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MARKETS, BUSINESS AND REGULATION

INTRODUCTION

Markets and large corporations are often portrayed as either purveyors of development and modernity, or causes of social deprivation and inequality. In reality, their impacts depend on the institutional contexts in which they operate. What is clear is that markets alone cannot deliver development evenly across regions, countries and social groups. So-called market failure—that is, the inability of markets to allocate resources efficiently due to imperfections and externalities—is a common feature of development processes. For these reasons, economists and others have long recognized the need for regulatory institutions and redistribution.

The relationship between the market and the state has undergone major transformations in recent decades, in the context of globalization and the collapse of Soviet communism. Globalization has been associated not only with increasing economic interdependence and the apparent contraction of space and time, but also a new orthodoxy related to macroeconomic policies and institutions of "good governance". In the 1960s and 1970s, some strands of development planning and analysis were preoccupied with such questions as how to control transnational corporations and restructure North-South trade and aid relations, as well as the potentially positive role of government and international regulation in promoting economic and social development. The new orthodoxy of the 1980s associated with neoliberalism highlighted, instead, the potentially positive developmental impacts of deregulation, privatization and export orientation, as well as foreign direct investment led by transnational corporations (TNCs). In the 1990s, this perspective was broadened to include new institutional arrangements associated with corporate social responsibility (CSR) and public-private partnerships (PPPs). Economic liberalization not only created new business opportunities and rights for private firms, it also increased the capacity of private investors and corporations to influence government policy, through the threat of capital flight if governments strayed from neoliberal policies, and via lobbying and direct forms of participation in governance structures.

The Institute's concern with the roles of different actors and institutions in development has resulted in projects examining market and business regulation. In the 1960s and 1970s there were studies of state-centred or collective institutional arrangements that might curb the propensity of markets to generate "uneven development". More recent UNRISD research has examined the changing nature of market-state relations and their implications for social development. This inquiry has centred on two main questions. First, why is it that structural adjustment programmes, food policy reform and the privatization of public services have often failed to promote economic and social development? Second, can the business sector assume a more proactive role in social development through voluntary CSR initiatives and PPPs?

PLANNING AND CO-OPERATIVES

In the 1960s, UNRISD carried out research projects on development planning and rural co-operatives. Work on co-operatives, which involved 40 case studies in 13 countries in Africa, Asia and Latin America, identified their advantages in terms of regulating markets and promoting more equitable forms of resource allocation, but it also revealed their limitations. If co-operatives were to contribute effectively to social and economic development, there needed to be a favourable sociopolitical context where they were supported by state policies and local social structures. Often, however, co-operatives were controlled by local elites—and when they did challenge existing power structures, they were easily neutralized (Carroll et al. 1969; Fals Borda 1971; Pugh et al. 1970; Apthorpe 1972; Inayatullah 1972; UNRISD 1975). The work also revealed situations where both planning and a strong public administration could make a positive contribution to development. But it highlighted the difficulties for development planning per se to transform inequality when this was reinforced by powerful interests (Kuklinski 1975, 1977).

Concerns about uneven development were examined in two other major projects on the Green Revolution and food security, in the 1970s and 1980s, respectively. The former revealed that improved access to "miracle seeds" could potentially raise yields and incomes of foodgrain producers in developing countries. In practice, however, the new technology locked agricultural producers into markets for credit, labour and technology, benefiting some but harming others who were exploited, repressed or marginalized by merchants, moneylenders, banks, agribusiness, landlords and government institutions. Moreover, the "fixes" associated with Green Revolution policies did little to protect producers from fluctuations in commodity prices and the terms of trade (Hewitt de Alcántara 1976; Palmer 1976; Pearse 1980).

Although property rights are key to the success of strategies that aim to protect the environment and promote food security and sustainable development, they have often been overlooked. UNRISD research findings asserted that achievement of these goals requires policies and institutions that recognize and defend the rights—including customary rights—of less powerful stakeholders; that balance the property rights of large corporations with social and environmental obligations; and that prevent gross inequalities in ownership of and access to land and other natural resources (Barraclough 1991).

