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## The Reconstruction of Business Interests after the ISI-collapse: unpacking the effect of institutional change in Chile and Uruguay

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### Note on Contributor

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## **Abstract**

This paper focuses on understanding the different evolutions of business' associational paths in post-ISI Chile and Uruguay, offering an explanation at the crossroads of the institutional change and international trade literatures. The argument is that the different forms in which ISI institutions were transformed during the liberalization period facilitated a greater mobility of factors to different degrees, triggering divergent enduring associational strategies on the part of business. The proliferation of narrow-based special benefits during the ISI fuelled preferences for the formation of sector-based coalitions oriented towards rent-seeking activities. Nevertheless, while ISI regulations were displaced in Chile during the military period, Uruguay followed a gradual process of layering of new rules alongside old ones. These diverging strategies, having different effect on established inter-sectoral regulatory distortions, propitiated alternative associational paths of local business.

Keywords: Business, Latin America, State, Institutional Change, Regulation

## **Introduction**

The political construction of business interests has taken different forms across societies and historical periods. Business relation with the structure of economic governance and the state has been a belated but increasing focus of research for political scientists during the last couple of decades. This is an important topic as it recognizes employers are not just economic but political actors. Precisely, the study of the political construction of business interests in Latin America allows for a better understanding of opportunities and barriers for the formation of different types of political coalitions. Understanding when and how business may cooperate with governments and even organized labor which is relevant in Latin America for promoting not only economic efficiency, but also –in coordination with governments and labor movements– successful politics of solidarity as evidence suggests for the developed world.<sup>1</sup> . This paper looks into the role regulatory schemes have in affecting business incentives to centralize their interests in peak associations and how the form in which regulatory schemes are modified may alter their strategies. The transition from the Import Substitution Industrialization (ISI) model to the open market economy in Latin America offers a suitable setting for such a task. While ISI policies tended to incentivize business to strengthen sector-based lobby strategies, business' strategy moved towards long-term interests' centralization under the umbrella of a peak association in the post-ISI period in some countries, as it is the case of Chile; while in others business' attempt to form such a peak association in the post-ISI period was short-lived. Uruguay belongs to this second group.

Building on the insights offered by the literatures on international trade and on institutional change, this paper offers an explanation for the consolidation of enduring interests' centralization in peak associations by showing how the state –as regulator– acts as an endogenous cause of business organization. Inter-sectoral regulatory distortions, usually born from the distribution of ad-hoc industry-based special –particularistic– benefits in the case of the ISI, incentivizes business to abandon encompassing strategies for engaging in rent-seeking. Given this initial context, institutional change towards open market policies affects the organization of business interests. Building on the framework for explaining institutional change proposed by Mahoney and Thelen<sup>2</sup>, I argue that the Chilean transformation, based on institutional displacement, rapidly lowered business' associational costs by eliminating narrowly-oriented benefits. This encouraged enduring coordination in a peak association nucleating different sector- or industry-based associations. Conversely, institutional change based on gradual layering –the introduction of new rules alongside old ones– at a slower and more uneven pace in Uruguay, made possible for a more effective defense of sector-based benefits encouraging the prevalence of sector-based lobby.

Substantial intersectoral variation in regulation in a given economy has been shown to be correlated with the existence of conflict across class- or industry-lines. High levels of internal regulatory asymmetries lower the mobility of factors, making businesses from different sectors to be at odds with one another over policy. When factor mobility increases as regulatory distortions are reduced, the effects of trade on earnings divide actors along class lines<sup>3</sup>. The argument is that a combination of long-term institutional characteristics and short-

term processes of institutional change explain long-term patterns of political organization of business interests in the post-ISI period. The innovation is to focus on the form and pace of institutional changes as a causal factor for long-term business associational strategies. While institutional change has historical causes, the political organization of business interests depends on the particular form in which such change is processed.

The first section of the paper develops the theoretical framework. The second section details the research methodology and introduces the main hypotheses under analysis. The third section advances the analysis and conclusions about the merits of each hypothesis. A discussion about the grounds for generalizations of the argument is advanced in the conclusions.

