

# A Learning-Centered View of Business Associations: Building Business–Government Relations for Development

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**ABSTRACT** *The problems of rent seeking and state captured by business associations have been prominent among the concerns of economic development theory. This paper argues that firms and the state can make possible the building of new institutions that foster improvements in economic performance through arrangements that emphasize goal setting, problem solving, and continual evaluation of progress toward defined goals. The paper reviews key ideas on the learning-centered approach and builds on them to analyze the kinds of government–business relations that contribute to economic development. It uses case study material based on Chile’s agro-industry business association FEPACH. It illustrates how innovative state policy coupled with private firms’ efforts led to the discovery of group-based coordination that fostered rapid diffusion of new technology and production organization among Chilean enterprises. This work discusses the institutional reshaping of the business association and business–state relations to encourage learning and advance a process of development.*

## 1. Introduction

Prominent among the issues in economic development theory are the problems of government capture by business associations that adversely affect economic performance.<sup>1</sup> In this dynamic, business groups extract rents through lobbying, distorting competitive markets and undermining economic growth in developing countries.<sup>2</sup> For example, firms may use government protection of their markets to secure increased revenues without acquiring competitive know-how. Firms may pressure the state to assume much of the business risk instead of investing

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1. Business associations are also known as employer’s associations, trade associations or business interest associations.
2. The negative consequences of the cooperation among firms, and of business–government relations have been a central issue in the collective action literature (Olson 1965, 1982). For a recent elaboration of this view see Olson (1997). For its extensions into the New Institutional Economics see Clague (1997).

productively.<sup>3</sup> Trade associations in Africa, Asia and Latin America commonly establish privileged relationships with government, excluding competing groups, and with little concern for long-term economic performance.<sup>4</sup> The predominant view that business associations are negative for economic performance has advanced institutional solutions that attempt to curb rent seeking by reducing the state and insuring free markets.

Paradoxically, there is a significant body of literature that stresses the importance of associative activity to economic performance in advanced economies. A dense social infrastructure of association and coordination characterizes industrial districts marked by technological dynamism, innovative capacity and high productivity. This organization provides the basis for cooperation among firms, and between firms and the government on issues of training, technology diffusion, research and development, service provision, and new product ventures.<sup>5</sup> Similarly, an expanding literature on economic governance in advanced economies highlights the ubiquitous presence of networks, including business groups, business associations and collections of cooperating firms in the private sector.<sup>6</sup> The literature on clusters also emphasizes the role of business associations as a forum for firms to address common needs to improve their group competitiveness.<sup>7</sup>

The positive contributions of business associations to economic growth have been the focus of recent research on developing economies.<sup>8</sup> In contrast to the literature on rent seeking, these studies demonstrate that business associations can enhance economic performance. These kinds of associations have been termed “developmental” because they foster wider interests among members, and produce benefits to the economy.<sup>9</sup> Some contributions include: helping to implement macroeconomic policy reform;<sup>10</sup> providing support for members with a range of market-complementing and market-enhancing functions;<sup>11</sup> and as

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3. See Jadresic (1990, p. 52) in reference to business-government relations in Chile during the import-substitution period.

4. See Moore and Hamalai (1993) on the pervasive tension between pluralist and corporatist tendencies among business associations in developing countries. Also Manzetti (1994) analyzes the negative consequences of “distributional coalitions” in Argentina.

5. One of the central lessons that emerged from the 1980s literature on industrial districts was that their technological dynamism depended on inter-firm cooperation and the resolution of potential collective action problems. See, for example, Piore and Sabel (1984), Pyke and Sengenberger (1992), Saxenian (1996).

6. See Granovetter (1995) for an extensive discussion of the collections of cooperating firms, bound together in formal or informal ways, rather than atomized firms, that constitute the market. For a sample of the works on economic governance in advanced economies, see Hollingsworth and Boyer (1997).

7. Porter (1998, p. 258).

8. Among recent works, see Biddle and Milor (1997), Campos and Root (1996), Doner and Schneider (2000), Maxfield and Schneider (1997).

9. See Sabel (1994). Also, Stark and Bruszt (1998) further elaborate this term referring to associations that coordinate restructuring processes.

10. See, for example, Silva (1996, 1998), Tirado (1998).

11. The market-enhancing functions include vertical coordination of upstream and downstream producers, horizontal coordination among producers, enforcement of standards, among others. See, for example, Doner and Schneider (2000), Nadvi (1999a and b), Schmitz (1995). For an earlier analysis of the role of trade association in the development of Japanese industry, see Saxonhouse (1974).

primary actors in democratic construction processes.<sup>12</sup> Recent research on Asian and Latin American countries supports the view that relations between firms and government are key to explaining differences in economic performance.<sup>13</sup> In particular, concepts such as “growth coalitions” convey the notion that development requires supportive and cooperative business–government relations.<sup>14</sup> A common concern expressed in this literature is how and why some trade associations and public–private arrangements contribute more to economic development than others.

This article analyzes the role of business associations in productive upgrading processes, and aims to increase understanding of the kinds of state–business relations that contribute to economic development.<sup>15</sup> Building on the insights of the learning-by-monitoring (LBM) literature,<sup>16</sup> I focus on how business associations and government policy can enhance the conditions for collective learning among firms in developing economies. Collective learning is the process of generating and acquiring technical and organizational knowledge to increase the competitive capabilities among firms within a sector, group or cluster of enterprises. The literature on networks, clusters and innovation shows that learning depends on knowledge and information being shared among firms (in groups, network, cluster or region).<sup>17</sup> Virtually all the empirical cases referred to in the LBM literature are from advanced economies (Japan, Western Europe and US), or from well-known success stories in advanced developing economies, such as South Korea and Taiwan. I use a case from Chile to analyze how learning conditions develop that allow firms to improve their competitive capabilities and overall economic performance in a developing country.<sup>18</sup>

## **2. Three current views: developmental states, strong associations and learning**

In the current literature there are three views about the kinds of institutions that

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12. Bartell and Payne (1995), Lucas (1997), Spalding (1998), Johnson (1998), McBeath (1998).