Both the Green Revolution and food security studies emphasized the crucial role of the state in promoting peasant-based or "popular" food and development strategies and regulations that alter the distribution of costs and benefits to

favour the rural and urban poor. Policy transformations such as these depend on the political and social organization and mobilization of disadvantaged groups and their allies (see chapter 5).

UNDERSTANDING MARKETS

As discussed in chapter 2, structural adjustment programmes in developing countries often failed to achieve their objectives in terms of stimulating economic growth and rural development. Why? The answer lies partly in the failure of their proponents to understand the nature of markets in general, and the idiosyncrasies of markets in concrete local and national settings. Markets do not exist in the abstract, nor do they necessarily function according to textbook theory. Rather, the way they allocate resources, and their distributional and developmental impacts, depend largely on the interaction of social groups, as well as on how individuals and groups use resources in response to not only economic circumstances, but also social relations and cultural contexts. The different histories, values, balance of social forces and relations with the world economy that characterize different societies all have profound impacts on the way markets work (Hewitt de Alcántara 1993).

This perspective, which sees markets as socially and politically constructed, challenges some of the basic assumptions and elements of neoliberal theory and practice, notably the notions that resources are allocated optimally through the impersonal interplay of supply and demand; that the root cause of market failure lies in the distortions of market signals that result from government

"THE ROLE OF UNRISD CONTINUES TO BE AS IMPORTANT AS I FELT IT TO BE IN THE SEVENTIES WHEN I HAD MY FIRST CONTACTS THROUGH SIDA AND THE SWEDISH DEBATE ON DEVELOPMENT CO-OPERATION. IN MY PRESENT POSITION AT TRANSPARENCY INTERNATIONAL, I AM HAPPY TO NOTE THAT ISSUES OF EQUITY AND TRANSPARENCY

CONTINUE TO OCCUPY THE LION'S SHARE OF UNRISD'S WORK PROGRAMME. THE PRESENT EMPHASIS ON BOTH PUBLIC AND PRIVATE SECTORS OF SOCIETY IS MOST WELCOME."

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intervention and regulation; that "getting the prices right" is the key to improving the situation of small farmers; and that broad-based social development necessarily flows from shifts in relative prices.

Understanding markets requires consideration of a wide range of institutions that define who can participate, what are considered legitimate objects of exchange and ownership, the process of exchange itself, as well as each participant's rights and obligations (Chang 2001). These rights and obligations, in turn, are products of political conflict and bargaining, whether formal or informal.

Governments obviously play a crucial role in the definition of rights and obligations. Neoliberal discourse, however, suggests that intervention should be minimal in relation to such aspects as the social obligations of firms or controls on foreign direct investment (FDI) and TNCs. Indeed, certain types of government regulation are pejoratively labelled "command and control", being regarded as somewhat passé or "ideological". Yet this perspective is at odds with the way economics, as a discipline, has historically viewed regulation—not as the antithesis of market efficiency, but as an essential instrument for improving the functioning of markets. Even the founding fathers of *laissez faire* economics were not free-marketeers in the neoliberal sense. Adam Smith, for example, recognized the importance of government regulation for getting markets to better allocate scarce resources and for facilitating competition, as well as addressing pressing social problems (Rothschild 1996).

Until recently, neoliberal theory downplayed the role of social organization and institutions in shaping economic outcomes, and the balance of power between winners and losers. UNRISD research on the social effects of structural adjustment in African and Latin American countries illustrated the flaws of the assumption that individuals pursue their narrow economic self-interest. Not only are economic actions conditioned by institutions and social relations, but these are likely to change significantly in times of recession and crisis—when, for example, traditional values, family and other networks, social solidarity, reciprocity, corruption and crime may become important means of survival (Bangura 1994a).