### **The Political Organization of Business Interests**

The political organization of business interests had been given scarce attention in Latin America until the last couple of decades. The works of Frieden<sup>4</sup>, Silva<sup>5</sup>, Schneider<sup>6</sup>, Kingstone<sup>7</sup>, Shadlen<sup>8</sup>, Tacker<sup>9</sup>, Fairfield<sup>10</sup>, Etchemendy<sup>11</sup> are among the most comprehensive ones on this puzzle. The works of Gates<sup>12</sup> and Fairfield<sup>13</sup> on the related topic of the sources of business power are also relevant contributions. Most works on the region cluster within the institutional change literature, identifying the state as the prime organizer of business interests; or within the international trade literature, focusing on business economic interests. The work of Schneider<sup>14</sup>, within the first cluster, proposes that business organization depends on the cumulative effect of actions by state actors. The works of Frieden<sup>15</sup> and Silva<sup>16</sup>, among

the second group, focus on how business groups' influence policy making during the debt crisis in Latin America. Still another literature, addressing how class position affects collective action, has been particularly informative on the organization patterns of business in Latin America<sup>17</sup>.

These state-centered approaches depart from the literature addressing the issue in the context of advanced industrial economies, which identifies labor activism and party politics as the main explanations for cross-national variations. The labor activism argument builds on the idea that encompassing is a consequence of business opposition to labor mobilization when the state does not adopt a repressive strategy. The strong encompassing tendency is aimed to oppose pro-labor legislation<sup>18</sup>. The theory on partisan origins of encompassing argues that business is more likely to be represented in a single party than in multiparty systems with proportional representation. Conversely, two party systems tend towards catch-all units with employers dispersed across parties<sup>19</sup>.

Still a third approach to the problem, going back to Olson, is the classic collective action literature postulate about that less and more powerful actors have higher likelihood to overcome collective action problems to organize<sup>20</sup>. If such were the case, then the level of atomization of business firms and the level of disparity of their interests make more or less likely for them to organize in a peak association.

Finally, the literature of institutional change suggests that paths with increasing returns are found after critical junctures<sup>21</sup>. Therefore, either organizational or ideological changes at a critical juncture should make such path-dependencies possible.

The argument advanced in this paper builds on the notion that the state is an important agent influencing the organization of business interests. However, the argument qualifies this assertion in the following way: instead of state actors, is the regulatory scheme governing the ease at which factors are mobile in the production system the pivotal causal agents of change in terms of business interest organization. This insight about the effect of regulation on patterns of political conflict is drawn from the literature on international trade<sup>22</sup>. Of particular importance is Hiscox's finding that sector-based coalitions are more likely when factor mobility is low, while class coalitions are more likely as factor mobility increases<sup>23</sup>.

In other words, although business does react to government actions in the short term, long-term organizational strategies depend mostly on incentives coming from the structure of the production system. From this, it follows that an increase in inter-sectoral regulatory distortions reduce business' encompassing incentives, while processes of institutional transformation reducing or eliminating such asymmetries are expected to increase encompassing strategies. Mahoney and Thelen's institutional change theory, which proposes that there are different types of institutional transformation among which are *displacement* and *layering*—the process of setting new rules alongside the old ones--, is particularly useful for this analysis<sup>24</sup>.

Chile and Uruguay are among a select group of countries in the region whose production systems embarked in a strong industrialization process during the second part of the 20<sup>th</sup> century. In both cases the state sheltered different export-oriented sectors with tariffs, quotas, and subsidies. This created sector-based competence for those subsidies, usually

incentivizing rent-seeking strategies, discouraging centralized associational strategies. Business interests remained independent, non-coopted by political interests in these two countries, unlike in Brazil, Mexico and Argentina<sup>25</sup>. However, the form in which Chile and Uruguay transitioned from the ISI posed different organizational incentives for business.

In Uruguay, the transformation operated as a slow-moving cumulative process with a slow-moving outcome: economic opening<sup>26</sup>. The process of institutional change was one of *layering*, where strong veto players opposed liberalization and the reforms were processed in successive layers. In Chile, the change took the form of a rapid and profound displacement of ISI institutions under authoritarian rule, producing a strong discontinuity with previous arrangements<sup>27</sup>. Therefore, while Chilean business encompassed in a peak association during the post-ISI period, Uruguayan business remained organized by sector after a failed encompassing attempt.

