</tr>
<tr>
<td>Population size</td>
<td>0.435*</td>
<td>−0.212</td>
<td>−0.100</td>
<td>−453.33***</td>
</tr>
<tr>
<td>% Black</td>
<td>0.008</td>
<td>−0.001</td>
<td>−0.006</td>
<td>−3.89</td>
</tr>
<tr>
<td>Geographic Locationb</td>
<td>Metropolitan</td>
<td>0.184</td>
<td>0.060</td>
<td>0.890**</td>
</tr>
<tr>
<td>Nonmetro adjacent</td>
<td>−0.156</td>
<td>0.333</td>
<td>0.074</td>
<td>17.57</td>
</tr>
<tr>
<td>Major highway</td>
<td>0.066</td>
<td>0.312</td>
<td>−0.091</td>
<td>34.63</td>
</tr>
</tbody>
</table>
alone. These variables all have statistically significant relationships with each of the dependent variables. As discussed below, these significant metro–nonmetro differences disappear in two models and markedly decline in the remaining two models when other independent variables are added, indicating these differences are largely function of other county characteristics. Nearly all independent variables above differ significantly by metro–nonmetro status. Rural disadvantage is greatest across variables indicating poorer local economic structure and lack of government capacity and greatest for remote rural (nonmetro, nonadjacent) counties. Thus, rural–urban differences are largely rooted in other territorial inequalities related to institutional, economic structural, population, and historical factors reflecting rural disadvantages.

**Changes in Economic Development and Social Services Activities**

Preliminary models regressing economic development and social service activities on metropolitan status variables alone follow a distinct spatial pattern: metro governments, followed by adjacent governments, report increasing a greater number of activities relative to remote governments.

Table 2. (Continued)

<table>
<thead>
<tr>
<th>Historical Factors</th>
<th>Economic Development Activity</th>
<th>Social Service Activity</th>
<th>Reported Funding Shortages</th>
<th>Median Family Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Past AFDC per capita</td>
<td>0.005</td>
<td>0.020</td>
<td>0.006</td>
<td>5.68</td>
</tr>
<tr>
<td>Median family income, 1990 Census</td>
<td>0.074c</td>
<td>0.492c</td>
<td>−0.212c</td>
<td>1.43***</td>
</tr>
<tr>
<td>Economic development activity</td>
<td>—</td>
<td>—</td>
<td>0.008</td>
<td>−49.35**</td>
</tr>
<tr>
<td>Social service activity</td>
<td>—</td>
<td>—</td>
<td>0.130***</td>
<td>25.35</td>
</tr>
<tr>
<td>Reported funding shortages</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>33.60</td>
</tr>
<tr>
<td>Adjusted-$R^2$</td>
<td>0.384</td>
<td>0.202</td>
<td>0.194</td>
<td>0.931</td>
</tr>
</tbody>
</table>

*Unstandardized OLS regression coefficients are reported. Significance levels are based on t-values using robust standard errors.

* $p<0.05$,

** $p<0.01$,

*** $p<0.001$.

bComparison category for metro/nonmetro adjacent counties is remote rural (nonmetro, nonadjacent) counties.

cCoefficients X 1,000.
In both models, these statistically significant differences disappear when other independent variables are added. Here, I focus on significant findings for the remaining independent variables.

The first model (Table 2) shows attributes associated with increases in the scope of economic development activities. Findings for institutional arrangements indicate that both business and the state influence activities. Significant increases in activities are found in counties the report higher budgeting for business attraction and greater influence of general business firms (i.e., in manufacturing and services) in county development activities. These findings are expected from the local institutional literature, where larger budgets and political involvement of business sectors that may be targeted program beneficiaries, should increase the number of policy tools used (Jenkins et al., 2006; Reese & Rosenfeld, 2002). Increases in the scope of economic development activity are also found where populations have greater per capita dependence on income transfers (suggesting the need to expand private sector investment), and where a county service was privatized. Counties located in states that devolve welfare to county government report increased economic development activities. This may be related to the historical context of devolution, insofar as such states may have a political culture of county government activism. However, it also suggests that with devolution of TANF, counties in such states now face greater pressure to engage in economic development to supplement welfare activities. Government capacity and resources, reflected in grant writing staff and having an industrial park, are related to increased development activities as expected. Other variables related to increased activities include: a slower growing population, which suggests a need to attract investment; and larger population, also indicative of large localities’ ability to engage in economic development.

For social services, increases in the scope of activities are most closely associated with institutional arrangement variables (see Table 2, second model). Increases are reported where: counties are experiencing greater pressure from devolution (e.g., index of pressures); service demands from citizens have risen; the influence of both the nongovernmental and business community in county development activities is greater; and welfare is devolved to the county level. Counties that privatized a service in the past five years, also had greater social service activity, in contrast to expectations from the political economy perspective. This finding suggests that privatization thus is not necessarily a harbinger of broader social service dismantling and may be undertaken for other local efficiencies. Where past welfare (AFDC) benefits were higher, counties also have undertaken a
greater scope of activities, indicating that local traditions of greater support for the poor persist over time. These results suggest where decentralization processes are stronger, counties have responded not by cutting back, but by increasing the scope of their activity. Local actors also play a role in increasing social service activities. Findings for the general business community suggest its needs complement the local state’s increased involvement in redistribution, a finding in accordance with recent work from the general political economy perspective (Peck & Tickell, 2002). Finally, government capacity variables are all significantly positive associated with increased social service activities.

The Well-Being of County Governments and their Citizens
Most studies on the determinants of subnational governments’ economic development and service activities fail to extend the research question further, to assess whether these activities have outcomes for well-being. Analysts, however, recognize the importance of this question (Jenkins et al., 2006). To what extent are increased local responsibilities related to other aspects of well-being? Does decentralization produce a race to the bottom or top? I provide a limited analysis of well-being outcomes. To examine county well-being, I used two measures. The first was directed to county government itself, reported funding shortages. Officials were asked “Does your county government face funding shortages for any of the following social services?” I summed the number of affirmative responses to a menu of 15 social services. Cronbach’s alpha for this index is 0.88. The second is median family income, as noted, a commonly used measure of economic well-being. Funding shortages for social programs are anticipated by the political economy approach as an outcome of decentralization; and both the political economy and neoliberal perspectives would expect impacts on family incomes, but in opposing directions. Independent variables used in the models were all those noted above, plus the indexes for increases in economic development and social service activity.

Funding shortages. A preliminary model (not shown) confirms earlier descriptive findings that metro counties experience funding shortages in a greater number of areas than both adjacent and remote rural counties. As shown in Table 2, these differences diminish, but remain significant between rural remote and urban counties when other independent variables are added.

Counties that increased the scope of their social service activities report funding shortages in a greater number of areas. Increases in economic development activities are not significantly related to funding shortages.
However, counties that devote a higher proportion of their budget to outside business attraction report somewhat more funding shortages ($p = 0.06$), indicating that budgets directed to less sustainable growth strategies may stress social programs. Funding shortages are also related to other institutional variables, where: counties face greater pressures in responding to decentralization; service demands from citizens are higher; and welfare is devolved to the county level. Where involvement of the real estate industry in county economic development activities is greater, funding shortages are reported to be higher. This suggests that real estate interests may contribute to social service funding problems as they push for growth-machine initiatives that increase population (Logan & Molotch, 1987). Funding shortages are also greater where the Latino population is higher. Analysts (Saenz, 2005) have noted that owing to educational attainments and need for English language skills, Latinos are disadvantaged in the labor market: counties with a higher proportion of Latinos may face greater funding stress on social programs as they respond to the distinct service needs of this population. To sum, with regard to the three perspectives on the neoliberal roll-out, relationships for decentralization-related variables show that decentralization appears to usher in funding pressures, a finding that is most clearly expected from the second perspective, the political economy approach.

**Median family income.** In the final model in Table 2, I regress median family income (from the 2000 Census of Population) on all the previous variables above. Since median family income (from the 1990 Census) is included as an independent, control variable, it provides most of the explained variance as would be expected. Counties reporting greater increases in the scope of economic development activities have significantly lower median family income. This suggests the ineffectiveness of growth promotion activities, a finding which corresponds to some local institutional perspectives (Logan & Molotch, 1987). That is, local governments are expected to have no or minimal effects on improving local fortunes whose determinants are more deeply rooted in structural economic conditions. Further, in contrast to neoliberal criticism that publically provided social services will reduce local income levels, an increase in the scope of social services has no significant effect. Where counties have greater expenditures relative to revenues, indicating better fiscal conditions, and a population less dependent on federal income transfers, indicating a less needy citizenry, income growth is higher. Higher income growth is also associated with higher durable manufacturing (a higher wage sector), lower extractive and nondurable manufacturing employment (both lower wage sectors), and
lower unemployment. These relationships follow past studies that find better quality employment, and lower unemployment are related to higher county economic well-being over time (Lobao et al., 1999; Nielsen & Alderson, 1997). Population attributes such as a higher proportion of college graduates, population growth, and lower Latino population are also related to income growth, relationships which follow past studies above as well. When all covariates are included, metro areas have greater income growth relative to other counties.

CONCLUSIONS

This paper informs a large public and social science debate over the appropriate role of the state in society. Two opposing positions on this debate, the neoliberal and radical political economy frameworks have developed. The former framework now overpowers the latter in economic development and social policy discourse and guides the roll-out of the neoliberal development model. I evaluate how claims from both frameworks operate “on the ground” for the local state and across the subnational scale. In doing so, I introduced a third, intermediate view which takes account of institutional and path-dependent processes that may modify results expected from the two general frameworks above.

To empirically assess the three respective positions, I draw from a unique survey of county governments, now the fastest growing local governments. These data have both strengths and weaknesses. The survey provides the first nationally representative data on county governments’ economic development and public service activities. Little is known about these activities, as detailed, generalizable secondary data do not exist. As discussed, surveys of government officials are used widely by those studying other units (e.g., states and municipalities) to collect data unavailable from secondary sources. However, surveys of officials have limitations, among them the types of variables that can be collected. In addition to survey issues, it should be noted that the topic of this paper centers on policy responses in terms of the scope of activities undertaken. This topic follows a long tradition in political sociology but it is not the same as assessing spending, a point made by Jenkins et al. (2006) who examine the scope of activities undertaken by state governments. Finally, it should be recognized that there are quality differences in economic development activities. An order to condense discussion, these differences was not pursued separately in multivariate analyses.
This study provides the following assessment of the three previous perspectives on the neoliberal roll-out. First, the study supports the view of a broad movement towards decentralized government, a policy shift advocated by the neoliberal development model. But in contrast to the neoliberal and political economy perspectives, there does not appear to be a trade-off between pursuit of growth and redistribution activities – rather counties are actively engaging in both economic development and social/other public service activities. Nationally across counties, increases rather than decreases in the scope of economic development, general public, and social services were reported. The same counties reporting increased economic development activity are also more likely to report increased in public service and social welfare activity. Multivariate regression analysis findings that counties in states that have devolved welfare (TANF) to the county level are more activist in both economic development and social services, particularly illustrate that counties are not trading off one activity for another. In contrast to neoliberal hopes that devolving welfare to subnational governments would reduce the social safety net overall, the scope of activities has in fact widened in these counties.

In sum, the policy agenda behind neoliberals’ calls for decentralization, to dismantle government involvement in public/social services does not appear to have materialized. If counties were embracing the neo-liberal model (and low road to development according to political economists), we would expect to see: counties’ cutting the public/social services they provide as opposed to expanding these services; and incompatibility between activism in economic development and public service provisioning as opposed to the compatibility of activism in both arenas.  

Second, the study tends to support the third, intermediate framework on the neoliberal roll-out, which argues for path dependence in response to decentralization and anticipates the continuation of long-term rural–urban patterns of inequality. As expected from this framework, an expanded scope of activities are associated with larger, urban governments, and with greater governmental capacity and resources. Evidence of continued marginalization of rural governments under decentralization include: comparative increases in less sustainable development activities as reflected in budgeting for outside business attraction; less ability to place welfare recipients in jobs; and greater fiscal pressures reported from loss of federal and state funds. At the same time, nonmetro officials report facing fewer funding shortages for social programs because they simply have fewer programs in the first place.

Third, there are implications for a presumed global march toward neoliberalism anticipated by the neoliberal and political economy frameworks.
Survey findings show the spatial unevenness of this trend. Some governments will provide a strong social safety net, protecting their poor and citizens at large, while being players in an increasingly territorially competitive environment. Others will provide a minimal social safety net and remain in the backwaters of the global economy. Findings also caution against grouping changes related to decentralization as a homogenous, neoliberal package. For example, the most activist counties combine business attraction, human capital upgrading, and research and development, as opposed to mainly pursuing the former policies at the expense of the latter two. Privatization is not necessarily a marker of reduced public commitment and was related to expanded social service activity.

Given neoliberal emphasis on decentralization as a way to unleash market forces, generate growth and raise living standards – Is there evidence that citizens and their communities have reaped benefits over the past decade? My findings suggest that is not the case. Counties as a whole report increased funding shortages, indicating negative outcomes of decentralization as expected from the political economy framework. While this may serve neoliberal interests (insofar that it could lead to reduced government), counties are expanding their activities despite these pressures. Findings for median family income dispute neoliberal assertions that social service activities depress growth and that business promotion activities increase it. In sum, an increased burden of responsibilities has meant pain for local governments but no clear gain for citizens and their localities. Of the three views about how local government and citizens fare, findings are thus closer to the political economy and to the spatially sensitive, mixed approach. In contrast to the neoliberal view, there is no evidence of a race-to-the-top. Findings show that local governments are stressed, but their expanded social service activity provides little evidence they are marching in a race-to-the-bottom at this time.

NOTES

1. By neoliberal roll-out, Peck and Tickell (2002) refer to expansion of the neoliberal development model, its preferred form of market relationships and system of governance. I employ neoliberalism in three ways to refer to: the neoliberal development model; the current period of presumed deployment of this model; and a conceptual framework on the state.

2. Analysts view decentralization as a process by which local governments, whether by mandate or by choice assume responsibility for a wider range of public
functions (Kodras, 1997; Razin, 2000). National shifts toward decentralization of growth promotion and public service activities cannot be simply reduced to the roll-out of the neoliberal development model which analysts note began in the Reagan era (Peck & Tickell, 2002). U.S. local governments have historically engaged in growth promotion, but their role expanded in the Reagan era (Peterson, 1995). Decentralized public service provision has long been advocated to increase the responsiveness of government to citizens (Tiebout, 1956). However, critics of the neoliberal roll-out stress that regardless of the origins of decentralization, it is now a pillar of the neoliberal development model because it is assumed to produce a more minimalist social safety net and increase the power of the corporate sector (Brenner, 2004; Ruben, 2001).

3. The Census of Governments has other limitations in studying economic development and public service activities. Data collected by the Census is provided in many states by the state (not the county directly), creating variations in data quality. The Census is the only national source of financial data on own-source county expenditures. But missing data for economic development and public services is excessive, aggregated upward into general financial categories and not available in disaggregated form for many counties.

4. To develop the questionnaire, the research team worked extensively with NACo in conducting focus groups and in protesting the survey instrument with county officials in each of 46 states. For more details regarding survey methodology, see Lobao and Kraybill (2005).

5. To examine response bias, I used logistic regression with response/non-response as the dependent variable and with major county attributes as independent variables: unemployment, median family income, population size, metropolitan status, and region of the county. Counties that responded to the survey did not vary in significant ways from those not responded. I also examined the potential for bias due to officials’ characteristics. I regressed three dependent variables shown in Table 2 (index of economic development, index of social service activities, and funding shortages) on officials’ education, age, gender, and length of time in county employment. There were no statistically significant differences.

6. Median government size as measured by employment is 840 for metro counties, 268 for adjacent counties, and 125 for remote counties.

7. Officials were asked, how has the focus of your county’s economic development efforts changed? Fifty-two percent of metro governments, 41% of adjacent governments, and 34% of remote governments report a greater focus on business retention and expansion activities today as compared to five years ago. Thirty-three percent of metro, 29% of adjacent, and 26% of remote governments report a greater focus on small business development for local entrepreneurs. Forty-two percent of metro, 41% of adjacent, and 36% of remote governments report a greater focus on business attraction. Thus, over the past five years, while metro counties have shifted their portfolio of development activities toward business retention and expansion, remote counties place somewhat more emphasis on fiscally less sustainable business attraction activities.

8. These studies treat the scope of activities as the policy arenas in which government operates, and likewise use a count of activities as dependent variables. A different research question entails government spending. Expenditure data below the
state level (for counties as well as municipalities) does not exist systematically across
the nation for the detailed functional domains used in this study, economic
development, public services, and social welfare services.

9. Other methods of coding these variables such as counts of increases only or
counts of decreases only produce nearly identical results. Since few (1–4%) counties
reported any cutbacks, this response was combined with the “not done” category.
The index of economic development activities is composed of the following policy
tools: tax abatements, national advertising of county as a place to do business,
national travel to recruit new business, travel outside U.S. to recruit new business,
workforce development for low-income workers, worker training for local
businesses, technology transfer to small communities, subsidized loans, loans/grants
for exporters, tax increment financing of infrastructure, collaborative planning with
other local governments, economic development assistance to small communities.
The number of policy tools used (i.e., activities undertaken) by local governments is
often used to measure the degree of economic competition in which these
governments are engaged (Reese & Rosenfeld, 2002). The index of social service
activities includes: child care, drug-alcohol rehabilitation, elder care, food pantry,
homeless shelter, housing assistance, mental health services, nutrition programs,
Senior citizens program, and shelter for battered persons. Separate logistic
regressions were performed using each economic development tool and social
service activity as a dependent variable; also, different combinations of these tools/
activities were employed in the models of funding shortages and median family
income. As a whole, results are similar for those reported in Table 2 which uses the
summary indexes. Confirmatory factor analysis was used to verify that the items
(activities) in each index are highly intercorrelated and load on a single factor. To
condense discussion and because each activity cannot be included separately (due to
collinearity) in the models for funding shortages and family income, I use the
summary indexes.

10. The original source of these data is the 1997 Census of Government.
11. The detailed measures of local economic base are available only from the
Census of Population and the 1990 Census is used since it is prior in time to the
change indexes. For construction of the AFDC per capita measure, see Lobao and
12. These issues include the potential for collinearity, use of state-effects, spatial
autocorrelation, and heteroskedasticity. Variance inflation factors indicate no high
collinearity. I considered the use of fixed-effects for state (since random effects
require independent variables that are independent of state, an assumption not
tenable in a study of local governments). However, state-effects create high levels of
collinearity in the models in part because the decentralization variables already
account for much of the state-level variation between counties. Therefore, because in
a large sense the state-level state is already controlled and because of collinearity, I
chose not to include state-effects in the models. Sociologists normally address spatial
autocorrelation when they have a set of contiguous counties from which they can
model spatial dependence and error. The data here, however, are not contiguous
counties, but rather are a subnational sample. Heteroskedasticity, where the error
term is not constant across all values of each of the independent variables, is often
found in models using county-level data and is a minor issue here. The significance
levels reported in Table 2 are based on the \( t \)-statistics using robust standard errors based on White’s (1980) correction. Only three coefficients in the entire table are affected. Since Table 2 is lengthy in number of independent variables, I do not show the standard errors or the \( t \)-statistics, but they are available from me.

13. Variables to assess well-being impacts are limited. The survey focused on determinants of decentralization but contains few items that serve as outcome measures. Data to assess general population well-being, such as median family income, is mainly available from the 2000 Census of Population, which is a limitation to assess outcomes. Median family income, as most economic variables in the Census, refers to the previous year. The social service/economic development items refer to changes from 1997 to 2001, so that there is not an ideal time lag in assessing family income outcomes. It should be noted that the model for median family income is a cross-sectional model that controls for the previous Census’ value of median family income. It is not a true time-series model where Durbin–Waston \( d \) or Durbin \( h \) are appropriate tests. However, an assumption of OLS regression is that the residuals are not correlated with the independent variables, which may be a problem when a lagged variable is included in a cross-sectional model. I checked but did not find a significant correlation between the 1990 Census value of median family income and the residuals.

14. Another question involves direct spending on activities which one reviewer pointed out, might show that expenditures for social services increased but at a slower rate than economic development expenditures increased. As noted, no data exists that would allow examination of this relationship nationally across counties and the same is true for municipalities (Reese & Rosenfeld, 2002, p. 55; Wolman, 1996).

REFERENCES


PART III: POLITICAL AND ECONOMIC CHANGE AND NEOLIBERALISM IN DEVELOPING SOCIETIES
NEOLIBERALISM AND RACIAL REDRESS: INDIGENIZATION AND POLITICS IN TANZANIA AND FIJI

Erik Larson and Ron Aminzade

ABSTRACT

Accounting for the effects of neoliberalism on race relations in post-colonial societies requires analysis of processes of group formation and the meaning of neoliberal policies in relation to political contention about racial inequalities. To this end, we compare the politics of neoliberalism and racial redress in Tanzania and Fiji, examining political contention and the contextual effects of colonial legacies, post-colonial development strategies, and the timing of reform. In Tanzania, opposition politicians advanced indigenization policies as a defensive reaction against the redistributive consequences of neoliberal policies, whereas in Fiji proponents of indigenization used neoliberal economic policies as a means to advance their goals for racial redistribution. Consequently, indigenization policies and alternatives in Tanzania were framed as issues of race and citizenship, while in Fiji debate about these policies centered on the difference between race- and class-based preferences. Our findings highlight the role of political parties as an institutional terrain of identity-group formation and the importance of considering how implementation of neoliberal policies distributes costs and benefits in a manner that can remake political alliances.
What are the consequences of neoliberal policies for race relations in racially divided post-colonial societies? Amy Chua (2004) argues that such free market policies set the “world on fire” by increasing group-based inequalities. In a context of electoral democracy, impoverished majorities express grievances about these inequalities by intensifying racial and ethnic hostilities, spurring often violent action against economically privileged minorities. While this account provides grounds for understanding the potential unintended consequences of economic and political liberalization, it leaves out important socio-political dynamics that bring together interest and identity groups and that shape the meaning of policy in particular domestic contexts. To address these gaps, we analyze the connections between neoliberal policies, political contention, and policies of indigenization. We use the term neoliberalism to refer to market-oriented reforms – such as tax cuts, tariff reform, deregulation, and privatization – designed to reduce the role of the state in the economy, promote private ownership, and liberalize the flow of trade and investment. Indigenization policies are a specific form of affirmative action, granting preferential treatment to certain groups based on these groups defining themselves or being identified as “indigenous” to a particular country. Framed explicitly as racial redress – i.e., as attempts to correct racial inequalities by redistributing opportunities to historically disadvantaged groups – indigenization serves as a particularly insightful example of policy targeting economically privileged minorities.

We seek to understand the reciprocal effects of neoliberalism and indigenization policies on political contention by examining two related questions. (1) How did the politics of colonialism and post-colonial development strategies create the inequalities that subsequently gave rise to demands for racial redress (i.e., indigenization) in a context of neoliberal economic reforms? (2) How did the dynamics of competition for state power and political party formation shape debates about neoliberal and indigenization policies and influence the relationship between these two polices? To answer these questions, we document the racial legacies of colonialism and post-colonial development strategies and examine how multi-party contention for state power shaped both neoliberal and indigenization policies and international reactions to these policies.

Our analysis advances the developing bodies of literature in political sociology on comparative neoliberalism and on race and the state. We extend the literature on comparative neoliberalism by making two contributions. First, we supplement research concerning the paths to neoliberalism by analyzing the historical legacies that have shaped both the adoption of neoliberal economic reforms as well as the on-going
institutional effects of these reforms. Recent sociological analysis of neoliberalism finds that while a variety of international processes have led to the world-wide diffusion of neoliberal economic policies, differences in national conditions are associated with variation in the adoption of these policies (Fourcade-Gourinchas & Babb, 2002; Prasad, 2005). We extend this analysis by examining both colonial and post-colonial legacies that influence the adoption and consequences of neoliberal policies and the effects of neoliberalism on policies concerning racial redress. Second, in analyzing the implementation of neoliberal policies, we highlight the distributional effects of neoliberalism, drawing attention to the ways in which political contention shapes such distribution and, especially, to how distributing the costs and benefits of neoliberal reforms may remake race and class inequalities as well as political alliances.

In addition, we contribute to the literature on race and the state by analyzing the influence of political parties on racial identity and its political salience. In their recent review of this literature, James and Redding called on scholars “to identify the institutional arrangements that emphasize the importance of race and those that do not” (2005: 198). While studies of social class and political change have identified political parties as central determinants of how individuals experience their lives in terms of identities and class (Sartori, 1969; Przeworski & Sprague, 1986), scholars of nationalism and race relations have been much less attentive to the role of political parties and party struggles in the creation of national and racial identities. Institutions like parties are typically viewed as translators rather than creators of shared meanings of the nation or of the indigenous racial group. In contrast, we treat national and racial identities, as well as public policies, as outcomes of a continual process of political contention within the electoral arena and explore how divisions within and among parties shape political agendas and policy outcomes. Our analysis of political conflicts highlights the role of party politics as a terrain on which race and class relations are contested and institutionalized.

Our research compares how contemporary neoliberal policies in two racially divided former British colonies – Fiji and Tanzania – relate to current debates over the contentious political issue of racial redress for “indigenous” inhabitants. After explaining the logic of our case selection, we outline our analytical framework. We then present our comparative case analysis. We start this analysis by examining the historical legacies of colonial rule on post-colonial racial structures in Tanzania and Fiji. We next consider how post-colonial development strategies shaped contemporary debates about race relations and racial redress. Drawing
on a range of documentary materials – particularly parliamentary debates and newspapers, as well as interviews with key political actors – we then analyze how indigenization policies framed demands for racial redress in distinctive ways and how political parties and multi-party politics connected indigenization policies differently to neoliberal economic policies. We focus on the period from the mid-1980s to contemporary times, when debates over indigenization became salient features of the political landscape in both countries.

THE LOGIC OF CASE COMPARISON

Tanzania and Fiji share a number of important colonial legacies, as both are former British colonies whose legal system is based on commonwealth law. During colonialism, both countries saw considerable in-migration of South Asians, along with a variety of restrictive laws excluding the indigenous populations from capitalist activities. In both Tanzania and Fiji, British colonial rulers established tripartite racial divisions that constituted Asians/Indians (i.e., people of Indian and Pakistani origin), Europeans (i.e., all whites), and natives (i.e., all black Africans and all Pacific Islanders) as distinct races, in spite of the inherent complexities which this categorization hid. Despite considerable differences in the relative concentration of Asian populations – in Tanzania, Asians have always been a very small minority, while in Fiji both Indians and indigenous Fijians have comprised between 40 and 50% of the total population – both countries attempted to reject radical racial nationalism and suppress the most extreme elements of racial political mobilization after independence. Tanzania is an especially interesting case since, unlike other racially divided African countries that experienced popular hostility toward economically privileged minorities, post-colonial Tanzania embarked on a race-blind state socialist project designed to promote racial, as well as class and ethnic, equality. Finally, despite differences in population and per capita income, both Fiji and Tanzania occupy peripheral locations in the world capitalist economy and are similarly connected to international institutions, such as intergovernmental organizations and international non-governmental organizations (Larson & Aminzade, in press).

Comparing the dynamics of neoliberalism and indigenization in these two cases provides a solid basis to assess the potential of the policies to influence race and class inequalities, as well as to analyze the process and consequence of their institutionalization. Both countries have recently
experienced both the implementation of neoliberal economic reforms as well as impassioned debates about policies providing preferential treatment for groups identified as indigenous. Although similarities between the colonial legacies and post-colonial developments led to the proposal and adoption of relatively similar policies of indigenization and neoliberal reforms in each case, these two countries took different paths to neoliberalism and institutionalized race in the state and electoral politics in different ways.

We find a distinct relationship between neoliberal economic reforms and indigenization in our two cases, with affinities between neoliberal economics and indigenization in Fiji and conflict between these policies in Tanzania. In Fiji, indigenization and neoliberal economic policies reinforced one another when there were limitations on multiparty political contention, as both sets of policies were justified as necessary in response to political instability. In periods of open political contestation, parties debated about who benefited from indigenization policies, pitting class-based political mobilization against race-based mobilization. In Tanzania, the two policies were in conflict. Opposition political parties of the early 1990s targeted the growing racial inequalities resulting from neoliberal economic policies, using the issue of indigenization to challenge the ruling party and to call for race-based restrictions on property ownership and racial preferences in the privatization process. The ruling party responded by shifting the terms of the indigenization debate away from the Indian racial minority and toward foreign investors – especially South African investors – in an effort to redefine the meaning of the term indigenous.

**NEOLIBERALIZATION AND INDIGENIZATION: DISTRIBUTING INEQUALITY**

Neoliberal economic policies are fundamentally redistributive, while indigenization policies are responses to claims about the need for preferential treatment in the distribution of costs and benefits. Despite this fact and despite the simultaneous spread of affirmative action policies and neoliberal economic reforms in a number of countries (Alexander & Jacobsen, 1999; Parikh, 1997; Abdullah, 1997; de Silva, 1997; Gros, 1999; Fejos, 1996), the existing literature exploring the relationship between neoliberalism and indigenization is sparse and inconclusive. Most studies of indigenous politics either ignore the connection to neoliberal reforms or assume that
neoliberal policies, which sacrifice local interests in favor of greater participation in a competitive global economy, necessarily undermine or contradict efforts to attain preferential treatment for indigenous populations (Seuffert, 2005); however, some scholars have noted that neoliberal policies can promote indigenous identity (Tilley, 2002). Indeed, claims for indigenous status and rights may provide one of the few grounds to rationalize or legitimate group-based claims on scarce resources in a world in which neoliberalism has become increasingly hegemonic (Sissons, 2005).

While scholars have focused on neoliberalism as a defining feature of the contemporary world economy, recent critiques have suggested that these portrayals give insufficient attention to the “institutional hybridity, path specificity, and uneven development” characteristic of neoliberalization (Peck, 2004, p. 395; Larner, 2003). One such avenue of inquiry has successfully demonstrated the importance of variation in the specific national origins of neoliberalism (Fourcade-Gourinchas & Babb, 2002). While neoliberalism in countries in dependent positions in the global economy may often have external origins (Babb, 2005), this characterization does not capture the range of variation within the global south (Peck, 2004), which may be influenced by the legacies of colonial development and post-colonial development strategies. Further, characterizing neoliberalization as a top-down imposition underestimates the ways in which the changes associated with neoliberalism create possibilities for agency for some social actors (Larner, 2003; Peck, 2004), particularly as this agency relates to political party formation and contention for state power.