13. See, for example, Amsden (1989), Campos and Root (1996), Doner (1992), Evans (1995), Friedman (1988), Silva (1996).

14. The notion of “growth coalitions” is found in Doner (1992) and in Silva (1996) in reference to an alternative conception to previous models that emphasized strong, dominant and insulated states. The alternative idea focuses on cooperation among diverse economic actors, instead of state domination.

15. This article does not presume that this is the only entry point for business–government relations. Business–state interaction also occurs through networks, personal and informal relations, and other forms of governance (Hollingsworth and Boyer, 1997, chapter 1).

16. I am referring here to the work of Sabel (1994, 1995).

17. Learning through networks and by interacting is seen as essential for the ongoing success of an innovative cluster. There is a large amount of literature on the dynamics of networks of firms where firms compete intensely while at the same time learning from one another about markets and technologies through repeated interaction; see, for example, Piore and Sabel (1984), Piore (1992), Powell (1990), Saxenian (1996), Sabel (1992).

18. On the case of Chile, several works address business–state relations to show how close collaboration between business and the Pinochet government that took power in 1973 influenced and shaped government policy to achieve macroeconomic policy reform (Silva 1993, 1996 and 1997). In this paper, however, I focus on the adjustments and upgrading processes at the level of the firms, given the macroeconomic regime changes.

foster economic development, and limit the potential for rent seeking.<sup>19</sup> One view focuses on the internal characteristics of the state, a second highlights the attributes of the associations, and the last emphasizes principles characterizing business-state relations that induce learning.

Evans (1995, 1997) argues for the possibility of “state-society synergy” resulting from the institution of states characterized by “embedded autonomy.” The developmental potential of business–government relations differs depending on the internal structure of the state. The states with professional civil services have the capacity to enforce honest, productive behavior by business. When the state is a coherent bureaucracy,<sup>20</sup> and it has dense ties with the business elite, information flows and the state’s knowledge increases. In this case, the state can encourage entrepreneurial exploration of new sectors and new strategies, and boost an economy beyond narrow private interests.

Evans’ work is important for understanding differences in state structure, and for illustrating that state policy can shape the capabilities of the business community. This view, however, relates to a centralized bureaucratic model, with ties between government and business elites (or individual enterprises). It neglects relationships among firms (inter-firm networks, business associations, and groups) that play a key role in economic coordination.<sup>21</sup> The state has ties with numerous societal groups and networks, and very often, the interlocutors are not individual companies but groups of firms. Moreover, recent studies show that coherent bureaucracies are scarce in the developing world.<sup>22</sup> In their absence, business associations often constitute important alternative institutions of economic governance.<sup>23</sup>

A second view focuses on the institutional strength of associations. Particular internal characteristics of business associations counteract the potential for rent seeking and the state capture by firms. Doner and Schneider (2000) identify specific internal and external factors that characterize associations that deliver more developmental benefits than others. Associations that have the capacity to induce members to comply with rules and decisions designed to further collective goals are considered more developmental. The capacity to induce changes in members’ behaviors constitutes institutional strength, which is characterized by: high member density, provision of valuable benefits and resources to members, and adequate interest mediation mechanisms. The productive use of institutional strength requires companion external enforcement (i.e., competitive markets and a disciplining state) that channels strength into efficient activities. Market vulnerability can force firms to seek ways to enhance their competitiveness. The combination of institutional strength and external pressures ensures productive use of that capacity, creating developmental associations.

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19. This article does not intend to make an exhaustive review of the literature. For a wider overview of the literature see Maxfield and Schneider (1997, chapter 2), and Lucas (1997).

20. A coherent bureaucracy, in the Weberian sense, is based on meritocratic recruitment and promotion, and procedural rationality.

21. For a critique of Evans oversight of inter-firm networks, see Stark and Burszt (1998).

22. Maxwell and Schneider (1997, p. 21) make this point based on a review of various country cases.

23. See, for example, Biddle and Milor (1997), Sabel (1994).

Doner and Schneider show that associations vary qualitatively with respect to their internal features and their external context, a point missed in theories of collective action.<sup>24</sup> There are several unanswered questions about the dynamic qualities of developmental associations. By what processes do these kinds of associations emerge and what sustains them? Well-functioning or existing developmental associations exhibit largely static conditions and characteristics at one point in time. The characteristics found in today's developmental associations might play only a small or transitory role in an association's life. Moreover, the value of selective benefits and resources to firms could diminish or become obsolete over time, in the current context of market volatility, trade liberalization, and fast technological changes. As firms cope with new competitive pressures by adapting, adjusting and even turning away from established activities and practices, their goals and requirements change and diversify. A set of uniform institutional conditions may not meet the diversity of goals and problems.

The third view offers a learning-centered approach that focuses on the emergence of institutions that address two central problems for achieving economic development: learning and monitoring.<sup>25</sup> Learning refers to the process of firms' catching-up to the international standards of quality and productivity; it involves generating technical and organizational knowledge. Monitoring refers to the assessment by transacting parties that each is getting a fair deal according to the agreed standards between them. For Amsden (1989, 2001), this dilemma is addressed when the "principle of reciprocity" prevails in the relations between the state and firms, in contrast to the "principle of giveaway." With the principle of "reciprocity," the state demands certain performance standards to insure that selective benefits (subsidies, quotas, protection) are used for productive purposes. More specifically, the state disciplines business actors through export performance requirements in return for subsidies. For example, governments monitor whether firms are meeting performance targets, rewarding better performers with support and ceasing support to non-performing ones. In this learning-based view, increased reciprocity in business-government relations correlates with higher economic growth rates.

