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Business Associations and Democratic Reform

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Although most groups involved in the process of democratic, market-based reform are well aware of the important economic policy fundamentals – such as macroeconomic stabilization, trade liberalization, and privatization – necessary to achieve it, there is perhaps less awareness of the political dimensions of the reform process. This dimension is critically important because in a democratic society economic reform is difficult to sustain if it is implemented outside of the political process.

Experience in reforming countries is showing that economic reform is untenable without the support of business associations acting as advocates of reform, a function they may carry out in a variety of ways. The concept of advocacy is an important one in building a democratic system. As one of the many groups that constitute civil society, business associations have much more of a role than that of a special interest group which lobbies national legislatures. Business groups represent an important segment of society – one that stimulates economic growth through the creation of goods and services and the jobs that accompany them. Their voice needs to be heard in the policymaking process if it is to be truly democratic.

It is important to keep in mind, however, that not all business groups will be in favor of reform. In fact, it can be argued that two key interrelated factors – the types of businesses in the associations and their relationship to the state – largely shape their behavior toward market-oriented reform. If associations are dominated by firms that depend on the state for special privileges, they are likely to promote cronyism and anti-market economic policies. Although the objectives and structure of business associations may seem an esoteric aspect of reform at first glance, their impact on how reform evolves in a newly democratic society is significant.



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The Center for International Private Enterprise is a non-profit affiliate of the U.S. Chamber of Commerce and one of the four core institutes of the National Endowment for Democracy. CIPE has supported more than 700 local initiatives in over 80 developing countries, involving the private sector in policy advocacy, institutional reform, improving governance, and building understanding of market-based democratic systems. CIPE programs are also supported through the United States Agency for International Development.

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Freedom of Association

Like-minded businesses, through their associations, can and generally do exert political influence on legislative proposals that affect their interests. This may happen in a variety of ways that can either advance or hinder market-oriented reform. The manner in which an association does this also depends on whether its organization is defined under public law and whether membership is mandatory or a completely voluntary association.

The most basic way voluntary-membership associations can promote reform is through policy advocacy on behalf of measures that foster competition and open markets. These associations can advocate directly on a particular legislative issue. They can also advance a legislative philosophy by maintaining channels of communication with policymakers. For example, the U.S. Chamber of Commerce presents its “National Business Agenda” to the President of the United States every year. This agenda incorporates the chamber’s approach to specific legislative issues, but also sets forth policy goals in a more general way, communicating its philosophy of government to executive branch policymakers. This input is useful for shaping future policy goals, as well as specific policies.

All business associations can advance reform by supporting research institutes, also known as think tanks, which advocate specific policy measures through research publications as well as through analysis of pending legislation. They can assess the costs and benefits of pending legislation to the private sector in general and/or to the particular business segment that they represent. They then communicate those costs and benefits to legislators before a vote is taken. One of the first think tanks to play this role in the developing world was the Center for Economic Orientation, founded in 1985, in the Dominican Republic. In Peru, the Institute for Liberty and Democracy (ILD) has played a similar role. Because of their importance in democratic reform, CIPE has supported these two institutions as well as similar ones in numerous developing and transition countries.

Business associations also can support democratic reform by training local entrepreneurs on various aspects of organizing and running a business in a market-based economy. The Lviv Institute of Management in Ukraine and the Hungarian Management Institute in Budapest offer world-class programs in business education. In these and other transitional countries, entrepreneurial training is vital to creating momentum for continuing reform by creating constituencies that favor it.

The Corporatist Approach

The public-law business association is common in many developing countries, where, prior to the onset of market-based reforms, the state had a large, hands-on role in the economy. These associations have often been used as mechanisms for government economic control. For example, in Latin America some governments have negotiated broad-ranging agreements with unions and business groups that establish targets for wages, prices, and other basic economic elements. While these agreements promote stable economic conditions, they often restrict the responsiveness of markets to changing conditions, as well as the openness of markets to competing firms that do not belong to key business organizations.

This corporatist legacy of public-law, state-controlled business associations often prompts them to adopt an anti-reform posture. Brazil offers a telling example of this phenomenon. Beginning in July 1994, then Finance Minister (and later President) Fernando Henrique Cardoso introduced a new currency, the real, that has helped bring about macroeconomic stability. The more stable currency has also strengthened consumers’ purchasing power, particularly for imported goods now that tariffs have been lowered. For example, tariffs on imported cars were cut in October 1994 to 20% from 35%.