We focus on three aspects of the context-dependent relationship between neoliberalism and claims for racial redress. First, legacies of the history of the political economy of a country influence the meaning of policy proposals and, consequently, contention about and national patterns of policy-making (Prasad, 2005). Second we examine colonial legacies, since colonial states and economic orders have continuing effects on contemporary race relations (Mamdani, 1996; Steinmetz & Hell, 2006) and economic prospects (Lange et al., 2006). Finally, while the pace of neoliberalization serves as an important cross-national difference (Fourcade-Gourinchas & Babb, 2002), we suspect that other temporal characteristics – particularly sequencing and simultaneity – define the context of policy.

While neoliberal policies have similar types of effects – benefiting some actors with increased authority and access to resources, while imposing costs on others by decreasing their access to services and social support – the ways in which these effects are distributed may vary. In adopting and implementing neoliberal programs, policymakers confront questions about
how to allocate these costs and benefits. In privatizing state-owned enterprises, governments can select from different mechanisms to distribute ownership, such as vouchers, management buyouts, or competitive auctions (Stark, 1992, 1996). To decrease social spending, policymakers could eliminate programs, increase co-payments or user fees, or limit access to services to only targeted groups. Similarly, governments providing investment concessions could establish tax holidays targeted by industry or investor status. Given the varied consequences of neoliberal economic policy for inequality, we anticipate contention surrounding the distributional effects of such policies. In racially divided post-colonial societies, questions about distributing economic costs and benefits seem likely to involve the politics of racial redress.

While previous research has examined how states may promote policies of racial redistribution – such as indigenization policies – with economic growth (Esman, 1987), and how such policies create new indigenous capitalist classes (Larson & Zalanga, 2003), this research has not examined how neoliberal policy can interfere with or enhance policies of indigenization. Given that the implementation of neoliberal policies involves decisions about how to distribute inequality, we posit – in contrast to others (van der Westhuizen, 2002) – that neoliberalism does not simply limit states’ opportunities or abilities to implement indigenization. We do, however, suspect that in distributing inequality, these policies may remake political and economic alliances – including relations with foreign capital – which can influence domestic political contention and subsequent policymaking (Zeitlin & Ratcliff, 1988; Dezalay & Garth, 2002).

**HISTORICAL LEGACIES OF COLONIALISM IN TANZANIA AND FIJI**

The transitions to neoliberal economic policies and indigenization that we compare have occurred in countries whose populations and national institutions reflect the impact of colonialism and the transition to independence. The tripartite racial division of European, Asian/Indian, and native in Tanzania and Fiji differed based on how the subordinated groups were positioned economically and politically. As was the case in other parts of the globe (Marx, 1998), these differences in categorization affected the racial structures of the countries at and after independence.

Racial antagonisms in contemporary Tanzania are rooted in decades of British colonial policy that constituted Africans, Asians, and Europeans as
distinct races. All three of these groups were internally divided along lines of class, religion, and language, but colonial policymakers treated them as three distinct racial groups, with Asians occupying an intermediate location between Europeans and Africans in the racial hierarchy. The majority of South Asian migrants to East Africa arrived during the 20th century—many as “coolie” laborers on the railway at the beginning of the century or, after World War II, as merchants, shopkeepers, and clerks in the British colonial civil service (Gregory 1993; Nagar, 1996; Voigt-Graf, 1998). For example, colonial policies fostered a racial division of labor that prevented Africans’ access to credit and commerce and established Asians as commercial intermediaries (Coulson, 1982). Colonial officials discouraged Africans from obtaining trading licenses, colonial regulations limited the amount of goods that wholesalers could provide on credit to Africans to 600 shillings, and commercial courses in colonial schools were reserved for Asians (Rweyemamu, 1973, p. 29). Asians constituted a very small minority of the population in Tanzania throughout the 20th century, numbering only 71,660 in 1957 (Hopkins, 1966, p. 84) and never accounting for much more than 1–2% of the total population. But Asians were a highly visible and culturally distinct minority; they remained socially, residentially, and politically segregated from Africans, with few ties of marriage, kinship, or friendship across racial boundaries (Mangat, 1969; Gregory, 1993; Nagar, 1996; Voigt-Graf, 1998). Asians in British East Africa constituted what sociologists refer to as a “middleman minority,” occupying an intermediate niche in the economic system as traders, shopkeepers, moneylenders, and professionals (Bonacich, 1973).

The creation of an Asian middleman minority in East Africa was closely linked to the British colonial government’s political construction of race. The British created a political system in which each of the three races elected its own representatives, with separate voting rolls for Africans, Asians, and Europeans. Colonial rule created a rigid tripartite racial order reinforced daily by segregated schools, hospitals, prisons, and social clubs, racial patterns of residency and marriage, and a racial salary structure. Although Europeans were at the top of the colonial racial hierarchy, Africans directed their racial hostilities much more against Asians. As occupants of intermediate positions above Africans, Asians had more direct contact with Africans on a regular basis than Europeans, and they occupied the intermediate positions in the occupational hierarchy to which educated Africans aspired. Asians monopolized trade through interconnected family firms that joined importers to wholesalers to financiers to local shopkeepers, leaving Africans no point of entry. As supervisors of
African labor, shopkeepers selling daily necessities, or merchants purchasing African agricultural products, Asians came to be perceived by many African men and women as responsible for their exploitation and domination.³

During the struggle for independence, nationalist leaders in Tanganyika⁴ fought bitterly over both the role race should play in defining citizenship and over race conscious policies of Africanization. Opponents of racial nationalism, led by Julius Nyerere and the Tanganyika African National Union (TANU),⁵ confronted the African National Congress (ANC), a political party that advocated “Africa for the Africans.” Whereas the ANC advocated a citizenship law that distinguished between “indigenous inhabitants” and “other races who have made their homes in Tanganyika,” Nyerere and TANU leaders attacked advocates of race-based citizenship as racists and insisted that citizenship should be based solely on loyalty to the country (Tanganyika National Assembly Debates, October 17–18, 1961, pp. 333–334). Although the Asian minority constituted a small proportion of the population and posed no demographic threat at the polls, their privileged position made them the targets of proposals for redress of racial inequalities. After independence, a heated conflict over Africanization emerged; ANC leaders argued that true independence required limiting the civil service exclusively to black Africans. Opponents of rapid Africanization, led by Nyerere, contended that this restriction constituted reverse discrimination that would introduce inefficiency into the civil service and discourage foreign investment (Aminzade, 2000).

The historical legacy of colonial rule in Fiji also set the stage for subsequent conflicts over racial inequalities. On October 10, 1874, a group of high chiefs led by Ratu Seru Cakobau signed the Deed of Cession of Fiji to Great Britain, granting the British Crown sovereignty over the group of islands in return for a guarantee of security of Fijian landownership over nearly 90% of the land that had not been alienated by “Europeans or other foreigners.” After cession, the British established a system of indirect rule, through which a separate Fijian Administration insulated the Fijian populations from the colonial economy. The sugar-plantation based economy, however, faced a labor shortage, due to restrictions on Fijian participation and limited sources of labor from neighboring islands. In response, the British introduced a system of indentured labor, recruiting plantation workers from India under five-year indenture agreements (girimiti). Between 1879 and 1916, 60,965 girmitiyas (indentured laborers) came to Fiji, with a large majority remaining in Fiji at the end of the indenture period (Lal, 2004 [1983]).
This pattern of settlement led to a tripartite division in colonial Fiji: a small minority of European settlers, a largely plantation-laborer class of Indian immigrants, and a relatively isolated Fijian population. This division, and its associated separate paths of political development, influenced the composition of the colonial Legislative Council. Initially, the Council consisted of a super-majority of elected European members with a minority of Fijian members appointed by the Governor-General upon recommendation from the Council of Chiefs, the apex body of the Fijian Administration. An Indian member was first appointed in 1916 and, after a period of political mobilization, limited communal franchise was extended in 1929. Indian political leaders advocated for a common roll of voters, rather than separate European and Indian rolls. Due to the disproportionate number of seats on the Legislative Council granted to Europeans and the alliance between the European and Fijian members, these proposals were blocked. In 1963, as Fiji made initial moves toward independence, franchise was extended to Fijians and to women, although voting continued on communal rolls (Lal, 1992; Howard, 1991; Sutherland, 1992).

Economic and social divisions were also prominent in Fiji. The Fijian population was largely confined to village life and educational opportunities were limited primarily to missionary-schools for all but those of chiefly class, who attended elite boarding schools. Policies that restricted the movement of Fijians and their individual participation in the formal economy further cemented their confinement (White, 2001; Ministry of Finance and National Planning, 2002). By the 1940s, Indians constituted an absolute majority of the population. Most of the Indian population remained involved in agricultural production, but a small minority of “free” immigrants and former agricultural laborers established retailing businesses, forming an emerging Indian middle class. The largest enterprises, however, were owned by European families and foreign investors. Given the limited opportunities for political expression and restrictions on land ownership, Indian leaders frequently resorted to cane harvesting strikes (Ali, 1980; Lal, 1990). At the same time, the growth of the farming population required extending cane farming to indigenously owned land. The Fijian administration collected rent from the largely Indian farmers on behalf of the Fijian landowning groups.

The colonial legacies in Fiji and Tanzania differ mainly due to the economic and political positioning of subordinated groups. In contrast to Tanzania, colonial policies in Fiji more directly exploited the labor of the Indian population and imposed a greater degree of isolation on the indigenous population from formal economic activity. While this pattern changed over time (as free Indian farm labor was able to earn profit and as
shops were established), the nature and extent of economic contact was not one of direct exploitation of an indigenous majority by a racial minority, as in Tanzania. Perhaps more important, however, was the degree of contact between the Fijian chiefly elite and Europeans in Fiji. Efforts to integrate the elite through formal education and the continued common basis of Christianity enabled Fijians to draw on the Deed of Cession as the basis of loyalty to and identification with the Crown. (Indeed, a number of Fijians served in World War II for Britain, while Fiji Indians refused to serve, due to their disenfranchisement.) In addition to these historical and cultural connections, the European and Fijian leaders shared an interest in blocking demands for common roll, which could have resulted in an Indian-led government that was seen as potentially destabilizing the land ownership arrangements (Lal, 1990). In this sense, there is similarity between the cases: the non-indigenous, non-European immigrant was seen as a threat. The nature of the threat, however, was different: an uncontrollable majority in Fiji and a powerful economic minority in Tanzania.

In contrast to Tanzania, which used race-based representation in its pre-independence parliamentary election of 1958–1959 but then abandoned communal representation after independence, the British government plan for Fijian independence involved continued institutionalized racially based representation, in which seats were reserved for each major group. Some seats were elected solely on a communal basis, while other “cross-voting” reserved seats were elected by the entire population. Under Fiji’s 1970 Constitution, there was little dispute over who should be allowed to become a citizen; people who were born in Fiji or naturalized as commonwealth citizens in Fiji were automatically granted citizenship. In addition, individuals who were commonwealth citizens “deemed to belong to Fiji” were eligible to register for citizenship (Lal, 1992). Despite the lack of contention about citizenship, the creation of separate voter rolls and the distinct social positions of the groups created legacies of patterns of identification with the state, as noted by Steven Ratuva:

Not only was separation institutionalised, indigenous Fijian police and military were readily deployed to contain any threat to the colonial state by Indo-Fijians. An example was the use of the predominantly indigenous Fijian police and military to suppress Indo-Fijian strikes. (1999: 87)

In both Tanzania and Fiji colonial rule institutionalized a tripartite racial order that subsequently shaped post-independence development strategies and struggles over racial inequality. These racial orders excluded indigenous African and Fijian populations from formal economic activity, while either
encouraging or, at least, not limiting Asian/Indian participation in the formal economy. This colonial racial order had the effects of concentrating wealth and capital disproportionately in the hands of Asians/Indians and constructing races as separate groups. The combination of these two colonial legacies laid the foundation for the political salience of racial inequalities. In the next section, we document how post-independence governments grappled with racial inequality in their development strategies and in addressing demands for racial redress.

INDIGENIZATION, NEOLIBERALISM AND POST-INDEPENDENCE DEVELOPMENT STRATEGIES

The post-independence development strategies of Fiji and Tanzania influenced the meaning and consequences of neoliberalism and indigenization in both countries. In this section, we focus on the place of these policies in relation to the trajectories of post-independence economic policies. In Tanzania, neoliberal economic reforms were introduced in a short period of time by the same ruling political party that had directed the socialist experiment, sharply reversing two decades of state socialism. In Fiji, neoliberal reforms were introduced over a longer period of time. The most concentrated changes occurred under unelected governments in the aftermath of coups, which also coincided with realignments of political parties. Advocates of indigenization in both cases based their arguments on economic inequality (whether actual or perceived), contending that an “immigrant” group (as opposed to colonial settlers or their descendents) had succeeded economically either at the expense of (in the case of Tanzania) or instead of (in the case of Fiji) an “indigenous” group.

After independence, Tanzanian nationalists instituted a single party socialist state, restricting freedom of association and assembly and prohibiting the public expression of racial, ethnic, or religious hostilities as a threat to national unity. The newly independent government rejected the tripartite racial order that had underpinned colonialism and called on all citizens, regardless of race, to help build the new nation. In 1967, the government announced a socialist development strategy calling for the equality of all citizens regardless of race. In rejecting group-based preferential treatment based on race, the government insisted that its economic policies were aimed at capitalists of all races.

Despite race-blind policies, anti-racist admonitions from top political leaders, and laws preventing the public expression of racial animosities,
African hostilities toward the minority Asian community persisted. These animosities were expressed in a racially coded discourse of class which targeted wealthy Asians as capitalist exploiters. Most of the people arrested during the socialist government’s campaigns against illegal hoarding, corruption, racketeering, and black market activities were Asian businessmen, who came to be seen by many black Tanzanians as enemies of the nation engaged in economic sabotage. In response to a socialist state that had nationalized trade and commerce, Asian businesses adopted a variety of illegal strategies to protect their wealth and maintain their privileged status: transferring money and assets overseas; double-invoicing of imported goods and under-pricing exported goods, with the difference paid on their foreign accounts; exchanging currency illegally; engaging in lucrative black market activities; and bribing government officials to secure permits and goods or to evade taxes (Voigt-Graf, 1998: 117–118).

In addition, the socialist leadership code that accompanied the Arusha declaration of 1967 prevented black Africans who held political positions from engaging in “capitalist activities.” Government and party officials were not allowed to rent houses, earn more than one salary, own shares in private companies, or serve on the board of directors of a private company (McHenry, 1994, p. 30). Though designed to curb corruption, the code continued to prevent the emergence of an African capitalist class, thus allowing Asians to maintain their dominance of the private sector.

After years of economic crisis, a failure to achieve sustained economic development, and in response to internal as well as external pressures, Tanzania’s socialist experiment was gradually abandoned during the late 1980s and early 1990s. Although Julius Nyerere, the central architect of Tanzania’s socialist experiment, initially resisted International Monetary Fund (IMF) recommendations, the regime of his successor, Ali Hassan Mwinyi, implemented structural adjustment reforms after 1985 (Gibbon, 1995; Tripp, 1997; McHenry, 1994). Like other former socialist countries, Tanzania experienced a relatively rapid and simultaneous transition to market economics and multiparty politics in the final decades of the 20th century. Tanzania implemented the same structural adjustment policies enacted in Eastern Europe, Asia, Latin America, and elsewhere in Africa, including currency devaluation, trade liberalization, cutbacks in state-provided social services, the introduction of user fees for schools and hospitals, the withdrawal of subsidies for basic food staples, and the privatization of public enterprises. As a consequence of these policies, the poor suffered from sharp cutbacks in social services, wage freezes, dismissal of around 80,000 civil servants, the end of price controls on thousands of
items, including basic commodities, and massive currency devaluations that reduced their purchasing power. For urban residents, the cost of living index skyrocketed by 257%, from 1986, when free market policies were first introduced, to 1990 (Mmuya & Chaligha, 1992, p. 39).

The indigenization debate in Tanzania focused on ownership of economic assets – i.e., the distribution of income and wealth. A leading spokesperson for indigenization, Idi Simba, argued that it would “empower the historically disadvantaged citizens” and ensure that African Tanzanians would not continue to “play a marginal role in the development of the private sector.” He contended that “The modern sector of the economy is largely controlled by foreign entities and non-indigenous Tanzanians,” and that indigenization will serve “our national goal of economic liberation of the historically disadvantaged people …” (Simba, 2003, pp. 1, 4, 8, 11).

Although racially based class inequalities existed prior to the implementation of neoliberal economic reforms, the state socialist regime had prohibited public expressions of racial nationalism as part of its commitment to non-racial politics. When democratic political reforms made public discussion of these issues possible, the focus was on ownership and economic empowerment, especially on privatization and who should be allowed to purchase formerly state-owned assets. “Privatization under the present distribution of economic power,” warned the Tanzania Chamber of Commerce, Industry, and Agriculture in 1995, “is bound to further entrench the economic hold of an ethnic minority over the national economy” (1995: 7).

Policies of economic indigenization aimed to increase the ownership of assets by black African Tanzanians, while limiting such ownership by Indians and foreigners in Tanzania. Initially, staunch proponents of indigenization like the racial nationalist opposition politician Christopher Mtikila demanded the expropriation of Asian properties and expulsion of Asians, as had occurred in Uganda under Idi Amin; however, the debate evolved to focus on practical measures to reduce income and wealth inequalities between Asian and African Tanzanians. Proponents of indigenization advocated government financial assistance to the indigenous urban unemployed to encourage them to start their own businesses, restrictions on property ownership by non-indigenous residents, and preferential treatment for indigenous Tanzanians in the privatization process, in the licensing of businesses and awarding of government contracts, and in employment in foreign-owned firms (The East African, September 13–19, 1999, p. 11). A detailed report (“Policy Study on Economic Empowerment of Indigenous Tanzanians”) by the Economic and Social Research Foundation (ESRF) and PACE Developments Limited
(2001) included 18 policy proposals targeted at “those groups who were disadvantaged by deliberate colonial policies” and aimed at enhancing participation of indigenous Tanzanians in the economy. The proposals included preferential treatment in government procurement, various credit and savings schemes to provide funds for indigenous investors, special training programs for indigenous entrepreneurs, and measures to promote the participation of indigenous small investors in capital markets and privatization.

In contrast to Tanzania, the adoption of neoliberal economic policies in Fiji did not represent a dramatic reversal from previous policies. Social welfare spending was a small portion of total government expenditure (Government of Fiji and United Nations Development Program, 1997), and since independence the economy had been based upon a free-enterprise model, albeit one which relied to varying degrees on protection for domestic manufacture. Further, the process of adopting neoliberal policies in Fiji was more sporadic and shaped by political developments; the most rapid liberalization occurred under the rule of unelected post-coup interim governments.

Fiji made initial moves toward explicitly pro-business reforms during the middle of the 1980s, when the government faced increasing fiscal pressures and a stagnant domestic economy. In response, the government followed World Bank recommendations by introducing wage controls and placing stricter limits on social welfare spending. After two coups in 1987 and faced with dwindling foreign reserves due to trade restrictions and a decrease in tourist arrivals, the Fiji dollar was devalued and government salary cuts were imposed (Thomson, 1999). Interim military and civilian governments decreed a number of policies of economic liberalization: establishing tax-free trade zones for export production, reducing the power of labor unions, lifting import restrictions on locally manufactured items, reducing import licensing, and moving to privatize some large-scale government enterprises (Fiji Times, November 20, 1987, December 2, 1987, January 18, 1988, January 28, 1988, March 7, 1988, August 9, 1989). An IMF team assisted in the development of an economic liberalization policy initiative, which included provisions to limit government spending, to limit wage growth to foster international competitiveness, to deregulate the economy, and to decrease income taxes by shifting to a consumption-based value-added tax (VAT) (Fiji Times, October 21, 1989). The pro-investment policies and wage controls had the predictable effect of increasing poverty and decreasing the real wages of the working class (Fiji Times, April 12, 1989). At the same time, net social spending decreased; for instance, per capita health expenditure fell from FJ $37 in 1986 to FJS 23.50 in 1989 (Fiji Times, October 4, 1989).
After the return to elected governments in 1992, the pace of economic liberalization slowed considerably and was partially reversed in 1999 with the election of the Fiji Labour Party-led People’s Coalition Government, which removed VAT from basic food items and put privatization plans on hold. After the removal of the People’s Coalition Government in 2000, an interim administration advanced neoliberal economic policies, reinstituting VAT on basic food items and renewing privatization initiatives.

In Fiji, there were efforts since independence to increase indigenous Fijian participation in the formal economy; however, these efforts were often limited to regional development of small-scale industries and to education programs emphasizing “individual initiative and self help” (Central Planning Office, 1985, p. 9). Although Fijians owned approximately 90% of the land, they participated only marginally in the formal business sector. After the coups in 1987, interim governments enacted programs “to create opportunities for fuller Fijian participation in the economy and for their social advancement” (Fiji Times, November 9, 1987: 3). The interim government formed a Fijian Initiative Group that developed a Nine-Point Plan for the basis of a series of affirmative action policies targeted to increase Fijians’ economic status (Ministry of Finance and National Planning, 2002; Ratuva, 1999). Policies adopted under this framework include: reservation of a proportion of government-issued licenses, import quotas, and government contracts for Fijian-owned businesses; concessionary loan programs for Fijians in commerce; government loans and grants for large-scale Fijian business development; expanded benefits to indigenous landowning groups, such as increased royalties on natural resource extraction and provision of means to buy freehold land; and positive discrimination in civil service hiring.

While neoliberalism and indigenization in Tanzania and Fiji included similar provisions, these policies’ place in the political-economic trajectories differed due to the countries’ divergent post-independence development strategies. In the next section, we analyze how these differences influenced the meaning of and association between neoliberalism and indigenization by examining political contention surrounding these policies.

POLITICAL CONTESTATION OF NEOLIBERAL ECONOMICS AND INDIGENIZATION

Although neoliberal economic policies and the issue of racial redress generated intense political conflict in both Tanzania and Fiji, the social and
political consequences of neoliberal economics varied, as did the meaning of indigenization and targets of indigenization policies. In Tanzania, a dominant ruling party and weak opposition parties enabled the ruling party to co-opt the issue of indigenization, redefine the meaning of indigenous, and shift the target of indigenization policies from race to citizenship and, thereby, from Asian-Tanzanians to foreigners. In Fiji, where no single party dominated the political landscape, contention extended beyond the electoral arena, in the form of coups, political instability, and unelected governments instituting major reforms.

**Tanzania**

Simultaneous democratization and economic liberalization in Tanzania created an environment which substantially transformed contention. The emergence of competing political parties made mobilization of potential supporters an important aspect of political dynamics. Economic liberalization created a fundamental shift in the provision of goods and services, opening a myriad of potential issues for debate. Both sets of changes converged on the issue of race-based inequalities – an issue that had long been politically off-limits under one-party socialist rule. Neoliberal economic policies brought about two fundamental changes that impacted race relations. First, they helped to create an emerging black African capitalist class and strengthened the economic power of an already powerful Asian-Tanzanian capitalist class that had strong connections to global markets. Second, they heightened the visibility of existing racial inequalities.

During the socialist period, the black African elite controlled the government but, until February 1991, a leadership code prohibited them from engaging in capitalist activities. After 1991, neoliberal reforms created new economic opportunities for those who could mobilize capital, facilitating the emergence of a black African capitalist class. Many of the new African entrepreneurs are former public officials who used their cultural capital and social connections to develop businesses in hotels, restaurants, transportation, trade, and manufacturing. These black African businesspeople have been in the forefront of efforts to implement policies of racial preference in the transition from state socialism to capitalism, although these leaders differ over the preferred content of indigenization policies. Whereas some have called for racially based measures to restrict the property and citizenship rights of Asian-Tanzanians and to shift control of the economy into the hands of African Tanzanians, others deny any racial
motivation and frame indigenization as a form of affirmative action (Heilman, 1998; Simba, 2003, p. 13). The policies advocated by black African business leaders range from calls for redistributing resources to the historically disadvantaged black majority to exclusionary racial policies targeting the Asian population. African business leaders have demanded that priority be given to “indigenous” Tanzanians in the sale of state-owned enterprises and have also called on the government to issue business licenses exclusively to “indigenous” Tanzanians. Ally Sykes, a prominent businessman who became a spokesman for the emerging black African bourgeoisie, called on the government to give economic power to indigenous Africans by refusing to grant Asians licenses to run businesses and by granting the right of first purchase of former government properties to indigenous Tanzanians. “Asians have been thrown out of business everywhere in the world,” he stated in an interview in 1996. “We have seen this in Singapore, Malaysia, Nigeria, Ghana, etc. Why should we allow these people to run the economy the way they are doing?” Sykes also praised the policies of former Ugandan dictator Idi Amin, commenting in 1993: “Unfortunately, people say Amin was a bad fellow, but the Ugandan expulsion was very well done” (Evans, 1993, p. 36).

A second key social consequence of neoliberal economic policies has been heightened class-based racial inequalities. The privatization of government-owned firms, known as parastatals, which many Africans feared would further increase the economic privileges of Asians, also fueled racial conflict. Critics argue that free market policies have made the correspondence between class and race more visible. These critics have complained that Asians, alongside Europeans and Arabs, “fill ‘high class’ nightclubs and restaurants, control prime real estate and good farmland, monopolize commerce, and dominate policy-making in government projects and programmes supported by donors…” (Tanzania Gender Networking Programme, 1994, p. 49). The privatization of social services, including education and health care, produced further racial divisions in access to basic services. The government could no longer afford the social services that it once provided, and it imposed user fees for education and health care, which large numbers of the impoverished black African population could not afford. Many Asian-Tanzanians could afford to pay for costly privatized services, making racial inequalities even more visible. The deterioration of public services had a less severe impact on the Asian community, because its communal institutions, financed by generous contributions from Asian businessmen, provided schools, health care, and social services. “The perception of Asian businessmen conscientiously honoring their own

The racial antagonisms fostered by neoliberal economic policies emerged in a new political context of multiparty democracy in Tanzania, a context which allowed public expressions of racial hatred that had been suppressed during more than three decades of single party rule and state socialism. Discontent over enduring racial inequalities provided opposition politicians a populist campaign issue, calling for policies of preferential treatment for “indigenous” Tanzanians. In their effort to mobilize popular support, opposition party politicians seized on racial nationalism as a way to address the grievances generated by free market policies that deprived growing numbers of people of access to schooling, health care, clean water, and living wage jobs. Whereas racial hostility was once expressed in class terms, in popular denunciations of Asians as “capitalist exploiters,” it was now expressed in racial terms, by the labeling of Asians as “non-indigenous” people whose loyalty to the nation and claims to citizenship were questionable. While socialist rhetoric targeted the capitalist practices of Asian merchants, racial nationalist rhetoric of the neoliberal era targeted Asian participation in a “free market” global economy in which the mobility of capital purportedly undermined national loyalties.

The law legalizing opposition political parties explicitly prohibited the registration of any party based on race, religion, or ethnicity (Msekwa, 1995). Despite these regulations, opposition parties emerged which mobilized popular support by denouncing Asian-Tanzanians and demanding preferential legislation for “indigenous” Tanzanians. The most popular advocate of racial nationalism in the early years of multiparty politics was Chistopher Mtikila, who led the unregistered Democratic Party (DP). Mtikila targeted Asians as enemies of the nation and coined a new racial nationalist vocabulary of indigenization, to express his exclusive sense of who was a real Tanzanian. While attending Malangali Government Secondary School in Mufindi district, Mtikila was nicknamed “Hitler” by fellow students because he ardently advocated some of Hitler’s ideas while participating in school debates (Weekly Mail, May 31–June 1, 1993, pp. 4–5). Mtikila denounced Indians and Arabs as thieves and looters of the country’s wealth who sold out the nation and exploited dispossessed Africans. Mtikila claimed that 161 Asian-Tanzanians ran the economy to benefit their own communities at the expense of indigenous Africans, the
“downtrodden people.” He called for the expulsion of Asians and Arabs from Tanzania and urged neighboring African countries to repay the assistance Tanzania provided during their liberation struggles by sending troops to drive the Asians and Arabs out of Tanzania. In July 1992, his inflammatory speeches provoked supporters to destroy Arab and Asian-owned shops in Dar es Salaam and in 1993 he gave an anti-Asian speech which prompted youthful supporters to stone the cars of Asian residents, a number of whom were injured (Daily News, January 26, 1993). In that speech, Mtikila declared war against non-indigenous Tanzanians, whom he accused of looting the country’s wealth. His fiery speeches included accusations of corruption directed against top government and ruling party leaders who, in his view, had betrayed the nation. He denounced the ruling party for embracing Asian tycoons, whom he claimed were looting national resources, exporting capital, and corrupting politicians.

Although some Tanzanian commentators denounced Mtikila’s message as “the gospel of hate thy neighbor” and labeled his political party “the incarnation of fascism,” others defended his actions and called for popular protests and a boycott of Asian businesses (The Express, February 11–17, 1993). In 1995, a poll found Mtikila to be one of the most popular politicians in the country, second only to Julius Nyerere (Africa Confidential, July, 1995). The poor street vendors of Dar es Salaam, mostly young black males who had recently migrated to the city in search of employment, were his strongest supporters. These poor underemployed urban youth engaged in the informal economy constituted a sizable political constituency. Each day an estimated 4,500 youth migrated to Dar es Salaam, which had an annual growth rate of 11% and was Africa’s third fastest growing city (The Express, April 24, 1995). In September 1993, police swept through the streets of Dar es Salaam, arresting street vendors and dismantling their stalls. The city council justified the police actions by claiming that unlicensed roadside kiosks posed a threat to public health, citing a recent cholera epidemic that claimed over 100 lives. A group of over 100 African youths responded to the raid by looting Asian shops and stoning cars driven by Asians in the city center. The rioters viewed the municipal government’s actions as a response to complaints by Asian shopkeepers determined to eliminate African street vendors, many of whom depended on Asians for their goods, so that people would be forced to buy goods at higher prices in the shops. Rumors circulated that Asian shopkeepers had paid local authorities a bribe of $80,000 to rid the center of the city of African street hawkers who occupied sidewalks outside their shops. “Foreigners cannot remove us from our motherland … We shall die
here,’” shouted the rioters (The Express, October 15, 1993). The confrontation between police and demonstrators lasted over four hours, resulting in two deaths and scores of injuries. Similar confrontations between street vendors and Asian shopkeepers took place in Morogoro, located 150 miles west of Dar es Salaam, in July 1994. Hundreds of African street vendors attacked and looted Asian-owned stores to protest what they regarded as a concerted effort by Asian shopkeepers and municipal authorities to remove them from the center of town (Business Times, July 8–15, 1994).

