

Delegative Dilemmas and Horizontal Logics: Subnational Industrial Policy in Spain and Brazil

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Scholars of “decentralization” have recently revealed the importance of subnational industrial policy in responding to the challenges of globalization. But these treatments tend to make endemic assumptions about either the universal efficiency or inefficiency of decentralization. This article argues that subnational industrial policy performance is politically contingent and develops national patterns that are more composite than endemic. Political contingency is analyzed in terms of subnational incumbents’ incentives to delegate authority and resources to industrial policy agencies and the degree of symmetry in authority and information flows across these agencies. A cross-regional/cross-national comparison of several subnational units in Spain and Brazil demonstrates that subnational industrial policy is implemented and maintained where incumbents delegate and policy-making agencies are symmetrically integrated.

One unexpected parallel to the widely held view that globalization has challenged the utility of national industrial policies is the finding that subnational governments have become more active in spurring industrial investment and higher productivity, and enhancing access to technological innovation (Evans 1997; Tandler 1997). These findings are surprising for several reasons. First, they challenge the conclusion of some that state intervention in markets along the lines of industrial policy is obsolete or dangerous given high capital mobility.¹ Second, they raise doubts about the view that globalization reduces the importance of location in the investment strategies of international and even national firms. The demonstration that subnational governments can have a role when they do not have control over the macroeconomic policy

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Studies in Comparative International Development, Fall 2001, Vol. 36, No. 3, pp. 58–89.

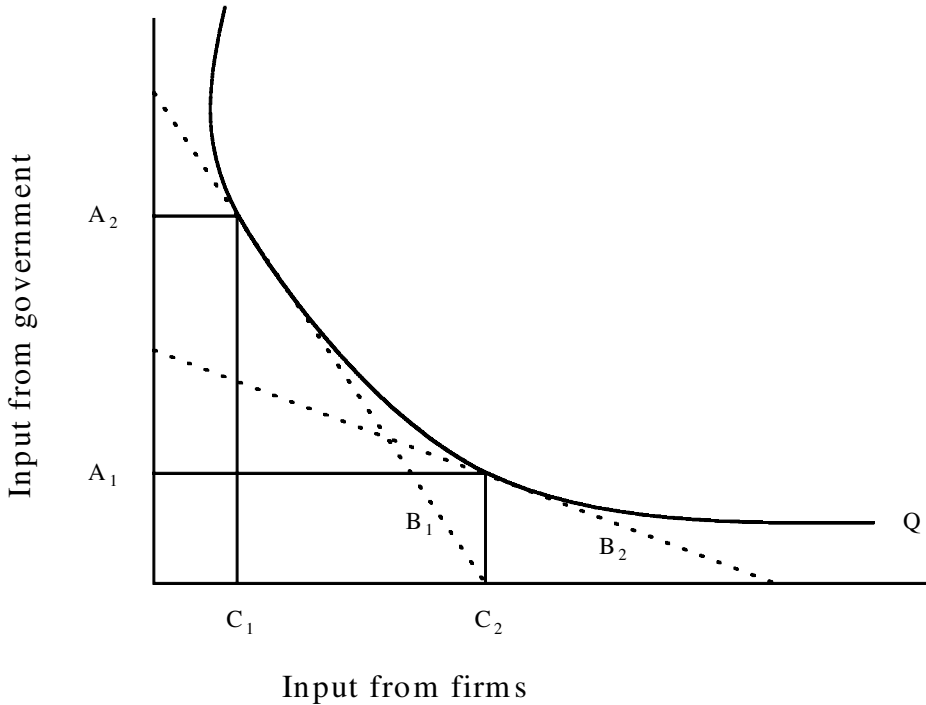
mechanisms that served national industrial policies in decades past only highlights the need for additional work on what Erik Swyngedouw has described as *glocalisation*—the “double movement of globalisation on the one hand and devolution, decentralisation or localisation on the other...” Far from being limited to kowtowing to the interests of multinational investors, some subnational governments have become more aggressive in organizing their own development policies to diversify local economies and promote investment externalities, higher productivity, and growth.

However, recent scholarship on economic policy in federal and/or decentralized states has failed to clarify the effects of this trend. Scholars have divided into two competing camps: those who argue that decentralization enhances economic policy (the optimists) and those who posit that it endangers it (the pessimists). The optimistic view typically sees decentralization as a means for improving the economic performance of markets by limiting central intervention, encouraging policy innovation among competing subnational units, and enhancing allocative efficiency through local provision of goods.² The pessimists argue that political factors impede the realization of these benefits. Pervasive subnational clientelism, especially in developing countries, leads to the misappropriation of resources.³ This logic sets up a kind of “delegative dilemma” which holds that the benefits of decentralization cannot be realized at the subnational level if patronage-maximizing incumbents centralize control over policy resources and fail to delegate authority to technocratic agencies.