As the institution that induces learning is mainly the state, Amsden underplays the role of private sector and public-private institutions in monitoring and solving collective firms problems.<sup>26</sup> Even strong states have limits to their capacity to monitor firm performance, or their ability to enforce reciprocity by

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24. Cohen and Rogers (1992) advance a similar argument in the context of advanced economies and in relation to democratic governance. Their sketch of various features of qualitative variation in groups, however, focuses on those characteristics consistent with norms of egalitarian democracy. They argue that certain attributes such as leadership accountability, and inclusiveness of group membership, are more likely to represent interests than groups with hierarchical relations. Also, see Lucas (1997) for an analysis on qualitative differences among associations.

25. I include in this view the works of Amsden (1989, 2001) and Sabel (1994) because both take these central problems as their departure points, and both focus on the principles guiding relations among economic actors, rather than the internal characteristics of the state or associations. There are, however, significant differences between the two authors that I discuss in the paper.

26. For an elaboration of this point see Doner (1992).

disciplining bad-performers.<sup>27</sup> The state may lack sufficient or receive inaccurate information. In addition, the administrative and technical requirements to monitor performance and discipline firms may exceed the bureaucratic capacity of governments.<sup>28</sup>

A different institutional alternative to meet the demands of learning and monitoring central for economic development is Sabel's concept of "learning-by-monitoring" (LBM).<sup>29</sup> In the LBM view, economic actors create institutions that enable a self-sustaining learning process. Learning-by-monitoring is an organizing principle that connects the state and firms as well as firms to one another. Actors focus on setting provisional goals, and then force themselves to continually reevaluate those goals as they assess progress toward their intended ends. Actors set goals and make an effort to reach defined targets through continuous review and monitoring of the partners' performances and capacities to reach those targets. Learning is an indeterminate process, in which both firms and government do not know in advance what has to change and how. No actor is dominant, no hierarchical center has definitive knowledge, and there are no institutional prerequisites. Instead, actors learn from new information that arises through continuous discussion, experimentation and self-monitoring. Learning-by-monitoring creates the possibility that, instead of pursuing rent seeking, actors (firms, business associations, government) can redefine objectives and pursue improvements in economic performance with beneficial developmental consequences.

The specific concern of this paper is how economic actors in developing economies discover and build institutions that improve the conditions for learning among many firms, and what role business associations play in this process.<sup>30</sup> As developing country firms face greater competition in unprotected domestic and foreign markets, they must search for new technologies, market opportunities, and develop capabilities that improve their competitive abilities and economic performance. This entails unlearning knowledge that is not valued in markets, and mastering current technical and organizational know-how.

I argue that collective problem solving can transform the role of business associations, and reveal new arrangements between firms and the state, and among firms that undermine rent seeking and better serve developmental goals. A central challenge when existing firm networks have knowledge that is not valued in markets, or is too backward to compete against international standards of quality and productivity is how to enhance the conditions for learning to improve competitive abilities. Economic actors can build institutions that make collective learning possible. The effectiveness with which knowledge can be generated, diffused and shared among firms depends on the emergence of the

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27. Maxwell and Schneider (1997, Chapter 2, p. 10) raise this point, which is also discussed by Biddle and Milor (1997) in reference to the Turkish case.

28. Evans (1995) analysis of the Brazilian informatics industry illustrates the difficulties the government agency faced in monitoring the computer market.

29. The "learning-by-monitoring" concept is developed in Sabel (1994), and is also referred to as "bootstrapping" (Sabel 1995).

30. To clarify, learning refers to the process of generating technical and organizational knowledge, including the ability to continuously improve current production organization and practices, or to develop new ones.

new principles of LBM in the interactions between the state and firms, and in the relations among firms. As the state and firms establish links that focus on goal setting, through comparisons that reveal performance problems and possibilities, they enable the building of new institutions that enhance the conditions for firms to learn and improve economic performance.

As learning disrupts existing production practices and processes to develop new or better products, firms face major uncertainty and risk associated with changing the known ways of producing. State policy can play a role in the initial stages of establishing links and lines of communications among firms, when they are non-existent, or when localized knowledge is not advanced enough to produce products valued in world markets. The state can induce firms to learn by encouraging them to look beyond their domestic market, instigating them to set goals with reference to some prevailing standard so that shortfalls in performance are apparent to firms. Specifically, the state and firms create problem-solving groups to coordinate their interactions and focus on finding solutions to common technological and organizational problems. A key aspect of this coordination centers on the setting of new standards, which provides a basis for coordination and sharing of knowledge among firms, and between firms and the state. This coordination helps firms to discover, understand and foster innovations in productive practices, and change the relations among them and with the state.

### **3. Rebuilding business associations to foster collective learning: a Chilean case<sup>31</sup>**

I illustrate this argument with a case from Chile. I discuss the transformation of the Chilean business association of agro-industry processing firms, ASFACO later known as FEPACH,<sup>32</sup> along with the simultaneous growth of the tomato processing industry. Below I discuss the changes in ASFACO from the 1960s to the late 1990s at two levels: the state-association relations, and among firms within the association. I use the case study of the tomato processing industry, a newly created agro-industrial cluster, to demonstrate both the significant technological and organizational problems firms faced, and the process of destroying the old while building new connections among firms, and between firms and the state in which learning-by-monitoring flourished.

During most of the 1980s and 1990s, Chile enjoyed high rates of economic growth, with its GDP growing at an average rate of 6.1 percent per year. The export sector was the driving force behind this performance. Since the early 1980s, exports grew dramatically, from about 10 percent of the country's GDP

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31. This section is based on original field research conducted in Chile during 1996, and information collected in 2002. Much of the data reported in this section was obtained from author's interviews with Chilean managers of all the large agroindustrial processing firms producing processed tomato products, and representatives of FEPACH.