Although other opposition political parties raised the issue of indigenization, they initially did so very cautiously, until Mtikila demonstrated its popular appeal. Mtikila gained popular support by speaking out on an issue that most other politicians were initially hesitant to address. Despite his electoral marginality, he played an important agenda-setting role, raising issues that were taboo in the electoral arena and taking his followers into the streets to challenge the regime on its racial policies. Mtikila’s popularity gradually declined after 1995, in large part because other more mainstream political leaders embraced the issue of indigenization.

Unlike opposition parties, the ruling Chama Cha Mapinduzi (CCM) party had welcomed Asians into its ranks. Prominent Asian businesspeople ran for office as CCM candidates in the 1994 by-elections and many more helped to finance ruling party campaigns. CCM pronouncements emphasized themes of national unity in the face of growing racial, religious, and ethnic divisions. The ruling party has always governed with a consensus political style characterized by co-optation of certain issues and concessions to certain opposition demands. This pattern is evident in the party’s response to the indigenization debate. In the face of internal party divisions and growing popular support for indigenization, the party took the dramatic step of appointing a vocal proponent of indigenization, prominent business leader Idi Simba, as Minister of Commerce and Industry.

As minister, Simba proposed a new law to reserve certain sectors of the economy exclusively for indigenous entrepreneurs and others for joint ventures with foreign investors. The law, entitled the National Employment Promotion Service Act of 1999, gave the minister the power to designate certain industries as reserved for citizens and closed to foreigners and required that certain large-scale industries have 50% or more ownership by a Tanzanian citizen (Tanzanian Affairs, May–August, 1996; The East African, April 5–11, 1999). Although many critics denounced the indigenization legislation as racist, the restrictions in the final bill targeted foreigners rather than “non-indigenous” citizens, including Tanzanians of Asian background among the indigenous people. Advocates of racial
nationalism contended that the legislation did not go far enough because its restrictions were directed at non-citizens, rather than non-indigenous people, thereby allowing Asians to continue dominating the economy. Proponents of indigenization called for a more comprehensive indigenization policy that would cover the sale of state enterprises, the licensing of businesses, the awarding of government contracts, immigration regulations, and employment policies in foreign-owned firms (Sunday Observer, August 29, 1999). The new policy was quickly abandoned, however, after the IMF and World Bank pressured the President to reassure foreign donors and investors that the ruling party rejected preferential treatment for Tanzanian citizens and discrimination against those of Asian origin (The Guardian, September 24, 1999). The government retracted the lengthy list of businesses reserved for Tanzanians drawn up by Minister Simba. The government was caught between popular demands for indigenization – an issue which it could no longer be ignored or leave in the hands of populist opposition leaders – and international pressures to maintain free market investment and trade policies – a prerequisite for debt reduction and future donor aid. The irony is that the same global financial institutions that promoted the neoliberal policies which unintentionally fostered heightened racial antagonisms also intervened to prevent a political expression of those antagonisms that threatened to jeopardize neoliberal policies.

Fiji

In contrast to Tanzania’s history of a one-party socialist state, Fiji’s political system since independence has been characterized by racially based multi-party politics, punctuated by two periods of unelected interim governments established after coups ousted left-leaning elected governments.\textsuperscript{11} Given this longer and more variegated history (summarized in Table 1), the characterization of Fiji’s trajectory is necessarily somewhat less tidy than Tanzania’s trajectory.\textsuperscript{12} Nonetheless, for the purposes of analysis, we divide this history into three eras, during which the nature of political contention and party competition surrounding indigenization and neoliberalism changed. In each of these eras, a different ethnic Fijian party aimed for prominence and ideological debates shifted based, in part, on the response of these parties to their primary challengers. This trajectory reveals key points of difference with the history of contention about neoliberalism and indigenization in Tanzania. First, early racial nationalist appeals in Fiji included an explicit class-based component, setting the stage for class-based
Table 1.  Primary Political Parties and Racial and Economic Ideologies in Fiji, 1970–2004.

<table>
<thead>
<tr>
<th>Year</th>
<th>Racial Ideology</th>
<th>Economic Ideology</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970–1987</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Alliance</td>
<td>Multiracialism</td>
<td>Liberal</td>
</tr>
<tr>
<td>National Federation Party</td>
<td>Non-racialism</td>
<td>Liberal</td>
</tr>
<tr>
<td>Fijian Nationalist Party</td>
<td>Fijian nationalist</td>
<td>Populist</td>
</tr>
<tr>
<td>1987</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fiji Labour Party</td>
<td>Non-racialism</td>
<td>Socialist, populist</td>
</tr>
<tr>
<td>National Federation Party</td>
<td>Non-racialism</td>
<td>Liberal</td>
</tr>
<tr>
<td>Alliance</td>
<td>Multiracialism with racial appeals</td>
<td>Liberal</td>
</tr>
<tr>
<td>Fijian Nationalist Party</td>
<td>Fijian nationalist</td>
<td>Populist</td>
</tr>
<tr>
<td>Taukei Movement (launched post-election)</td>
<td>Fijian nationalist</td>
<td>Varied</td>
</tr>
</tbody>
</table>

*Government was deposed by a military coup and succeeded by an interim administration that accelerated indigenization and neoliberalism*

<table>
<thead>
<tr>
<th>Year</th>
<th>Racial Ideology</th>
<th>Economic Ideology</th>
</tr>
</thead>
<tbody>
<tr>
<td>1987–1992</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interim Administration</td>
<td>Racial favoritism</td>
<td>Neoliberal</td>
</tr>
<tr>
<td>Included Alliance and taukei</td>
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<td></td>
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</tbody>
</table>

*1990: Promulgation of a more racially exclusive Constitution, including indigenization and additional Fijian representation in Parliament*

<table>
<thead>
<tr>
<th>Year</th>
<th>Racial Ideology</th>
<th>Economic Ideology</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992–1999</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Soqosoqo ni Vakavulewa ni Taukei</td>
<td>Racial favoritism</td>
<td>Liberal, increasingly restrained</td>
</tr>
<tr>
<td>National Federation Party</td>
<td>Non-racialism</td>
<td>Liberal</td>
</tr>
<tr>
<td>Fiji Labour Party</td>
<td>Non-racialism</td>
<td>Socialists, populist</td>
</tr>
<tr>
<td>Fiji Nationalist United Front (only 1992–1994)</td>
<td>Fijian nationalist, non-exclusive</td>
<td>Populist</td>
</tr>
</tbody>
</table>

*1997: Promulgation of moderate Constitution, including provisions for affirmative action on the basis of disadvantage rather than race*

<table>
<thead>
<tr>
<th>Year</th>
<th>Racial Ideology</th>
<th>Economic Ideology</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999–2000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>People’s Coalition (Fiji Labour Party, two Fijian parties)</td>
<td>Non-racialism</td>
<td>Populist, reform socialist</td>
</tr>
<tr>
<td>Soqosoqo ni Vakavulewa N-i Taukei - National Federation Party coalition</td>
<td>Multiracialism, limited racial favoritism</td>
<td>Liberal</td>
</tr>
<tr>
<td>Christian Democrat Alliance (post-election coalition)</td>
<td>varied</td>
<td>Populist</td>
</tr>
<tr>
<td>Taukei Movement (launched post-election)</td>
<td>Fijian nationalist</td>
<td>Varied</td>
</tr>
</tbody>
</table>

*Government was deposed by a coup, succeeded by an interim administration that instituted expanded indigenization programs and pursued neo-liberal policies*
mobilization against subsequent indigenization policies. Second, policies of economic liberalization and indigenization had affinities in Fiji, as ruling parties used economic liberalization to promote indigenization.

**Liberalism and multiracialism, 1970 – 1987.** During the first era, the dominant economic ideology was liberalism with a racial ideology of multiracialism, in which the government united separate, but cooperative, racially specific parties. The cross-voting system enabled the ruling Alliance – a three party coalition representing the three racial voting blocs – to include representatives of the main racial groups. Under the cross-voting system, members of all of the separate racial electoral rolls voted for representatives from each of the racial groupings. The Alliance, led by Ratu Sir Kamisese Mara, a Fijian High Chief, received the majority of support from Fijian Electors and General Electors (voters who are neither Fijian nor Indian). The National Federation Party (NFP), supported primarily by an Indian base, sat in opposition and argued for the establishment of a common roll of voters (non-racially based), but shared a liberal economic ideology with the Alliance.

As in Tanzania, initial moves toward racial nationalism were associated with an individual political leader and with a populist economic challenge to the ruling party. Sakeasi Butadroka, an assistant Alliance minister, challenged multiracialism as not doing enough for Fijians and was subsequently expelled from the party. Butadroka responded by founding the Fijian Nationalist Party (FNP) in 1974, combining ethno-nationalist and economic populist appeals: calling for the repatriation of Indians to India, questioning the manner in which the Fijian Administration distributed land rental proceeds to Fijian landowners, advocating for greater control over and distribution of profit from extractive industries that used indigenous

<table>
<thead>
<tr>
<th>Year</th>
<th>Racial Ideology</th>
<th>Economic Ideology</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000–2001</td>
<td>Interim administration</td>
<td>Racial favoritism</td>
</tr>
<tr>
<td>2001–2004</td>
<td>Soqosoqo Duavata ni Lewenivanua</td>
<td>Racial favoritism</td>
</tr>
<tr>
<td></td>
<td>Fiji Labour Party</td>
<td>Non-racialism</td>
</tr>
<tr>
<td></td>
<td>Conservative Alliance/Matanitu Vanua (post-election coalition)</td>
<td>Fijian nationalist</td>
</tr>
</tbody>
</table>

Note: Ruling parties and coalition partners are listed in **bold text** for each elected government.

Table 1. (Continued)
land, encouraging expanded support for Fijians to enter commerce, and challenging the predominance of Fijian leaders from the Lau group (a number of relatively smaller, isolated islands in the east of Fiji). While the FNP achieved only modest electoral success, it affected the outcome of elections in tightly divided constituencies by drawing support away from Alliance candidates.

The founding of the Fiji Labour Party (FLP) in 1985 heightened the challenge to the Alliance. After a period of economic stagnation and the first moves to implement wage controls and further limit social expenditures, a group of labor union leaders and academics formed the FLP as a race-blind, leftist party with support and leadership from both Fijians and Indians, with Timoci Bavadra, a Fijian, serving as party leader. For the 1987 Parliamentary elections, the FLP formed a coalition with the Indian-dominated NFP. To achieve the coalition, the FLP moderated some of its more radical economic positions, such as an earlier call to nationalize mining operations. Despite differences in economic policy, much campaign rhetoric employed race-based appeals. The FNP claimed that the Alliance had not done enough to improve economic status of Fijians, arguing that Indian income was much higher than Fijian income and that there were great differences in civil service employment, even though the income gap had narrowed considerably over the previous decade and Indian unemployment was actually higher than Fijian unemployment (Fiji Times, March 21, 1987; Central Planning Office, 1985). A splinter group of the NFP claimed that the FLP-NFP Coalition was selling out Indian interests. The Alliance used racial appeals to target each of the three groups of voters (Indian, Fijian, and General Electors), noting that the Coalition’s race-blind stance made no assurance for representation of any particular group. The Alliance also questioned some Coalition leaders’ commitment to non-racialism. The combined challenge of Fijian nationalism and the Coalition’s blend of non-racialism with populist economics brought an end to liberal multiracialism.

The FLP-NFP Coalition won the election, yet advocates of non-racialism had overcome neither the legacy of the race-based mobilization for voters under multiracialism nor the challenge of Fijian nationalism. Marking the beginning of a transition to a second era of political alignment, almost immediately after the election, the taukei (indigenous) movement was launched in the name of Fijian rights, organizing road blocks and marches against the government, with some prominent Alliance members taking on leadership roles. Butadroka and the FNP called for moderation, focusing attention on removing Ratu Mara from his leadership position in the
Alliance. In the wake of continuing taukei marches and some NFP leaders’ law offices being fire bombed (one by an Alliance Senator), Lieutenant-Colonel Sitiveni Rabuka staged a coup just one month after the election. Over the next three months, tentative steps were taken to form a caretaker government consisting of both Alliance and Coalition members. Three days after an accord was reached, Rabuka staged a second coup. Within a week, Rabuka had declared Fiji a republic, revoked the constitution, and appointed himself head-of-state. He installed a short-lived military government consisting of Alliance politicians and military and taukei leaders. He then handed power to an interim government headed by Ratu Mara that expanded Alliance representation at the expense of the taukei leaders.

Indigenization and restrained neoliberalism, 1987–1997. The second era was marked by a ruling racial ideology of favoritism for Fijians, exemplified by indigenization and unequal political representation. Economically, the era was marked by an ideology of neoliberalism, although populist pressures restrained neoliberal policies after the return to elected governments.

After the interim government implemented a number of neoliberal and indigenization policies, a new Constitution was promulgated in 1990 that enhanced indigenous Fijians’ rights, giving shape to the political dynamics of the second era. The 1990 Constitution made specific provisions for affirmative action in government programs to benefit Fijians, including quotas for civil service employment. Elections were to be conducted on a strictly communal basis; the Constitution called for separate representation and voting rolls for the different racial groups and allocated a disproportionate number of seats to Fijians. Under this arrangement, political parties increasingly competed only within racial groups. The most important development was the formation of Soqosoqo ni Vakavulewa ni Taukei (SVT, the Fijian Political Party) by the Great Council of Chiefs (GCC). The Fijian seats were distributed on a provincial basis, and SVT leadership hoped to use Provincial Councils to select candidates. Intra-provincial disputes led to the formation of rival parties; a number of these parties allied under the banner Fiji Nationalist United Front (FNUF), joining Butadroka in contesting the 1992 election. Butadroka sharply criticized some of the Interim Government’s economic policies, opposing the VAT as “unfair taxation ... that only served to oppress the poor and underprivileged” (Fiji Times, August 12, 1991: 3). His platform called for scrapping the VAT and nationalizing the Emperor Gold Mining Company. These anti-capitalist sentiments, while not universal, were not uncommon among many
indigenous Fijian nationalists, as evidenced when a letter to the editor of the *Fiji Times* claimed that the coups in 1987 happened “when the indigenous Fijian realized the irrelevance and capitalistic principles of Western democratic ideology” (November 8, 1991: 6).

The FNUF secured a small bloc of the Fijian seats in Parliament and sat in opposition along with the NFP and the FLP, which split the Indian seats. The FNUF bloc emphasized class rather than racial inequality, arguing that the SVT economic policies of deregulation, privatization, and government support of large-scale indigenous enterprises would only make the rich richer (*Fiji Times*, November 20, 1992). The FNUF continued to push for indigenous interests, but it focused its efforts on government administration of land, criticizing the intermediary role of the Fijian Administration while contending that greater control over natural resources should be given to land owners. After Butadroka was suspended from Parliament for making derogatory statements about the President, the FNUF bloc proposed including all underprivileged individuals (including Indians) in the Fiji Development Bank (FDB) soft loans program that had been one of the main components of indigenization (*Fiji Times*, July 13, 1993: 5).

Continuing divisions among the Fijian representatives in Parliament compelled SVT leadership to rely on side deals with Indian representatives to retain power. The inability to maintain a stable governing majority, as well as concessions to Indian opposition parties, led to the founding of a Constitutional Review Commission (Reeves et al., 1996), which marked a transition to the third era.

*Contesting Disadvantage, 1997–2004*. The resulting Constitution, adopted in 1997, contained a chapter on Social Justice and Affirmative Action “for all groups or categories of persons who are disadvantaged.” The new Constitution also abandoned first-past-the-post voting in favor of the preference (alternative) vote system and replaced one-third of the communal seats with open seats. In this third era, early promises of multi-racialism or non-racialism broke down as debate focused on the basis of determining disadvantage in implementing the Social Justice provisions of the constitution, as exemplified by legislative debates in 2000 and 2001. Division on affirmative action increasingly corresponded with division on neoliberalism.

The 1999 elections under the new Constitution pitted a restrained neoliberal, multi-racialist coalition against a populist non-racial coalition. The SVT and NFP formed a coalition that promoted its ability to bring about a stable transition to multiethnic government. Both parties produced
their own manifestos, attempting to mobilize their respective voting bases, while emphasizing the ideologies of multiracialism (with limited preferences for Fijians) and gradual neoliberalism. In contrast, the People’s Coalition (PC) developed a common non-racial, economic populist manifesto, bringing together the FLP and two Fijian parties. Two other Fijian parties contested the election outside of formal coalitions. The Nationalist Vanua Tako Lavo Party (NVTLP) attempted to garner support by taking an anti-constitution, anti-Indian, and anti-government stance. The Veitokani ni Lewenivanua Vakaristo (VLV, Christian Democrat Alliance), relied on economic populism, promising to decrease corruption in government and vowing to strengthen anti-poverty programs and to review the VAT.\textsuperscript{17}

The contours of political party and movement mobilization became more defined after the election of the PC, as the government pursued race-blind populist policies and the opposition responded with race-based appeals. Ongoing efforts by nationalists and dissident Fijian leaders to destabilize the PC government escalated in early 2000 when the taukei movement was re-launched as the government started to address issues related to the expiration of cane farm leases.

Against this backdrop, contention about public policy served as a means to activate support for particular forms of affirmative action. Debates about redress became struggles over the mobilization of political supporters and over whether eligibility for affirmative action should be based on race or class. To implement the Social Justice and Affirmative Action chapter of the constitution, the PC government proposed the Social Justice Bill (No. 3) of 2000 to provide a framework and constitutional-legal foundation for existing affirmative action programs. The bill largely followed the language of the chapter in the constitution providing for recognition of disadvantage, rather than targeting particular ethnic groups.

In introducing the Bill at its second reading, Prime Minister Mahendra Chaudhry remarked about disadvantaged groups:

> Sometimes these groups represent whole ethnic communities such as indigenous Fijians with regard to commerce and Indo-Fijians and Melanesians with regard to agricultural land. But very often Sir, they do not. ... In some instances ethnicity is not really relevant at all. In areas like housing, education, family assistance and micro-finance, there are groups within all ethnic communities who endure hardship and disadvantage. The common denominators are much more likely to be socio-economic status, gender, age or rural location. \textit{(Chaudhry, 2000)}

Chaudhry’s remarks exemplify the shift in focus from ethnicity or race\textsuperscript{18} to class, characteristic of the PC’s approach to affirmative action.
This shift provoked harsh rhetoric against the proposed Bill. An opposition SVT Parliamentarian commented:

It will be a big irony to the expectation of the majority of native Fijian people that the very sections of the Constitution that were intended to assist and alleviate them, are now being used by the Government to limit those assistance [sic]. . . The Bill has removed ethnicity of indigenousness of the Fijian people as a benchmark . . . native Fijians are bundled with others because the only qualification for assistance is that, you are to be disadvantaged . . . History has told us that the reason why native Fijians are lagging behind is not because they are disadvantaged but simply because of their cultural values and therefore their attitude to school, work and commerce is different. (Lalabalavu, 2000)

The argument about the “removal” of ethnicity was framed in terms of indigenous rights, which exceed those granted to other members of society, regardless of advantage. Furthermore, the choice of language about “removal” of ethnicity rhetorically worked to highlight a threat to Fijian culture. This rhetoric of threat was more explicit in the contribution to the debate by an independent opposition Fijian Parliamentarian who characterized the proposed policy as “a ploy against the interests of the Fijian community with its distinctive communal culture and needs” and claimed that government officials “deliberately want to do away with the Fijian race” (Kaitani, 2000). The move to base policy on disadvantage without consideration of race or ethnicity was held to undermine the distinctive characteristic of indigenous Fijian culture.

An alternative rhetoric against the government proposal held that it was important to cater to the needs of Fijians, because they were the “most disadvantaged” group. One SVT Parliamentarian argued that “[T]he Fijians are lagging behind in many areas of national life; in business, education, in the professions, in learning standards and so on. They are at the bottom of the pile.” Noting that “this situation is dangerous and can be a cause of instability,” he urged legislators to “be very sure that affirmative actions programmes proposed in the legislation will mainly benefit the Fijians” and to assure Fijians that “they will get the biggest share of affirmative actions because they are the most disadvantaged” (Tokainavo, 2000). These claims, while not as stark as the “removal” arguments, were framed at the aggregate, rather than individual, level. Additionally, references to a “dangerous” situation and “instability” resonated with the rhetoric of other arguments against the Bill and foreshadowed subsequent events.

Indeed, as the third reading of the Bill began, a small band of armed men led by George Speight stormed Parliament and took members of the
Government hostage, declaring a civilian coup. When the military refused to back the coup, a stand-off ensued. After negotiation between the army and rebels produced an accord, the rebels released the hostages and the GCC appointed Laisenia Qarase, the former head of the Fiji Development Bank, to head an interim administration. Qarase’s interim administration proposed a Blueprint for the Protection and Advancement of Indigenous Fijians and Rotumans, which would enhance native land ownership rights, establish a Fijian trust fund and savings scheme, provide tax concessions for Fijian-owned companies, reserve half of government contracts and licenses for Fijians, and provide grants for Fijian education and commerce. After a high court ruled the interim administration illegal, the interim administration called for new elections in 2001.

The election brought to power a new political party led by Qarase, Soqosoqo Duavata ni Lewenivanua (SDL, United Fiji Party). The SDL ran an essentially communal campaign appealing to Fijian voters; it centered its campaign on the Blueprint, and only the Conservative Alliance/Matanitu Vanua (CAMV) served as credible opposition to the SDL for the Fijian seats and Fijian-dominated open seats. The CAMV sought to counter the Blueprint as mere patronage (particularly in light of a multimillion agricultural assistance program that coincided with the 2001 election), but the Blueprint was not the critical issue. Rather, CAMV attempted to mobilize voters by arguing that the punishment of the rebels who led the take-over of Parliament should be reduced or overturned. While a fragmented FLP swept the Indian communal seats and won a number of Indian-dominated open seats, the SDL was able to form a post-election coalition with the CAMV, which won six seats.

After the elections, the SDL government moved to introduce its own Social Justice Bill (No. 5 of 2001). While much of the 2000 bill reappeared in the 2001 bill, the SDL Bill included the addition of 15 additional provisions, most of which targeted indigenous Fijians and Rotumans, such as directing funding to Fijian schools and reserving a minimum percentage of post-secondary scholarships for indigenous students. Additionally, the SDL Bill allowed the Cabinet to amend affirmative action programs on the basis of a recommendation of the relevant minister, whereas the PC Bill had required parliamentary approval for any amendment to affirmative action programs. Opposition members of Parliament, primarily from the FLP, contrasted the bill with the 2000 bill: “We on this side of the House … wish to emphasise class orientation, group orientation of social justice as opposed to the SDL’s programme which directs us now only to fulfill ethnic supremacy notions; that is the difference” (Datt 2001). Opponents of the Bill also emphasized
that an ethnic criterion would prevent assistance from going to those who need it: “The problem is that many of the affirmative action programmes benefit those who deserve the least and deny those who deserve the most. It will be very interesting to look at the statistics on the award of scholarships through the Fijian Affairs Programme” (Chand, 2001). Given the lack of means-testing for some of the programs, opponents questioned if there would be sufficient resources to assist the lower or middle classes.

Arguing in favor of the bill, Government members pointed to threats both to and from Fijians. Echoing the debate against the 2000 Bill, some Government members emphasized the importance of affirmative action for Fijian survival in the face of threats:

Fijians and Rotumans, Sir, make up the majority in Fiji, but globally we are very much a minority. There are fewer than half a million of us worldwide … The threats to Fijians and Rotumans’ existence and well-being are both external and internal and are not a perception. (Kepa, 2001)

Aside from stressing the threat to Fijian survival, however, some members argued that such plans were important to control political unrest:

It is politically driven because it is the result of the reality of the situation of the things that happened in 1987 and in May 2000 which we seemed to have conveniently forgotten. We should have learnt some lessons from the events of 1987 and May 2000. Mr. Speaker, Sir, I do not know the true reasons for those events or upheavals, perhaps no one would know. But one thing I do know, that these events actually … (Vuetilovoni, 2001)

The speech was interrupted by a point of order that the member was bordering on sedition with his comments. Other speakers, however, echoed Vuetilovoni’s comments by stressing that the policy was important to control instability.

Comparison: Political Contestation of Neoliberal Economics and Indigenization

In Tanzania and Fiji, neoliberal economic policies contained similar elements – privatization, a reduction in government services, increased openness toward foreign trade and investment, and shifting of tax burdens. Furthermore, these policies were similar in their consequences for large majorities of the populations in both countries, as lower-income people lost access to support services, while control over economic life simultaneously shifted to non-governmental actors. In both countries, policies of
indigenization emphasized wealth redistribution, aiming to increase the ownership of national resources by those identified as indigenous. Despite these basic similarities, however, our analysis demonstrates important variations in the patterns and processes of implementation, as shown in Table 2. Our comparison of neoliberal policies and indigenization policies in Tanzania and Fiji highlights four important differences: (1) in the creation of an indigenous capitalist class and its subsequent influence on policy formation; (2) in the timing of neoliberal economic reforms vis-à-vis democratization; (3) in the character of political contention over indigenization; and (4) in the alternatives articulated to indigenization.

A nascent indigenous capitalist class formed in both countries; however, the responses of these indigenous capitalists to neoliberal economic policies

<table>
<thead>
<tr>
<th>Trajectories of Neoliberal Economic and Indigenization Policies and Political Contention about Indigenization Policies in Tanzania and Fiji.</th>
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<tbody>
<tr>
<td><strong>Tanzania</strong></td>
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<tr>
<td><strong>Origins of Indigenous Capitalist Class</strong></td>
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<tr>
<td><strong>Timing of Neoliberal Economic Policy Changes</strong></td>
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<tr>
<td><strong>Political Contention about Indigenization Policy</strong></td>
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varied, due in part to their different origins in neoliberal and indigenization policies. The emergent indigenous elite in Fiji formed largely as a consequence of indigenization policies (Larson & Zalanga, 2003), rather than from neoliberal economic policies – the opposite of the experience in Tanzania. In later periods (e.g., post-2000), these indigenous capitalists in Fiji played an important role in promoting pro-capitalist policies and resisting attempts to reverse economic liberalization, whereas in Tanzania the nascent indigenous African capitalist class resisted free trade policies that threatened local industry, and they called for anti-liberal indigenization policies to restrict property ownership and curtail the economic power of the Asian minority. In Fiji, an indigenous capitalist class benefited from neoliberal economic policies and provided a means to mobilize support for these policies in the face of class-based opposition. The affinities between the policies in Fiji were based on some measures – e.g., privatization – that could achieve both sets of objectives, particularly in times of crisis. In this regard, attempts to achieve indigenization could drive economic reform, enabling a faster pace or broader reach than may have otherwise been possible.

Differences between indigenous capitalists’ links with foreign capital also shaped subsequent policy. Since foreign capitalists who wish to invest in Fiji often need to gain access to Fijian-owned land, the practice of collaboration with international investors has created a history of viewing such joint investments as mutually beneficial. In contrast, most indigenous capitalists in Tanzania resisted neoliberal economic reforms; they saw such policies as favoring Asians and foreigners and threatening local industries. Opponents of these policies and international actors framed indigenization as a protectionist threat to neoliberal economic reform. Early political reforms, such as the Zanzibar Resolution of 1990, eliminated restrictions prohibiting government and party officials from engaging in “capitalist activities,” thereby liberating these indigenous elites from relying on the Tanzanian state to seek income and wealth and enabling them to take advantage of neoliberal reforms that allowed the private accumulation of wealth in the market economy. But the reforms also opened up the economy to foreign capitalists’ investment and trade, thus posing a threat to the nascent indigenous Tanzanian capitalist class, since international investors and domestic capitalists had a competitive rather than collaborative relationship.

Second, the trajectories of reform in Tanzania and Fiji were distinct, as neoliberal economic reform in Fiji was not part of a simultaneous process of democratic reform as it was in Tanzania. The simultaneity of economic and political reform in Tanzania made state legacies of non-racialism vulnerable
to challenge. Simultaneous implementation of neoliberal economic policies and political reforms increased the likelihood that opposition parties saw all aspects of the single-party state-led socialist past as open to challenge, including the principle of non-racialism on which the nation had been built. In contrast, neoliberal economic reforms in Fiji did not occur in tandem with democratic reforms. To the extent that these economic reforms accompanied political changes, the reforms were responses to “crisis” situations caused by political instability. In the aftermath of the 1987 coups, devaluation and tax-free export processing were means to avert a foreign-exchange crisis. Similarly, after the overthrow of the People’s Coalition government in 2000, privatization became a means to make-up for budgetary shortfalls.

A third difference concerns the meaning that the rhetoric and politics of indigenization had in relation to domestic development legacies in Tanzania and Fiji. Although the challenges of Mtikila and Butadroka to the ruling parties both involved race-based appeals, they differed in an important respect. Butadroka’s appeals included a class-based component, particularly when attacking the indigenization policies of Rabuka’s SVT government in the 1990s as only benefiting the wealthy. These appeals laid the groundwork for non-racial class-based appeals concerning neoliberal policies in Fiji. In contrast, opposition parties in Tanzania portrayed the consequences of neoliberal policies largely in racial terms, rejecting the language of class that had informed the failed economic policies of the discredited socialist past. Only some moderate advocates of indigenization like Idi Simba offered rhetoric of economic empowerment, and then only in response to charges of racism by fellow ruling party members.

The politics of indigenization also differed, as political elites and ruling parties in Fiji used indigenization policies to promote and reinforce neoliberal reforms, whereas opposition parties in Tanzania used indigenization to protest the consequences of neoliberal economic reforms. This difference suggests that strategies of indigenization can be used for quite different purposes. The legacies of single-party rule and state socialism in Tanzania influenced both the nature and content of struggle: claims about the negative impact of neoliberal reforms were targeted at the ruling party and employed by opposition parties to mobilize voters around the issue of racial inequality in the wake of the discredited socialist experiment. In Fiji, the most far-reaching neoliberal reforms were instituted by unelected, interim governments, and class-based contention served as an alternative to racial mobilization in regard to both neoliberal policies and indigenization. In addition, indigenization policies in Fiji enabled interim governments to
restrain social spending, because they provided a means to limit expenditure only to a target group of beneficiaries.