The upshot is that standard policy packages may have very different outcomes in different societies and localities, and cannot be determined in the abstract. Measures intended to benefit one group may, in practice, benefit another; incentives that aim to encourage a specific response may have the opposite effect; and benefits intended for the local level may never be realized (UNRISD 1995). UNRISD research showed why policies need to be grounded in an analysis of real societies and real markets, and adapted to concrete local and national settings (Hewitt de Alcántara 1992, 1993; see also box 7.1).

Box 7.1—Food markets and strategies

UNRISD research on food policy and food security has resulted in a number of influential books.

The Political Economy of Agrarian Change: An Essay on the Green Revolution explores the economic, social and political implications of introducing high-yielding varieties of rice and wheat into rural areas of Asia and Latin America (Griffin 1974).

Seeds of Plenty, Seeds of Want: Social and Economic Implications of the Green Revolution provides an overview of the Institute's work on the Green Revolution and highlights the polarizing effects of new agricultural technologies and the need for "peasant-based strategies" (Pearse 1980).

An End to Hunger? The Social Origins of Food Strategies evaluates the capacity of food systems in different types of societies to provide all social groups with sustained and assured access to sufficient amounts of food, and identifies the types of policies, institutions and alliances that enhance food security (Barraclough 1991).

The Family Rice Bowl: Food and the Domestic Economy in China provides a unique insight into food security issues in China in the early 1980s (Croll 1983).

La modernización forzada del trópico: El caso de Tabasco—Proyecto integrado del Golfo is a groundbreaking systemic and multidisciplinary analysis of the economic, social and environmental dimensions of development in southern Mexico (Tudela 1989).

Real Markets: Social and Political Issues of Food Policy Reform presents case studies from Africa, Asia and Latin America to illustrate the enormous variety of "real" market settings, and the way these variations condition the outcomes of food policy and market reforms (Hewitt de Alcántara 1993).

The analysis of food policy reform in developing countries revealed that in agrarian societies where market power is concentrated, it is meaningless to talk of free markets, even when there is no government intervention. Rather, many small producers are obliged to part with the bulk of their crops in order to repay landowners, moneylenders and merchants. In situations of food shortage, trading interests are more likely to move grain not from surplus to deficit areas, but to areas where effective demand is highest. Such situations suggest the need for more government intervention rather than less.

Part of the standard policy package related to agricultural reform and modernization in many African countries has involved the dismantling of state marketing boards, largely on the grounds that they are inefficient and distort prices. The findings of the Insitute's research cast doubt on these assumptions and policies. While such systems could harm producers by requiring them to deliver their produce

at a fixed price, the dismantling of agricultural support prices and services could have major negative impacts on the livelihoods of farming families.

In recent years, the institutional dimensions of economics have regained some of their earlier status. This is evident in the way terms like governance, social capital, transparency, partnership, accountability, responsibility and participation have been adopted by international development and finance agencies. Important differences persist, however, in the way these terms—and institutionalist approaches—are interpreted and applied. One approach, known as New Institutional Economics (NIE), is particularly interested in understanding how people respond to policies of economic liberalization, and the way institutions constrain individual behaviour. NIE seeks to diminish political "interference" in the "natural" functioning of markets or to establish "a correct" boundary between state and market.

Some research has been critical of NIE, emphasizing the importance of institutions not only in relation to their impact on human action, but also in terms of their capacity to shape individual motivations and worldviews (Chang 2001). This approach—sometimes called Institutionalist Political Economy—has also criticized the way in which NIE tends to accept as given the basic neoliberal goals of liberalization and privatization. Institutions are bolted-on in order to enhance the realization of these goals. Rather than simply "getting the institutions right" or finding the correct boundary between the state and the market, however, UNRISD research has emphasized the fact that institutional arrangements derive from a political process in which bargaining, conflict and compromise take place between individuals and groups in an attempt to maintain or change the existing structure of rights and obligations.