32. The Federation of Chilean Food Processors [Federacion de Procesadores de Alimentos de Chile (FEPACH)], which was previously the Association of Canning Firms [Asociación de Fabricantes de Conservas (ASFACO)]. In the text, I refer to ASFACO when discussing the early years of the association, and FEPACH for the current period.

to approximately 35 percent. More than 70 percent of these exports are natural resource-based products, derived from the agricultural, mining, forestry and fishing sectors.<sup>33</sup> Most of Chile's leading exports, such as fresh and canned fruits and vegetables, fresh-frozen seafood, and forestry products are essentially new economic activities. The tomato processing industry is one example of a new export activity. This product was never exported before, but achieved substantial competitiveness in the 1990s, accounting for an important share of processed exports.<sup>34</sup> Chilean producers became so adept that by 1994, Chile occupied the fifth place among the world's tomato paste producers, after the USA, Italy, Turkey, Greece, and tied with Spain. Not only did Chile increase its share of the world market, but it also penetrated very demanding ones.<sup>35</sup> Production networks grew substantially. In 1985, only two companies existed and contracted 210 suppliers. A decade later, by 1995, nine large firms worked with nearly 5000 raw material suppliers. These new specialized processing firms and suppliers of processed tomato products concentrated geographically in the southern central valley of Chile, a region where there was no prior experience with new or traditional industrial tomato varieties.<sup>36</sup>

Success was not instant, nor automatic. Just two decades ago, Chile lagged far behind other exporting nations. None of the indigenous firms had the capacity to export. Becoming exporters presented at least four technological challenges. First, producers used poor quality local fruit (discard quality) and varieties inappropriate for industrial purposes. Second, the volumes produced at the time were insufficient to achieve a relevant presence in foreign markets. Third, the existing local plants used dated small-scale reconditioned second-hand equipment, which did not compare to that used by the established competitors (California, Italy, Portugal). Fourth, the firms could not meet nor knew of the quality standards required for exportation, and lacked basic connections to foreign markets.

The rise of the agro-industry from low-quality and inefficient production, to being competitive at the global level entailed a process of destroying old practices and forms of organization, and constructing new alternative ones. Chilean government action nurtured the emergence and upgrading of local production networks, fostered new product standards, technologies and production organization, and attracted private investment in new industries. Synergistically, domestic firms formed new local networks, or reorganized existing ones, while investing in upgrading their organization of production to compete

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33. For more data on exports see Meller and Saez (1995), on the share of natural resource exports see Vial (1994).

34. Export sales of processed tomato products grew from merely two million dollars in 1981, to more than 100 million dollars in 1995, a fifty-fold increase (FEPACH 1996). During this period, the total volume of processed tomato production increased eight times, from 14,420 metric tons per year to 113,650 metric tons.

35. For example, in 1980, Chile exported little to Japan, accounting for a .65 percent share of their total tomato paste imports. By 1985, Chile's share had increased to 4.46 percent, by 1990 it rose to 12.52 percent, and by 1992, it had reached 16.86 percent. By comparison, China's share in Japan's total tomato paste imports only increased from 6.63 percent in 1980, to 9.05 in 1990, and decreased to 8.07 percent in 1992. By 1992, Chile accounted for a larger share of Japan's tomato paste imports than Taiwan, which until 1990 had been the major exporter to Japan (CORFO 1995).

36. For an analysis that focuses on the emergence of the agroindustrial cluster in Chile and the productive reorganization within and among firms see Perez-Aleman (2000).

in global markets. As firms and the state sought ways to improve performance, they rebuilt and discovered a new role for the business association that was critical in fostering collaboration to upgrade production among large Chilean firms.

The Association of Processed Foods (ASFACO) was founded in the late 1950s.<sup>37</sup> For more than two decades, it typified a corporatist organization that represented the canned products processors in negotiations with the state. It was born during a period of protectionism and import substitution industrialization, under the government of Pedro Aguirre Cerda. During the 1950s and 1960s, one of ASFACO's roles was to voice the concerns of canning firms in their business dealings with the Pacific Steel Company (Compania de Aceros del Pacifico or CAP), a state-owned enterprise that was the sole producer of steel and tin products in Chile. Processors felt that CAP's prices were too high and tin can quality was deficient. ASFACO addressed the firms' primary concern, high tin prices, organizing all the canning firms in order to make joint purchases of the needed cans from CAP, resulting in lower prices for its members.<sup>38</sup> Secondly, ASFACO voiced demands for higher quality tin. During this protectionist period, the firms could not import tin products, and CAP was their only available source. ASFACO members seriously considered building collectively their own tin products plant, and even purchased the land for a plant site as well as plant equipment.

The next most important item on the Association's agenda was lobbying the government for higher prices for their products. For most of the 1950s and 1960s, Chilean governments had a system of price controls covering nearly every retail food item.<sup>39</sup> ASFACO representatives engaged in constant negotiations with the Ministry of the Economy, attempting to raise the controlled prices of their processed food products. Resolving problems with CAP and constant negotiation with the government consumed the Association's resources.

At that time, neither ASFACO, nor the firms had as a priority the upgrading of production to improve their international competitiveness. All the canning firms oriented their production for the protected domestic market, and there was resistance on the part of private firms to learn new practices. For example, during the late 1960s and 1970s, the state attempted to foster the growth of an internationally competitive agro-industry. State-financed projects under the government agency CORFO<sup>40</sup> attempted to introduce new product standards, foreign technology and a different production organization to replace the old model of relying on discard quality raw materials to produce processed products that could never meet the requirements of foreign clients. At the time, existing domestic producers resisted experiments with new organizing principles and new varieties and even considered it a threat to their survival. While CORFO had detected new export opportunities that required investments in new technologies,

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37. Author's interview #18.