Fourth, the primary alternative to indigenization advanced in Fiji was a shift in the focus to class-based disadvantage. This focus contrasts with Tanzania, where the alternative was an exclusive citizenship policy targeting foreigners, and where class-based politics were linked to a socialist experiment that had failed to achieve economic development. In Fiji, two primary attempts were made to justify indigenization in light of the alternative of class-based affirmative action. Indigenization was held both to be the means with which to uphold a set of Fijian cultural rights derived from the Deed of Cession and international documents on indigenous rights and also to constitute a “pragmatic” response to avoid the threat of violence, with reference made to political instability in 1987 and 2000. Appeals to class-based mobilization, therefore, were portrayed as a threat – either as a direct threat to indigenous Fijian culture, or as a threat to stability.

CONCLUSIONS

While our comparative analysis of neoliberalization and indigenization in Tanzania and Fiji finds an association between these policies and racial conflict, we also find a contingent association between the two types of policies and their consequences for inequality. In contrast to claims that a combination of neoliberal reform and electoral democracy necessarily increases ethnic and racial tension (Chua, 2004), our analysis demonstrates that political party formation and contention and the meaning of policy in national contexts mediate the association between and consequences of neoliberal economic reforms and policies of racial redress. The difference in political dynamics in the two cases underlies differences in the rationale behind and meanings of neoliberalization and indigenization, along with differences in the association between these policies. In Tanzania, neoliberal economic reforms were part of the process of international financial institution-led structural adjustment and represented a sharp reversal from previous state-led socialist development. They were promoted by advocates of neoliberalism as the only viable alternative to failed socialist development policies and as a development strategy that would position Tanzania advantageously in a highly competitive global economy. In Fiji, neoliberal economic policies were advanced over longer periods of times and often as a response to economic downturns caused by political crises, but they were also adopted as a means to help advance the goals of indigenization.
The distinct paths to neoliberalism in these cases also influenced the institutionalization of indigenization policies reflecting the importance of interest groups and alliances. In Tanzania, attempts to implement non-race-based indigenization met with resistance from donors and international financial agencies, which interpreted indigenization policies as an abandonment of liberal economic reforms in favor of protectionism for local industries and restrictions on property rights. In contrast, neoliberal economic reforms and indigenization in Fiji were pursued simultaneously by a number of different governments. Both sets of policies accelerated after the coups in 1987 and 2000. The affinities between the policies demonstrate that attempts to achieve indigenization can drive neoliberal economic reform. In addition, indigenization policies in Fiji provided a means to restrain social spending, to the extent that indigenization was a means to limit expenditure only to a targeted group of beneficiaries. This strategic targeting highlights a manner in which the distributional effects of implementing neoliberal policies can enhance the agency of some domestic political actors.

We identify three primary factors that account for variations in both the trajectories of reform and the contention concerning neoliberal economic and indigenization policies in the two cases. First, colonial legacies shaped the nature of political structures and contending parties in each country. While tripartite racial divisions existed in both countries, the particular character of race relations influenced the formation of alliances between racial groups. These colonial legacies were manifest in the transitions to independence, shaping post-independence political alignments. Second, the experience of national economic development models adopted prior to neoliberalization – state socialism in Tanzania, and free-enterprise with protection of domestic manufacture in Fiji – affected the meaning of policies within each country. Third, variation in the timing of the transition to neoliberal economics in relation to democratic political reforms shaped the salience of class-based mobilization and potential alliances between political parties in relation to policy changes. Given the dual transition in Tanzania, class-based mobilization against neoliberalization was discredited as part of the failed socialist experiment. In Fiji, claims about the disparate impact of neoliberal and indigenization policies on class historically had been made by several challengers to ruling parties.

Even when the particular content of neoliberal economic policies is quite similar, the policies may be connected to claims for racial redress in distinct manners in different countries. Colonial legacies and legacies of national political economy influence the meaning and effects of policy by creating
alliances, structuring party competition, and connecting sets of policies that may valorize or discredit particular policies and that can influence the speed and nature of implementation. neoliberal economic and indigenization policies, therefore, are not necessarily connected with each other, but the history of governmental strategy – e.g., the historical connection between state socialism and non-racialism in Tanzania – may lead to institutionalized understandings of these policies within a polity. These conceptions influence the likely reception of proposals, both by the public at large and by contending political parties.

We also find that racial identities are products of political contention and historical legacies, and that the latter have an important influence on the potential of neoliberalism to trigger racial violence that sets the “world on fire.” In addition to the path-dependent material interests that result from policies of earlier eras (Prasad, 2005), we find influential interests in the preservation, protection, and promotion of particular identities. Contests over policy may, therefore, take the form of contests over meaning. These bases of identity take on particular importance when competing political parties attempt to mobilize support by invoking identity in relation to public policies. Our comparison of the relationship between neoliberal and indigenization policies reveals the central role of political parties, and of the dynamic process of party competition, in shaping contested meaning of “indigenous” and the contours of neoliberal policies. Political parties played a central role in the creation of identity in both of our cases and they continue to contest and shape racial and economic policies in the current era.

The contradictions and complementarities between policies of neoliberal economics and racial redress are worked out in manners specific to the intersections of national historical legacies and patterns of political contention. Variations in these legacies and in contention may intersect differently with global norms and structures of power (Larson & Aminzade, in press), which helps to explain variation in international reaction to policy changes. In Fiji, neoliberal economic policies were used both as a short-term tool to manage the national economy in times of crisis and as a mechanism to support efforts to indigenize enterprise. In Tanzania, neoliberal policies were a tool to position the post-socialist national economy to be competitive in a global marketplace. Further, policy transitions may remake historical legacies in ways discontinuous with institutionalized patterns. Prior research has highlighted the role of social movements in creating such discontinuous patterns (Meyer, Jenness, & Ingram, 2005) while our research suggests that such discontinuities may be associated with the emergence of newly
empowered actors in the wake of large-scale structural changes, shifts in electoral alignments and coalitions, and internal divisions in ruling and opposition parties.

NOTES

1. The term “indigenous” is the subject of political contention. In global human rights discourse, it typically refers to a minority culture at risk from the nation state, whereas nationalist politicians calling for indigenization policies have used the term to refer to the “original” inhabitants of a particular territory, who may be a dispossessed majority rather than a minority (Larson & Aminzade, in press).

2. In part, the literature may be sparse because scholars presume that the policies are contradictory, given liberalism’s emphasis on individual rights and the group-based focus of affirmative action policies (Skrentny, 1996; Graham, 1992). However, as we argue below, implementation of neoliberalism requires distributing the costs and benefits of these policies. Despite the variety of means of implementing economic liberalization, the underlying logic of neoliberalization of re-allocating authority from states to markets provides a limited basis for states to make national-interest–based market interventions (Scott, 1997). In this light, group-based claims for redress become an important ground for arguing in favor of state intervention, as claims for favorable access to the benefits of or protection from the costs of neoliberal policies based on membership in a racial or ethnic group may be grounded in contemporary nation-state politics, in international obligations, or in long-standing commitments to historically disadvantaged segments of the populace.

3. Individual attitudes corresponded to the colonial racial order. Most Asians shared European racist views of Africans as inferior. “Within the Asian communities,” observes Richa Nagar (2000, p. 666), “discourses of Asians’ cultural and moral superiority over Africans play a critical role in legitimating Asian racism and economically privileged status.” Gendered constructions of pollution and purity among upper class Hindu members of the Asian community reinforced religious, class, and caste boundaries within the community, as well as racial, religious, and class boundaries separating Asians and Africans (Nagar, 1998, p. 127). Most Asians equated dark skin color with inferiority, reflecting popular stereotypes in India that dark skinned women were of lower caste origin and often of loose morals, and they referred to mixed race Afro-Asian women with the derogatory Gujarati term “jotawa,” which meant bastard or mongrel (Bharati, 1972). Limited survey data are consistent in findings concerning African racial stereotypes of Asians as clannish, greedy, dishonest, and unpatriotic and the very low tolerance among Africans toward the Asian community (Fordham & Wiltshire, 1963; van den Bergh, 1968; Evans 1966). A paucity of recent survey data about racial attitudes makes it difficult to judge the extent to which these stereotypical attitudes persist.

4. Tanganyika became the United Republic of Tanzania after it united with Zanzibar in 1964.

5. For a list of acronyms, please consult the appendix.
6. This formal tripartite division simplified the differences both within and between groups. Within groups, both Fijian and Indian populations differed in geographic origin (and, for Indians, religion). Further, the boundaries of groups have changed over time. People who originated from other, nearby Pacific Islands were the first to be brought over as plantation labor through blackbirding – the unscrupulous practices of “recruiting” workers by kidnapping or otherwise deceiving them. Colonial policy treated this group as Fijian, but since 1990, the government of Fiji has classified them as part of the category of “other,” because they are not indigenous to the Fiji Islands. The government classifies people with both Fijian and non-Fijian (usually European) heritage according to patrilineal heritage, either as Fijian or “part-European” (Riles, 1997). Additionally, a small Chinese merchant minority became part of the non-Fijian/non-Indian “other” population at independence.

7. Indians continued to be the largest group in Fiji until after the 1987 coups, when Fijians became the most numerous group due to a combination of greater Indian out-migration and higher Fijian birth rates. As of 1996 – the date of the most recent census – Fijians were about 51% of the population, Indians were 44%, with the remaining 5% divided among other groups (Fiji Islands Bureau of Statistics, 2005).

8. The division within the Indian population in Fiji between tenant farming and merchant activity and the relative politically privileged position of indigenous Fijians have created a “polydominal” system of race relations and attitudes, in that there are multiple axes of inequality – Fijians claiming economic disadvantage and Indians claiming political disenfranchisement (White, 2002). As in Tanzania, data concerning racial attitudes are sparse; however, recent survey data show that indigenous Fijians tend to have stronger in-group identification and ethnic supremacy aspirations than Indians (de Vries, 2002).

9. The report defined indigenous Tanzanians as “all citizens of Tanzania by birth and who are of African origin (natives or blacks) whose origin in the country can be traced back to at least three generations.” The report further stated that

   the definition of indigenous Tanzanians should be included in the constitutional provisions relating to rights and responsibilities of citizens of the United Republic of Tanzania ... Such a definition in the constitution will provide the legal basis for implementation of economic empowerment programmes and avoid its implementation being challenged on discriminatory or unconstitutional grounds. (2001: viii, xiii, 5)

10. Instructive in this regard are similarities in political party manifestos. In the first 15 years after independence, there was a general consensus of support for competitive free enterprise economics and government provision of essential infrastructure and necessary regulation (e.g., NFP-Western United Front Coalition, 1982; Central Planning Office, 1985).

11. The December 2006 coup is beyond the scope of the analysis of this paper.

12. For the purposes of simplicity, we have generally excluded discussion of many smaller political parties, particularly those focused on General Electors.

13. Ratuva provides an explication of taukei: “The term taukei, which means original owner of the soil or land, is normally used by indigenous Fijians as a dichotomy to the term vulagi or ‘foreigner’ – referring to Indians” (1999: 120).
14. The FNP did not exactly embrace the situation warmly, but rather blamed the situation on Ratu Mara’s leadership. At a meeting of the FNP, Butadroka called on the nation to give Dr Bavadra’s Coalition Government a chance to show its leadership capabilities. ‘We should not pass judgment on them now. We have to wait for a while to really gauge their performance. Our stand has always been a Fijian Prime Minister, and key Ministers like Home Affairs, Fijian Affairs, Agriculture and Forestry, and Labour and Immigration should be in Fijian hands. Dr Bavadra has done this and has removed some of our fears’. (Fiji Times, May 3, 1987)

15. The cause of the coups remains a source of wide-ranging popular and academic debate (e.g., Lal, 1990; Dean & Ritova, 1988; Robertson & Tamanisau, 1988; Kelly & Kaplan, 2001). The coups have multiple causes, likely including concerns about stability (in the wake of the taukei-initiated unrest), economic policy (on the part of those affected by populist or socialist policies), the institution of a stable non-racial order (for those with a nationalist ideology), diminished political influence (on the part of politicians who had lost office), and Cold-War era alliances (U.S. Congress, 1987).

16. Labour increasingly became an Indian-focused party during this period. While a number of the Fijian leaders of the FLP continued to speak out against deregulation and liberalization, these leaders became marginalized within the FLP and a number of them eventually broke from the party over issues of electoral strategy and leadership.

17. Media coverage of the VLV focused on debate about imposing a ban on commercial activity on Sunday (a position which the party never formally supported, but which was popular among some Fijian nationalists). While a minority of VLV leaders with strong ties to the Methodist Church argued strongly in favor of the Sunday ban, some media outlets reported that the party favored the Sunday ban, despite not having a clear position on the issue. This reporting continued even after Poseci Bune, former Fiji Ambassador to the United Nations, was elected as party leader and stated “The party does not want to impose the ban. I can assure you as party leader that it will not happen” (Fiji Times, April 21, 1999: 3).

18. The terms ethnicity and race are used somewhat synonymously in Fiji. To some extent, “race” tends to be used to refer to essential qualities of a more limited number of groups, while “ethnicity” tends to be used by those wanting to portray a greater variety of groups.

19. The claim that the bulk of the benefit should flow to the Fijian population due to the relative status of disadvantage reflects an oft-repeated popular belief that Fijians comprise the majority of the disadvantaged population. This belief, however, is not supported by the best available evidence, which shows that while Fijians are underrepresented at the top of the economic ladder, poverty rates and lack of access to quality housing are essentially the same between indigenous Fijians and Indians (Government of Fiji and UNDP, 1997; Chand, 2000).

20. There is no direct evidence that Speight’s take-over was timed to prevent the passage of the legislation. Speight did, however, take advantage of a march organized by the NVTLP for the same day, potentially pre-empting a different coup. The causes of this coup likely include a combination of intra-Fijian rivalry,
Fijian nationalism, opportunism, and possibly concerns about the potential for the PC government to succeed in restraining liberal reforms and indigenization (Robertson & Sutherland, 2001, Field, Baba, & Nabobo-Baba, 2005).

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APPENDIX. LIST OF ACRONYMS

Tanzania

ANC  African National Congress
CCM  Chama Cha Mapinduzi (Party of Revolution)
DP   Democratic Party (unregistered)
TANU Tanganyika African Union

Fiji

CAMV Conservative Alliance/Matanitu Vanua
FDB  Fiji Development Bank
FLP  Fiji Labour Party
FNP  Fiji Nationalist Party
FNUF Fiji Nationalist United Front
GCC  Great Council of Chiefs
NFP  National Federation Party
PC   Peoples’ Coalition
SDL  Soqosoqo Duavata ni Lewenivanua (United Fiji Party)
SVT  Soqosoqo ni Vakavulewa ni Taukei (Fijian Political Party)
CHINESE FIRMS UNDER TRANSFORMATION: CORPORATE RESTRUCTURING, EMPLOYEE LAYOFF AND MANAGER TURNOVER IN 1990s

Lu Zheng and Jean Oi

ABSTRACT

China’s reform has favored gradual change and institution-building over rapid, large-scale social engineering. While multifaceted reforms are still in progress and market supporting institutions such as a social security system are still under construction, corporate governance and firm performance is being enhanced. Based on evidence from a 2001 survey of 451 Chinese firms, we found that firms initiated restructuring and lay-off program in response to financial concerns in general, while the specific methods were mediated by social and political constraints. Another finding is that top managers with poor financial performance tended to be removed from post at the juncture of corporate restructuring.
INTRODUCTION

The 1990s witnessed a large wave of corporate restructuring throughout China as the regime attempted a new round of reforms to improve enterprise performance and turnaround loss-making public enterprises. Earlier reforms, such as the manager responsibility system, delegated decision-making power to firm managers and hardened budget constraint without restructuring property rights. In contrast, the new wave of reform initiated in the 1990s has brought a dilution of the state’s sole proprietorship of state-own enterprises (SOEs).

The once secure life-time employment system in the state sectors began to erode in the early 1990s and by the mid-1990s, massive labor force layoff was in progress (Gu, 1999, 2000). While the number of dislocated workers due to restructuring is much lower than in Russia and East European countries, millions of Chinese workers were laid off or, in a smaller number of cases, unemployed. Despite the government’s effort to alleviate suffering of dislocated workers, social unrests among laid-off workers occurred in urban areas (Cai, 2002; Chen, 2000, 2003).

Although the organizational change for Chinese firms in the past had attracted much attention (e.g., Walder, 1987, 1989, 1995; Lardy, 1998; Keister, 1998; Guthrie, 1997, 1999), we are only beginning to understand the nature, process, and the consequences of this new wave of corporate restructuring in Chinese firms (Lin & Zhu, 2001; Oi, 2005). Studies have been done on the privatization of township and village enterprises (TVEs) in rural China (see Oi, 1999; Peng, 2001, 2004; Li & Rozellel, 2003). Our study shifts the focus to their urban counterparts, especially to the SOEs. We begin by considering China’s reform against the backdrop the neoliberal economic model that seems to have won out as centrally planned economies have disappeared or are being reformed.

We argue that while China is embracing many institutions of a market economy, it is not necessarily following a neoliberal model. As we will detail below, China’s economic reform is quite deviant from both the script of neoliberalism and its prescription to follow a big bang approach, like that taken in Eastern Europe and Russia. In contrast to the big bang approach, China’s state-directed, gradualist and multifaceted strategy has contributed to building supportive or complementary institutions for market discipline to work, but it has done so with a concurrent political agenda that often distorted the accompanying economic agenda. Yet, this ongoing, but imperfect, development, nonetheless, overtime, has been conducive to improving financial discipline and corporate governance of Chinese firms.
Drawing on a unique survey data of 451 firms in five Chinese cities, we explore the nature, process, and the consequences of this new wave of corporate restructuring in Chinese firms. We examine three aspects of firm operation during the corporate restructuring wave in 1990s. We divide our analysis into these three aspects to test whether restructuring, worker layoff, and manager accountability are necessarily one and the same, or whether these processes are separate and may occur during different stages of reform and may be driven by differentlogics. Thus, we first examine the conditions that have resulted in organizational restructuring of firms. Our analysis suggests that corporate restructuring is driven by an economic rather than political logic. Second, we examine the conditions that drive the decision to layoff workers. As suggested above, one of our interests is to compare whether these two changes follow the same pattern as many previous studies implied (i.e. that restructuring and workforce downsizing proceed hand in hand) (e.g., Gu, 1999). Our finding disproves this misperception. Third, we examine manager turnover at the juncture of corporate restructuring. We find that by the later stage the corporate reform in 1990s, top managers were held accountable for firm performance. We argue that understanding these dimensions of corporate restructuring require an analysis of the institutional environment in which the firms operate and the peculiarities of China’s economic reform.

**CHINA’S ECONOMIC REFORM AND NEOLIBERALISM**

China’s average GDP growth rate of more than 8% for almost three decades suggests that China’s economic reform has been an astounding success. China’s integration into the global economy and market-oriented economic reforms might be perceived as a triumph for neoliberalism (e.g., Beeson, 2007). It may be true that China’s reform program has reflected two key elements of the neoliberal model, namely market liberalization and privatization. However, the reform path China has taken is quite different from International Monetary Fund (IMF)/World Bank prescription. Not only Sachs and Woo (2000) admitted that China’s strategy is the result of conditions that are unique to China, but Stiglitz (2002) went further by regarding China’s economic reform as a policy challenge to the IMF/World Bank. As the history has shown, the “big bang” or “shock therapy” policy package designed by neoliberal economists resulted in an economic
catastrophe in Russia and some other Eastern European countries (e.g., King, 2003). In our view, although neoliberalism points to a desirable destination, it frequently fails to achieve its goals.

Rather than leaving development and growth to the market, the China state developed industrial policies to build internationally competitive businesses and exerted a firm guiding hand in directing the shape and direction of the market. For example, in October 2006, the Industrial and Commercial Bank of China’s (ICBC) $19 billion initial public offering (IPO) was the world’s largest IPO. Also, China Mobile, a wireless service provider with a market capitalization close to $200 billion, is one of the largest companies in the world. Yet, it must be understood that these were state conceived and sponsored projects. Such state involvement in building those flagship companies runs counter to the neoliberal model, which is premised on the market as the guiding hand.

Another distinguishing feature of China’s gradual approach to reform is the leadership’s decision to experiment with and settling for limited institutional changes in exchange for limited social costs even if these fail to achieve economic goals. This approach, characterized as “grasping for stones to cross the river,” sets in motion a series of limited reforms that yield economic growth and political support for reform before moving to further reform. This contrasts with the big bang approach that resulted in a “mass privatization” in Russia that caused a vicious cycle of capital starvation, asset stripping and “demodernization” (King, 2003), which failed to achieve its intended goals of encouraging economic restructuring, hardening budget constraints and mitigating agency problems. China’s gradualist approach, while incurring some delayed economic efficiency, has avoided the deleterious consequences of rapid large-scale privatization.

While neoliberals attributed the failure of the economic transition in Russia to incomplete implementation of neoliberal policies by local elites, the experience from China suggests the importance of institution building for a successful transition. As Polanyi (1957) claimed, markets do not create institutions so much as institutions create markets. The neoliberal model with its belief in the efficacy of markets ignores the importance of market supporting institutions and the time required to build and perfect such institutions. Over the course of China’s gradualist reform, social and market institutions that are conducive to improving financial discipline and corporate governance are being crafted. As the following sections will detail, China’s corporate restructuring rests on the development of a series of complementary institutions such as reforms in the taxation and banking system, as well as intermediate strategies like corporatization.
and shareholding while a sufficient social welfare system was still being built.

A CHANGING INSTITUTIONAL ENVIRONMENT

Students in socialist economies have long attributed poor corporate governance to governments’ limited monitoring capacity and soft budget constraints (e.g., Kornai, 1992). Nevertheless the successful take-off of China’s economy has called for a closer look on China’s idiosyncratic institutional arrangements (Oi, 1999; Oi & Walder, 1999). Previous research has maintained that China’s decentralized industrial hierarchy and strong financial incentives of local governments, especially which are at a lower levels, had offered direct monitoring on firms under jurisdiction, and therefore boosted industrial output (Oi, 1992, 1999; Walder, 1995). We follow this line of research as we still pay close attention to China’s institutional environment in which firms operate. But we find that over the course of the reforms, the source of discipline and incentives has changed. For example, Walder (1995) examined China’s decentralized industrial hierarchy, and attributed China’s rapid industrial growth to the changing incentives for government officials, who in turn acted like “top management team” and exerted administrative discipline on firms under their jurisdiction. However, in contrast with the earlier stage of the reform in 1980s or early 1990s when various level of government more involved in firms’ daily operation, later corporate reform measures granted more autonomy to firms. It is firms that directly participate and compete in the market economy. Consequently, in this study we shift the focus to an examination on the incentives for firms themselves, and on the day-to-day market constraints.

In Kornai’s (1992) cogent analysis of the soft budget constraint in redistributive economies, he stressed the non-financial interests that governments have in the enterprises under their jurisdiction. These interests, such as the supply of scarce inputs for other enterprises, maintenance of full employment, funding of pensions, medical insurance, and provision of housing and social services, conflict with the financial interest in strong economic performance. The non-financial interests lead to the problem of soft budget constraints, which protected firms from being subject to financial discipline and market competition. In the sections below, we will show that reforms in China have decreased these non-financial interests of the government and have increasingly embedded firms in markets.
For example, the government has gradually withdrawn from routine involvement in production, and allowed firms to unload much of their non-production related social responsibility costs, such as operating schools and hospitals as part of the work unit (danwei) system, to local governments. The economic incentives for both firms and local governments are now such that economic performance is increasingly a top priority.

**From Shortage to Surplus: The Declining Role of SOEs**

The economy of shortage is no longer a correct characterization of China today after three decades of rapid market-oriented economic growth. Nor do governments worry about scarce inputs for the firms under their jurisdiction. Bureaucratic coordination in input and output has been replaced in large measure by market mechanisms. Moreover firms must now be concerned about marketing and sales. In sharp contrast to the past, the central government, from time to time, has tried to cool down over expansion and growth of the economy. Moreover, the development of the private sector by the late 1990s has meant that the government’s dependence on SOE output has greatly decreased. When the reforms in China began in 1978, 78% of total industrial output came from SOEs. By 1995, the SOEs’ share had shrunk to less than one-third and further declined since then (China Statistical Yearbook, 2000). This change in the structure and dynamics of the economy has also consequently allowed the state at all levels to be more firm in disciplining public firms.

**Building up a Government-run Social Welfare System**

The transition to a social security system from a work-unit–based welfare system has been under way since mid-1980s. The “cradle-to-grave” welfare system had worked well under the soft budget constraint in the planned economy. As the market-oriented reforms brought market competition from the emerging private sectors as well as foreign ventures, the redundant workforce and huge burden of social welfare provisions have disadvantaged state firms and kept them from being profitable even if they are efficient in production (Gallagher, 2005). To level the playing field, since 1986 the government has imposed a series of welfare reforms to shift responsibilities from SOEs to a combination of government, enterprises, communities and individuals. Local governments rather than work units are now responsible
for the administration and payment of pension and medical insurance to employees in public sector (Smuthkalin, 2006). Meanwhile, in 1990s in urban areas unemployment insurance and minimum living standards have been established, although resource scarcity and administrative incapacity still hinder the creation of a national, unified social welfare system (Solinger, 2002; Smuthkalin, 2006; Oi, 2005, 2006). At best, the system is only unified to the provincial level, at worse workers have been left with a firm-based welfare system that may mean little or no assistance in spite of regulations that provide laid off workers and pensioners with benefits. The inability of some firms and localities to provide the promised benefits has resulted in social unrest by the laid-off and unemployed workers and by pensioners. Knowing the potential political costs of using layoffs to restructure, state during the early phases of restructuring favored those forms of restructuring, such as shareholding, as an interim solution to keep as many workers as possible employed until a sufficient welfare system was in place. Thus, in spite of the continued shortcomings in national welfare institutions, first steps in effective restructure could proceed (Oi, 2006). Moreover, recent fieldwork by the authors suggests that local governments, if they are lucky enough to have increased revenues and opportunities for alternative employment opportunities, i.e. a thriving private sector, now are moving more aggressively to terminate the relationship between workers and their firms by providing them with sufficiently lucrative severance packages (maiduan gongling).

Unloading Social Services

Firms in China’s pre-reform period were both social as well as economic entities. The reforms have slowly but surely diminished the burden of providing public housing and other services connected with the work unit system. From 1990s onward, provision of housing has been replaced by a rapidly developing real estate market. Old housing owned by public sectors, including enterprises, was sold to individual employees at discounted price. New housing has to be purchased from real estate developers. Social services, such as day care centers, medical clinics, reading rooms, entertainment centers, are either closed, sold to private owners, or transferred to local governments. Some may suspect the revocation of these long time rights for workers may most likely touch off labor unrest (e.g., Walder, 1991). However, as long as they are compensated well with increasing wages,
workers seem more than happy to receive better service from the growing service sectors outside of work unit.

**Taxation and Banking Reform**

While changes have been happening within the SOEs themselves, the larger local economic context also has changed. Since early 1980s, a fiscal contracting system between levels of governments had spurred a rapid, local government-led economic growth by giving officials both the incentive and investment funds (Oi, 1999). A second effort was made with the 1994 tax reform (fenshuizhi) that divided revenues into central and local revenues, aimed at recovering for the central government the extra-budgetary funds that had been allocated to local governments under the 1980s reforms. This change created a situation where the revenue base for central and local governments was further clarified, requiring that local governments turn over more revenues to the upper levels, thus requiring local authorities to cut more costs. This would include hardening the budget constraints and placing a harder financial discipline on firms under their administration.

At approximately the same time, banks began to curtail the access of money-losing SOEs to credit after mid-1993 (Lardy, 1998). Banks were forced to become more commercially oriented rather than continue as an administrative arm of the finance bureau, freely doling out policy loans. In 1997, for the first time in many years, banks only used half of their authorized 800 billion yuan credit quota. This new conservative spending was not a coincidence – it coincided with a new state policy that stipulated that the heads of banks who failed to improve their financial performance would be fired (Lardy, 1998). Interviews in banks as well as firms reveal that individual bankers did indeed fear that they would be held personally responsible for non-performing loans given under their watch. There is anecdotal evidence that some local banks had to be ordered to extend additional loans so SOEs could pay wage debt to workers and thus keep social stability in their communities. If so, this could be interpreted in a sign that banks have become more concerned about their own bottom line.

Overall, the tightening pressure on banks means that money-losing firms are less likely to be given loans by banks. If bail outs come, it will have to be at the explicit instruction of local governments, to be given as a last resort in the case of worker demonstrations. Scattered statistics provide some evidence of hardened budget constraints and enforcement of fiscal discipline
by both banks and local governments. The number of SOE bankruptcies jumped greatly from 710 in 1993 to 6,232 cases in 1996 (Cao, 1997). Between 1996 and 2000, the state approved the merger or bankruptcy of 5,335 industrial SOEs (Holz, 2003). To let insolvent SOEs go bankrupt has great implications and is still not readily used. However, the fact that SOEs have been allowed to go bankrupt cannot but have an impact on managers, workers, and government officials.

Taken together, the above described changes in China’s rapidly expanded economy have decreased a firm’s bargaining power with local governments and limited bailout options. Lifting social security and welfare services from enterprises has a side-effect of making it easier to measure firm performance – they no longer have the excuse that they are saddled with the burdens of the *danwei* system. The 1994 fiscal reforms help align local government revenue with firm profitability. Finally, the banking reforms impose more stringent standards for access to bank loans. In all, the sum of the reforms, which we briefly described above, added up to greater pressure to press firms to adhere to greater financial discipline and improved economic performance. The changed fiscal context created the incentives for firms and local governments to act in a more disciplined way with regard to costs, including the layoffs of surplus workers and the firing of managers who performed poorly.