Concerns such as these are arising in current work on the privatization of public services. This research, related to health care and utilities (water, electricity and telephones), is concerned not only with the social impacts of privatization and targeting (see chapter 2), but also with institutional explanations as to why privatization often fails to achieve both efficiency and equity objectives. Policy makers and others have paid insufficient attention to the role of non-market institutions—including regulatory and redistributive ones—that need to be in place. This is particularly crucial in contexts where state monopolies are replaced by private monopolies, as in the case of certain utilities (Ugaz and Waddams Price 2003). The dominant approach to the commercialization and privatization of health care sees the latter not as a range of life-enhancing services, but in terms of atomistic exchange among individuals. While this approach can yield important insights into the role of market incentives in reducing inefficiency, it ignores the crucial role of institutions—regulation and redistribution, as well as reciprocity and solidarity (Mackintosh and Koivusalo 2002).

CORPORATE SOCIAL RESPONSIBILITY

An important aspect of the changing discourse on markets and regulation is the notion that companies themselves—and transnational corporations in particular—should assume a degree of responsibility for social and sustainable development beyond what is conventionally understood as their role in terms of providing employment, paying wages and generating tax revenue.

A primary goal of economic liberalization has been to stimulate FDI flows toward developing countries. This process has induced a sharp rise in the number of TNCs. As the size and global spread of the largest TNCs has increased dramatically, so too have the views that they reap the bulk of the benefits of globalization and liberalization, and that their increasing rights and freedom are not balanced by commensurate obligations and responsibilities (UNRISD 1995).

With the expansion of NGOs and global civil society activism centred on environmental, labour and human rights issues, the activities and behaviour of TNCs have come under closer scrutiny (Murphy and Bendell 1999; O'Neill 1999). International development agencies and United Nations summits, as well as social democratic parties in North America and Europe, have also joined in calls for the private sector to assume greater responsibility for social development and environmental protection.

In response to these pressures and demands, some TNCs and industry and business associations are projecting a new role, encapsulated in the terms corporate social responsibility (CSR) and corporate citizenship. The new discourse of CSR recognizes that modern firms need to be responsive to multiple "stakeholders"—not merely their shareholders—and that companies should be concerned not only with the bottom line that registers profit or loss, but also with a "triple-bottom line" that includes social and environmental goals. This discourse implicitly recognizes that corporations should assume additional responsibilities, but it maintains that improved social and environmental performance can be achieved primarily through corporate self-regulation and voluntary initiatives (see box 7.2).

Box 7.2—Corporate responsibility terms and concepts

Corporate social responsibility—refers to the ethical behaviour of a company toward various stakeholders. The term may be interpreted to involve compliance with the law, but is generally associated with voluntary initiatives—such as codes of conduct; social and environmental reporting; and improvements in occupational health, safety and environmental management systems.

Corporate accountability—implies that companies must be held to account for their actions not only in relation to financial performance, but also social, environmental and human rights impacts. Achieving this is likely to depend on a range of participatory and legal mechanisms that go beyond voluntary initiatives.

Corporate citizenship—involves the notion that companies should adhere to shared or universal values pertaining to social and sustainable development, and that the rights of companies need to be balanced by commensurate responsibilities and obligations.

Corporate self-regulation—refers to the ability of companies to improve their social and environmental performance through voluntary initiatives, often unilaterally designed and implemented by the company concerned. Proponents of corporate self-regulation generally see this as a preferable alternative to government regulation.

Greenwash—refers to embellished or inaccurate information disseminated by a company or business association so as to present an environmentally responsible public image.

Public-private partnerships—are forms of collaboration between private for-profit organizations and non-profit or public-interest organizations, where the partners are expected to share goals, risks and benefits. In practice, the term refers to a broad range of collaborations, including situations where private funds and management know-how are channeled into public works and services through an agreed contractual framework, or philanthropic activities where companies support the development projects and programmes of multilateral organizations or NGOs.

Source: UNRISD 2000e.