38. Author's interview #134.

39. For an elaboration of the government's role in price control regulations see Bennett (1968).

40. CORFO stands for Production Development Corporation.

the private firms were reluctant to adapt to new standards and to venture beyond the protected domestic market with new or better products.<sup>41</sup>

The new policies of the Pinochet government radically transformed the economic environment of Chilean firms, and rendered ASFACO's traditional role obsolete. In the 1970s and 1980s, the Chilean government introduced macroeconomic reforms that changed previous government relations with firms. As Velasco (1994) notes, the uniform tariff limited the scope of private sector lobbying for import protection; the privatization of social security and changes in budgeting procedures limited the amount of lobbying on fiscal matters; and the independence of the Central Bank ended the partial control that private sector interests had on credit policies. Market liberalization allowed for foreign imports, and thereby eliminated CAP's tin can monopoly in the domestic market. Moreover, the government also eliminated price controls.

The two issues that had consumed ASFACO ceased to be relevant in the new economic environment. As the opening of the economy and the deregulation of domestic consumer prices made ASFACO's traditional role irrelevant, the organization began a period of decline and inactivity. In the words of a long-time member: "ASFACO became like a club of a few members who would meet to exchange opinions at a monthly breakfast."<sup>42</sup>

A popular view credits the neoliberal macroeconomic reforms for the high levels of growth that Chile experienced in the 1980s and 1990s. An analysis of the experience of the agroindustrial processors shows, however, that the firms' adjustment to new competitive pressures was not automatic, nor immediate. Increasing export production required new technology and investments to deal with highly perishable products, as well as strict timing coordination demands. Firms had to upgrade, adopting technological and organizational innovations in production, processing and marketing to compete successfully in international markets.<sup>43</sup> Much of this technology change involved tacit, practical and organizational knowledge that could not simply be purchased and transferred as "turnkey" operations. The process of adjusting and upgrading is an investment, as it takes time and resources to acquire the new skills and unlearn backward practices. In the period following the economic reforms, large Chilean processing firms failed in their multiple attempts to export processed tomatoes.<sup>44</sup>

At the time, neither the firms, nor the Association (ASFACO) had the skills, know-how, or vision of how to reorganize production to improve their products. Gradually, however, in a process of close interaction between the state and firms, the enterprises began to explore, discuss, search and generate new knowledge

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41. CORFO nonetheless proceeded with local experimentation to adopt and adapt foreign technologies. These public efforts produced important local innovations that provided significant inputs to private firms' restructuring in subsequent decades. For more on this, see Perez-Aleman (2000).

42. Author's interview #122.

43. Technological innovations include the type of plant varieties, soil preparation used in raw material production, pest controls, handling and procurement of raw material supply, plant processing technology, packaging, product types.

44. For a decade, from the mid-1970s through the mid-1980s, grave problems plagued the processing firms: low yields; bad quality and rotting of highly perishable raw material; irregular flow and untimely supply; lack of synchronization between suppliers and the processing plant; and low volumes of product.

concerning new production methods and practices to improve their existing capabilities. As firms searched for new standards, technologies and markets, they created institutions that fostered collective learning and supported the growth of the new cluster. In joint partnership, the state and firms discussed the development of new standards and benchmarks to identify where their performance was deficient. They also initiated discussion on new goals, and devised projects to meet them. This process led to the reorientation of ASFACO, and to the reconfiguration of business–state relations.

Pinochet's policies changed as time went on, and became more supportive of private-sector export development programs. As several studies show, the collapse of Chile's economy in 1981–1982 prompted a revision of the policies of the first decade of the Pinochet government.<sup>45</sup> Having been too rigid and unsuccessful with the macropolicies of its first decade in government, that led to several recessions (in the late 1970s and early 1980s), Pinochet's team revised economic policies and became pragmatic after 1984.<sup>46</sup> The peak business association, the Confederation for Production and Commerce, worked closely with government policymakers to manage these 1980s reforms.<sup>47</sup> The new policy included open encouragement of export sectors and state-sponsored loan programs for entrepreneurs.

The government's goal to increase exports in the post-1982 period led them to form groups of firms focused on the upgrading of production methods and products. Specifically, the state used funding to prod firms to upgrade existing products or to develop new ones. It provided government grants through the state agency PROCHILE.<sup>48</sup> The government pushed firms to engage in collaborative efforts to design and improve production processes and develop new export products. In stark contrast to the popular free market ideology of the Pinochet government, in the mid-1980s, the state agency PROCHILE promoted the formation of alliances between agroindustrial firms to assist their explorations into unknown foreign markets. The central focus of these state-promoted, but self-coordinated groups was to help firms to learn how to improve the product quality to meet international standards, as well as examine production practices while exploring what to produce for world markets.

The Export Promotion Fund, with a yearly budget of five million dollars in the mid-1980s, provided resources to co-finance export projects proposed by groups

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45. For more on the reformulation of the Pinochet government's economic policies see Meller (1990). Also see Silva (1993, 1996) on the multiple coalitions formed between business and government to pursue market reforms.

46. This term is from Silva (1996) who elaborates on the shift from the first decade of the Pinochet government to what he calls *pragmatic neoliberalism*.

47. As mentioned in the first part of this paper, this experience is cited as a notable example of the role business associations can play in the successful implementation of macroeconomic reforms. Silva (1993, 1996, 1998) provides detailed analysis of this experience.

48. PROCHILE means Export Promotion Bureau of Chile, and it is part of the Ministry of Foreign Affairs. It was created in 1975. During its initial years, PROCHILE's activities were relatively tame: gathering information on export procedures and international regulations; identifying potential clients and export products; supporting the participation of firms in international trade fairs, by financing and setting-up the booths; creating catalogs of Chilean products for foreign distribution; and sponsoring local seminars.

of firms in the same sector.<sup>49</sup> The financing could only be given to firms in a group, not individually; and the government financed 50 percent of the project, with private firms financing the other half.<sup>50</sup> PROCHILE promoted the association of firms into sector-specific export committees that would then define a project. Projects fell into two categories: (1) improving quality to meet international standards; and/or (2) develop new products.