Subnational industrial policy making is particularly prone to the delegative dilemma. The economic justification for industrial policy typically invokes the need for the public sector to provide public goods such as infrastructure, education, finance, and research and development that are sub-optimally produced by markets. Since the supply of these goods responds to highly particular needs by sectors and firms, the most effective forms of industrial policy making involve high and continuing levels of cooperation between public agencies and businesses.⁴ While national governments have the advantage of shifting fiscal resources and adjusting macroeconomic policy to deflect opposition and promote cooperation, subnational governments must deal with the fiscal constraints national governments place on them. They also face competition from other regions for a finite pool of fiscal resources. The poorest regions are further handicapped by shallow tax bases and a dependency on enclave economies such as heavy (sometimes public) industry, mining, and agriculture. Intergovernmental competition, institutional and historical limits raise the costs of the long-term thinking the most workable models of industrial policy require. In this context, politicians seeking political support and access to a larger piece of the national fiscal pie are loath to fully delegate authority over scarce resources to technocratic agencies.

Evaluation of “success” and “failure” of industrial policy in a subnational setting and over a short period of time should thus be based on indicators that show evidence of cooperation between public agencies and firms, despite the delegative dilemma. Empirically this means the existence of close and continuing coordination of common resources between agencies and firms (e.g., information, financing, etc.) to produce desired economic outcomes (e.g., pro-

Figure 1
Production Function for Synergistic Industrial Policy



ductivity improvements, positive externalities, growth, etc.). The benefits of such collaboration can be illustrated using a production function of costs to government and firm participation (“input”) in policy provision. In Figure 1, the costs of implementing an industrial policy are lowest if both public agencies and firms collaborate in policy formulation. In the absence of collaboration (unilateral provision of the good—finance, information, etc.) budget constraints (represented by B_1 and B_2) raise the opportunity costs to government (B_1 at the Y intercept) and firms (B_2 at the X intercept). The least costly combination in producing Q would occur at $A_2 C_1$ and at $A_1 C_2$, in which sharing of information and use of common resources would prevail.⁵

The main purpose of this study is not to explain the causes of positive economic outcomes but to examine the political causes of the cost-effective forms of public-private cooperation illustrated by Figure 1. By doing so, it challenges optimistic and pessimistic approaches to decentralization. Both views suffer from the tendency to treat subnational governments and the process of decentralization as systems with *endemic* positive or negative attributes. Empirical evidence from decentralized states in both advanced capitalist and developing countries reveals that the pattern of success or failure of subnational economic policy cannot be summarized by national models (Locke 1996; Remmer and Wibbels 2000; Snyder 2000). Subnational performance takes on more *composite* configurations *within* countries.

This article develops a theory for explaining the composite national pattern of industrial policy making by first highlighting the conditions under which subnational politicians delegate authority and resources to policy-making agencies. I argue that incumbents are more risk accepting if the level of polarization among elite groups is low. Such conflict can occur in terms of both partisan competition over votes and social conflicts involving labor and business. These two dimensions of elite competition can intersect, generating cases in which majority parties/coalitions that might otherwise make incumbents more risk-accepting eschew delegation when faced with union and business opposition. Where partisan and social polarization are muted incumbents lead what I call *delegative governments*.

Where levels of elite conflict are high, incumbents feel vulnerable and are more likely to discount future gains from economic policy success. They face incentives to garner short-term rewards such as the cultivation of personal votes in imminent elections or the buttressing of patronage support. These conditions are typical of *populist governments*. Populist governments will *centralize* their control over economic policy so as to minimize the opportunity costs of garnering personal support.

My argument then posits the institutional arrangements that enhance innovation and protect subnational agencies from clientelism. Delegation, while necessary for initiating industrial reform, is insufficient for maintaining this policy type. Shifts in political conditions may create incentives for incumbents to manipulate agencies *ex post*. Even without the threat of intervention bureaucracies may by themselves fail. Technocrats may shirk their responsibilities for the sake of personal or collective gain, an outcome that is more common when oversight functions are weak. I posit that these tendencies are muted in subnational policy networks in which industrial policy agencies and decision-making “partners” such as unions and business associations are organized into a *horizontal* network in which no agency maintains supremacy over the others; each is specialized, the group retains continuous contacts, and it is coordinated through mutual planning and goal-setting functions.⁶ Such a structure facilitates information flow and oversight across agencies, reducing the costs for innovative decision making and raising the costs for shirking. I call this *horizontal embeddedness*. This format is superior to strictly vertical/hierarchical ties in which bureaucrats may more easily hide information from principals (e.g., politicians, the voters, and fellow agencies). In sum, subnational governments will implement and maintain industrial policy, generating allocative efficiencies and minimizing clientelism, only when delegative government and horizontal embeddedness are present. Both are necessary and cumulatively sufficient.

The real costs presented by the delegative dilemma directly challenge the optimists who under-analyze subnational political interests and bureaucratic structure.⁷ The pessimistic view of decentralization supplies an incomplete assessment. It has not been able to explain the advent of numerous examples of “success” in diverse policy areas (industrial reform, fiscal and social policy, etc.) in advanced capitalist and especially developing countries, where such cases are only presently coming to light. These experiences suggest something

other than the presence of *endemically* clientelistic subnational politicians and dysfunctional bureaucracies.