### **Methods and Hypotheses**

The empirical strategy builds on a congruence analysis-based comparison<sup>28</sup>. The analysis establishes first the comparability of Chile and Uruguay under a “most-similar” cases design, pondering and judging antecedent conditions that were the same despite differing outcomes –i.e. moving from the Import-Export model to ISI and the similarity in business strategies for the political organization of its’ interests up until the post-ISI period–. Then, five proposed hypotheses (see below), drawn from relevant theories on the subject, are evaluated for the transition out of the ISI within each case. This within-case congruence based analysis serves

the purpose of ruling out proposed causal conditions and assessing the plausibility of each of the proposed hypotheses. Once the hypotheses are evaluated within each case, a comparative analysis based on Mill's method of difference rule each hypothesis out as plausible causes of either outcome. The main and alternative hypotheses advanced in this paper are the following:

H<sub>1</sub>: [Chile] Rapid institutional change in the form of displacement allowed for the elimination of regulatory distortions between sectors of the economy, rapidly lowering the costs for business to encompass their interests, facilitating enduring centralization of business interests.

H<sub>1</sub>: [Uruguay] Gradual institutional change in the form of layering new rules alongside old ones obstructed the elimination of regulatory distortions between sectors of the economy, slowly lowering the costs for business to encompass their interests, producing only ad hoc centralization of business interests.

H<sub>2</sub>: Long-term encompassing in a peak association is a response to an intense period of class-conflict.

H<sub>3</sub>: Having both Chile and Uruguay a centralized political system, long-term encompassing in a peak association is a response to the existence of a pro-business party with close linkages with the business community.

H<sub>4</sub>: Long-term encompassing in a peak association is a response to a process of firm concentration, which lowers the costs for growing cohesion in the business sector.

H<sub>5</sub>: Long-term encompassing in a peak association is a response to the form in which political conflicts at critical junctures are resolved which generate the necessary path-dependencies to sustain such encompassing process.

Evidence is gathered from four main sources; secondary sources; parliamentary documents –50 transcripts from committee briefs and documents handled to those committees by interests groups-; press research –300 releases in the two countries-; and 60 in-depth interviews with business, labor and politicians.<sup>29</sup> Every analyzed hypothesis is served by at least two different sources of evidence. In the congruence analysis, evidence is used to establish the value of independent and dependent variables, to then compare the value of the dependent variable with that predicted by the theory. The possibility of a causal relationship is evaluated for each hypothesis. The ulterior comparison eliminates any condition present in both cases, as it cannot account for the difference in the outcome. Conditions that are not present in both cases are regarded as possibly causally associated with the variance of the outcomes<sup>30</sup>. This strategy of a congruence analysis nested in the comparison strengthens reduces the danger of false positives or negatives.

Some final issues associated with these hypotheses need to be discussed. First, it is important to distinguish between causes for the formation of peak associations from causes for the sustenance of long-term centralization of interests. The first is a necessary albeit not sufficient cause for the second. The argument may arise about that the main cause for encompassing during the post-ISI period is the presence of a strong actor that breaks down path dependence processes. As Offe and Wiesenthal<sup>31</sup> find, maintaining unity among

business remains a problem when interests strongly diverge. Short-term factors may be suitable explanations for long-term ones only if associational costs are modified. This paper sheds light over the sustenance of long-term centralization of interests.

Second, for the proposed causal mechanisms to work, institutions have to be strongly path dependent. The analysis shows how sector-based organization of business interests consolidated during the ISI.

Third, two potential selection problems are addressed. In terms of exogenous selection, as rapid openings aren't randomly distributed, any perceived consequences of a rapid reform in terms of business organization should be a consequence of the reform and not of the social and economic conditions that drove it. This potential problem is addressed by showing how the revitalization of the Chilean peak association did not follow the military's overthrow of Allende's government but occurred a decade later in the context of the liberalization process. In terms of endogenous selection, a question about the direction of the relationship may arise. Does the institutional displacement process produce interests' centralization or does the latter allow for an unopposed displacement process? The analysis distinguishes, therefore, between the formal existence of peak organizations and the actual political lobby through them.

### **Comparative and congruence within-case analysis**

The analysis begins by exploring the pre-ISI and ISI tendencies for the political organization of business interests. There is sound secondary historical evidence to sustain that it

experienced a centralizing tendency between the turn of the twentieth century and the post-1929 crisis, in both countries, mostly as a reaction to governments advancing pro-labor legislation. This is consistent with business organizational trajectories in advanced industrial democracies<sup>32</sup> and with the neo-corporatist theory of a centralization pattern in small economies subject to the perils of the market<sup>33</sup>.

While Chilean business formed the Commerce and Production Corporation (CPC) in 1934, business in Uruguay formed the Economic Surveillance Committee (CVE) within the Rural Federation (FR) organizational structure in 1929, to act as a watch-dog for government economic policy<sup>34</sup>.