Once a project was approved, PROCHILE supported the export committees by providing all the specialized services that firms needed to develop their exports: acquiring information on foreign standards; organizing trips abroad to visit the factories of foreign competitors, as well as product discovery missions; and providing information on market trends. These committees provided a base from which firms, with government assistance, could discuss the building of new standards for the local firms, and discuss new product ideas acquired during visits to trade shows or to potential foreign clients. These activities proved particularly valuable to managers and owners who lacked export experience.

In line with the Pinochet government's unwillingness to work with the existing business associations,<sup>51</sup> PROCHILE contacted and recruited firms directly, bypassing existing organizations, such as ASFACO, to bring together members and non-members of existing associations to form new sector export committees. Early committees represented the following sectors: processed fruits and vegetables, salmon and other processed seafood, fresh fruit, furniture, footwear, textiles, wine, and paper products. In all, some sixty-five committees consisting of six to fourteen enterprises each, and integrating over 700 firms were in place by 1988.<sup>52</sup> This state program contributed to create new networks between firms, professionals, and government officials who jointly discovered new ways to face the competitive challenges.

The new government policy contributed to create opportunities for reconfiguring the associations' role and goals. In the specific case of the agroindustrial processing firms, the PROCHILE committees sparked the reorganization of ASFACO, as firms experienced a new sense of common identity. Firms began to look differently at ASFACO, seeking ways to recreate it as an organization that would serve to improve the competitiveness of their industry. The PROCHILE committee brought them together in a way that ASFACO on its own could not. As important, the state's efforts interacted with private firms' own

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49. Author's interview #20.

50. The discussion on PROCHILE draws on author's interviews #20, #21, #22, #23, #122, and #138.

51. As Velasco (1994, p. 398) discusses, US trained technocrats staffed Pinochet's economic team, in contrast to previous conservative governments that had teams largely staffed with businesspeople. Silva notes that the Pinochet government broke away with traditional channels of communication with existing business associations.

52. See Pietrobelli (1993). Some credit has been given to PROCHILE in increasing the number of Chilean firms that export. In a period of four years, between 1986 and 1990, the number of firms that exported more than doubled. In 1986, only 200 enterprises exported between US\$1 million to 10 million dollars, and another 235 exported more than US\$10 million dollars. Four years later, in 1990, 526 enterprises exported between US\$1 and 10 million, and 526 firms exported more than US\$10 million dollars (Meller and Saez, 1995, p. 19).

strategizing for ways to improve products and organization, jointly forming crucial inputs to the adjustment process.<sup>53</sup>

As some of the leaders recounted:

Suddenly, the enterprises that came together in PROCHILE's committee began to feel that ASFACO could fill an important vacuum, not as an organization destined to lobby, pressure and protest against the government, as it had done in the protectionist period, but as one that would address the daily production problems that managers face in their enterprises.<sup>54</sup>

Soon we had a new group in ASFACO (besides the traditional members), which included not only owners, but also the firms' professional managers who believed that an ASFACO of the old type made no sense [...] what did make sense was to change ASFACO to become committed to improving our enterprises. This change began to occur gradually in the 1985–88 period.<sup>55</sup>

As PROCHILE continued its elaboration of public relations campaigns (road shows) abroad, thematically focused around specific products (i.e., processed foods, salmon, and wine) and staged in key markets (like Japan, Europe, and the USA), groups of firms began to feel that the reputation of the group, rather than just one firm, was key to attracting foreign buyers to Chilean products.<sup>56</sup> With this sense of group identity came the realization that poor product quality created problems for both Chilean processors and their foreign customers. The agroindustry firms identified the need for uniform quality standards as fundamental to the process of becoming reputable exporters.

Originally, ASFACO included only producers of canned products. As other types of fruit and vegetable processors began to join, the firms decided in 1989 to divide into groups forming four associations under one umbrella organization, which led to the organization of FEPACH.<sup>57</sup> It grouped not just the ASFACO members, but all the various agroindustrial sub-sectors, including producers of frozen, juice, and dehydrated products that had come together in the PROCHILE export committees. FEPACH currently has the same four associations with ninety-one member firms, which includes:<sup>58</sup> ASFACO (twenty-five member firms), ADECH (twenty-nine firms), AGEPCO (twenty-five firms), and ASECO

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53. A discussion of the reorganization within firms is beyond the scope of this article. For an elaboration of this aspect, see Perez-Aleman (2000 and forthcoming).

54. Author's interview #122.

55. Author's interview #134.

56. Author's interviews #18, #23, #34, #128.

57. The four associations in the federation have one central administrative office that provides services to all. Members interviewed expressed that by strengthening one office that serves all four associations they were able to pool more funds to hire well-trained, better-experienced professionals. The funds to finance the association come from two main sources: membership fees, based on a percentage of each member's sales; and from the tailored services provided to member firms on a request basis.

58. Except for three multinationals (Nestle, Malloa, and ANCOR) that integrate the association, all members are Chilean owned firms. Author's interview # 18 and FEPACH membership list, 2001.

(twelve firms).<sup>59</sup> FEPACH currently focuses on four activities: (1) developing quality standards to improve and maintain the reputation of the sector; (2) organizing technological missions jointly with PROCHILE; (3) working jointly with the government in negotiating bilateral and regional trade agreements like APEC, MERCOSUR, and NAFTA; and (4) gathering and distributing information to members regarding exports and international market trends.