**DATA**

The data used in this paper is from a survey carried out in 451 enterprises of different ownership forms in four provinces, five cities, and four industrial sectors in 2000 and early 2001\(^3\) (Table 1). The five cities are Wuxi and Yancheng in Jiangsu Province, Hangzhou in Zhejiang Province, Zhengzhou in Henan Province, and Jiangmen in Guangdong Province. To control for variations across industrial sectors, we limited our focus on four major sectors: machinery, electronics, textiles, and chemical engineering. One of the main purposes of the survey was to document the timing and forms of enterprise restructuring. The respondents were factory managers and their accountants. With the assistance of researchers in China we asked questions concerning restructuring and obtained economic data including an enterprise’s output, profits, loans, workers, etc. in 1990s, as well as background information on its history, including questions such as year established, registration, and ownership. Our collaborators in China conducted the survey through face-to-face interviews.
The sample of enterprises was drawn from the total number of enterprises in each of the four sectors selected in each city. The complete lists of the firms came from the Statistical Bureau in these cities. Firms were arranged according to size and grouped. Firms were then chosen from each group according to set intervals on the enterprise name list. Assuming that small- and medium-sized enterprises would dominate our sample, we added additional large sized enterprises to the sample. Of course, this process means that our sample was not random. Our analysis shows that our sample is biased towards the large and middle enterprises, especially in Wuxi and Yancheng.

We caution that the over representation of the larger firms in our sample may underestimate the degree of privatization. But the value of our survey results remains high given that we are mainly interested in what is happening in the larger, more complex SOEs. These are the firms that have the complex mixture of institutional forms and present the greatest challenges in terms of layoffs. These are the enterprises that have attempted to adopt the institutions of western corporate governance such as boards of directors.

### Table 1. A Summary of Survey Data.

<table>
<thead>
<tr>
<th>City</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wuxi</td>
<td>83</td>
<td>18.4</td>
</tr>
<tr>
<td>Yancheng</td>
<td>58</td>
<td>12.9</td>
</tr>
<tr>
<td>Hangzhou</td>
<td>43</td>
<td>9.5</td>
</tr>
<tr>
<td>Zhengzhou</td>
<td>130</td>
<td>28.8</td>
</tr>
<tr>
<td>Jiangmen</td>
<td>137</td>
<td>30.4</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Industry</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery</td>
<td>101</td>
<td>22.6</td>
</tr>
<tr>
<td>Electronics</td>
<td>114</td>
<td>25.5</td>
</tr>
<tr>
<td>Textile</td>
<td>107</td>
<td>23.9</td>
</tr>
<tr>
<td>Chemical engineering</td>
<td>125</td>
<td>28.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Firm Size (self-reported)</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Small</td>
<td>207</td>
<td>46.3</td>
</tr>
<tr>
<td>Medium</td>
<td>157</td>
<td>35.1</td>
</tr>
<tr>
<td>Large</td>
<td>83</td>
<td>18.6</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Firm Type before Restructuring</th>
<th>Frequency</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>SOE</td>
<td>232</td>
<td>51.9</td>
</tr>
<tr>
<td>Urban collective</td>
<td>67</td>
<td>15.0</td>
</tr>
<tr>
<td>Rural collective</td>
<td>97</td>
<td>21.7</td>
</tr>
<tr>
<td>Other</td>
<td>51</td>
<td>11.4</td>
</tr>
</tbody>
</table>

Note: “Other” includes cooperatives, joint ventures and other types of firms.  
Source: Author’s survey in 2001.
From our perspective, this over representation of larger firms is a plus rather than a serious flaw. Finally, we should note that while we had a high response rate to our complex survey in four out of the five cities in our sample, in Hangzhou city we received responses from only about a third of the enterprises selected for the sample. Such problems necessarily limit the conclusions and generalizations that could be drawn from our results. The remainder of this paper will use our survey data to see whether there are any indications that these institutional changes created new incentives that allowed corporate restructuring and governance to improve.

CORPORATE RESTRUCTURING

Historical Context

The Chinese government has carried out three stages of SOE reforms since 1979. The first reform was to increase financial incentives to enterprises, on one hand, and hardened budget constraint, on the other hand. This phase featured the “tax for profit” (li gai shui) policy that introduced the concept of profits for firms and “replaced grants with loans” (bo gai dai) reform that made firms responsible for funds provided by the state through the banking system. For the first time, firms had to pay interest as well as principle. Together these policies more clearly demarcated revenues and financial responsibility between firms and government.

Later in 1984, the state introduced the second stage of reform, the so-called factory director responsibility system, to all state industrial enterprises. This reform aimed to enhance the decision-making authority of SOE managers and provided greater monetary incentives. Despite some initial improvement in performance, urban enterprises entered the 1990s with continued financial difficulties and heavy losses (Holz, 2001). The deteriorating performance of the state sector and its inability to pay back loans also caused a huge burden on the state-owned banking sector and the economy as a whole (Lardy, 1998).

In the party’s third plenum of the 14th central party committee in November 1993, a third stage of reform began with the goal of restructuring SOEs to create a “modern enterprise system.” The main avenue for establishing the modern enterprise system was to follow the model of western corporations and restructure state sector enterprises into shareholding corporations, while maintaining state ownership. Before long, however, the state realized that it was too ambitious to turn around all
firms under state ownership. In 1995, the government then decided to adopt a differentiated and phased policy and began to pursue a reform strategy known as “zhua da fang xiao” – “grasp the large enterprises and let go of the small.” This reform initiative did not gain real momentum until the 15th Party Congress in 1997, when corporate restructuring was sanctioned as a political task to carry out. This paved the way to restructure large SOEs into shareholding limited liability companies (LLC), and to turn small SOEs into shareholding cooperatives and private enterprises. Notably, in the latter case of the small SOEs, both property rights and control of the firm would transfer to private hands. Taken together this two-pronged strategy allowed corporate restructuring to include incorporation, merger, arranged sale, auction, leasing, and bankruptcy. The central government hoped that the restructuring reforms would further increase managerial autonomy and provide stronger incentives to managers and workers. In addition, by letting go of small-sized SOEs, the government bodies could achieve more effective monitoring of the remaining large (and most important) SOEs.

**Types of Corporate Restructuring**

Our data shows by the time the survey was conducted in 2001, the majority of firms in the sample had gone through at least one restructuring. Out of 451 firms in the sample, only 146, or less than one third of the total, had not been restructured. Table 2 provides further information on different types of restructuring.

<table>
<thead>
<tr>
<th>Type of Restructuring</th>
<th>N</th>
<th>% Among all 451 Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shareholding</td>
<td>168</td>
<td>37.3</td>
</tr>
<tr>
<td>Sale</td>
<td>27</td>
<td>6.0</td>
</tr>
<tr>
<td>Joint venture with foreign firms</td>
<td>67</td>
<td>14.9</td>
</tr>
<tr>
<td>Lease or similar arrangement</td>
<td>61</td>
<td>13.5</td>
</tr>
<tr>
<td>Bankruptcy</td>
<td>9</td>
<td>2.0</td>
</tr>
<tr>
<td>Other types of restructuring</td>
<td>36</td>
<td>8.0</td>
</tr>
<tr>
<td>No change</td>
<td>146</td>
<td>32.4</td>
</tr>
</tbody>
</table>

**Note:** “Other types of restructuring” mainly include restructuring types in between. For example, part of a firm was sold or merged, and part of it was rent out.

**Source:** Author’s survey in 2001.
Incorporation into shareholding companies is the most popular form of restructuring. Among restructured firms, more than half of them (or around 37% of all firms including the unrestructured) are now shareholding companies (see Table 2). Shareholding companies can be further categorized into shareholding LLC and shareholding cooperative. SOEs with equity capital beyond 10 million yuan can become a shareholding LLC under the guideline for the 1993 Company Law. Some of the shareholding LLCs managed to get approval to get listed on China’s domestic stock markets; some went public in overseas stock exchanges. In those listed SOEs, controlling shares are still held by a variety of governmental branches or by state-owned legal persons, i.e. other enterprises. Only about one third of the shares are allowed to be freely traded on stock exchanges.

Shareholding cooperatives are owned wholly or predominantly by a firm’s employees. Two types are commonly seen in share holding cooperatives: shares equally held by all employees and majority shares held by management. The former choice is closer to socialist ideology and more appealing to the government and workers. However, managers in charge of this type of firm often complain about lack of decision-making power and authority because workers have voting powers and thus intervene in managerial issues. Managers want larger shares to facilitate decision making. Managers have pushed hard to fight for a controlling share in this type of restructured firms. Our survey data suggests that over time, managers are getting larger shares. Recent interviews suggest that this trend is being continued in a number of localities as both managers and local officials realize that there needs to be big “stake holders.”

Turning formerly public-owned firms into private firms deviates most from the collective ideology. In our sample, only 6% of firms were sold to private hands (see Table 2). Privatizations at lower government levels are widely criticized for their lack of transparency and for giving away state assets. Perhaps equally, if not more important, local governments are constrained in their sale of firms by their inability to provide adequate severance packages for workers who would lose their jobs in the sale of firms. As a result, outright sales are still limited in number although there is evidence to suggest that these are increasing (Oi, 2005).

In between shareholding and outright sell, 15% of the sample became part of a joint venture with a foreign company. Around 14% of the sample was leased to individuals, often managers of the firm. In some cases, this arrangement eventually led to the complete privatization of the leased firm.

Whether privatization will ultimately solve the problems plaguing SOEs is a subject of debate. Some economists argue that private ownership is
necessary for achieving firm efficiency (e.g., Zhang, 1997; Lardy, 1998). However, empirical studies in both developed market economies and in post-socialist societies cast doubt on this simple causal relationship. An excellent review of the relationship between ownership and firm performance by Kang and Sorosen (1999) finds that the effect of ownership form on firm performance was at best mixed in the United States. Former Soviet and Eastern European countries achieved wildly divergent results in the abrupt transition from state ownership to private ownership (Kogut & Spicer, 2002). A rigorous analysis on China’s industrial firms by Holz (2003) finds the profitability of both SOEs and non-SOEs followed the same patterns over the last two decades in the 20th century. The profitability gap between them can be more than explained by just two factors, i.e. higher circulation taxes and higher capital intensity in SOEs. All of these studies suggest that private ownership is not a sufficient condition for generating a greater level of efficiency. Whether privatization has actually increased the efficiency of firms in China that have been privatized is beyond the scope of this paper, and ultimately must await further research. For now, in this paper, we ask a more limited question that will allow us to examine whether corporate restructuring that we described above has resulted in greater accountability by the managers of firms and whether firms are taking corrective action in response to economic failures, i.e. worker layoffs.

Initiators of Corporate Restructuring

Who are the main actors in these corporate restructurings? As in previous corporate reforms, the key players are the state and its agents at various levels of government. Our data shows 44% of all the restructurings were initiated by local governments (Table 3). And another 17% was led by specific industrial ministries or bureaus within government. It is worth noting that managers took initiative in about 31% of the restructuring cases. Although manager may initiate the restructuring, ultimately the decision must be approved by the local government.

Some researchers have pointed out that in order to get rid of the burden of loss-making SOEs, local governments have incentives to privatize them (e.g., Cao, Qian, & Weingast, 1999). While there may be incentive for local governments to privatize, local governments are also under political and economic constraints. It cannot be assumed that they have the financial resources to carry out privatization. Local officials also need to calculate the
consequences of their actions, not only for their communities but also their own political future.

**Corporate Restructuring: Theories and Hypotheses**

Theories on structural change in firms fall into two camps. The economic approaches focus on efficiency and market mechanisms. Organizational changes, e.g., vertical integration, diversification, and the adoption of M-form, are considered as rational responses to market conditions in order to reduce transactional cost or/and achieve higher level of efficiency (e.g., Williamson, 1975; Coase, 1937; Chandler, 1962, 1977). In contrast, sociological theories, especially institutional theory have been prevalent in explaining firm’s practice or structure in terms of response toward regulatory, normative, or cultural-cognitive aspects of institutional systems. According to this line of reasoning, changes in organizational practice or structure have less to do with efficiency than taken-for-granted and concerns about legitimacy (Meyer & Rowan, 1977; DiMaggio & Powell, 1983). More specifically, pressures originating from the state are the most direct mechanism of institutional diffusion based on coercion. As long as the state controls critical resources, dependent organizations are likely to adopt behavior sanctioned by the state. Logical deductions from these two traditions would provide competing hypotheses with regard to structural change of firms in general and corporate restructuring in Chinese firms in particular. To what extent these hypotheses hold would help us gauge to what extent Chinese firms have changed to profit-oriented market players from production units in a planned economy.

Following the market discipline argument, we would expect that firms under stiff market competition tend to act more quickly to adopt a modern

<table>
<thead>
<tr>
<th>Initiator</th>
<th>N</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial ministry or bureau</td>
<td>52</td>
<td>17.5</td>
</tr>
<tr>
<td>Local government</td>
<td>131</td>
<td>44.0</td>
</tr>
<tr>
<td>Manager</td>
<td>92</td>
<td>30.9</td>
</tr>
<tr>
<td>Workers</td>
<td>8</td>
<td>2.7</td>
</tr>
<tr>
<td>Outside buyer</td>
<td>2</td>
<td>0.7</td>
</tr>
<tr>
<td>Multiple initiators</td>
<td>13</td>
<td>4.4</td>
</tr>
</tbody>
</table>

*Source: Author’s survey in 2001.*
organizational form as an attempt to survive and get ahead. Therefore, we hypothesize that:

**Hypothesis 1A.** Firms under more financial pressure are more likely to restructure.

On the other hand, if this wave of restructuring is just more of the same—mere conformity to yet another government directive, then the overall pattern would follow an institutionalization process, in which restructuring is a taken-for-granted organizational fad. It has nothing to do with market discipline or efficiency concerns. Following this line of argument, we would expect a competing hypothesis in contrast with Hypothesis 1A as:

**Hypothesis 1B.** Whether or not a firm carries out a restructuring has nothing to do with its financial situation.

Another interest of us is to look at how different types of firms may respond differently to corporate restructuring. The main comparison lies between SOEs and collectives. Firstly, the state considered SOEs the backbone of the state industrial plan. Therefore SOEs had priority in resource and benefit allocations under central planning. In contrast, urban collectives were established by local government or SOEs to accommodate workers or their family members who needed a job; rural collectives were under township or village authority to create local revenue. Employees in SOEs received substantially better income and benefits than those in collectives (Lin & Bian, 1991). As collectives were never part of the plan and thus not entitled to state subsidies such as cheap credit and low-priced inputs, collective firms were less protected by the state than SOEs (Walder, 1986; Peng, 2001). As collectives proved to be one of the main engines of China’s economic growth in the 1990s, researchers maintained it was because collectives are more subject to the harsher discipline of market competition (e.g., Peng, 2001). The second reason which may make SOEs and collectives respond differently in corporate restructuring is related to the idea of “structural inertia” (e.g., Hannan & Freeman, 1984). Relative to SOEs, collectives tend to be small in size, less complex in structure, and less bureaucratic in decision making. Moreover, collectives have fewer policy burdens and are younger in organizational age than SOEs. With less organizational inertia, collectives are likely to have fewer constraints that would hinder organizational restructuring. The third reason lies in stronger incentives for collectives to restructure. Collectives had been described as “semiprivate” or “hybrid” firms with vaguely defined property rights in the past (Peng, 1992; Nee, 1992). The corporate restructuring provides an opportunity to
clarify and allocate ownership shares by incorporating the firm into a shareholding company. Therefore, collective firms have stronger incentive to act promptly to restructure.

Therefore we hypothesize that:

**Hypothesis 2A.** Collective firms are more likely to restructure than SOEs.

Meanwhile, as far as the institutional coercive isomorphism (DiMaggio & Powell, 1983) argument goes, firms closer to the institutional center i.e., the state, would respond more promptly to institutional pressure and act more quickly to government policy. Therefore a competing hypothesis of Hypothesis 2A would be:

**Hypothesis 2B.** SOEs tend to act more promptly to restructure than collectives.

We should be clear that we are not implying that corporate governance for Chinese firms is fully established and fully effective. We are only arguing that the reforms to date help to expose Chinese firms to a greater level of market discipline. The question is to what degree are firm decisions and actions following an economic logic.

*The Pattern of Corporate Restructuring: Findings from Event History Analysis*

We employed a piecewise exponential model to examine the hazard rate of having the 1st restructuring from 1995 to 2000. We analyze and compare the effect of a series of independent variables across three time periods (1995–1996, 1997–1998, and 1999–2000) covered in our survey. The period of 1995–1996 was the earlier stage of the corporate restructuring reform. This reform did not pick up much momentum until the 15th Congress of the Chinese Communist Party in 1997 when it was emphasized as an important political task. To provide direction to future economic reform, the then President and Party General Secretary Jiang Zemin announced that “we should combine the reform of state-owned enterprises with their reorganization, upgrading and better management … We shall quicken the pace in relaxing the control over small state-owned enterprises and invigorating them by way of reorganization, association, merger, leasing, contract operation, the joint stock cooperative system or sell-off.” This political directive from the ruling party changed the incentive structure for decision makers for carrying out corporate restructuring. We define 1999–2000 as the
last period. We are interested to see how the model estimates would be for these three periods.

The independent variables are (1) debt asset ratio to measure a firm’s financial health; (2) profit to measure a firm’s profitability; (3) asset and number of employees in their natural log form respectively as measurements for firm size; (4) age of the firm; (5) type of the firm; (6) industry of the firm; and (7) city of the firm. Table 4 reports univariate analysis of the above

Table 4. Means/Percent for Variables Used in Multivariate Analyses in Selected Years.

<table>
<thead>
<tr>
<th>Variables Used</th>
<th>1994</th>
<th>1996</th>
<th>1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt asset ratio</td>
<td>0.71</td>
<td>0.70</td>
<td>0.74</td>
</tr>
<tr>
<td></td>
<td>(0.3)</td>
<td>(0.3)</td>
<td>(0.4)</td>
</tr>
<tr>
<td>Profit (in millions of yuan)</td>
<td>3.79</td>
<td>3.69</td>
<td>3.39</td>
</tr>
<tr>
<td></td>
<td>(13.8)</td>
<td>(19.2)</td>
<td>(29.2)</td>
</tr>
<tr>
<td>Asset (in millions of yuan)</td>
<td>118.26</td>
<td>155.11</td>
<td>180.20</td>
</tr>
<tr>
<td></td>
<td>(235.6)</td>
<td>(358.8)</td>
<td>(438.6)</td>
</tr>
<tr>
<td>Asset in thousands (log)</td>
<td>10.59</td>
<td>10.78</td>
<td>10.76</td>
</tr>
<tr>
<td></td>
<td>(1.6)</td>
<td>(1.6)</td>
<td>(1.7)</td>
</tr>
<tr>
<td>Number of employees</td>
<td>936</td>
<td>922</td>
<td>765</td>
</tr>
<tr>
<td></td>
<td>(1,292.9)</td>
<td>(1,387.9)</td>
<td>(1,273.0)</td>
</tr>
<tr>
<td>Number of employees (log)</td>
<td>6.1</td>
<td>6.1</td>
<td>5.8</td>
</tr>
<tr>
<td></td>
<td>(1.3)</td>
<td>(1.3)</td>
<td>(1.3)</td>
</tr>
<tr>
<td>Firm age (in years)</td>
<td>20.2</td>
<td>21.2</td>
<td>21.6</td>
</tr>
<tr>
<td></td>
<td>(14.7)</td>
<td>(15.2)</td>
<td>(15.8)</td>
</tr>
<tr>
<td>Type</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State-owned</td>
<td>56.2</td>
<td>54.7</td>
<td>52.5</td>
</tr>
<tr>
<td>Urban collective</td>
<td>15.0</td>
<td>16.5</td>
<td>15.2</td>
</tr>
<tr>
<td>Rural collective</td>
<td>21.2</td>
<td>20.8</td>
<td>21.0</td>
</tr>
<tr>
<td>Others</td>
<td>7.6</td>
<td>8.0</td>
<td>11.3</td>
</tr>
<tr>
<td>Industry</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>24.4</td>
<td>24.5</td>
<td>22.8</td>
</tr>
<tr>
<td>Electronics</td>
<td>24.1</td>
<td>24.3</td>
<td>25.1</td>
</tr>
<tr>
<td>Textile</td>
<td>24.7</td>
<td>24.8</td>
<td>24.0</td>
</tr>
<tr>
<td>Chemical engineering</td>
<td>26.8</td>
<td>26.4</td>
<td>28.1</td>
</tr>
<tr>
<td>City</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wuxi</td>
<td>20.3</td>
<td>19.5</td>
<td>17.5</td>
</tr>
<tr>
<td>Yancheng</td>
<td>13.8</td>
<td>13.1</td>
<td>12.9</td>
</tr>
<tr>
<td>Hangzhou</td>
<td>8.2</td>
<td>8.5</td>
<td>8.5</td>
</tr>
<tr>
<td>Zhengzhou</td>
<td>23.8</td>
<td>26.9</td>
<td>29.7</td>
</tr>
<tr>
<td>Jiangmen</td>
<td>33.8</td>
<td>32.0</td>
<td>31.3</td>
</tr>
</tbody>
</table>

Note: Numbers in parentheses are standard deviations.
Source: Author’s survey in 2001.
independent variables in selected years i.e., 1994, 1996, and 1999. Although the average debt asset ratio was around 0.70, it went as high as 3 in some firms. The value for profit also had a wide range from negative 296 million yuan to positive 385 million yuan. In terms of firm age, some firms had been in business for over 70 years, while there are many new entries every year.

Examining the effects of independent variables over time requires a model that allows the effects of the variables to vary across historical periods. For this purpose, we used piecewise exponential models that allow intercepts and effects of covariates to vary across historical periods. We estimated models with maximum likelihood (ML) method. In addition, the method handles right-censored event history data in a statistically appropriate way. By using likelihood-ratio $\chi^2$ statistics (Tuma & Hannan, 1984), we can also test nested models. In our analysis, we constrain the coefficients of covariates, except for the intercepts, to be constant in every historical period; let us call this as “model A.” We also let all parameters vary across the historical periods; this is “model B.” Since model A is nested within model B, we can test whether the effects of covariates vary significantly across the historical periods. The likelihood ratio test comparing our model B against the model A is significant at the level of 0.05, which enables us to reject the null hypothesis that effects of independent variables do not change in different periods.

Table 5 gives the maximum likelihood estimates of the models. The first column tells the estimates for model A, and the next three columns give the period-specific estimates for model B. Estimates for model A provide the overall trend for the whole time period. In this period of 1995–2000, firms making more profit are statistically less likely to have a restructuring, other things being equal. In other words, loss-making firms have a higher chance to have a restructuring. The effect of debt-asset ratio does not reach significance level. Older firms tend to have restructuring although the effect is marginally significant at 0.05 level ($p=0.07$). Compared to SOEs, both urban collectives and rural collectives are more likely to restructure. Firms in chemical engineering tend to have lower hazard rates to have a restructuring. Again, the difference is only marginally significant. Relative to firms in Wuxi, firms in Zhengzhou and Jiangmen are less likely to restructure. Central to our theoretical concerns, the results from the model for all years by and large favor the hypotheses derived from the economic rationality model ($H1A$ and $H2A$) that less profitable firms are more likely to reform and collectives act more promptly to have a restructuring.

The model for different time periods reveals richer and subtler information. It turns out that, in the first period (1995–1996), debt asset ratio had marginally significant positive effect on the likelihood of corporate

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt asset ratio</td>
<td>0.149</td>
<td>0.386</td>
<td>−0.027</td>
<td>0.372</td>
</tr>
<tr>
<td></td>
<td>(0.208)</td>
<td>(0.219)</td>
<td>(0.484)</td>
<td>(0.543)</td>
</tr>
<tr>
<td>Profit (in millions of yuan)</td>
<td>−0.006*</td>
<td>−0.020</td>
<td>−0.010</td>
<td>−0.009*</td>
</tr>
<tr>
<td></td>
<td>(0.003)</td>
<td>(0.019)</td>
<td>(0.009)</td>
<td>(0.004)</td>
</tr>
<tr>
<td>Asset in thousands (log)</td>
<td>−0.075</td>
<td>−0.268</td>
<td>−0.032</td>
<td>−0.057</td>
</tr>
<tr>
<td></td>
<td>(0.088)</td>
<td>(0.188)</td>
<td>(0.125)</td>
<td>(0.163)</td>
</tr>
<tr>
<td>Number of employees (log)</td>
<td>−0.024</td>
<td>0.406</td>
<td>−0.065</td>
<td>−0.096</td>
</tr>
<tr>
<td></td>
<td>(0.117)</td>
<td>(0.282)</td>
<td>(0.159)</td>
<td>(0.209)</td>
</tr>
<tr>
<td>Firm age (in years)</td>
<td>0.010(\uparrow)</td>
<td>0.016</td>
<td>0.012</td>
<td>−0.00005</td>
</tr>
<tr>
<td></td>
<td>(0.006)</td>
<td>(0.014)</td>
<td>(0.008)</td>
<td>(0.012)</td>
</tr>
<tr>
<td>Type(c)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Urban collective</td>
<td>0.587 **</td>
<td>0.644</td>
<td>0.342</td>
<td>1.113 **</td>
</tr>
<tr>
<td></td>
<td>(0.201)</td>
<td>(0.485)</td>
<td>(0.290)</td>
<td>(0.354)</td>
</tr>
<tr>
<td>Rural collective</td>
<td>0.475 *</td>
<td>1.077 *</td>
<td>0.327</td>
<td>0.418</td>
</tr>
<tr>
<td></td>
<td>(0.204)</td>
<td>(0.499)</td>
<td>(0.278)</td>
<td>(0.401)</td>
</tr>
<tr>
<td>Others</td>
<td>−1.058 *</td>
<td>−0.307</td>
<td>−2.020 *</td>
<td>−0.567</td>
</tr>
<tr>
<td></td>
<td>(0.479)</td>
<td>(1.097)</td>
<td>(1.027)</td>
<td>(0.660)</td>
</tr>
<tr>
<td>Industry(c)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electronics</td>
<td>−0.081</td>
<td>−0.604</td>
<td>0.174</td>
<td>0.054</td>
</tr>
<tr>
<td></td>
<td>(0.210)</td>
<td>(0.514)</td>
<td>(0.286)</td>
<td>(0.443)</td>
</tr>
<tr>
<td>Textile</td>
<td>−0.389</td>
<td>−0.533</td>
<td>−0.266</td>
<td>0.026</td>
</tr>
<tr>
<td></td>
<td>(0.218)</td>
<td>(0.467)</td>
<td>(0.300)</td>
<td>(0.468)</td>
</tr>
<tr>
<td>Chemical engineering</td>
<td>−0.395(\uparrow)</td>
<td>−0.654</td>
<td>−0.500</td>
<td>0.033</td>
</tr>
<tr>
<td></td>
<td>(0.212)</td>
<td>(0.440)</td>
<td>(0.318)</td>
<td>(0.412)</td>
</tr>
<tr>
<td>City(c)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yancheng</td>
<td>0.073</td>
<td>−1.224 *</td>
<td>0.259</td>
<td>0.880 (\uparrow)</td>
</tr>
<tr>
<td></td>
<td>(0.240)</td>
<td>(0.590)</td>
<td>(0.332)</td>
<td>(0.502)</td>
</tr>
<tr>
<td>Hangzhou</td>
<td>−0.193</td>
<td>−0.726</td>
<td>−1.003 *</td>
<td>0.976 *</td>
</tr>
<tr>
<td></td>
<td>(0.272)</td>
<td>(0.646)</td>
<td>(0.506)</td>
<td>(0.480)</td>
</tr>
<tr>
<td>Zhengzhou</td>
<td>−0.544 *</td>
<td>−1.088 *</td>
<td>−0.442</td>
<td>−0.166</td>
</tr>
<tr>
<td></td>
<td>(0.244)</td>
<td>(0.554)</td>
<td>(0.336)</td>
<td>(0.523)</td>
</tr>
<tr>
<td>Jiangmen</td>
<td>−0.512 *</td>
<td>−0.471</td>
<td>−0.321</td>
<td>−0.702</td>
</tr>
<tr>
<td></td>
<td>(0.225)</td>
<td>(0.445)</td>
<td>(0.315)</td>
<td>(0.518)</td>
</tr>
<tr>
<td>Intercept – Model A(a)</td>
<td>−1.975 **</td>
<td>−0.896</td>
<td>−1.205</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.743)</td>
<td>(0.748)</td>
<td>(0.762)</td>
<td></td>
</tr>
<tr>
<td>Intercept – Model B(b)</td>
<td>−2.567</td>
<td>−0.646</td>
<td>−1.582</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(1.725)</td>
<td>(1.077)</td>
<td>(1.445)</td>
<td></td>
</tr>
<tr>
<td>Number of events</td>
<td>191</td>
<td>38</td>
<td>98</td>
<td>55</td>
</tr>
</tbody>
</table>

*Source: Author’s survey in 2001.*

\(a\)Model A has time-varying intercepts, which are listed under the historical period for which they apply. Effects of covariates are time-invariant and are listed under “All Years”.

\(b\)Model B has time-varying effects of covariates, as well as time-varying intercepts. Time-varying parameters are listed under the time period for which they apply.

\(c\)Reference category is SOE, Machinery, and Wuxi respectively. Numbers in parentheses are standard errors.

\(\uparrow p < 0.10\)

\(* p < 0.05\)

\(** p < 0.001\)
restructuring, meaning firms burdened with larger proportion of debt were more prone to restructuring. This effect appeared in the next two periods. In contrast, the significant effect of the profit variable does not exist in the first two periods, but does in the third period (1999–2000). Interestingly, during the heyday of the corporate restructuring wave (1997–1998), both debt asset ratio and profit value lost their predicting power. In other words, whether or not a firm carries out a restructuring in the second period has nothing to do with financial factors. This finding partially supported Hypothesis 1B. There are at least two reasons to help explain the faded (or distorted) effects of financial indicators. One is that government bodies began to financially support the wave of corporate restructuring from 1997, encouraged by the 15th Party Congress. Under this circumstance, local governments infused capital into firms to carry out restructuring and wrote off debt owed to banks. The other reason is that because of the Party’s encouragement, corporate restructuring became a political task carried out by various levels of governments. Those governmental bodies often set up deadlines by which time a specified proportion of firms under their jurisdiction should be restructured. It then became economically rational and politically correct for a firm to restructure, if at all possible. After this frenzy subsided, firm behavior seems to come back to normal at the end of 1990s, when economic concerns were once again the primary reason for restructuring.