The ISI, however, drastically changed the role of the state in the economy incentivizing governments to deliver special benefits to certain business sectors because of either organizational strength or strategic importance. Once again, this change occurred in both countries affecting business-encompassing strategies through two mechanisms. First, sector-specific protectionist regulations and decision-making instances in the state benefited the interests of some sectors over others. Second, these provided the opportunity for rent-seeking.

Once business interests were protected against market perils, the need for inter-industry aggregation was highly reduced. Both the CPC in Chile and the CVE in Uruguay languished, the former becoming a marginal political actor during the following decades, the latter eventually disappearing<sup>35</sup>. A path dependence process of divergence of business interests was at play.

In Chile, business abandoned the CPC after the Production Development Corporation (CORFO) was created in 1939. There is agreement among scholars about the decline of the CPC at the expense of industry-based associations<sup>36</sup>. A detailed account of business participation in state planning commissions and development projects, offered by Silva<sup>37</sup>, illustrates the effect that ISI regulations had on business organizational strategies. Major business sectors were given a seat in the central bank and CORFO.

In Uruguay, governments also granted sector-based institutionalized participation in decision making through the creation of the Import and Export Control Commission (CIE) in the 1930s. This Commission controlled foreign exchange decisions, a prime tool for economic policy making during ISI. Industrialists and exporters had also more than eighty delegates each in other state commissions<sup>38</sup>.

ISI in the two cases offered a buffer for the distributive conflict in the form of a state capable of cushioning it, at least in the short-run. As business embraced the new model, peak associations became less necessary and even problematic as special benefits were granted to sectors.

#### *Diverging Outcomes during the Post-ISI Period*

Strategies for the political construction of business interests diverged during the transition from ISI to the open market economy. Business in Chile emerged from this process organized in a strong and well-connected peak association. Over the course of the next three decades, business successfully lobbied over policy-making, with the overarching objective of

defending the status-quo inherited from the military period. The CPC has been the most important agent for channelizing business lobby.

Similar to the case of Pinochet in Chile, Samper in Colombia, or Etcheverria in Mexico, the Lacalle administration (1990-1994) pushed business to form a peak association in Uruguay in the midst of a second liberalization attempt. The debate over entering the MERCOSUR found business bitterly divided along sectoral lines, with the manufacturing sector against it, and exporters and commerce favoring it. Finally, business did form a peak association -Business Superior Council (COSUPEM)- reuniting the main seven chambers in the economy. However, it was short-lived and mostly ineffective, collapsing a decade later, in the midst of the 2002 crisis. How do we account for this divergent outcome during the post-ISI period?

The paper proposes to explore the five abovementioned hypotheses, among which the one in the intersection of the international trade and institutional change literatures is proposed as the main innovation. For this hypothesis to hold, we should find long-term encompassing strategies evolving alongside the elimination of regulatory distortions across sectors of the economy, or the lack of such long-term encompassing otherwise. Therefore, a first step is to assess the pace and extent at which ISI regulations were reformed. Second, evidence should be found to link business organizational strategies to these processes of regulatory change.

In Chile, ISI regulation was displaced between 1974 and 1979. Again, this process has been largely documented in the literature. Trade opening began with a plan to cut tariffs

and quotas. While in 1974, tariffs ranged from 0 to 750 percent, with a mean of 105 percent; in 1977 dropped to a 10 to 35 percent range, with a mean of 20 percent. By 1979, Chile met the goal of a uniform tariff rate of 10 percent on all imports<sup>39</sup>. At that point, ISI was officially abandoned and encompassing costs for business greatly reduced. While after the early 1980s economic turndown, tariffs were increased to 15 percent until 1990, no industry-based exceptions were made. In addition, two major tax reforms were advanced in 1975 and 1984. The first one introduced a flat-rate VAT at 18 percent. The second one simplified and reduced corporate taxes. The reforms suppressed exemptions and special categories, and lowered corporate taxes at a 10% flat-rate<sup>40</sup>.

The opening process in Uruguay, on the contrary, included gradual reforms with tailored exceptions and particularities for different sectors. The military government approved a development plan in 1973, but reforms only began in late 1974 and were advanced more rapidly in the capital market than in the trade sector until 1978. Tariffs were scheduled to drop to an average of 35 percent by 1985, a process that was modified in late 1979 by including additional selective cuts over some 500 items<sup>41</sup>. While taxes on exports were lowered from 21 percent to 2 percent of export value by 1976 for traditional goods, financial and fiscal subsidies were put in place for non-traditional exports. Tax rebates amounted to 15 percent of the value of exports by 1979<sup>42</sup>.