Promoting new standards for improving quality became the central role of FEPACH. This is not unusual, as the literature notes that an important role for “developmental” trade associations is enforcing standards (or export quotas) so that member firms comply with the rules.<sup>60</sup> This article, however, highlights the role of BAs in providing conditions that make crucial technological knowledge explicit among the collective of firms, and second, in transforming the collective interests of firms. The process of setting and monitoring the implementation of new standards is primarily a coordination activity through goal setting. The group discussion to set new standards allows all firms to understand the reasons behind their performance deficiencies, and the changes required in their existing practices and routines to reach better standards. The establishment of a new standard involves firms discussing product specifications and common technological problems.

As adopting new standards implies changes in existing production processes and practices, firms might resist moving in the new direction, or they might feel uncertain that investing in the changes will be beneficial. Through discussion, firms begin to convince each other that the new standards are crucial for their collective reputation in world markets. This process begins to develop and shape common interests among firms that focus on improving performance rather than on extracting rents. As important, not all firms start out with equal levels of knowledge. Some are further along than others in experimenting with changes. The standard-setting process serves to communicate more effectively among firms; it supports new product development activity and learning to learn. The association creates a space for firms to evaluate their individual knowledge, and the coherence between their existing practices and those of the most advanced ones. This constant comparison fosters information flow from one firm to another.

The collective discussions that ensue to identify where practices and institutions are deficient, contribute to generate a shared knowledge among firms. Firms develop new product standards based on the new awareness of what clients demand, as well as the technical information that firms acquire on their explorations of international markets, and their contacts with foreign customers. The information gathered abroad on new products and production processes becomes useable knowledge as firms begin to understand and to make explicit

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59. ASFACO currently stands for Association of Canned Food Producers (Asociación Gremial de Procesadores de Alimentos de Chile) mainly includes firms processing tomatoes, peaches, apples, and cherries; ADECH for Chilean Driers Association (Asociación de Deshidratadores de Chile) includes dehydrated products such as apples, raisins, plums, peppers, and tomatoes; ASECO is the (Asociación de Exportadores de Jugos Concentrados) including apple, grape, kiwi and peach juices; and AGEPCO for Association of Frozen Products Exporters (Asociación Gremial de Exportadores de Productos Congelados) including corn, peas, green beans, raspberries and strawberries.

60. See, for example, Doner and Schneider (2000), Nadvi (1999b), and Sabel (1994).

the tacit knowledge that is not easily transferred. Through discussion in groups, firms share knowledge on how to organize the production process and where to market. The groups of firms create conditions for collective learning.

An important part of the new institutional arrangements is the formation of quality control labs and certification programs. The labs provide data and measurements necessary to support the enforcement and diffusion of new standards. Specifically, the associations that constitute FEPACH establish mechanisms for widespread quality control and the certification of export products. While each processor has their own internal quality control lab, FEPACH promotes the use of an independent certifying company, in addition to the quality control of each firm. Standard setting becomes particularly important in the initial development stages of a new export product or sub-sector when firms are not familiar with, nor have developed the capacity to meet the strict foreign standards for imported food products. Recently, for example, FEPACH has been working with the firms that export frozen fruits and vegetables to establish a code of quality standards and promote the certification process, which results in the use of a certification seal from experienced independent certification firms if standards are met.<sup>61</sup>

FEPACH promotes yearly trips abroad for what they call *technological missions*, which go beyond the habitual participation in international trade fairs, which they also do. In these technological missions, the general managers, plant managers and operators, and agricultural managers, go on *apprenticing* trips, lasting up to a month in some cases, to visit leader foreign firms producing similar products. They go to see how Chilean firms compare to the competition, as well as to learn about new technology and practices in order to improve their own. The firms use FEPACH as the trip coordinator, and then plan the trip with PROCHILE in order to gain the benefits of their expertise in contacting the foreign embassies and governments for foreign missions.

For example, the tomato processing firms have organized trips to China, Turkey, Italy, and California, visiting management, quality control labs, processing plants and raw material production. In their visit to Turkey, for example, the Chilean enterprises were received as a group by Turkish private firms that would not have talked to an individual firm. One manager reported how they learned a way to improve Chilean cultivation practice by adopting a Turkish technique for measuring the distance between seedlings in a more exact way than before, with an important reduction in production costs and increased productivity performance.<sup>62</sup> Trips to California and Italy had as one of their purposes learning ways to improve the quality attained in the handling, processing, and packing of

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61. Like at FEPACH, the issue of quality standards to build the reputation of the industry also became the central role of the Association of Salmon and Trout Producers (Asociación de Productores de Salmon y Trucha A.G.), which integrates 42 producers of cultivated salmon, and trout (PROCHILE's committee also sparked the birth of this organization). Chile is the second producer of salmon after Norway. I conducted interviews with some of these firms and their association. The managers pointed out that of most relevance to their sector's success was the development of a Code of Quality Standards, which provides standards for each step from salmon cultivation to processing, and the collectively self-imposed requirement to have an independent certifying enterprise do the certification for the quality seal according to that code.

62. Author's interview #113.

the products; crucial to maintaining and expanding exports to demanding foreign markets. In addition, the firms visited these countries to explore the mechanization of tomato harvesting. Trips abroad also contribute to improve the exchange between managers, increase friendships, and create a path for continued discussions after they return to Chile. Moreover, the firms often engage in joint experimentation of new practices they discover.

FEPACH also provides important collective services to the large firms. For example, it helped large processing firms face a crisis caused by a sudden rise in ocean shipping prices in 1988. This was a highly sensitive issue for Chilean producers, given the travel distances from its targeted markets. The shipping companies (both Chilean and foreign) established equal prices for shipments from Chile to the east coast of the USA. Virtually overnight, they raised the container shipment price from U\$1,400 to U\$2,600 dollars, an 86 percent increase. The firms banded together to create enough unified pressure to negotiate down the shipment prices to U\$1,150 dollars per fleet through a collective contract. All of these processing firms decided to do future contracting with the shipping companies as a group, and gave the coordination and negotiation task to FEPACH. The joint contracting of shipments brought substantial savings to firms. One manager reported savings of U\$5 million dollars per year as a result of better pricing for shipments.