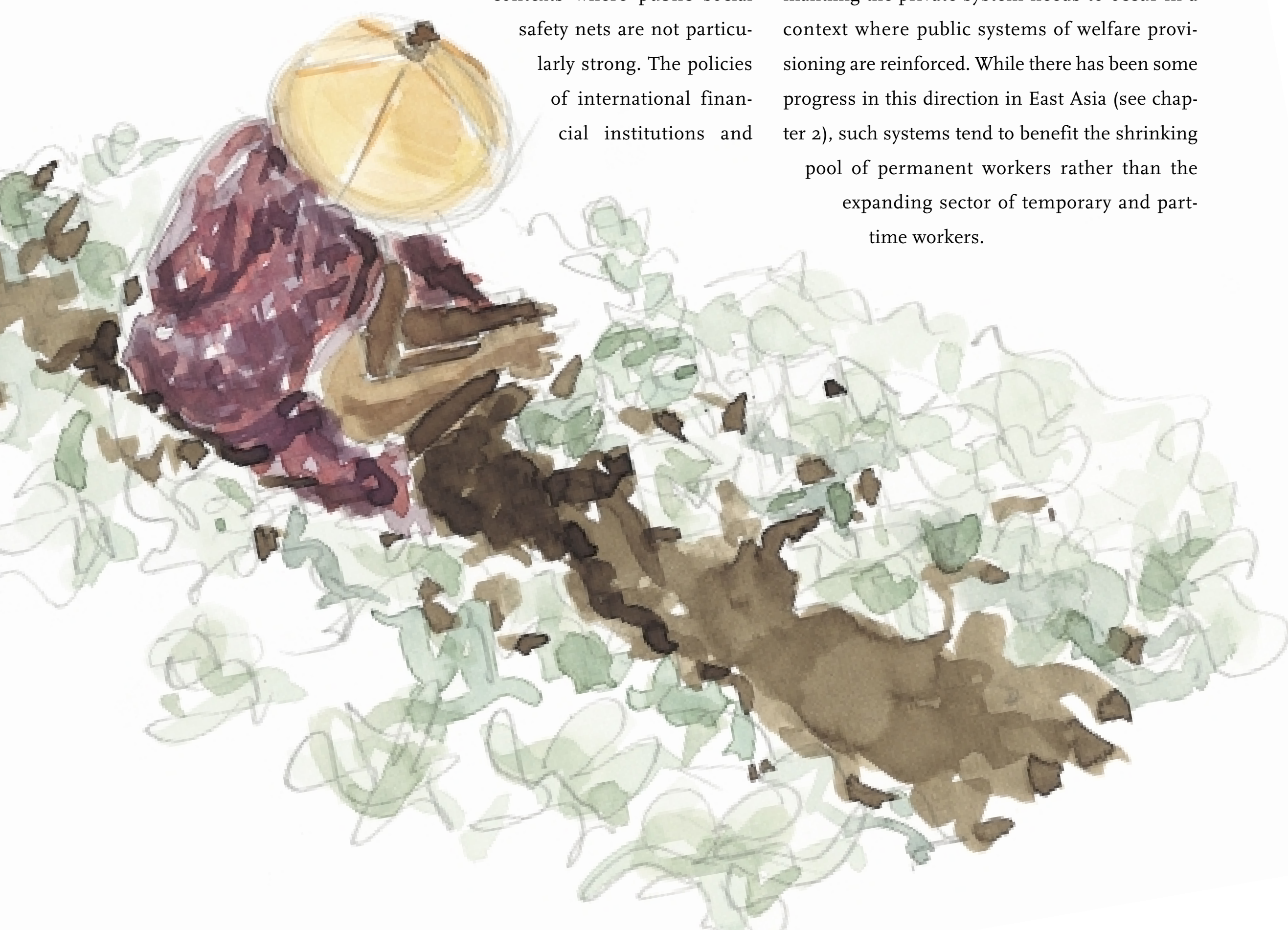
In the 1980s and 1990s some of the world's largest corporations and business associations began to support various types of voluntary CSR initiatives: codes of conduct; improvements in environmental management systems and in health and safety standards; social and environmental reporting; corporate social investment—for example, in community development projects; and more conventional forms of philanthropy. Since the late 1990s, UNRISD research has examined the record of CSR, and the potential and limitations of voluntary initiatives as an approach for promoting social and sustainable development.