The argument states, then, long-term patterns of business organizational strategies are caused by these changes in the regulatory environment. In both cases, it is the government that suggests business should form a peak association. In the 1970s, business in Chile divided

in an internationalized group led by the finance sector that pushed for a quick and radical economic opening, and a gradualist domestic capital led group<sup>43</sup> also pushing for liberalization, but at a slower pace. Both groups supported the military coup and subsequent regime, but did not coordinate but rather competed for political influence.

As late as 1982, the government forced business to resolve inter-industry conflicts before sitting at the negotiation table, asking them to agree on a single development plan. Pinochet's regime refused to deal separately with each sector. This led to bitter conflicts between liberalization promoters and an industrial sector with protectionist preferences. One of the most problematic issues was tax reduction and tariffs<sup>44</sup>. Although the conflict was solved in favor of the liberal side, industrialists decided not to abandon the CPC. This process of forced business reorganization is at the base of business political and industrial relations strategies from then to present. During the dictatorship, the CPC had a hegemonic role in restructuring the productive system, especially after the Social and Economic Council (SEC) was created to advise Pinochet in 1984<sup>45</sup>.

A former President of the CPC during the 2000s agreed on that the process of institutional change from ISI to a market economy was particularly helpful for building inter-industry alliances:

'The ISI was very conflictive in terms of business relations, but the liberalization process produced an institutional balance, with differential adaptive costs. Special benefits did not survive' (Former CPC President, personal interview 2010)

This piece of evidence from a key business actor, in conjunction with the evidence provided from secondary sources about business just being able to agree on short-term ad hoc

centralization strategies before 1982, is a keystone to the proposed argument as refers to the change in the regulatory environment as a prime factor changing business relations over the long-run.

In Uruguay, the abovementioned gradual regulatory change produced many loops and holes, which did not lower the cost of encompassing for business. These two citations from the Economy Undersecretary and an Industry Chamber leader with reference to the overarching tax reform the first Frente Amplio administration put forward, as late as 2007, are important evidence in showing how this gradual layering process had long-term consequences for business associational strategy.

‘This reform seeks to generate stable, credible and consistent rules that facilitate decision making with respect to investment and employment in the long term. The actual tax regime is undermined by historical reasons or the action of groups of interest’. (Mr. Bergara, Economy Undersecretary. *El Observador*, 2006a)

‘In the case of the manufacturing industry, the reality is totally different to the one of trade sector or those that sell non-tradable goods or services. Therefore, this situation [making employer’s contributions to social security the same in all sectors at 7.5 percent] is harmful for the industrial sector because it is not fair to tax similar sectors with different realities’ (Mr. Villamil. Industry Chamber General Manager. House Hacienda Commission; Commission Brief 55, June 1st 2006).

The following citations, from business and labor leaders, a former Economy Secretary and a former Labor Secretary, provide further evidence about how problematic was for business to centralize its’ political interests. These pieces of evidence together strongly suggest business inability for long-term encompassing was strongly related to the narrow defense of inherited special benefits acquired during the ISI period, which survived the gradual regulatory change.

‘The COSUPEM was dismantled when it faced the first problem. The FA government has a strategy of atomizing chambers instead of recognizing the largest ones as interlocutors. However, the economic opening has collaborated in improving synergy among chambers.’ (CNCS Directive, personal interview 2010)

‘The COSUPEM had strong contradictions; each one looked after its own little business and there were huge problems with hegemony. For example, when the National Institute for Employment and Professional Training board of directors was formed [INEFOP], it had twenty one members: 9 members from government, 6 from business and 6 from PIT-CNT. Business had to have 6 seats to be able to represent the whole sector, while PIT CNT had enough with 3’. (Oil Public Firm [ANCAP] union leader, PIT-CNT leader and FA MP 2005-2009, personal interview 2010)

‘COSUPEM did not work because of internal divisions in business sector. The extreme positions were the industrial sector, which was born protected by the state during the Batllismo period and then during the ISI; the export oriented sector has a strong liberal tradition.’ (Ex-Economy Minister, Personal Interview 2010)

‘Business does not understand the importance of building central institutions for bargaining. This is their most important weakness. In practice, the industrial and service sectors coordinate and this palliates the lack of central institutions.’ (Labor Minister, Personal Interview, 2010)

Overall, there are strong grounds against rejection of  $H_1$  in both countries. Testing the other four hypotheses will provide further elements of analysis for assessing the overall picture.