The varying effects of the firm type variable also provide revealing information about the timing of restructuring for different types of firms. Compared to SOEs and urban collectives, rural collectives were more likely to restructure in the first period (1995–1996). During the second period (1997–1998), no differences existed among these three types of firms. Then urban collectives showed higher hazard rate of restructuring in the third period (1999–2000). For other independent variables, fewer differences existed between industrial sectors across these time periods. In terms of regional difference, firms at Yancheng and Zhengzhou tended to move less promptly than those in Wuxi in the first period. The difference between Zhengzhou and Wuxi disappeared in the second and third period, while the difference between Yangcheng and Wuxi got reversed in the third period. None of the size variables, the log form of asset or the log form of employee, showed significant effect in any period.

In summary, the findings suggest that, overall, firms behaved in a financially responsive way in corporate restructuring. Firms with higher debt level tended to restructure during the first period, while firms with lower profit level tend to do so in the third period. When this reform became a “political movement” sanctioned by the 15th Party Congress in 1997,
corporate restructuring temporarily became frenzied and financial concerns had less effect on firm behavior.

\textit{Workforce Downsizing}

After China eliminated its life-time employment policy in the mid-1990s, corporations began to lay off their workers. It is estimated that layoffs increased to about 11.5 million in 1997 from 5.5 million in 1995 (Gu, 1999). Other estimates suggest that between 1998 and June 2003, 27.85 million workers were laid off from Chinese SOEs.\(^8\) In many cases, laid-off workers venture to the more prospering non-state sectors to find new jobs. However, the non-state sectors tend to prefer either rural migrants or more educated workers. The re-employment training projects offered by the firms or local labor bureaus have rendered little help to laid-off workers, who are typically middle aged and suffer from interrupted education caused by the Cultural Revolution.

These conditions have created substantial labor unrest. Laid-off workers engaged in protest or other forms of collective actions, asking for better compensation or confronting corrupt managers (Cai, 2002, 2005; Chen, 2000). In some other cases, workers oppose restructuring and charge that their enterprises have excluded their participation, ignored their interests, and therefore infringed upon their rights (Chen, 2003). As Chen puts it, labor protests against restructuring SOEs represent workers’ attempts to resist the formation of capitalist or quasi-capitalist property relations that are detrimental to their interests or to ensure their basic welfare after restructuring. In order to safeguard social stability, local governments have negotiated various provisional arrangements regarding labor relations with the workers in order to reduce the high rate of unemployment on one hand, and to institutionalize labor and unemployment on the other (Gu, 2000; Oi, 2005).

The communist leadership has been very sensitive to the potential for worker unrest as concern for “social stability” always goes hand in hand with “economic growth” in the state’s priority list. The fear of possible sanctions on the local officials or managers when there is social unrest has made restructured firms more reluctant to lay off workers (Oi, 2005). In his work on Chinese factories in 1980s, Walder (1989) characterized Chinese enterprises as a social-political community, where the director was acutely concerned about “public opinion” and tried to win the good will and support of subordinates in order to avoid intentional decline of worker’s
productivity. This speaks to the dilemma faced by managers when they consider laying off workers. The possible outcome of internal conflict and social unrest staged outside of the factory walls may often outweigh the attempt to lay-off workers. Therefore, if firms, nonetheless, reduce the number of workers under financial pressure, then this should be regarded as an improvement from the earlier situation where they kept full employment, with little concern for efficiency or costs. In the context of increasingly intense market discipline and the building-up of a social security system, we hypothesize that:

**Hypothesis 3.** *Firms lay off more workers when they face graver financial troubles.*

**Findings on Workforce Downsizing**

We used random-effects negative binomial regression model and maximum likelihood estimation on number of laid-off workers of each firm pooled over the 1994–1999 period. Our dependent variable, the number of laid-off workers has certain characteristics. It is not only a non-negative repeated count variable, but also exhibits overdispersion, as values range from zero to several thousand. These characteristics make the choice of negative binomial regression necessary. We included all the independent variables used in previous model for corporate restructuring. In addition, we added a dummy of “having been restructured” to test the association between restructuring and laying off workers, and the original form of the number of employees.

The results show that whether or not a firm cuts the workforce largely depends on a firm’s profit level and the number of its total labor force (Table 6). Firms at lower profit levels tend to have more laid-off worker. The same is true for the number of the total workforce, which means a firm with larger number of workers is more likely to downsize. These findings provide supportive evidence to the Hypothesis 3. In addition, we also found older firms tend to lay off more workers, controlling for other things. This may due to the possibility that firms with longer history may have accumulated more redundant workers. Also, more workers were laid off in machinery industry than in electronics or textile industry. Compared to the reference city Wuxi, firms in Hangzhou tended to lay off more workers. We were puzzled by the opposite significant effect of the two variables measuring firm size. This may be due to the collinearity between number of employees and the natural log of it.
**Table 6.** Maximum Likelihood Estimates of Negative Binomial Model of Number of Laid-off Workers in Chinese Firms in 1994–1999.

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Estimate</th>
<th>Std. Error</th>
<th>p-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt asset ratio</td>
<td>0.322</td>
<td>(0.199)</td>
<td></td>
</tr>
<tr>
<td>Profit (in millions of yuan)</td>
<td>-0.006***</td>
<td>(0.002)</td>
<td>0.001</td>
</tr>
<tr>
<td>Number of employees</td>
<td>0.163*</td>
<td>(0.065)</td>
<td>0.05</td>
</tr>
<tr>
<td>Asset in thousands (log)</td>
<td>0.511***</td>
<td>(0.095)</td>
<td>0.001</td>
</tr>
<tr>
<td>Number of employees (log)</td>
<td>-1.227***</td>
<td>(0.145)</td>
<td></td>
</tr>
<tr>
<td>Restructured (dummy)</td>
<td>-0.391</td>
<td>(0.213)</td>
<td></td>
</tr>
<tr>
<td>Firm age (in years)</td>
<td>0.035***</td>
<td>(0.006)</td>
<td></td>
</tr>
<tr>
<td><strong>Type</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Urban collective</td>
<td>0.370</td>
<td>(0.271)</td>
<td></td>
</tr>
<tr>
<td>Rural collective</td>
<td>-1.734***</td>
<td>(0.407)</td>
<td>0.001</td>
</tr>
<tr>
<td>Others</td>
<td>-2.741***</td>
<td>(0.668)</td>
<td></td>
</tr>
<tr>
<td><strong>Industry</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electronics</td>
<td>-1.451***</td>
<td>(0.237)</td>
<td>0.001</td>
</tr>
<tr>
<td>Textile</td>
<td>-1.159***</td>
<td>(0.227)</td>
<td></td>
</tr>
<tr>
<td>Chemical engineering</td>
<td>-1.174</td>
<td>(0.232)</td>
<td></td>
</tr>
<tr>
<td><strong>City</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yancheng</td>
<td>-0.195</td>
<td>(0.324)</td>
<td></td>
</tr>
<tr>
<td>Hangzhou</td>
<td>0.738***</td>
<td>(0.224)</td>
<td></td>
</tr>
<tr>
<td>Zhengzhou</td>
<td>-0.172</td>
<td>(0.246)</td>
<td></td>
</tr>
<tr>
<td>Jiangmen</td>
<td>-0.461</td>
<td>(0.262)</td>
<td></td>
</tr>
<tr>
<td>$\chi^2$</td>
<td>202.79***</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: Author’s survey in 2001.

aReference category is SOE, Machinery, and Wuxi respectively. Numbers in parentheses are standard errors.

* $p<0.05$

*** $p<0.001$
Although it has been a common conception that laying off workers always accompanies restructuring (e.g., Gu, 1999), our analyses show that it is not always the case. The nonsignificant coefficient for the "restructuring" dummy implies there is no association between corporate restructuring and downsizing. Actually, around 74% firms that restructured in our sample had no laid-offs (Table 7). In short, whether a firm would lay off workers largely depends on its financial situation, regardless of whether it has restructuring. Although both governments and managers are concerned that labor force downsizing may result in turmoil within the firm and instability to the community, managers nevertheless do resort to reducing the number of workers when the firm faces economic problems. The assumption here is that there are no outside bailouts that would ease the financial situation.

### Table 7. Arrangement for Employees upon Restructuring.

<table>
<thead>
<tr>
<th>Type of Employee Arrangement</th>
<th>N</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm keeps a portion of employees</td>
<td>67</td>
<td>22.1</td>
</tr>
<tr>
<td>Firm keeps all employees</td>
<td>225</td>
<td>74.3</td>
</tr>
<tr>
<td>Government takes all employees</td>
<td>5</td>
<td>1.7</td>
</tr>
<tr>
<td>Other</td>
<td>6</td>
<td>2.0</td>
</tr>
</tbody>
</table>

*Note:* “Other” includes two cases of “no arrangement for workers” and four unspecified answers.


Although it has been a common conception that laying off workers always accompanies restructuring (e.g., Gu, 1999), our analyses show that it is not always the case. The nonsignificant coefficient for the “restructuring” dummy implies there is no association between corporate restructuring and downsizing. Actually, around 74% firms that restructured in our sample had no laid-offs (Table 7). In short, whether a firm would lay off workers largely depends on its financial situation, regardless of whether it has restructuring. Although both governments and managers are concerned that labor force downsizing may result in turmoil within the firm and instability to the community, managers nevertheless do resort to reducing the number of workers when the firm faces economic problems. The assumption here is that there are no outside bailouts that would ease the financial situation.

### Top Manager Turnover

One important issue in corporate governance is whether the CEO or top manager can be held accountable for a firm’s economic performance. A good indictor is whether top managers with poor records are removed from office. As we indicated above, a major objective of the industrial reforms was to increase the decision-making authority of firm managers. Despite the effort to linking formal rewards of managers to the performance of their enterprises, in the past the link had been weak. Managers enjoyed a high level of discretion in using corporate accounts to buy luxury sedans and spacious apartments, not to mention business related banquets and entertainment. As many managers behave as the de facto owner of a firm, some have gone so far that managerial corruption has been one of the main causes of labor unrest by lay-off worker (Chen, 2000).
Although the SOE reforms emphasized the delegation of greater decision power and provision of more incentives to managers, little attention is given to their actual performance or to hold them accountable. If ordinary workers face unemployment as the firm’s bottom line goes down, would managers face the possibility of losing their position under the same situation? To hold a manager accountable, the first and foremost thing is to solve the problem of how to measure a manager’s performance. Without being too optimistic, we believe that the cumulative effect of many piecemeal reform measures provides the means to hold management accountable. For example, relieving SOEs from the burden of pension and other welfare items has shortened the list of pretexts managers used to have for poor profitability. To secure their revenue base, government agencies are also likely to pay more attention to the bottom line of firms. Moreover, stricter accounting and auditing practices have been implemented with China’s adoption of international standards in its entry to WTO. This makes it more difficult for managers to manipulate balance sheets at will. Furthermore, corporate restructuring may be a critical juncture to put incumbent managers under closer scrutiny. An asset evaluation work team, consisting of government officials, professional accountants and auditors, must obtain a firm’s basic financial parameters before restructuring is permitted. In the highly contentious atmosphere often found in firms under restructuring, manager’s malpractice is more likely to be exposed. Although the above factors may not work together all the time, they provide a measurement of a manager’s performance. Therefore we propose that:

**Hypothesis 4.** *Managers in poorer economic perform are more likely to be removed from the post during restructuring.*

**Findings on Manager Turnover**

What was the fate of managers after restructuring? Our data shows that 70% of the managers maintained their position after corporate restructuring. We used a series of multivariate logistic regression to test what factors may affect whether a manager can keep his or her position after the restructuring. In order to capture as much information as possible, we ran models for all years and different time periods. Due to small number of cases, we were able to get estimation to converge by combing two consecutive years. Using this technique, as reported in Table 8, we combined 1995 to 1998 since the models from these years behaved consistently. The
### Table 8. Maximum Likelihood Estimates of Logistic Regressions of Whether the Top Manager Keeps Position after Restructuring in Chinese Firms (in Log Odds).

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt asset ratio</td>
<td>–0.565</td>
<td>–0.103</td>
<td>–3.613 *</td>
</tr>
<tr>
<td></td>
<td>(0.608)</td>
<td>(0.900)</td>
<td>(1.566)</td>
</tr>
<tr>
<td>Profit (in millions of yuan)</td>
<td>0.027</td>
<td>–0.012</td>
<td>0.123 *</td>
</tr>
<tr>
<td></td>
<td>(0.024)</td>
<td>(0.035)</td>
<td>(0.060)</td>
</tr>
<tr>
<td>Asset in thousands (log)</td>
<td>–0.265</td>
<td>0.046</td>
<td>–1.468 *</td>
</tr>
<tr>
<td></td>
<td>(0.241)</td>
<td>(0.306)</td>
<td>(0.651)</td>
</tr>
<tr>
<td>Number of employees (log)</td>
<td>0.129</td>
<td>–0.315</td>
<td>1.301 +</td>
</tr>
<tr>
<td></td>
<td>(0.308)</td>
<td>(0.422)</td>
<td>(0.727)</td>
</tr>
<tr>
<td>Firm age (in years)</td>
<td>0.022</td>
<td>0.039 †</td>
<td>0.018</td>
</tr>
<tr>
<td></td>
<td>(0.017)</td>
<td>(0.022)</td>
<td>(0.033)</td>
</tr>
<tr>
<td><strong>Type</strong> †</td>
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<tr>
<td>Urban collective</td>
<td>0.494</td>
<td>–0.265</td>
<td>2.390 *</td>
</tr>
<tr>
<td></td>
<td>(0.541)</td>
<td>(0.708)</td>
<td>(1.120)</td>
</tr>
<tr>
<td>Rural collective</td>
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<td>–0.334</td>
<td>–0.965</td>
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<tr>
<td></td>
<td>(0.600)</td>
<td>(0.776)</td>
<td>(1.177)</td>
</tr>
<tr>
<td>Others</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
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<td></td>
<td></td>
<td></td>
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<td>(0.596)</td>
<td>(0.752)</td>
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<td></td>
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<tr>
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<td>(1.084)</td>
<td>(1.239)</td>
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<td>(0.713)</td>
<td>(1.180)</td>
<td>(1.146)</td>
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<td>–1.333</td>
<td>–0.608</td>
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<tr>
<td></td>
<td>(0.703)</td>
<td>(0.878)</td>
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</tr>
<tr>
<td>Jiangmen</td>
<td>–1.220 †</td>
<td>–1.821 *</td>
<td>–0.227</td>
</tr>
<tr>
<td></td>
<td>(0.648)</td>
<td>(0.837)</td>
<td>(1.258)</td>
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<td>Constant</td>
<td>3.172</td>
<td>2.078</td>
<td>11.403 *</td>
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<tr>
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<td>(2.379)</td>
<td>(3.038)</td>
<td>(5.763)</td>
</tr>
<tr>
<td>$\chi^2$</td>
<td>20.23</td>
<td>22.88 *</td>
<td>23.29 *</td>
</tr>
<tr>
<td>Number of events</td>
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<td>76</td>
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</tr>
<tr>
<td>Number of cases</td>
<td>154</td>
<td>104</td>
<td>65</td>
</tr>
</tbody>
</table>

*Source: Author’s survey in 2001.*

*Others” category in firm type variable was automatically dropped during model estimation because of perfect prediction, or in other words lack of variation. Reference category is SOE, Machinery, and Wuxi respectively. Values for economic variables are from the previous year of restructuring. Numbers in parentheses are standard errors.

† $p < 0.10$

* $p < 0.05$
results show that during the period of 1995–1998, whether or not a top manager can keep her/his position after restructuring had nothing to do with financial performance of the firm. However, in the period of 1999–2000, debt asset ratio and profit level (in previous year) have significant effects in keeping the manager in position. Managers who are better at churning out profits or lowering debt level are more likely to stay in power. In contrast, managers with poorer performance were more likely to be removed from the position. The linkage between the firm performance and manager turnover after restructuring indicates that managers are held responsible for firm performance, which supports our Hypothesis 4.

**CONCLUSION AND DISCUSSION**

Based on the survey data of 451 firms in four cities, this paper examines three issues, corporate restructuring, worker lay-off, and manager turnover in China in the 1990s. We found that firms that initiated restructuring in early 1990s and the late 1990s were those under financial hardship. In contrast, during 1997–1998, when political pressure for restructuring was stronger after the 15th Party Congress, corporate restructuring became an institutionalized trend. It was not only economically rational but politically correct for a firm to follow the directive from the Party without regard to a firm’s financial situation. Our findings also show that only firms under financial hardship implemented a workforce downsize. This discounts a common perception that conflates restructuring and labor downsizing as the same mechanism. Lastly, our data shows that replacement of managers after corporate restructuring was related to the firm’s bottom line. Those findings by and large support our argument that China’s multifaceted reforms have built up an institutional foundation for enhanced corporate governance, even though political concerns required that an improved bottom line sometimes was compromised. As non-financial interests are largely eliminated, Chinese firms have become more responsive to market mechanisms.

Our close examination on the sets of political arrangements in China in which corporate restructuring occurs highlights the differences between China’s economic reform and the neoliberal model. While neoliberalism argues for the working of an unfettered market and minimal state intervention, the state in China has been and remains active in economic planning and management and reform. In contrast to neoliberalist prescription of quick and massive privatization, China has taken a gradualist approach to avoid major social costs and instability. The gradualist approach has allowed China to
build a set of complementary institutions (e.g., social security, banking, etc.) for a functioning market economy while taking smaller but nonetheless effective steps in restructuring. Overall, China’s reform has produced institutions consistent with a market economy but it is not converging towards the neoliberal model. Instead, this is a case of path dependence shaped by existing political and economic constraints, and entrenched interests. These constraints and interests are evident in the corporate restructuring examined in this paper. The state no longer is intimately involved with production but as our findings suggest it has played a key guiding role in shaping and directing the restructuring process.

We also should be clear that the process of restructuring and the incentives created are far from complete. Whether the corporate restructuring that has taken place in China will have positive impact on firm’s performance is a separate question and remains unanswered. From preliminary analysis of our existing data, we did not find a positive effect of restructuring on firm’s performance, despite the finding that a majority (70%) of managers in restructured firms in our survey believed that the overall operation of the firms are getting better. Moreover, for the society as a whole, corporate restructuring creates new problems. Besides the problem of illicit state asset transfer, a new “red hat” phenomenon has emerged that entails a tax exemption under certain conditions for shareholding cooperatives. Many firms also take advantage of restructuring as a way to evade bank debt.

We also should be prepared given the continued importance of political constraints for setbacks and perhaps changes in trend. We noted that the proportion of shares held by managers has been increasing in the restructured shareholding companies. This wave of management buy-outs (MBO) in restructured firms was going strong until the central government halted the process after outcries of illicit transfer of property rights. In most sales of small-sized SOEs, incumbent managers are more likely to be the new private owners of the firm. This type of insider privatization has attracted much attention and criticism from both media and academia (Wilhelm, 1999; Hu, 2004). The discussion is likely to continue for some time to come. In this study, we have focused on the first steps of restructuring. It must be left to future research to examine the subsequent steps and consequences towards privatization.

NOTES

1. In this paper, we use the term corporate restructuring to refer to the change of ownership structure of formerly public-owned firms, including SOEs and collectives.
The restructuring can take a form from incorporation into a shareholding company to full privatization, and from becoming a joint venture with foreign firms to being leased out; when none of these viable solutions works, then bankruptcy becomes last resort.

2. In China, there is a difference. Laid-off means that workers still have a relationship with a factory, received a portion of their salaries and may be recalled. Unemployment means that factories no longer maintain employment and financial relations with workers.

3. This research was generously supported by a grant from the Asian Development Bank Institute to one of the authors. The authors would also like to thank Thomas Heller who was the co-investigator on the grant. The Stanford Institute for International Studies also provided a seed grant for this project.

4. A few firms had more than one restructuring. For example, a firm was restructured to a shareholding company in 1994 and later became a joint venture with a foreign company in 1997.

5. Only those with equity capital of over 50 million yuan and having been making profit in previous three years in a row are eligible for listing in China’s stock markets. To go public in overseas stock exchanges needs special approvals from the state. By the end of 2006, there have been around 1,400 listed companies in China’s domestic stock markets. For a detailed study of China’s stock markets, see Walter and Howie (2006).

6. Few firms did experience multiple restructurings.

7. Excerpt from Jiang Zemin’s report in the 15th Party Congress.

8. Among them, 18.5 million found jobs afterward (International Labor Organization, 2004).

9. An analysis not included in this paper suggests that restructuring did not affect a firm’s performance.

ACKNOWLEDGMENTS

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REFERENCES


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Shilpa Ranganathan and Harland Prechel

ABSTRACT

This paper elaborates the theory of political capitalism to explain the implementation of market-based reforms in India. In response to the decline in the rate of capital accumulation that was manifested as a debt crisis in 1991, public policies and state structures were implemented that transformed corporate property rights. During this historical transition, the Indian economy was restructured from a mixed system characterized by family-owned business groups and state-owned enterprises to an economy characterized by a combination of domestic and foreign private ownership with substantially fewer state-owned enterprises. With support from transnational financial organizations such as the IMF, domestic elites used debt relief as political leverage to obtain market-based reforms. The new political-legal arrangements are the outcome of the
dynamics that emerged among domestic and transnational capitalist class interests, political parties, and India’s complex caste system and class structure.

In recent years, economists, politicians, journalists, and business leaders have argued that neoliberalism is the most viable model to advance economic growth. They criticize government regulation for constraining economic development, corporate flexibility, and individual innovation (Yergin & Stanislaw, 1998; Friedman, 1999, 2005). The central tenets of neoliberal reforms include limiting business regulation, strengthening corporate property rights, and creating free markets. Advocates of neoliberalism maintain that self-regulating markets effectively provide resources to individuals and that most problems are effectively managed by free markets or public-private partnerships. They are particularly assertive about the capacity of neoliberalism to solve social and economic problems in developing countries, and present it as the most viable model to replace national capitalism with transnational capitalism in the globalization process.

Despite its wide acceptance by business and political leaders, neoliberalism shares important characteristics with 19th century liberalism when the political-legal arrangements were restructured in ways that subordinated society to ‘self-regulating markets’ that had devastating consequences for society (Polanyi, 1944/2001). Like many theories in the social sciences that advocate a direction for social change (Mannheim, 1936; Zeitlin, 1968; Prechel & Sica, 1987; Ashley & Orenstein, 2005), neoliberalism contains an ideological dimension (see Prechel & Harms herein). The omission of politics from neoliberal theory is particularly problematic because it assumes that neoliberal policies and political structures ensure the effective redistribution of societal resources. There are two critical flaws in this neoliberal claim. First, the attempt to distance markets from politics and political structures disguises how markets are created and maintained. Second, it fails to recognize that policies and state structures cannot have the same effect on all economic segments. Instead, public policies create advantages for some classes and class fractions and disadvantages for others (Prechel, 1990).

While neoliberalism ignores the political dimension of social change, globalization theories tend to focus on outcomes, and give insufficient attention to how the globalization process is mediated at the societal level by political alliances and prevailing state structures and policies. Although these scholars have made important contributions (Sassen, 1998; Sklar,
2001; Robinson, 2004; Harvey, 2005), in the absence of an analysis of the political process that demonstrates how policies are enacted, there is a tendency to assume that transnational corporations and financial organizations such as the International Monetary Fund (IMF) and the World Bank are capable of imposing their agendas on society.

In contrast, some political sociologists (Poulantzas, 1978; Boies, 1989, 1994; Mizruchi, 1989; Block, 1990; Prechel, 1990, 2000; Akard, 1992, 2005; Grant, 1995; Morris, 2005) and development theorists (Evans, 1992; Babb, 2002) focus on process and show that the state plays a central role in policy initiatives that redistribute resources. The analysis here builds on this literature and examines how policies that are associated with neoliberalism are enacted. It shows that economic policies and the subsequent political-legal structure of the state are affected by historical contingencies, class politics, and alliances between domestic and transnational capitalists.

The analysis here examines how the Indian economy was transformed from a predominantly state-owned and managed economy to a market economy during the post-colonial period through 2005. Particular attention is given to the period following the economic crisis in the early 1990s, when public policies and state structures were redefined in ways that permitted increased ownership of business enterprises by transnational corporations. The analysis examines how conflict among castes, classes, and capitalist-class fractions affected the policy formation process, and how the policies and state structures that emerged in the colonial and post-colonial periods affected future state policies and structures.

POLITICAL CAPITALISM AND THE POLICY FORMATION PROCESS

The framework here examines how market-based reforms are enacted, how the particular form of national capitalism affects the enactment of neoliberal reforms, and who benefits from these reforms. To explain this process, we elaborate the theory of political capitalism, which entails the utilization of political outlets to attain conditions of stable and predictable economic growth, and to preserve the class structure essential to capitalist society (Kolko, 1963, p. 3; Prechel, 2000, p. 3). There are three interrelated dimensions of this theory: the relationship between economic segments and capitalist-class fractions, class-based political behavior, and historical contingencies.
Economic Segments, Class Interests, and Capitalist-Class Fractions

Contrary to the assumptions of neoliberalism, class theory maintains that everyone cannot win in a market-based economy because there is a structural relationship between classes and the branches of capital in the economy (Baran & Sweezy, 1966). That is, class fractions with different economic interests conform to the segments of capital in the economy (Poulantzas, 1978). Class fractions emerge as political actors, in part, because differential rates of capital accumulation exist within the various economic segments (Offe, 1975; Poulantzas, 1978; Aglietta, 1979). As a consequence of their distinct location in the production process, class fractions have specific political and economic requirements and concrete interests that may be contradictory to those of other class fractions. These conflicting economic interests generate opposing political interests and efforts to influence public policy (Zeitlin, Neuman, & Ratcliff, 1976; Berg & Zald, 1978; Zeitlin, 1980; Mizruchi & Koenig, 1986; Mizruchi, 1989; Domhoff, 1990; Prechel, 1990).

Moreover, the policy formation process itself generates political divisions among classes and class fractions because policies do not affect them equally. Business policy designed to overcome obstacles to accumulation in the economy as a whole or in one segment of capital often impedes accumulation in other economic segments. In short, because the economic realm is not dominated by a unified logic of capital accumulation, the political realm is not occupied by a single class or class fraction. Instead, power blocs emerge in the political realm that consist of a coalition of classes and class fractions whose composition varies historically. Whereas the mobility of capital enables capitalist-class fractions to overcome some of these obstacles by shifting their investments to economic sectors with the highest rate of capital accumulation, neither workers nor their skills are easily transferred among economic sectors.

Capitalist Class Political Behavior and the Policy Formation Process

Scholars from Marx and Weber to Schumpeter and Polanyi all understood the political nature of capitalism. For example, Weber maintained that political capitalism, which entails the accumulation of wealth and profit from political sources, occurs by collaboration between the commercial classes and political elites (Weber, 1951, p. 249, 1978, p. 164). Although Weber maintained that modernity is characterized by rational capitalism
and that antiquity was best characterized by political capitalism (Swedberg, 1998), he was fully aware that interested parties exercise power to advance their economic interests in a range of historical settings and that modern legal authority was vulnerable to political forces.

In the global economy, political capitalism is manifested as political alliances between transnational capitalists and internal elites (Frank, 1967; Amin, 1976; Cardoso & Faletto, 1979). Local elites gain access to information on political and economic conditions and influence domestic economic policies that allow transnational corporations to expand into domestic markets. These elites are then rewarded through joint business ventures or with financial compensation or employment in transnational corporations and financial organizations. In short, these class alliances provide a means for transnational corporations to influence public policies.¹ These alliances also resulted in policies that encourage developing societies to model their education system after the West or send their students to Western universities (Amin, 1976). The education of future state managers (e.g., administrators, policy makers) in neoliberal economics increases the probability that they will implement neoliberal reforms when they return to their home country (Babb, 2002).

**Historical Contingencies**

Examining social change addresses a central theoretical problem of historical sociology: the conditions under which groups that share an interest act or fail to act on that interest (Tilly, 1981). We address two questions that are related to this theoretical problem. First, what are the bases of social action? Second, to what extent do historical conditions and social structures affect political mobilization and the capacity of social actors to exercise power?

A primary concern here is with the disruption in the historical trajectory and the historical transition that result in political mobilization to enact social change. Whereas historical trajectories are interlocked and interdependent sequences of events that represent stability, historical transitions are stages along historical trajectories that entail radical shifts (Abbott, 1997). The concern here is with the departure from the previous historical trajectory and with the sequence of events that produce that shift. Identifying trajectories and transitions are essential to understand historical sequences that produce social change (Rueshemeyer & Stephens, 1997).
Social structure of accumulation theory suggests that historical transitions are the outcome of economic crisis, which emerge when the institutional arrangements (i.e., ideological, political, economic) are unable to ensure conditions favorable to capital accumulation (Gordon, Edwards, & Reich, 1982; Kotz, McDonough & Reich, 1994). However, a breakdown in one part of these institutional arrangements undermines capital accumulation. Research examining these historical transitions shows that in response to extended periods of capital dependence and economic crisis, the capitalist class unifies and mobilizes politically to redefine the political-legal arrangements in which corporations are embedded (Prechel, 2000). Public policies and state structures are enacted to institutionalize market stability in ways that ensure an acceptable rate of capital accumulation in the dominant power bloc. Decay-exploration transitions in the social structure of accumulation entail a shift in the dominant economic sector and the internal composition of the dominant power bloc.

Although historical transitions are the outcome of class-based political behavior that occurs in response to economic crisis, the dominant power bloc does not always have the economic and political power to overcome the economic crisis. The outcome of power struggles to establish a new power bloc are enacted as policies and manifested as state structures, which redefine the political-legal arrangements within which capital accumulation occurs.

The central concern here is with the historical transition in India’s political-legal arrangements that occurred in response to the prolonged decline in the rate of capital accumulation that was manifested as a debt crisis in 1991. Our research question is: How did the ownership structure of Indian companies change from a mixed system characterized by family-owned business groups and state-owned enterprises to an economy characterized by a combination of domestic and foreign private ownership with substantially fewer state-owned enterprises? In the following, we examine how corporate property rights were redefined politically as a response to domestic economic conditions and economic globalization. The analysis also shows how the caste and class structures that emerged in the colonial and post-colonial eras affected this historical transition.