Reflecting what *The Economist* calls Brazil’s “truly corporatist system of chambers of industry” (April 29, 1995, p. 23), however, the automotive manufacturers’ association lobbied the government, and tariffs were recently raised to 32%. Thus, while Brazil’s car manufacturers may benefit from higher tariffs on imported cars, dealers who sell and service imported cars are likely to be hurt by this hike.

Business Interests

The example of Brazil shows that it is a mistake to assume that business is a monolith, or, in other words, that all private enterprises have the same interests with respect to pending legislation. Indeed, different business firms and economic sectors often have diametrically opposed views on a number of legislative or policy issues.

A useful way of looking at where a firm may stand on reform issues is to look at how dependent the firm is on the state for its competitive advantages. Firms that have generated profits thanks to closed markets or other regulations that impede potential competitors have a vested interest in preserving their profits by supporting the status quo. Therefore, they will lobby the government to preserve the

status quo and can be counted on to oppose reform.

This pattern is evident in both developing and transitional economies. The Brazilian car example was all-too-often a behavioral norm for chambers throughout the developing world prior to the onset of reform. This is why as reforms unfold, policymakers and entrepreneurs should encourage the formation of voluntary business groups as alternatives to state-sponsored, corporatist chambers.

In transitional economies such as those in Central and Eastern Europe, state-linked chambers may also oppose reform. Privatization is a useful example. Typically, state-owned firms slated for privatization mobilize their resources to fight it. In many cases, it is not only workers who are worried about losing their jobs, but managers as well. The strongest interest groups in the ex-socialist countries – prior to their transition – were the leading executives of large state-owned enterprises. Privatization can be successful only when this resistance is addressed and overcome.

Many of the formerly socialist countries, such as Poland, once contemplated the adoption of the public-law chamber model. The words of Václav Klaus, President of the Czech Republic, on this issue should be noted. The adoption of the public-law model in these societies involves the risk of slowing reform by creating business associations that oppose it. This opposition stems from the links of the member firms of national chambers to the state, a legacy of central planning, which is corporatist in nature. Thus, public-law-based chambers in transitional economies run the risk of falling into a “corporatist trap,” becoming agents that work against reform.

Balancing the Public-Law Model

This is not to say public-law chambers are inherently opposed to economic reform or incompatible with a market-based democracy. However, their role as agents of the state must be balanced so as to diminish any anti-reform tendencies that they may have. In the established democracies of Western Europe where the public-law model originated, this balance is achieved in two ways.

On one hand, private voluntary groups have emerged to represent their members’ interests before the state and thereby serve as a counterweight to the influence of public-

law chambers. In Germany, for example, the Association of German Chambers of Industry and Commerce serves as the public-law chamber, handling such functions as apprenticeship and other training programs and foreign trade promotion. The Association of German Industries, however, has emerged as a voluntary-member organization that serves as an advocate and channel of communication for business on legislative matters.

On the other hand, Western European countries with public-law business associations also have strong democratic traditions, featuring institutional and legal structures that allow more freedom for market forces as well as guard against the state’s tendency to command these associations and, by extension, their member firms. An open legal system is one such mechanism, in that it gives firms the right to petition the government through an impartial judiciary to adjudicate disputes and redress grievances. Well-established private property rights, a free press, and accountability for public officials are also important in guarding against the potential of public-law business associations to dominate business as agents of the state.

Clearly, transitional economies – as well as many other emerging democracies – do not yet benefit from strong democratic traditions, and must take this into account as they decide how to structure business associations. It also does not make sense for them to copy association models from other countries without regard to their own culture.

In the final analysis, this is the ultimate consideration in structuring business associations. What policymakers can do is create conditions – in particular, vibrant economies that encourage entrepreneurial activity and small business formation – where reform will be supported. They must also ensure that the other democratic institutions and traditions, like an impartial judiciary and accountability for public officials, emerge as counterweights to state control. Through this process, constituent groups will emerge and momentum for reform will be successfully sustained.