The second one is on labor activism. Taking into account that both employers’ peak organizations languished –or disappeared– during the ISI, a long-lasting centralization of business interests is expected because of an increasing conflict across class lines. During the military period –1973-1990 in Chile and 1973-1985 in Uruguay– the labor movement was strongly repressed and therefore it is not possible to assess the hypothesis as such, even when conflict across class lines increased in both countries during the 1960s and up until the democratic breakdown.

After the military period, class conflict has not been a defining cleavage in Chilean politics. One of two conditions must hold for this hypothesis to be plausible, as it is presented in the literature: either a powerful center-left party emerges with strong ties to organized labor, or at least a strong labor movement credibly mobilizes in order to alter the status quo. However, neither of the two conditions are present in post-Pinochet Chile. On the one hand, the center-left Concertación coalition has had feeble roots in organized society, in particular the labor movement<sup>46</sup>. On the other, the labor movement has been unable to unite or affect policy during the past decades. In conclusion, labor did not present itself as a credible challenger for the status quo.

In Uruguay there is no attempt on the part of business to centralize its' political interests during the 1960s amid growing conflict across class lines. As shown before, only ad-hoc centralization was possible over single relevant issues. This pattern is observed during the COSUPEM period and after, as it is the case of business opposition to the comprehensive labor reform during the first Frente Amplio administration (2005-2009).

Differently from the Chilean case, Uruguay presents the conditions necessary for the hypothesis to be hold. A left-party with strong ties to labor grew electorally during the 1990s (Frente Amplio) and, since 2005 a stable partnership between labor and government formed, which even made possible a comprehensive labor reform centralizing wage bargaining at the sector-level. However, business has remained unable to produce long-term encompassing. Therefore, even conditions are present for an encompassing strategy on the part of business, the failure of the COSUPEM and the inability to achieve intersectoral coordination on a stable

basis demonstrates that labor activism is not a prime engine for business long-term encompassing after the post-ISI period.

The third hypothesis to be considered is on partisan competition. Having Chile and Uruguay a centralized administrative system, partisan competition hypothesis postulates that it is expected to observe long-term encompassing strategies as a direct result of business being closer to a pro-business party instead of being in a catch-all two party system.

The evaluation of this hypothesis is not straightforward in Chile. On the one hand, Chile has a pro-business party in the UDI, which was born as an alliance between conservative students from the Catholic University and a group of ‘Chicago Boys’ technocrats<sup>47</sup>. Luna<sup>48</sup> effectively demonstrates how the relation between business and UDI unfolds in terms of campaign financing and vote patterns.<sup>1</sup> A former president of the industrialists accounts for this long-lasting relationship:

‘After more than twenty years in office we [Sofofa] built confidence; but it has been the opposition [Alianza] the one that has had a more consistent pro-business position. Equality is more important than growth for the Concertación. The Alianza, instead, having a very well defined view on the equality topic, is well aware that those problems are solved promoting growth.’ (Former Sofofa President, Personal Interview 2010)

However, it is not only necessary to have the link between a pro-business party and long-term encompassing on the part of business, but to have the former causing the latter. As shown by secondary sources, the two processes –formation of the UDI and revitalization of the CPC– occurs almost simultaneously between 1982 and 1983. Nevertheless, it can be

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<sup>1</sup>See Luna 2014, pages 211 and 212 for detailed data on these issues.

argued that the military government had a pro-business profile in itself. However, H<sub>1</sub> better explains business centralization as regulatory displacement clearly antecedes business change in strategy.

Uruguay has had a party system with two catch-all parties up until the post-ISI period, when the Frente Amplio consolidated as a labor-based party<sup>49</sup>. While the COSUPEM is a response to the center-right Nacional government, it would be incorrect to label the Nacional party as a pro-business party. The following statement from a labor union leader about the relation between the Nacional party and labor during the liberalization process strengthens the point.

‘Public workers had a discussion table with MEF [Economy Ministry], MTSS [Labor Ministry] and OPP [Planning and Budget Office] held at the MTSS. They were not discussion tables as such, but they were a place where workers could express their interests. Mr. Lacalle gave a good impulse to public firms bargaining tables.’ (Oil Public Firm [ANCAP] union leader, PIT-CNT leader and FA MP 2005-2009, personal interview 2010)

Organized business lacked of alliances with the political system. Business chambers have been unable to build alliances even with center-right parties due to their atomized strategy focused on maintaining special benefits or exemptions. A former Economy Secretary from the center-right Colorado Party illustrates this point succinctly:

‘At the beginning of my tenure, business sectors asked for special benefits; all sectors but the Chamber of Commerce. We fought continuously as I told them repeatedly that the government just needs to provide good conditions for market competition. [...] But the attitude of the industrial sector has changed. They used to lobby for protection and subsidies, but now they are beginning to ask for better overall conditions.’ (Ex-Economy Minister, Personal Interview 2010)

Similarly, a Nacional Party Labor Secretary under a coalitional government with the Colorado party also illustrates the issue:

‘During my term as Labor Minister, around twenty percent of my activity was to call businessmen to ask them to rehire fired labor leaders. I had no legal provisions for pursuing this goal, but I called them anyway.’ (Labor Minister 2002-2005, personal interview 2010)

Overall, the lack of a pro-business party as a possible cause for business long-term encompassing weakens the partisan competition hypothesis as an alternative suitable explanation in Uruguay.

The fourth hypothesis is the collective action one (H<sub>4</sub>), which proposes that a process of business concentration is at the basis of growing cohesion among employers and therefore facilitates long-term encompassing on the part of business. Data on firm size is collected from economic censuses beginning in 1968-69. Figure 1 shows how in Chile there is a firm concentration process, but only taking off between 1985 and 1997. In Uruguay, a process of firm concentration takes place during the 1970s and 1980s, which is reverted between 1988 and 1997.

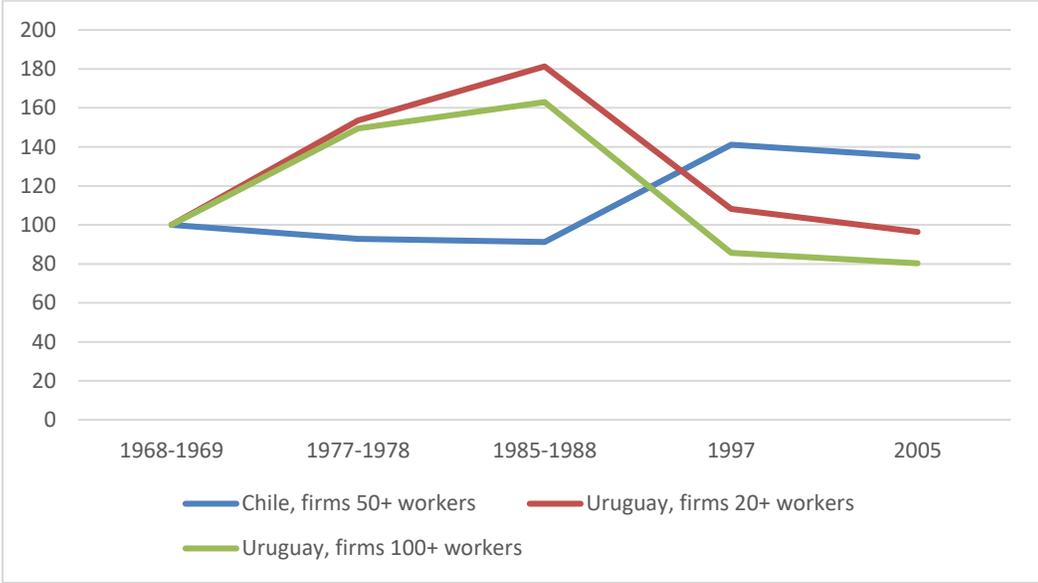
In Chile, the concentration process at the top does not occur before 1985, which is congruent with the idea that it is a consequence of the regulatory liberalization process. However, it is possible that the two processes of business interests’ centralization and firm concentration reinforce each other during the next decade. In Uruguay, the initial process of firm concentration is consistent with the formation of the COSUPEM in 1992, while the reversal of the process is also consistent with the difficulties business had for long-term encompassing under the COSUPEM. However, evidence from interviews and parliamentary

documents on business lobby during the 2007 comprehensive tax reform suggest the bulk of the conflict has consistently been across sectors. No reference is found about firm atomization caused conflicts. Consistent with this, Uruguayan sectoral chambers have been historically successful in representing the interests of their members, not being challenged from within.