THE CASE STUDY

India is an important case to study for several reasons. First, India is one of the BRIC countries (i.e., Brazil, Russia, India, China), which are expected to become the largest national economies in the world. Second, the number of
people in India below the poverty level is among the largest in the world. Reducing the level of poverty in India has been one of the central goals of state managers since the country’s independence from Great Britain in 1947. Third, advocates of neoliberalism characterize the Indian economy between independence and the early 1990s as “functionless capitalism” and claim that subsequent successes are attributed to neoliberal reforms (Yergin & Stanislaw, 1998). By examining how colonial and post-colonial policies, domestic politics and state structures affected subsequent political-legal arrangements, the analysis here assesses the extent to which the policies implemented in India conform to neoliberal ideals and provide solutions to its social and economic problems.

Historical Context

Eighteenth century India had well-developed agricultural and manufacturing sectors that provided the foundation for economic development. India’s market economy outstripped Europe in terms of manufacturing and economic capacity (Baran, 1957; Fernández Armesto, 1995). The Indian textile industry was among the most advanced in the world and produced high-quality muslin and other luxurious fabrics that were sold on Asian and European markets.

However, decades of plundering by the East India Company and nearly 200 years of British colonial rule destroyed many of India’s indigenous industries and domestic markets. By imposing unfavorable terms of trade on India (e.g., export taxes on India’s superior textile products, tariffs on imports) and forcing it to produce cotton for Britain’s emerging textile industry, the British deindustrialized the country (Dutt, 1902). Whereas the policies that the British imposed on India’s industrial sector destroyed much of its textile industry and its markets, the land taxation policy severely weakened the agricultural sector and crippled the village economy.

In addition, British colonial rulers co-opted local elites by creating enormous fortunes for those who cooperated with them (Baran, 1957, p.149). This relationship between Great Britain and Indian elites was formalized in 1858 by Britain’s Government of India Act, a proclamation by Queen Victoria that assured all Indian princes certain rights including the right to control their territories (Cohn, 1983).

During the 19th century, alliances were also created between the domestic capitalist class and the British. This alliance emerged from the conflictual relations between local merchants and bankers with the feudal princes.
These capitalist-class fractions loaned money to the princes to finance their wars with other states. After some princes refused to repay them, the moneylenders enlisted the East India Company to pressure the princes to repay their debts. Moneylenders also aligned with the expatriate firms, and later with subsidiaries of American and British transnational corporations (Tripathi, 2004; Tomlinson, 2005). In addition to cooperating with the expatriate firms, the moneylenders assisted with operations in British managing agencies that were set up to oversee business enterprises in the export-oriented sectors of the economy (e.g., jute, coal, tea). These management agencies typically held stock in these business enterprises. By the early 20th century, these family-based capitalists accumulated substantial amounts of wealth.

These class alliances served two important functions for the British. First, it created a hierarchy of loyal followers from village leaders to top government civil service officials. Second, these class alliances undermined the capacity of opposing classes and castes to unify and mobilize politically to advance their economic interests. With few capital accumulation opportunities available to other castes and classes, industrial development stagnated, few employment opportunities emerged, and poverty became widespread.

These economic arrangements persisted through the mid-1940s. Prior to attaining independence in 1947, changes in the political-legal arrangements transferred ownership of many expatriate firms to family-owned business groups, which further strengthened this domestic power bloc. The profits earned in these businesses provided the capital to diversify into a wide range of businesses (e.g., sugar, cement, paper, shipping, textile machinery, sewing machines, and airlines). This diversification and expansion strategy resulted in the emergence of conglomerates that controlled a large portion of India’s assets. During this transition to political independence, U.S. and British transnational corporations increased their economic presence in India (Tripathi, 2004).

As the movement toward independence accelerated, the family-owned business groups became closely affiliated with the Indian National Congress Party (hereafter Congress Party). This increasingly powerful class fraction provided substantial economic and political support to the Congress Party and actively influenced public policy. For example, in the mid-1940s, seven family-owned business groups formed a coalition and developed the Bombay Plan. This plan, which was released in two parts in 1944 and 1945, was in response to the widespread anticapitalist movement throughout India that began as an urban working class movement and quickly spread to the countryside where peasants mobilized politically to redefine landed
property rights. Although the movement was directed toward British imperialism, domestic capitalists attempted to create an alliance with the Congress Party in order to safeguard their interests against the increasingly widespread support for the government’s socialist agenda. Concerned that they would be marginalized and their property rights eroded, these family-owned business groups recommended a closer relationship between domestic private businesses and the state by proposing roles for government and business in economic development (Chibber, 2003). However, widespread support for the Bombay Plan never materialized. On the one hand, the majority of the capitalist class feared it permitted too much government control of the economy. On the other, opposition emerged from castes and other classes who were concerned that it would result in special privileges for family-owned businesses. The significance of this historical event is not that the Bombay Plan represented the interests of a unified capitalist class. Instead, it represents an early effort by some capitalists to influence and control private property rights by creating a role for big business in the policy formation process.

**Independence and New Political-Legal Arrangements, 1947–1950s**

The combination of British colonialism and unregulated domestic markets had devastating consequences for India. In addition to destroying its domestic textile industry, the Indian economy stagnated in the first half of the 20th century. Between 1900 and 1950, its growth rate was less than one percent a year (Das, 2006), which resulted in a fundamental distrust of unregulated markets and large corporations by Nehru and other political leaders (Das, 2006). After independence from British rule in 1947, with the support of the advocates of the defunct Bombay Plan, Prime Minister Nehru proposed a licensing system to facilitate an orderly transition from foreign to domestic ownership. However, other capitalist-class fractions including those represented by the Federation of Indian Chambers of Commerce and Industry (FICCI) organized politically to oppose this policy. After an extended period of conflict, the Nehru government passed the Industrial Development and Regulation Act, in 1951, to oversee and monitor economic activity (Chibber, 2003). Among the most important dimensions of this legislation was a licensing system. This regulatory structure required private-sector businesses to obtain a license from a government oversight agency to participate in economic activity (e.g., exports, imports, investments).
In addition to encouraging economic development by supporting family-owned businesses, Nehru’s economic program resulted in establishing state-owned firms to develop the infrastructure. In addition, import-substitution policies were implemented to ensure domestic control of industrial sectors that advanced the public good (Chibber, 2003). The Industrial Policy Statements of 1948 and 1956, identified 17 industries in which the public sector would play a predominant role. The primary focus was on transportation (e.g., railways), communication (i.e., postal, telegraph), and insurance and financial services (Tripathi, 2004, p. 313).

Under Nehru’s leadership, India invested heavily in its educational infrastructure to develop the human capital necessary for economic growth. In 1952, Nehru established the Indian Institute of Technology (IIT) in Kharagpur, West Bengal. This university was modeled after the Massachusetts Institute of Technology to promote science and technology. Following Nehru’s model, subsequent Prime Ministers Indira Gandhi and Rajiv Gandhi continued to invest in India’s educational infrastructure.

Among the most important changes during this period was the political mobilization of the family-owned business groups who organized politically to weaken the labor movement. Fearful that the government might not have the capacity to control growing labor and peasant unrest, capitalist and state managers succeeded in passing legislation that defined trade unions as the only legitimate representative of labor. This legislation also had devastating affects on the political power of labor because it placed tight restrictions on when labor could strike and severely limited their capacity to require employers to bargain in good faith (Chibber, 2003, p. 121).

Creating State Structures to Advance the Capitalist Agenda, 1960s–1970s

After legislation was passed to constrain the political power of labor, the dominant big business bloc utilized their political outlets to establish state structures to advance their economic agendas and preserve the class structure. The dominant capitalist class further aligned themselves with the Congress Party and began to use this political alliance to influence the policy formation process. The subsequent state structures legitimated state support of capitalist development, which included subsidizing private capital.

During this period, the Congress Party’s political base became increasingly pluralistic and included family-owned businesses, merchants, landowners, scheduled castes and tribes, Muslims, and other castes. Under the successive governments led by Nehru, Indira Gandhi and Rajiv Gandhi,
the Congress Party passed a range of policies to alleviate India’s massive poverty and the extreme economic inequalities. However, the pluralist political base of the Congress Party, which included many antagonistic classes and castes, was fragile and state managers were reluctant to raise taxes on business to finance anti-poverty programs. One of the primary obstacles to reducing poverty was the political and economic power of family-owned businesses that evolved out of the patronage system during the colonial period. Raising taxes on the dominant power bloc risked losing political support, which threatened the Party’s fragile majority. These conditions created a tension between the Congress Party’s policies and its funding source. On the one hand, the Congress Party resisted imperialism (Bhambhri, 1985). On the other, it was dependent on foreign capital to finance its social programs.

After Indira Gandhi became Prime Minister in 1966, she proposed the Monopolies and Restrictive Trade Practices Act of 1969 to regulate the private sector, especially the increasingly powerful family-owned businesses. The legislation was set up to prevent the concentration of economic power and monopolistic, restrictive, and unfair trade practices (Chakravarthy, 2001). This Act defined monopoly in terms of assets and control over market share. It also required new business ventures and existing companies with assets of more than 20 crore rupees (i.e., approximately $4 million) to register with the Monopolies and Restrictive Trade Practices Commission. Over time, this regulatory system became increasingly complex, centralized, and controlled most areas of production and investment in the private sector.

Family-owned businesses continued to lobby the government for protection from foreign corporations and in 1973 the government passed the Foreign Exchange Regulation Act (FERA), which revised the Industrial Policy Statement. This legislation encouraged the development of domestic big business and limited the capacity of transnational corporations to set up businesses in India and to merge with or acquire Indian corporations.

There were two interrelated parts to this legislation. First, it identified high-priority industries where foreign firms and large businesses would be allowed to operate. These high-priority industries were those whose products were not currently being produced in India or where a single (usually foreign) company was dominant. Second, Section 29 of this legislation required non-financial foreign firms that owned more than 40% of the equity in an Indian business to obtain permission from the Reserve Bank of India (i.e., central bank) to merge with or acquire any business engaged in trading, commercial or industrial activities (Report of Center for International Trade, Economics and Environment and National Council Political Capitalism, Neoliberalism, and Globalization).
of Applied Economic Research, 2002). Most important, this legislation required foreign corporations to reduce their ownership share to less than 40% in Indian companies in high-priority industries. This legislation also placed restrictions on the capacity of foreign corporations to establish subsidiary corporations in India. Rather than share ownership with Indian businesses, 57 foreign corporations including Coca-Cola and IBM closed their production facilities (Time Asia, 1977).

This regulatory structure benefitted family-owned businesses by increasing their ownership of domestic business enterprises and capacity to establish monopolies. In return, this dominant power bloc ensured support for the Congress Party from the regions where its businesses were located (Hankla, 2006). In addition to restricting the emergence of small private sector businesses and the spread of foreign corporations, this patronage system perpetuated inefficiencies within the big business fraction of the capitalist class.

**INCREMENTAL POLICY CHANGES, 1980s**

By the early 1980s, it became apparent that India was not achieving the level of economic development necessary to alleviate its massive poverty problem. The dominant power bloc within the capitalist class viewed this as an opportunity to argue that increased foreign investment was necessary to ensure stable capitalist development and growth. They pointed out that foreign direct investment in the 1970s was approximately $454 million or 1.2% of gross domestic investment, which was among the lowest of all developing countries (Park, 2004, p. 3551). Critics argued that a primary impediment to foreign investment was the 40% limit on foreign ownership of domestic businesses. They also identified the high rate of taxation, restrictive labor laws, and inadequate patent protection as barriers to foreign investment and economic development (Rao, Murthy, & Dhar, n.d.).

Public Policies to Facilitate Corporate Combinations

Slow economic growth undermined the Congress Party’s political base in several regional states. Its power was further compromised by the way in which Prime Minister Indira Gandhi handled ethnic conflict in the Indian state of Punjab. Then, in 1984, Indira Gandhi was assassinated. Her son, Rajiv Gandhi, became the leader of the Congress Party and was elected Prime Minister. Pressured by business coalitions, including the Association of Indian Engineering Industry, in 1985, Rajiv Gandhi amended
the political-legal arrangements to facilitate mergers and acquisitions. The public policy raised the asset limit for companies covered under the Monopolies and Restrictive Trade Practices (MRTP) five times higher than the previous limit.\textsuperscript{10} The primary effect of the policy was to permit corporations monitored by the MRTP Commission to expand without government supervision (Frankel, 2005).\textsuperscript{11} After this legislation was enacted, which legitimated larger mergers and acquisitions, corporations lobbied for even higher limits (Kochanek, 1986, pp. 1291–1292). That is, the initial policy provided a legitimate basis for capitalist-class fractions to lobby for even more favorable political-legal arrangements (Sinha, 2005). The government also transferred authority over the licensing approval process from the Ministry of Justice to the Industry Ministry, which was considered to be more favorable to business interests.

By the late 1980s, India’s economy continued to weaken and many businesses failed to realize a profit. To limit the number of business failures and the adverse effects on employment, the government took over several private businesses, especially those that were on the verge of bankruptcy. This resulted in a rapid increase in the state-owned sector, which increased from 8\% of its gross national product (GDP) in 1960 to 26\% in 1991 (Yergin & Stanislaw, 1998, p. 214).

These economic conditions and allegations of patronage, government corruption and scandal weakened the Congress Party. In response to political pressure from the business lobby, Rajiv Gandhi pledged to reform the licensing system (Yergin & Stanislaw, p. 1998, p. 216). He appointed several economists to develop market-based reforms, but these economic reforms were opposed by competing political parties such as the Bharatiya Janata Party (i.e., Hindu nationalist party) and the Communist Party.\textsuperscript{12} These opposing political parties maintained that the policies were not market-based that supported new entrants into the market. Instead, they represented pro-business strategies that further strengthened the state-big business alliance, and facilitated profit making among dominant family-owned businesses (Kohli, 2006a, p. 1256; Frankel, 2005). In 1989, Rajiv Gandhi lost the general election. In May 1991, he launched a reelection campaign, but was assassinated while campaigning.

\textit{Corporate Political Mobilization and Financial Contributions}

The political patronage system that was established under British rule continued in the post-colonial period. In the absence of regulations on
corporate contributions to political parties, the ruling Congress Party pressured family-owned businesses to donate large sums of money to finance their political activities. This patronage system did not go unnoticed and opposing political parties pressured the Congress government to pass the Companies Act of 1956. This legislation restricted public companies and its subsidiaries from contributing more than 25,000 Rupees (approximately US $555) or 5% of their net profits to political parties (Malik, 1989).

Despite these restrictions, the Congress Party continued to receive contributions from family-owned businesses. Following the disclosure of these contributions to the public, the Congress Party lost political support. In an effort to restore its public image, in 1969, the Party imposed a ban on contributions to parties and candidates for political purposes. However, family-owned businesses continued to devise methods to make contributions to political parties in exchange for favors. For example, companies paid to advertise in political party publications. In 1977, 800 public companies paid for advertisements to the Congress Party. In order to control business contributions to political parties, Rajiv Gandhi’s government passed the Companies (Amendment) Act in 1985, which legalized political contributions. This Act required private companies to disclose political donations in their corporate financial statements. However, political parties continued to receive donations through illegitimate means including kickbacks from domestic and foreign companies (Malik, 1989).

In addition, many family-owned businesses established alliances with powerful business lobby organizations. The Federation of Indian Chambers of Commerce and Industry was dominated by the Marwaris, and the Associated Chambers of Commerce and Industry (ASSOCHAM) was dominated by the Parsi ethnic community, transnational corporations, and businessmen from Bombay and Gujarat (Kochanek, 1987). These business lobby organizations used their economic power to establish political connections and obtain special favors from state managers. One of the outcomes of the alliance between state managers and family-owned businesses was control over the licensing system. Through its political connections, family-owned businesses obtained more licenses than they could use, which restricted other business enterprises from entering the market. In short, the regulatory structure had contradictory outcomes. Instead of limiting the spread of monopoly, by controlling the licensing system, the dominant power bloc used their political power and connections to establish monopolies in several geographic regions and economic segments.

India’s economic crisis deepened as a consequence of Saddam Hussein’s invasion of Kuwait in August 1990. First, the price of oil rose, which resulted in a substantial increase in manufacturing costs. Second, Indian workers in the Persian Gulf stopped sending their wages home, which reduced the availability of capital at the historical point when India desperately needed it. Third, investments from Non-Resident Indians in the Middle East declined considerably (Ahluwalia, 1999, p. 28). Fourth, the termination of exports to Iraq and Kuwait decreased India’s export trade and inflow of foreign capital. In addition, the decline of the Soviet Union in 1991 meant a rapid erosion of trade with India’s primary trade partner.

In an attempt to keep the economy from falling into a recession, the government borrowed heavily from Non-Resident Indian deposits and obtained loans from commercial banks. Although this facilitated economic growth, it increased India’s external debt, which rose from 12% of GDP in 1980–1981 to 23% of GDP in 1990–1991 (Ahluwalia, 1999). The shortage of capital reserves led to further restrictions on imports, which resulted in a decline in industrial production dependent on imports. Further, government deficits continued to increase and the country struggled under high debt payments. The primary option available to reduce government debt entailed cutting back on infrastructure spending, which would further undermine economic growth. In addition to the economic crisis, the Congress Party was confronted with a political crisis caused by conflicts among the pluralist classes and religious and caste groups.

In the absence of a candidate from the Gandhi family, the Congress Party supported Narasimha Rao who held a wide range of high-level bureaucratic appointments under previous governments. In 1991, Rao was elected Prime Minister. However, because the Congress Party’s political base had eroded, Rao did not have a majority when he was inaugurated and the Party lost its dominant position in the political arena. The government formed by Rao was the first in India without a majority in Parliament. The opposition parties agreed to cooperate with the Rao government on an “issue to issue basis,” which created additional opportunities for class and status groups to pursue their economic agendas politically.

Rao’s first acts as Prime Minister included the appointment of two neo-liberal economists to key government positions. He appointed Manmohan Singh as Finance Minister and P. Chidambaram as Commerce Minister. Like many state managers that are appointed to powerful positions in less
developed countries (Babb, 2002), these high-ranking state managers obtained advanced degrees from universities in the West that advocated neoliberal economics (i.e., Oxford and Harvard, respectively). Rao and his two top ministers considered the prevailing political-legal arrangements as oppressive, inefficient and unable to deliver quality products (Yergin & Stanislaw, 1998, p. 219). A primary agenda of the Rao government was to encourage foreign investment by transforming corporate property rights.

**Political Reforms to Encourage Corporate Combinations and Foreign Ownership**

The day after Rao took over as Prime Minister, Finance Minister Manmohan Singh informed him that India’s deficit was 8% of gross domestic product, public debt was 55%, and interest payment on foreign debt consumed another 4% (Yergin & Stanislaw, 1998, p. 221). Moreover, the country’s foreign exchange reserves covered only two weeks of imports. To address the deepening economic crisis, a pro-business coalition within the government that supported previous World Bank and IMF initiatives pressured state managers to obtain financial assistance from the IMF.

Like elites in the United States (Mills, 1956; Domhoff, 1967), many Indian elites rotated between high-level business and government positions. Several of India’s business and political elites previously held positions in the World Bank. Also, many former employees of the World Bank held important positions in the Reserve Bank of India (i.e., central bank of India) and in key government positions in the economic ministries and the Planning Commission of India. These relationships gave the transnational financial organizations like the World Bank an important base to influence the policy formation process (Bhambhri, 1985, p. 39).

Because the IMF considered India to be one of the most heavily regulated economies in the world (Nayar, 1998, p. 335), it used the economic stabilization package as leverage to pressure India to set up neoliberal reforms. These conditions included massive spending cuts by the government, privatization of state-owned enterprises, transformation of corporate property rights, and devaluation of the Indian rupee (Mohan, 2003). India’s neoliberal state managers complied and, in July 1991, Manmohan Singh outlined a plan to Parliament to initiate rapid industrialization by devaluing the rupee, cutting subsidies for domestic products, and reducing tariffs and trade barriers. This resulted in substantial opposition from conservative Hindu political parties. In contrast, the large family-owned
businesses took advantage of this opportunity to criticize state managers, and pressured them to implement policies that went beyond those stipulated by the IMF. They argued that the policies should redefine property rights in ways that facilitated privatization of the public sector, encouraged competition, and attracted foreign capital. This dominant power bloc also pressured state managers to control labor (Kohli, 2006b).

The primary target of these reformers was the Monopolies and Restrictive Trade Practices Act. Provisions constraining the concentration of economic power were eliminated, which included restrictions requiring prior approval for establishing new business ventures, and expanding current businesses through amalgamations, mergers and acquisitions. The new policy also raised the limit for market control to one-fourth of the market share (Chakravarthy, 2001). This provision, in most cases, eliminated size as a criterion to determine dominance within an economic sector. Over time, licenses for 80% of Indian industries were eliminated. In addition, the government disinvested from industrial sectors that provided crucial infrastructure and public services.

In order to attract foreign capital, state managers set up additional economic reforms that included rupee convertibility and removal of restrictions on repatriation of dividend income on foreign capital. This deregulation was designed to facilitate integration into the global economy (Andersen, 1994, p. 134). In response to the Confederation of Indian Industry business lobby (Sinha, 2005), state managers also relaxed provisions in the 1973 Foreign Exchange Regulation Act (FERA) to make it more viable for transnational corporations to own and acquire Indian corporations. The amended FERA revised property rights in ways that created a mechanism for automatic approval of up to 51% foreign ownership in 35 high priority, capital-intensive and high technology industries (Report of Center for International Trade, Economics and Environment and National Council of Applied Economic Research, 2002).

This change in property rights was extremely important because it allowed foreign parent companies, for the first time in decades, to establish ownership control over Indian firms. It also allowed them to set up subsidiaries: separate legal entities in which the parent company owns more than 50% of its stock. The property relationship between parent companies and their subsidiaries provides the parent company with the right to exercise ownership control: decision-making authority over these legally separate companies (Prechel, 2000).

After these policy changes, the number of domestic mergers and acquisitions increased. In a study of 45 corporate combinations, the majority
(i.e., 69%) were horizontal (i.e., between firms in the same industry) and the remaining combinations were divided equally between vertical (i.e., between firms that are complementary to each other) and conglomerate (i.e., between firms producing unrelated products) mergers and acquisitions (Beena, 2000; Kumar, 2000, p. 2852).

Deregulation in the Financial Sector

Prior to 1991, the government owned all the major banks. State-ownership of banks was initiated by the nationalization policy in 1969. Although the government encouraged private ownership of banks, its policy of bailing out poorly performing companies in order to mitigate employment and poverty problems led to state-ownership of insolvent and low-profit banks.\(^{20}\) By the early 1980s, state ownership accounted for 90% of total bank deposits.

By 1979, these conditions resulted in tight credit and restricted access to capital and criticism of the Congress Party from the working class and capitalist-class fractions. In response, the Congress Party began to monitor banks. The Party also encouraged its members who served on the board of directors of banks to provide lower interest rates to businesses and farmers (Hankla, 2006). In 1974, the Tandon Working Group was created by the Central Bank of India. This group consisted of representatives from other banks, financial institutions, and large family-owned businesses. One of its primary agendas was to facilitate the use of bank credit. In addition, the Credit Authorization Scheme required that state-owned banks complete a detailed analysis of businesses whenever they attempted to borrow large amounts of capital.

By 1991, the government began to deregulate interest rates, cut liquidity requirements for corporations pursuing external financing, and encouraged private ownership of banks (Shirai, 2002). These reform programs also created incentives for government-owned banks to place more emphasis on profits.

Political Reforms to Facilitate Equity Financing

State managers also began to deregulate the amount of equity capital a company could raise in a stock offering, which was specified under the Capital Issues Control Act of 1942. In 1992, state managers eliminated the 1942 act and replaced the office of Capital Issues with the ‘market-friendly’
Securities and Exchange Board of India (Kumar, 2000, p. 2851). Finance Minister Manmohan Singh maintained that government control over capital issues had lost its relevance, and that the new state structure gave companies the freedom to raise equity while protecting investors (Varshney, 1999, p. 234).

This deregulation of corporate securities had important implications. Between 1990 and 2001, equity finance became one of the largest sources of external capital for Indian corporations (Shirai, 2002). Between 1993 and 1995, India underwent a stock market boom when many firms raised capital from the equity market. The number of publicly listed firms also increased rapidly from 6,683 in 1991 to 8,747 in 1995. The share of market capitalization as a percentage of gross domestic product (GDP) rose from 32% in 1992 to 46% in 1995 (Shirai, 2002).

**Foreign Ownership**

After the securities market was deregulated and corporate property rights were redefined, foreign ownership rapidly increased. Several U.S. Fortune 500 companies including General Motors, Ford, Merck, Sony, Honda Motors, Coca Cola, Hewlett-Packard, and Texas Instruments invested in Indian corporations by purchasing stock and creating subsidiaries (Ahluwalia, 1999, p. 54). Non-U.S. based transnational corporations also acquired Indian companies. The transnational corporation Hindustan Lever acquired Tata Oil Mills (TOMCO) in 1994 and Lakme in 1995–1996 (Kumar, 2000).

The flow of portfolio capital (i.e., investment in securities such as stocks, bonds, or other financial assets) also increased foreign ownership (Park, 2004, p. 3551). Foreign stock ownership took two primary forms. First, in 1993, foreign institutional investors that met certain minimum standards were allowed to invest in equity and later in debt instruments. Soon, more than 500 foreign institutional investors registered with the Securities and Exchange Board of India and approximately 150 began to actively invest in Indian firms. Second, Indian companies were allowed to raise capital by issuing global depository receipts, which provided a means for foreign portfolio investors to purchase stock or invest in joint ventures (Ahluwalia, 1999, p. 56).

Investment from foreign institutional investors and individuals holding global depository receipts rose from $4 million in 1991 to $3.6 billion between 1993 and 1994. Between 1993 and the end of 1994, foreign investors purchased $2.8 billion of securities in Indian corporations. This amount increased to about $120 million a month in late 1994.
Property Right Laws and Corporate Form Change

Changes in India’s political-legal arrangements during this decay-exploration phase created the conditions that permitted Indian corporations to restructure as the multilayer-subsidiary form: a corporation with a hierarchy of two or more levels of subsidiary corporations with a parent company at the top of the hierarchy operating as a management company (Prechel, 2000, p. 12). Within this corporate form, parent companies can organize their entities as subsidiary corporations and establish ownership control over them by owning just over 50% of their stock.

This corporate form facilitates foreign ownership and increases corporations’ financial and organizational flexibility. First, it permits stock ownership in corporations and their subsidiaries via simple stock purchases, which facilitates investment in corporate securities. In India, this layered-subsidiary form facilitated foreign investment. After the Industrial Policy Statement of 1991 made several economic sectors eligible for automatic approval of up to 51% foreign ownership, foreign corporations could acquire domestic companies and incorporate them as subsidiaries. Foreign individuals and institutional investors could also easily invest in Indian firms. Second, because subsidiary corporations are legally independent entities, they can issue stock. This characteristic allows parent companies to use their subsidiaries to raise equity capital by issuing securities (e.g., stocks, bonds) in them. Third, this corporate form facilitates mergers and acquisitions because corporations can acquire other corporations or subsidiary corporations by purchasing just over 50% of their stock to establish ownership control. This is in contrast to other corporate forms that require 100% ownership of a business unit in order to incorporate it into the company. In short, these changes in corporate property rights made the multilayer-subsidiary form viable, which facilitated foreign investment and ownership.

POLICY PERIOD II: POLITICAL REALIGNMENTS, REDEFINING CORPORATE PROPERTY RIGHTS AND CORPORATE FORM CHANGE, 1997–2001

As described above, bribery and other scandals weakened the political base of the Congress Party in the early 1990s. Several senior members of the party including Rajiv Gandhi and Narasimha Rao were accused of receiving payments from a business group in return for securing business contracts for their steel fabrication company (Frankel, 2005, p. 690). The Bharatiya
Janata Party (BJP) used this opportunity to openly criticize the Congress Party’s patronage system and its policies to open the economy to foreign competition without providing protections for Indian-owned companies (Nayar, 2000, pp. 799–800). The BJP distinguished between internal-based liberalization and external-based liberalization and advocated for less intervention in the economy, more self reliance, and less privilege. BJP was able to retain the support of the Hindu nationalists, who belonged primarily to the upper castes, while attracting support from the middle class. Although the BJP won the 1996 general election, it was unable to obtain sufficient support to establish a government.

After an initial period of political instability, a coalition consisting of 13 minority regional parties formed a government called the United Front. This government included an unusual coalition consisting of the pro-labor Communist Party of India (M)\(^{24}\) and the right to center pro-business Congress Party. This political coalition emerged because of their shared interest in limiting the growing political power of the BJP (Singh, 2001; Frankel, 2005).

The BJP continued to build its political support by advocating the Hindu philosophy of *swadeshi* (i.e., self reliance)\(^{25}\) and in 1998 formed a coalition government called the National Democratic Alliance, which remained in power for only 13 months. In 1999, the National Democratic Alliance, under Prime Minister Vajpayee, was reelected (Singh, 2001). The National Democratic Alliance coalition modified Rao’s version of liberalization and advocated a “common minimum program” (i.e., An Agenda for a Proud, Prosperous India), which incorporated the economic objectives of the coalition parties. This alliance marked an important shift from single-party governments to multi-party coalition governments. It also entailed a shift in the political orientation of the BJP from Hindu nationalism to representing the economic and secular interests of its political base.

*Property Right Reforms to Facilitate Corporate Takeovers*

Throughout this period, the Confederation of Indian Industry continued to lobby state managers to establish policies favorable to big business. This business lobby pressured the National Democratic Alliance government to reform equity markets. Their primary agenda was to create a political-legal environment to facilitate hostile takeovers (Taraqqi, 2001). In a report issued by the Confederation of Indian Industry, they asserted the neoliberal argument that takeovers aid economic growth by creating economies of scale and scope and increased shareholder value (Dasgupta, n.d.).
In response, state managers established the Bhagwati Commission to review the takeover policy. This Commission recommended deregulating corporate takeovers. After the Takeover Code was adopted on February 20, 1997 (Kumar, 2000, p. 2851), state managers also proposed that the Companies Bill of 1997 replace the Companies Act of 1956. The new legislation, if passed, would allow corporations to buy their own stock, make capital transfers to subsidiary corporations, and loan capital to other corporations without obtaining permission from government oversight agencies. The new Takeover Code also created a mechanism for both hostile and negotiated takeovers, which were virtually impossible under previous political-legal arrangements. It also required target companies to register their securities so that they could be easily transferred, irrespective of the buyer (Roy, Bakshi, & Ghosal, 1997; Reed, 2002, p. 257). In addition, it eliminated the need to obtain government approval of takeovers. Together, the Takeover Code and the Companies Bill facilitated an increase in mergers and acquisitions and corporate form change.