The Institute's research on the "greening" of business and CSR has revealed many of the shortcomings of corporate self-regulation. At the most basic level, companies often cherry-pick among CSR initiatives and fail to implement stated policies. Furthermore, companies have few, if any, means of measuring CSR impacts; they may ignore key aspects of CSR, such as labour rights; they often limit CSR obligations to affiliates, as opposed to suppliers; and many pay insufficient attention to the need for independent monitoring or verification of compliance with new policies and standards (Jenkins 2001; Utting 2002b). Moreover, CSR initiatives remain confined to a relatively small group of companies, which are often large brand-name firms that are in the activist, consumer and media spotlight.

In Indonesia, CSR is essentially a Northern import (Kemp 2001). Here, as in other countries like Peru where CSR is not supported by strong national institutions, organizations and social movements, CSR is unlikely to become a dynamic force for change. Even in Mexico, where research showed the emergence of a new complex of institutions and organizations concerned with the environmental performance of companies, corporate self-regulation has been largely ineffectual in terms of its impact on sustainable development (Barkin 1999). Specific improvements in relation to corporate environmental responsibility at the company level tend to be dwarfed by negative macro trends involving the growth of polluting industries and the relocation of investment to environmentally fragile regions or areas where regulatory controls remain weak.

The fragmented and piecemeal character of the CSR agenda, and the prevalence of counter-trends associated with economic liberalization and competition, often gives rise to a scenario of double standards: many companies simultaneously pursue CSR initiatives and practices associated more with "deresponsibilization" or corporate irresponsibility (Utting 2000a). This has occurred, for example, in contexts where companies increase their reliance on temporary workers or subcontracting, and in the process shed social obligations and costs. UNRISD research has documented these trends in East Asia, a region where there is a relatively strong tradition of corporate social

responsibility, not least through commitments to job security. Studies on the impact of economic liberalization and the establishment of new institutions in East Asia in the wake of the financial crisis in the late 1990s have highlighted the dangers of encouraging labour market flexibility in contexts where public social safety nets are not particularly strong. The policies of international financial institutions and some Northern governments that have encouraged these institutional reforms often ignore the fact that social welfare and safety nets in countries such as the Republic of Korea and Japan have been provided, to a large extent, privately through companies (Woo-Cummings forthcoming). Dismantling the private system needs to occur in a context where public systems of welfare provisioning are reinforced. While there has been some progress in this direction in East Asia (see chapter 2), such systems tend to benefit the shrinking pool of permanent workers rather than the expanding sector of temporary and part-time workers.



CO-REGULATION AND ACCOUNTABILITY

Policies aimed at improving the social, environmental and human rights impacts of large corporations have evolved significantly in recent decades. The 1970s emphasis on controlling TNCs ceded ground in the 1980s and early 1990s to deregulation and corporate self-regulation. The latter half of the 1990s saw the rise of various forms of co-regulation. Particularly important have been a set of multistakeholder initiatives and public-private partnerships, where companies, NGOs, trade unions, and multilateral and bilateral organizations participate in specific projects or schemes that set social and environmental standards, monitor compliance, promote social and environmental reporting and auditing, certify good practice, and encourage stakeholder dialogues (Utting 2002b).

Policies, programmes and institutions associated with co-regulation reflect ongoing conflicts, compromises and bargaining within the arenas of CSR and development policy. These include the rekindling of interest within mainstream economics and policy making about the role of institutions; the rise or strengthening of "anti" (or alternative) social movements linked to sweatshops and globalization; and the frustration of certain sectors of big business with the proliferation of CSR initiatives and standards.

Multistakeholder initiatives, including codes of conduct, certification and reporting schemes—such as SA8000, Global Reporting Initiative, Clean Clothes Campaign (CCC), Ethical Trading Initiative, ISO14001, Forest Stewardship Council (FSC), and Fair Labor Association—have brought some degree of harmonization in standards, and they have often involved more rigorous standards, monitoring and reporting procedures. Yet UNRISD research has found that they have replicated several of the problems that characterized corporate self-regulation. These types of initiatives themselves have proliferated. With some notable exceptions, such as the FSC and CCC, Southern actors and concerns have been under-represented; and the procedures and methods for monitoring and verification have often remained ineffective.