‘Rural sectors did not want to be taxed while trade sectors wanted an opening process. The industry sector did not want it; they have always been more protectionist. In the 1990s, business resistance to Mercosur was strong.’ (OPP [Budget and Planning Office] Director 1993-1995, personal interview 2010)

‘After the 2002 crisis, business was very aggressive in demanding for special treatment, with the exception of the CNCS. But the government did not have to give anything except conditions for competition. Towards the end of the period and because the country began to grow again, business was quieter.’ (Economy Minister 2003-2004, personal interview 2010)

Figure 1. Industry concentration in the manufacturing sector  
(1968-1969 = 100)



Sources: Yearly Industrial Survey, Chile (years 1969, 1977, 1985, 1997, 2005). National Economic Census, Uruguay (years 1968, 1978, 1988, 1997, 2005)

To sum up, evidence from the Chilean case suggests the process of firm concentration may have been a reinforcing factor for the success of long-term encompassing on the part of business, but merits as an alternative explanatory hypothesis are not robust mostly because of a problem of timing. In Uruguay, the process of firm concentration first, and atomization later is consistent with the creation of the COSUPEM as an encompassing association and with its' dismissal a decade later. The within-case congruence analysis does not allow ruling out this hypothesis as an alternative or complementary explanation.

Finally, H<sub>5</sub> suggests long-term encompassing on the part of business is a consequence of path-dependencies born out of a critical juncture. Three critical junctures are identified during this period in Chile. First, the threatening to property rights during the Allende administration. Second, the Pinochet government forcing business to centralize its' lobby in 1982. Third, the process of regulatory displacement. It has already been shown how business engaged only in ad hoc centralization of strategies following Allende's overthrow, enduring centralization of interests being only observed after the second and third proposed critical junctures.

The question remains on how path dependence works in this case. While I do not deny the importance of authoritarian rule as a cause for enforcing business unity up until 1989, I argue that such an explanation remains incomplete if not considering the existence of internally coherent interests across sectors; coherence I propose is born out of the regulatory displacement process. Therefore, I propose H<sub>1</sub> and H<sub>5</sub> are complementary explanations, the

former nevertheless being more robust from a long-term perspective as business has remained united under the CPC for other 28 years after the end of the military rule.

Similarly, the main identified critical juncture in Uruguay during this period is the liberalization impulse taken by the Nacional Party administration between 1990 and 1994. Responding to government's proposition, business creates the COSUPEM, which was short lived and dissolved in 2002. The lack of success of this peak organization over the next decade is consistent with the gradual layering process of regulatory change that took place.

## **Conclusions**

The main hypothesis advanced in the paper ( $H_1$ ) has merits for improving our understanding of business interests' organization in these two countries. In particular, it specifies in a novel and useful form the classic institutional change hypothesis.

$H_1$  and  $H_4$  are complementary explanations. In the case of Chile the analysis suggests economic opening precedes the process of firm concentration, which is consistent with the idea of increased factor mobility being at the basis of both interests' cohesion and firm concentration. In Uruguay a lower increase in factor mobility is consistent with difficulties for long-term encompassing. The firm concentration and atomization processes, however, are also consistent with encompassing paths. However, less conclusive evidence from interviews and parliamentary documents strongly suggest business internal conflicts occur mostly on sectoral lines. It is also important to note that lack of evidence supporting  $H_2$  for understanding the political organization of business interests does not mean class politics are

unimportant for understanding contemporary politics in these countries. The success of the Frente Amplio in Uruguay and the breakdown of the Concertación in Chile points to the contrary.

The analysis advances our understanding of the mechanisms that shape long-term encompassing among business sectors in contexts of important changes in economic policy. The paper shows that the role of the state in defining regulatory environments triggers a stable differentiation in business associational strategies. The pace at which institutional change took place built different scenarios for the political construction of business interests.

While it is undeniable that the authoritarian political context in Chile facilitated the displacement process, it is also true that liberalizing governments in both countries succeeded in influencing business to centralize its' interests in a peak association –in the short-run-- irrespective of the form in which institutional change was being processed. The analysis shows that government initiative is not sufficient condition for maintaining business's long-term commitment to channelize its' political interests through peak associations. Therefore, considering the role of the state in shaping economic policy and institutional change allows a better understanding of the political construction of business interests in comparative terms.

Finally, a question remains on how far this argument can travel. Inferences from a comparison of two 'most-similar' cases should be done, at best, with extreme caution. However, evidence is consistent with the idea that encompassing costs are higher in contexts in which regulation is heavily distorted. If such premise is correct, then the argument advanced in the main hypothesis ( $H_1$ ) becomes a plausible hypothesis in the analysis of other

cases. Only in Latin America, the experiences of Argentina, Mexico and Colombia are of particular interest because of government involvement in suggesting business to coordinate. The Brazilian and Mexican cases also show how peak organization become dormant during different periods, suggesting meaningful changes in business strategies may have occurred.

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