Most importantly, contracting as a group with the shipping lines reduces the confidentiality of much of the firm-level proprietary information as FEPACH coordinates the amounts and the destination of all shipments. This coordination entails much sharing of information among firms in terms of destination, customer identities, products and volumes exported. In time, the association began to produce yearly reports containing data such as: member ranking by production and export sales, types of products, destination.

As the large processing firms rebuilt their association, it contributed to create conditions to insure continual information flow, learning, and to improve the ability of firms to solve technological and organizational problems to achieve successful export performance. Firms have continuous access to practices across other local firms and other countries, enabling them to benchmark and compare themselves to the competition, and to disseminate new information to their production network. These interactions promote continuous skill-building and upgrading.

The case discussed here is but one example, but there are similar ones in other sectors of Chilean economy. Government policy did not target or focus on a specific sector; rather it was economy-wide. The experience of the agro-industry processing sector reflects closely that of other sectors, particularly seafood and forestry processing.<sup>63</sup> Some of these PROCHILE export committees later evolved into strong associations that took over the role of providing supporting conditions to their firms' export endeavors. The most notable examples of the new associations that emerged include: the Chilean Food Processing Federation (Federacion de Productores de Alimentos Procesados de Chile or FEPACH, discussed in this paper); the Association of Salmon and Trout Producers

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63. See, for example, Meller and Saez (1995), and Schurman (1996).

(Asociación de Productores de Salmon y Trucha, A.G.); and the Association of Non-Traditional Manufacturing Exporters (Asociación de Exportadores Manufactureros no-tradicionales or ASEXMA), to cite a few.<sup>64</sup> State policy was a catalyst in the initial stages, with firms subsequently investing significant efforts to rebuild their existing business organization.

#### **4. Conclusions**

Business–state relations in developing economies can be directed to induce collective learning among firms through a strategy that emphasizes goal-setting, the development of new standards in a group forum that allow information exchange and knowledge sharing connected to the productive practices of firms. Given new competitive pressures due to drastic changes in world markets and domestic economies, firms face difficult technological and organizational problems. Solving them requires coordination among firms that allows them to access knowledge, skills, and information to build their competitive capacities. The state can facilitate the firms’ coordination by establishing relations with associations and groups of firms that focus on problem solving, and discussion guided by the goal to improve existing standards and practices. Learning is fostered as firms jointly discuss and compare current production practices and processes, and define alternatives to improve the uncovered deficiencies. In this process, the actors build alternative institutions that support economic development.

Rent-seeking activities and government captured by selfish interests are undermined or diminished as collaboration among firms, and between firms and the state focuses on how to enhance the capabilities of firms; improving existing products and production processes; determining what needs to be done to accomplish such goals; and constant evaluation of performance against those goals. While the existing literature notes the state’s role in shaping the business community, this paper identifies other mechanisms than the traditional ones that rely on distributing “selective incentives” such as quotas. Rather, the state assists the formation of new networks of firms that establish new local and global connections. It facilitates actors’ coordination through discussion and debate structured by standards and benchmarks that help identify shortfalls in performance and alternative practices and organization to improve it.

This process undermines the focus on distributional struggles over who gets what (quotas, subsidies, protection against imports, tax loopholes).<sup>65</sup> Interactively and incrementally, firms and the state reshape their relations and create institutions that fuel collective learning among firms, and enhance competitive abilities. Firms set new goals and engage in a joint search for ways to upgrade. This in turn creates a space for building and rebuilding ties between firms, and between firms and the state. The focus of business–state relations shifts, away from getting and distributing something from the state, towards the discovery of ways to continuously upgrade and adjust through learning-by-monitoring.

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64. Author’s interviews #23, #29, #139, #122.

65. I am referring here to the concept of “distributional coalition” developed in the literature on collective action; see especially Olson (1997) for a recent elaboration.

This research has implications for thinking about collective action and institutions. First, the prevalent theory of collective action views business interests as pre-determined and formed ex-ante.<sup>66</sup> According to Olson, business interests are narrow, focused on redistribution to itself, with detrimental consequences for economic development. Firms join an association only to further “distributional” goals, such as export quotas or to gain privileged access to government resources. The Chilean case, however, suggests that associations contribute to shape the firms’ interests through discussion and joint goal setting. Associations can shape and reorient business interests towards more encompassing ones, specifically, when firms focus on problem solving to improve their performance. Actors create institutions that allow for constant monitoring, effectively fostering associations that are beneficial to economic development. Monitoring serves to promote contacts between firms guided by the goal to improve their practices, organization, technologies, and products. “Encompassing” or “developmental” interests emerge as a by-product of the group interactions, rather than as a precondition for creating “encompassing” organizations.

Second, this research has implications for thinking about institutions and economic growth. The New Institutional Economic theory, derived from North (1990, 2000), assumes that institutions are the rules of the game under which firms undertake economic activity. The NIE analysis focuses especially on broad rules at the macro level, such as constitutions, property rights, contract enforcement, and judicial systems. The failure of this broad institutional framework explains failure to grow. These macro-institutional aspects are also the focus of the current second generation reforms that international development agencies promote in developing countries. The Chilean case suggests that institutions at the more micro level (industry, sector, region, firms, etc.) are as important to explain economic performance and growth. Firms and government actively experiment and create institutions at multiple levels that have direct effects on technological improvements, firm building, knowledge diffusion, and productivity with consequences for growth. The Chilean experience indicates there is a wide institutional variety, and business associations can constitute institutions for high-quality growth.

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66. Op.cit, p. 46–47; Olson (1982).

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