The ability of different schemes to promote CSR varies considerably. Some adopt relatively weak criteria for assessing corporate management systems or performance. Several of those that have more effective methods engage with very few companies. The reliance of some certification schemes on commercial auditing and consulting firms raises serious problems regarding quality and cost. UNRISD research has questioned whether it is feasible to significantly scale up co-regulatory systems that involve reporting, auditing and certification. The complexities and cost of accessing and effectively monitoring giant corporations operating on a global scale are likely to

be daunting. Such problems suggest the need for alternative co-regulatory initiatives, such as the development of complaints procedures, where attention focuses on detecting specific malpractices and abuses of corporate power.

The Institute's research has also questioned the scope for CSR in the economic circumstances or "straitjacket" in which many developing country firms and governments find themselves. This is apparent in two respects. First, companies that

form part of TNC supply chains often find themselves under pressure to raise standards (and costs), as well as to produce more cheaply and quickly for the market. Second, developing country governments are being urged to improve labour and environmental standards, while simultaneously deregulating and cutting expenditures and various support schemes for national industry.

UNRISD research on public-private partnerships has focused, in particular, on those between the United Nations and transnational corporations. In a context where the mainstream international development community proclaims partnership to be a key instrument of good governance and development, there are various grounds for urging caution (Zammit forthcoming).

First, almost any relationship, including sponsorship and donations, is being called a partnership. And almost any partnership is being associated with CSR—even certain initiatives to promote FDI in poorer countries. Second, too close a relationship with TNCs not only runs the risk of increasing self-censorship in UN agencies, but also of displacing from the UN agenda critical research on TNC impacts and the relationship between FDI and development, as well as the analysis of alternative policy and regulatory approaches. It may also heighten tensions between the United Nations and certain sectors of civil society, if the former is perceived to be officially supporting TNCs.

Initiatives such as the United Nations Global Compact, which encourages selected companies to adhere to nine principles associated with human rights, labour standards and environmental protection, can provide a useful forum to raise awareness of social, human rights and environmental issues among the business community in developing and transition economies. Yet the risk exists that this initiative may do more to enhance the image of TNCs than to address issues of poverty and inequality, given the minimalist response of many participating companies and the lack of effective mechanisms to ensure compliance with the nine principles.

Because many such initiatives have adapted to criticism and so-called learning by doing, there has been some tightening-up of standards contained in codes of conduct, procedures for company reporting and independent monitoring.

Alternative perspectives on CSR and TNC regulation are also challenging the conventional wisdom surrounding voluntary or multistakeholder initiatives. Against the backdrop of economic recession and the limits of CSR, there are some signs of a reaction from those who see CSR as undue interference in free markets and the natural role of business, as well as from those who see it as a Northern imposition on developing countries. But while these positions find some common ground in their concern with the contemporary CSR agenda, they part company in their analysis

of state-market relations and macroeconomic policy. Whereas one believes that unfettered markets are the key to economic and social development, the other is more supportive of regulatory action by national governments acting in response to pressures and compromises that emanate from democratic processes and institutions. Another perspective that is attracting some attention emphasizes the need for corporate accountability, including international regulation of TNCs (Bendell 2003b).

Dominant approaches to the privatization of public services are also being seriously questioned. There have been calls for a reassessment of the mix of market incentives and non-market institutions that is conducive to efficiency and equity, as well as greater recognition that this balance may vary considerably in different societies. Current UNRISD research is examining the need for stronger regulatory frameworks for privatized utilities, with particular attention given to the participation of civil society and consumer interests at both national and local levels.

These developments indicate that both CSR and the privatization of public services are likely to remain a highly contested terrain, where different interests attempt to maintain or change the existing structure of corporate rights and obligations. How this plays out will depend in great part on continuing changes in the balance of social forces.