Redefining Property Right Laws and Increased Foreign Ownership

To further encourage foreign investment, state managers stipulated that 48 industries identified in the Industrial Policy Statement of 1991 were eligible for automatic approval of up to 51% foreign ownership. Between 1997 and 1998, the limit on automatic approval of foreign ownership was raised from 51 to 74% in nine categories of industries (Indian Economic Survey, Ministry of Finance, 1997–1998). Foreign ownership was further facilitated by permitting 100% foreign investment in economic sectors that were (1) designated as crucial to economic growth and (2) not included in the automatic approval regulation. Deregulation also permitted transnational corporations to own 100% of joint ventures, if an Indian partner was not available and the firm divested at least 26% of its equity in three to five years. In addition, the limit on foreign portfolio (e.g., stock) ownership was raised from 24 to 30%, and later to 40% in most business sectors that were not previously deregulated. Also, the ceiling on the equity holding of a single foreign institutional investor was raised from five to 10% (Taraqqi, 2001).

The Confederation of Indian Industry lobby continued to pressure state managers to further weaken the Foreign Exchange Regulation Act, which regulated foreign ownership of domestic firms. In 1999, when the National Democratic Alliance Party replaced the United Front government, it eliminated the Foreign Exchange Regulation Act and created the Foreign
Exchange Management Act (Ahluwalia, 1999, p. 52; The Hindu, 2000). This legislation opened virtually all economic sectors to foreign corporate and individual investors.

After corporate property rights were redefined to eliminate most restrictions on foreign ownership in most economic sectors, several critical changes occurred. First, many corporations restructured as the multilayer-subsidiary form. Second, foreign individuals, institutional investors and corporations increased their ownership of Indian parent companies and subsidiaries by purchasing their securities. Third, other business policies established free-trade zones, which provide transnational corporations with state-subsidized operating facilities. Between 1995 and 1998, foreign investment in India increased from approximately $654 million to $3.682 billion (see Fig. 1).

**Redefining Bank Laws and Increased Foreign Debt**

Despite the extensive transformation in India’s organizational and political-legal arrangements, advocates of the neoliberal model inside and outside the

![Fig. 1. Foreign Investment in India, 1991–2005. Source: Ministry of Commerce and Industry (Department of Industrial Policy and Promotion), http://dipp.nic.in/foreign_direct_investment_statistics/India_yearwise.pdf](http://dipp.nic.in/foreign_direct_investment_statistics/India_yearwise.pdf)
state lobbied to further deregulate the banking sector. The Confederation of Indian Industry continued to be among the most politically active lobby group.\textsuperscript{27} Subsequent changes in banking laws included the Monetary and Credit Policy Act of 1997, which relaxed restrictions on bank financing and laid the foundation for the integration of Indian currency and foreign exchange markets (Roy et al., 1997). This legislation also allowed banks to determine corporations’ working capital requirements and to assess their risk levels. In addition, the government deregulated the guidelines governing the issuance of commercial paper. By making it easier to access debt financing, this change facilitated the use of private debt and commercial paper to mitigate corporations’ capital dependence (Kamesam, n.d.).\textsuperscript{28}

The Confederation of Indian Industry also lobbied the government to require financial institutions to sell their stock in corporations. This corporate lobby criticized the current political-legal arrangement where financial institutions (e.g., commercial banks, public financial institutions) were agents of the government. They argued that government-controlled financial institutions could not properly monitor firms because they had a conflict of interest as both creditors and shareholders, and this relationship permitted financial institutions to support corporate management, irrespective of performance. To resolve this conflict of interests, they advocated for decreased government ownership (Dasgupta, n.d.; also see Roy et al., 1997).

In response, state managers further deregulated the financial sector of the economy. In 1998, the government allowed banks and financial institutions to finance acquisitions through bonds or debentures (Dasgupta, n.d.). The new provisions also made it possible for corporations to borrow against their securities and commercial paper. This policy made it viable to set up leveraged buyout funds and transfer capital among corporate entities inside the same corporation. During the same period, state managers passed legislation (e.g., Income Tax Act), which cut corporate taxes by lowering the peak depreciation rate, reducing the capital gains tax from 20\% to 10\%, and removing taxes on corporate restructuring (e.g., mergers, acquisitions) (Roy et al., 1997). Whereas the previous legislation taxed capital transfer in mergers, the revised policy exempted companies that were either the target or the acquirer from this tax. Also, if both target and acquirer are Indian companies, the shareholders were exempt from paying a tax (Ramanujam, 2006). Next, the corporate lobby attacked the so-called double taxation policy (i.e., taxes on corporate profits and dividends distributed). In response, the government abolished taxes on dividends. This political-legal change further paved the way for change to the multilayer-subsidiary
form because profits are typically transferred from subsidiary corporations to the parent company via dividends. Now, profits could be transferred via dividends tax free.

The business lobby also pressured state managers to change the size requirement of initial public offerings (IPOs) of stock. They argued that this law was biased against small- and medium-sized firms because it restricted their capacity to raise capital in the equity market (e.g., public stock offering) (Shirai, 2002). In 1999, the Kumar Mangalam Birla Committee, which was appointed by the Securities and Exchange Board of India (Som, 2006, p. 4156), recommended deregulating IPOs for information technology firms. This change in the regulatory structure is important because it allowed corporations to restructure their smaller corporate units as legally independent subsidiary corporations and raise capital by issuing stock in them. Following these changes, IPOs rapidly increased and India underwent a stock market boom; market capitalization as a percentage of gross domestic product rose from 34% in 1999 to 85% in 2000 (Shirai, 2002).29

These new property right laws created incentives for corporations to change to the multilayer-subsidiary form. First, eliminating the tax on corporate restructuring reduced the cost of transforming to this layered-subsidiary form. Second, eliminating taxes on the distribution of profits via dividends reduced operating costs in this corporate form. Third, the deregulation of stock offerings made it possible to raise equity capital by issuing stock in smaller subsidiary corporations.

**POLICY PERIOD III: THE MERGER AND ACQUISITION WAVE, 2002–2005**

Although big business began to lobby for changes in the Monopolies and Restrictive Trade Practices Act in 1999, they increased their lobby efforts in response to the economic recession in 2001 that followed the stock market boom (Goswami, 2000). Foreign corporate consultants including KPMG advised their clients that “a slump in the economy is a good time to consolidate” (Maitra & Jayakar, 2001). However, the capacity of foreign corporations to acquire businesses was still constrained in some economic sectors by the regulatory environment that required domestic ownership control of corporations.

Beginning in May 2000, the business lobby maintained that further modification of corporations’ political-legal environment was necessary to
facilitate economic growth. The corporate lobby pressured state managers to restructure several dimensions of the political-legal environment in which corporations are embedded. First, to create a new regulatory body named the Competition Commission of India (CCI) to process merger applications. Second, to notify the CCI about proposed mergers where the assets of the merged entity exceed 500 crore rupees (i.e., $102 million), or when the assets of a subsidiary that is proposing a merger exceed 2,000 crore rupees (i.e., $410 million). Third, to give the CCI 90 days from date of the application to either accept or reject the merger. Fourth, to exclude predatory pricing as a criterion to prohibit the combination because lower prices can benefit consumers. Third, to make agreements between competitors (i.e., horizontal integration) and between buyers and sellers (i.e., vertical integration) subject to the law. Sixth, to ensure that combinations involving state monopolies and foreign companies are subject to examination and approval by the commission (Dasgupta, n.d.).

These recommendations were supported by the pro-business Finance Minister, Jaswant Singh of the BJP, who maintained that the new policy would enable domestic companies to grow and compete in the global economy (The Hindu, 2002). In January 2003, the revisions to the Competition Act were adopted by the President of India (Agarwal, 2005; Dasgupta, n.d.).

Additional concessions to business further weakened government oversight by permitting large corporations to voluntarily notify the commission of most kinds of combination. To justify these changes, the Competition Commission maintained that market share is a necessary but insufficient condition to determine dominance because firms with large market shares can face competition from potential entrants, existing firms, or the purchasing power of customers. The Competition Commission redefined market dominance of a firm as “the economic strength to behave, to an appreciable extent, independently of its competitors and customers” (Report of Department of Company Affairs, 2006). The clause “to an appreciable extent” is particularly important because it makes market dominance open to interpretation. Now, the primary criteria defining market dominance were the assets of the merged entities. The effect of this policy was to exclude from government oversight corporate combinations by large domestic and transnational corporations that control a substantial market share (Dasgupta, n.d.).

Restrictions on the percentage of foreign ownership were completely eliminated in some economic sectors during this policy period. In 1999 and 2000, the government enacted policy that permitted 100% foreign
ownership in some private sectors such as information technology businesses that focused primarily on exports (Panagariya, 2005, p. 15). The foreign ownership limit was also raised in aviation, banking, telecom, and real estate (Report of Grant Thorton India, 2005) and in industries that were previously in the public sector (e.g., insurance, pharmaceuticals, high demand consumer goods) (India Infoline, 2005).

Bank Deregulation

Continued deregulation of finance in the first decade of the 20th century eliminated many distinctions between banks and financial institutions. Many of India’s public sector financial institutions were transformed into commercial banks or non-banking financial corporations. After state managers enacted the Transfer of Undertaking and Repeal Act, the Industrial Development Bank of India incorporated as a private corporation. Similarly, the Industrial Credit and Investment Corporation of India (ICICI) incorporated as ICICI Bank in 2002. Like deregulation in the United States (Prechel, 2000), these new business policies allowed financial institutions to offer a wider array of financial products and services to individual customers (Daily Times, 2002).

In 2005, deregulation of the financial sector increased the ceiling on foreign ownership in banks from 49 to 74%, which permitted foreign banks to establish subsidiaries in India (Indian Economic Survey, 2004–2005). Because foreign banks had access to more capital and advanced technologies than many Indian banks, they quickly increased their presence both in terms of numbers and market share. Whereas 148 foreign banks were located in India in 1990, this number increased to 259 in 2005. Also, new limits on credit financing increased the availability of credit to private industry and other economic sectors. Following these changes, the use of credit in medium and large industries increased from five to more than 17% in 2004 and 2005. In 2005, credit in the industrial sector rose to 46% (Mehrotra, 2006, p. 9).

The Effects of Deregulation on Mergers and Acquisitions and Foreign Ownership

The changes described here created the organizational and political-legal arrangements that permitted rapid change in ownership of Indian firms.
Prior to passage of the Takeover Code in 1994, the majority of mergers and acquisitions (i.e., approximately 80%) were by Indian companies (Raju & Deepti, 2004). Deregulation in the second policy period was followed by several changes in merger and acquisition activity.

In the 1980s, approximately 60% of the mergers and acquisitions were in the manufacturing sector, 32% were in the tertiary sector (e.g., telecommunications, power generation, consulting services), and less than 10% were in the primary sector (e.g., agriculture, mining, petroleum). Moreover, most mergers and acquisitions were domestic. In contrast, mergers by transnational corporations steadily increased in the early 1990s and accelerated in the second half of the decade (Fig. 2). Between 1994 and 1997, nearly 40% of cross-border investment by transnational corporations occurred through mergers and acquisitions. Moreover, in contrast to the 1980s, the tertiary sector accounted for more than 60% of transnational mergers and acquisitions and mergers in the manufacturing sector fell to below 40% (Kong & Sakthivel, 2004, p. 34). Foreign direct investment in the tertiary sector rose from 5.2% in the 1990s to 58.7% between 1991 and 1997 (Park, 2004, p. 3552).

![Fig. 2. Number of Mergers in India, 1973–2003. Source: Research and Statistics Division, Department of Company Affairs, Agarwal (2002).]
Subsequent deregulation was followed by further increases in mergers and acquisitions. After the Competition Act was revised in 2003, merger and acquisition activity increased by more than 100% in the following year (Fig. 3). Also, the size of the largest deals increased from $5.11 billion in 2003 to $12.3 billion in 2004. The largest number of corporate combinations occurred in the technology sector followed by healthcare, biotechnology, and pharmaceuticals. In 2005, China was the only other Asian country with more mergers and acquisitions (Ramanujam, 2006). In addition to mergers and acquisitions by transnational corporations, several family-owned business groups pursued mergers and acquisitions, organized these companies as subsidiaries, and incorporated them into the multilayer-subsidiary form. Rayon corporation (i.e., part of the Aditya Birla Group) established ownership control of PSI Data Systems in July 2001 by acquiring just over 50% (i.e., 50.35) of its stock (Varadarajan, 2001). The embeddedness of the layered-subsidiary form in these political-legal arrangements allowed Rayon to increase its expertise in the crucial and expanding software development segment of the economy through simple stock transactions and incorporating the acquired companies as subsidiaries.

![Fig. 3. Number of Mergers and Acquisitions of Indian Corporations by Transnational Corporations, 1990–2005. Source: SDC Platinum-Mergers and Acquisitions is a product of Thomson Financial.](image-url)
Similarly, after deregulation, the Birla and Tata family-owned business merged with AT&T to create one of the largest telecommunication corporations in India. Then, in anticipation of the enactment of the 2002 Competition Act, two of the largest firms in the telecommunication industry, BPL Communications and Birla-Tata AT&T agreed to merge. This multilayer-subsidiary corporation created the country’s largest cellular service joint-venture company in India. According to the vice-chairman of JP Morgan Stanley, who was a financial advisor to the merger, “the consolidation took place in order to increase scale, cost effectiveness and the creation of a larger resource base” (Maitra & Jayakar, 2001). Deregulation had important benefits for large corporations; the extensive resource base of the parent company increases their capacity to raise capital from debt and equity markets. This gave them a clear advantage over smaller companies.

Foreign ownership also increased during this period of deregulation (see Fig. 3). During the first policy period (1991–1996), the number of mergers and acquisitions of Indian companies by transnational corporations gradually increased from four in the year prior to deregulation (1990) to 93 in 1995. The second policy period (1997–2001), which included adoption of the new Takeover Code in 1997, resulted in a rapid upswing in mergers and acquisitions that reached 268 in 2000. After a downturn in the number of mergers and acquisitions in the third policy period (2002–2005), which included the Competition Act, foreign mergers and acquisitions reached a record high of 283 in 2005. As Fig. 3 shows, transnational corporations rapidly increased their ownership of Indian corporations during this period of rapid deregulation.

**FINDINGS**

The analysis here shows that big business mobilized politically to change the political-legal arrangements in which corporations are embedded in order to advance their capital accumulation agendas. After this dominant power bloc successfully created state structures to contain the political power of labor, it succeeded in changing corporate property right laws. These changes were manifested in three interrelated changes in the ownership structure of Indian corporations.

First, deregulation facilitated change to the multilayer-subsidiary form. This corporate form change, in turn, allowed management to raise foreign equity capital by issuing stock in their subsidiary corporations. Together with changes in foreign ownership laws, this corporate form made it easier
for foreign individuals, institutional investors, and corporations to invest in Indian corporations because they can purchase stock in the parent company or its many subsidiary corporations.

Second, these political-legal changes were followed by a rapid increase in mergers and acquisitions. Whereas the average annual number of mergers and acquisitions between 1973 and 1990 was approximately 32, after the economic crisis and initial deregulation between 1991 and 1995, they increased to 90. After the stock market decline and further deregulation, the average number of mergers and acquisitions per year increased to 156 between 1996 and 2003 (see Fig. 1). Corporate consolidation was facilitated by the multilayer-subsidiary form because it reduces the cost of mergers and acquisitions. Instead of purchasing 100% of a firm, parent companies can establish ownership control by purchasing just over 50% of the stock in a company and incorporate it as a subsidiary corporation.

Third, foreign ownership rapidly increased (see Fig. 3). In 1990, the Indian economy was dominated by family-owned corporations and state-owned enterprises. By 2006, foreign individuals and corporations owned stock in more than 1,000 Indian companies, and 125 U.S. Fortune 500 companies had set up research and development subsidiaries in India (Das, 2006).

Although advocates of neoliberalism claim that India’s recent economic success is explained by deregulation and privatization of state-owned enterprises (Yergin & Stanislaw, 1998, Das, 2006), the historical record suggests otherwise. Deregulation has done little to solve India’s debt crisis. In fact, domestic public debt as percent of gross domestic product continued to increase after deregulation from 67.9% in 2001–2002 to 72.9% in 2002–2003. Also, foreign investment has done little to increase domestic capital formation. The profits from subsidiaries are transferred as dividends to the transnational parent company, institutional investors and wealthy individuals in proportion to the percent of their stock ownership. Moreover, because India eliminated the so-called double taxation policy, most of these dividends are transferred tax-free. It is noteworthy to acknowledge that the particular kind of deregulation that made the multilayer-subsidiary form viable in India occurred in the United States in the previous decade (Prechel, 2000). This suggests that a transnational capitalist class (Sklair, 2001; Robinson, 2004) influenced the form of deregulation in India. However, this hypothesis requires further exploration.

Although these neoliberal organizational and political-legal arrangements facilitated foreign investment and ownership, they have done little to solve India’s massive poverty and unemployment problems. In 2001, 35 million
Indians were unemployed and 370 million, or approximately one-third of the population, survived on one dollar or less per day (Perry, 2004).

Moreover, in the absence of proper regulatory controls, several projects that were initiated under the auspices of neoliberal reforms ended in financial disaster. For example, after widespread oppositions emerged to a $450 million project to build a giant dam along the Narmada River, the World Bank was forced to stop construction (Revolutionary Worker Online, 1997). Similarly, the large joint-venture with Enron Corp. to construct the multi-billion dollar Dabhol Power Corporation failed. After massive cost overruns, opposition from displaced villagers, farmers and fisherman, numerous lawsuits (Parry, 2001; Allison, 2001; McLean & Elkind, 2003) and accusations of corruption against the Congress Party, construction was stopped. In both cases, protests emerged because of the adverse social and environmental affects of these projects.

This analysis also challenges the claim that neoliberal policies are responsible for India’s economic growth. Economic growth increased substantially by 1980s, which was more than a decade before India began to set up neoliberal reforms in 1991. Moreover, although the information technology (IT) sector of the Indian economy expanded after foreign investment increased, the success of this economic sector was only viable because India developed an elaborate educational infrastructure beginning in the early post-colonial Nehru era. By the 1970s and 1980s, India was training some of the most talented practitioners and scholars in the fields of science and technology. The rapid economic growth in India’s most dynamic economic sector – software and business-process outsourcing – is also a product of its educational infrastructure. This domestic economic sector provides services that are outsourced to companies throughout the global economy.

The development of human capital through education also contributed to the expansion of the Indian middle class. In 2004, India’s IT sector employed approximately 800,000 people (Perry, 2004), which provided upward mobility opportunities for educated middle-class Indians. By focusing on the development of human capital, economic growth in India produced less of an increase in inequality than in other BRIC nations. Income inequality, based on the Gini index, is 0.33 in India. This is in sharp contrast to China where it is 0.45 and Brazil where it is 0.59 (Das, 2006). In fact, income is more equally distributed in India than in the United States where the Gini index increased to 0.45 following neoliberal reforms in the 1980s and 1990s (see Prechel & Harms, herein). The comparison between India and the United States is particularly noteworthy because modernization theorists
argue that inequality increases at early stages of development and declines during later stages of development. The higher rate of inequality in the United States than in India suggests that the way in which the political-legal arrangements enable capitalist growth and stability matters.

**CONCLUSION**

In response to the prolonged decline in the rate of capital accumulation that was manifested as a debt crisis in 1991, public policies were implemented that transformed the social structure of accumulation. During this historical transition, the Indian economy was restructured from a mixed system characterized by family-owned businesses and state-owned enterprises to an economy characterized by a combination of domestic and foreign private ownership with substantially fewer state-owned enterprises. Transnational financial organizations such as the IMF and the World Bank used debt relief as political leverage to obtain market-based reforms in India. Whereas the economic crisis in the early 1990s provided the catalyst for change, the contents of the policy were affected by the political dynamics that emerged among domestic and global business interests, transnational financial organizations, and India’s complex caste system and class structure.

Empowered by British colonial rule, the power bloc of large family-owned businesses dominated Indian policies during the initial policy period. After independence in 1947, the Nehru government was forced to concede to their demands. A key component of these political-legal arrangements was the licensing system that allowed the dominant capitalist power bloc to gain monopolistic control of key economic sectors. By 1991, India’s debt crisis and inadequate domestic capital formation weakened the Congress Party and its increasingly pro-big business leadership willingly accepted the conditions established by the IMF. These policies and state structures created legitimate bases for the dominant power bloc to further advance its capital accumulation agendas.

The Congress Party’s political power was also affected by shifting alliances and the tenuous bases of support for a single political party. During the first policy period, the prevailing Congress Party used its pluralist base to set up policies to facilitate economic growth. Overtime, these pro-business policies undermined support from this pluralist political base. Although the Bharatiya Janata Party (BJP) gained control over the government during the second policy period, its political base was unstable. To stabilize its political power, the BJP obtained support from business
interests and departed from its nationalist ideals to strengthen domestic industry. Under the BJP, the state transformed corporate property rights in ways that permitted a higher degree of foreign ownership. Although the Congress Party was able to establish a government in 2004, business interests had increased their presence in this political party. For example, Manmohan Singh, who was the financial minister responsible for setting up the liberalization policies in 1991, is the current Prime Minister.

In contrast to arguments claiming that neoliberal policies are market-based and reduce government involvement in the economy, the analysis here shows that these political-legal arrangements shifted resources toward some economic sectors, classes and class fractions at the expense of others. Political capitalism replaced state structures that were oriented toward the general welfare of society (i.e., employment, consumer protection) with state structures narrowly oriented toward advancing the welfare of domestic and transnational capitalists. This policy paradigm shift, which facilitated the transfer of capital from the rural to the urban economic sectors, had serious and negative consequences for society. In the rural areas of some states such as Andhra Pradesh, which is one of India’s information technology centers, inequality is so extreme that between 1997 and 2004 more than 2,000 farmers committed suicide (Perry, 2004).

The conception of political capitalism here shows that classes and class fractions organized politically to redefine state structures in ways that advance their narrow economic agendas. After these policies are embedded in the state as regulatory and enforcement structures, they create coalitions inside and outside the state who have an interest in maintaining them (also see Prechel, 1990, 2000). In India, these coalitions continue to support policies that shift society’s surplus from the working classes who produce it to large transnational and domestic corporations.

In summary, in the last century, India has gone through three transformations from (1) colonial capitalism that prevailed when the British occupied India, (2) to national capitalism in the post-colonial era, and (3) to transnational capitalism. In contrast to the colonial era when the British exercised political and military power to extract capital from India, in the 1990s, the domestic capitalist class engaged in political capitalism to establish state structures that enhanced their wealth and facilitated foreign investment and profit making.

The political-legal arrangements that were enacted during this period do not conform to central tenets of neoliberalism. These policies and state structures did not create self-regulating markets capable of solving India’s social and economic problems. Instead, they created capital accumulation
opportunities for the dominant power bloc and redistributed income and wealth to them. However, the injustices of these policies and state structures are generally not recognized because the neoliberal ideology of self-regulating markets and individual freedoms to make choices in the market conceals them.

NOTES

1. Capitalists and their managers do not always have a coherent conception of the relationship between their economic goals and the means to achieve those goals. Nevertheless, they exercise power to establish state policies that facilitate rationalization of the economy by creating political and ideological conditions that advance their economic agendas. Rationalization is not equivalent to efficiency or rational. Rationalization is a historical process that is characterized by contradictions, irrationalities, disequilibria, and conflicts (Weber, 1978; Antonio, 1979).

2. Family-owned business groups consist of one or more independent parent companies that are owned and controlled by family members. Each parent company may own and control several subsidiary corporations.

3. The Congress Party, which was founded in 1885, is one of India’s oldest political parties.

4. The FICCI was founded in 1927. Its members owned small, medium and large companies in the manufacturing, distributive trade, and service segments of the economy.

5. This licensing system, which allocated licenses to businesses in many economic sectors, is also known as “License-Raj” (rule).

6. Scheduled castes and tribes are entire communities that are accorded special status by the Constitution of India. They were considered “outcastes” and excluded from the caste system for thousands of years. Historically, these communities were subject to considerable social disadvantage and were excluded from most labor markets, were employed in menial occupations, and had little prospects for upward mobility.

7. Also in 1969, the Congress Party split into the Congress Party (I), which was lead by Indira Gandhi and the Congress Party (O).

8. When Indira Gandhi was Prime Minister, she personally approved of many licenses.

9. In 1895, the Engineering and Iron Trades Association was created. Its name was changed in 1974 to Association of Indian Engineering Industry. In 1992, the name was changed to the Confederation of Indian Industry. This trade association, which included companies in both the private and public sector, lobbied members of Parliament to advance their economic interests.

10. This political-legal change affected approximately 40% of the 1,334 companies covered under the policy.

11. Policies were also set to exempt MRTP companies from parts of the legislation, if they invested in any of 27 industries that were designated as high priority to
economic development (e.g., electronics, chemical plants, autos and other vehicles, oilfield services).

12. Based on a pro-labor platform, the Communist Party of India was founded in the 1920s as an alternative to development strategies of the Congress Party. Its strongest support was in the states of Kerala and West Bengal.

13. Between 1966 and 1968, the Birla group of family-owned industries contributed 1,645,000 rupees (approximately U.S. $36,555) and the Tatas donated 540,000 rupees (approximately U.S. $12,000) (Malik, 1989, p. 78).

14. ASSOCHAM was created in 1920 to represent British commercial interests in India. Currently, it represents small, medium and large corporations.

15. Non-resident Indian deposits were set up to encourage Indian workers in foreign countries to deposit their savings in Indian banks.

16. A coalition government is formed when an alliance among competing parties before the elections obtains the necessary number of votes. In contrast, a minority government is formed when no party or coalition establishes a majority (i.e., more than half of the total number of seats in Parliament). In this situation, the party with the highest number of votes is given a few days to establish a majority with support from other political parties.

17. The World Bank and its affiliates have been the largest source of funding for development projects in India. India has received U.S. $7.3 billion from the International Bank for Reconstruction and Development and soft credit of U.S. $12.5 billion from the International Development Association in the post-colonial period. By giving a large amount of aid to India, the World Bank has been able to pressure Indian policy makers to accept its model of development (Bhambhri, 1985, p. 39).

18. Corporations with assets of more than $20 million were still required to register with the (MRTP) Commission and firms that were designated as MRTP companies had to obtain permission from the MRTP Commission to engage in mergers and acquisitions (Beena, 2000).

19. Rupee convertibility implies that the Indian rupee can be transferred into any country’s currency without any limitations or control. A currency is considered to be fully convertible if it can be converted into some other currency at the market price of that currency.

20. By 1992 and 1993, the non-performing assets of 27 public sector banks amounted to 24% of their total credit.

21. These changes resulted in a dramatic increase in foreign investment from approximately $2 million in 1981 and $26 million in 1990 to around $109 million in 1991 (Rao et al., n.d.).

22. Global depository receipts are certificates issued by an international bank that can be circulated on world capital markets. They facilitate trading of shares, especially those from emerging markets.

23. Foreign exchange reserves increased from roughly $1 billion in 1991 to almost $20 billion at the end of 1994 ([61]Kumar, 2000, p. 2852).

24. In 1964, the Communist Party of India split when the Communist Party of India (M) (i.e., Marxists) was formed. A second division occurred in 1969 when the Communist Party of India (ML) (i.e., Marxist-Leninist) split from the Communist Party of India.
25. *Swadeshi* stresses self-reliance and is manifested as encouraging consumption of domestically produced goods. It is also associated with economic nationalism.

26. Also, under the previous corporate law, corporate raiders had to apply to the Securities and Exchange Board of India for permission to ensure that the competitive bid was beneficial to the target company. In some cases such as Bombay Dyeing’s attempt to compete with Torrent Group to acquire Ahmedabad Electricity Company, this takeover attempt was blocked by the Securities and Exchange Board of India.

27. Also, during a visit to the United States in 2000, Prime Minister Vajpayee requested an infusion of foreign capital of $10 billion annually (Frankel, 2005, p., 728).

28. Whereas commercial paper is low-risk short-term unsecured debt, private debt entails the sale of debt or securities to investors. The capital obtained from the sale of debt can be used to finance acquisitions and other expenses.

29. The particular form of deregulation in India paralleled those that occurred in the United States in the previous decade (Prechel, 2000).

30. The Act defined combinations as mergers, amalgamations, and acquisition of shares, voting rights or assets and acquisitions of control.

31. Following these policy changes, mergers and acquisitions increased in key economic sectors such as petroleum and banking. For example, Reliance Industries, India’s biggest private sector firm acquired a petroleum unit in a stock transaction.

32. In addition, the Securities and Exchange Board of India revised the amended Takeover Code in 2002 to deregulate the acquisition of significant shareholdings, takeovers, share buy-backs, and insider trading (Som, 2006, p. 4156). Following these changes, the volume of securities issuances (e.g., stocks, bonds) rapidly increased. The largest increase in stock equity issuance occurred in 2002, which was more than two times higher than the previous peak in 1995 (Indian Economic Survey, 2004–2005).

33. Deregulation in some industries was the outcome of a long-term strategy. For example, the 1994 National Telecommunications Policy opened up cellular as well as basic and value-added telephone services to foreign investors (Panagariya, 2005, p. 15). In February 2005, the ceiling on ownership of services in the entire telecom sector was raised from 49 to 74% (Indian Economic Survey, 2004–2005). Moreover, investment in certain internet services was raised to 100% foreign ownership. State managers also allowed 100% foreign direct investment in e-commerce.

34. The finance, metal and information-technology industries, which accounted for about 37% of total takeovers, are relatively small companies. As expected, capital-intensive industries accounted for the largest deal value. The petrochemical industry was first with 13.6%, followed by electronics and electrical with 13.2% and metal with 11.9%.

35. The rapid increase in mergers and acquisitions during this drop in the stock market is consistent with previous analyses, which shows that weak or unpredictable markets deter capitalists from making investments in new productive capacity. Under these conditions, corporations pursue mergers and acquisitions in order to consolidate existing productive capacity (Prechel and Boies, 1998, p. 332).

36. The Gini index is calculated on a scale of 0 to 1, where 0 is perfect equality.
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