Explaining the composite pattern of industrial policy making in decentralized states requires an understanding of the delegative dilemma afflicting the optimists and the horizontal logic of subnational policy networks evading the pessimists. Systemic/endemic approaches must be replaced by comparative cross-national and cross-subnational studies of decentralized public sectors to reveal the politically contingent conditions affecting policy performance. The remainder of this paper is organized into four sections. In the next section I outline the main argument and introduce the comparative method used in the study. In subsequent sections I detail one major subnational case in Brazil and Spain and include comparisons with two additional cases for each country. In the final section I offer conclusions.

I. The Argument and the Study

The delegative dilemma is similar to one Barbara Geddes (1994) terms the "politician's dilemma." While industrial policy does not ask politicians to forsake patronage altogether, the kind of industrial policy that generates positive externalities in the market requires that clientelistic exchange be minimized. Geddes argues that this is more likely to occur under conditions in which contending political parties are roughly equal in power. Parity reduces the relative political costs of delegation. But I find that delegation also occurs when incumbents are in a politically dominant position. Delegative governments, as the empirical cases demonstrate, do not discount the future as heavily as populist governments do. On the contrary, they estimate that the opportunity costs of delegation are low. The primary utility of both partisan parity and political dominance arguments is that they highlight the importance of low elite conflict. Highly conflictual political games are more likely to be associated with incentives to pursue clientelistic support than those in which the political opportunity costs of delegation are low. Politically vulnerable incumbents will centralize control over clientelistic resources while less vulnerable elites will entertain secondary incentives to decentralize.

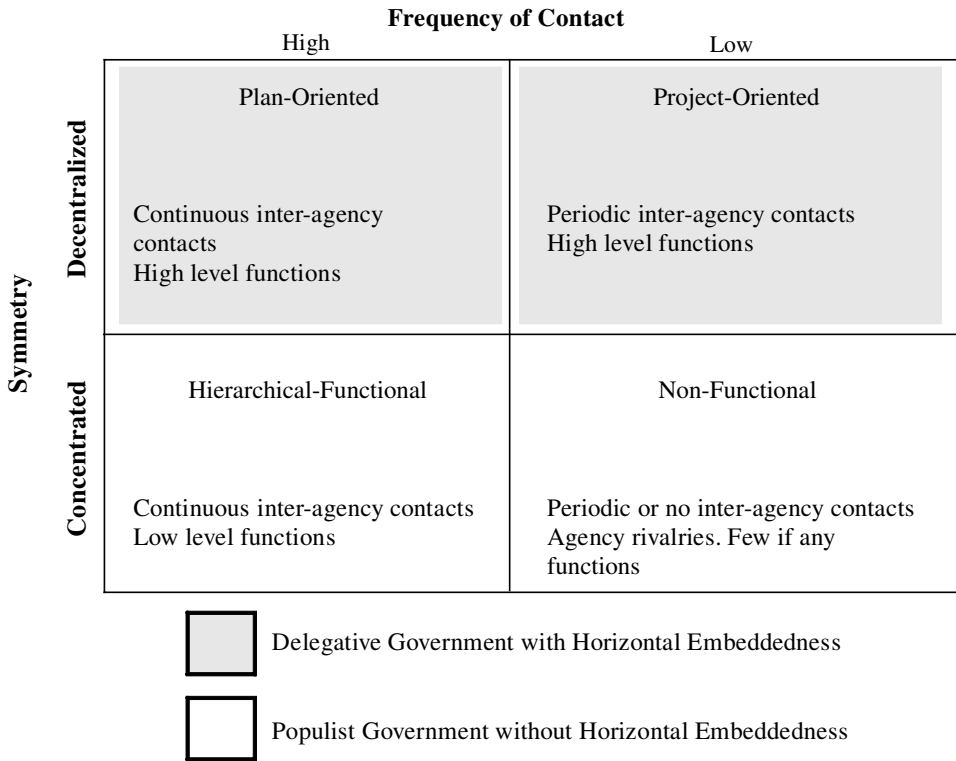
Secondary incentives to delegate operate in the absence of high levels of political conflict and they are based on the non-trivial benefits of delegation. The act of delegation provides its own political returns as regional leaders can tell their constituents that they are "doing something" about persisting economic problems and justify the need for additional resources and authority from central government managers. Alternatively, if things go wrong, incumbents can blame the agencies to which they delegated their authority, covering their own responsibility for policy failure under a cloak of ambiguity (Alesina and Cukierman 1990: 846). Doing nothing may become politically costly in the face of eroding economic performance and competition with rival subnational governments over the same pool of fiscal resources. Some significant concern for the larger economic welfare of a region *in addition to* expected political benefits accrued from ostensibly addressing these problems will motivate these executives to delegate.

Delegating resources and authority to “political technocrats” with the information to compose and implement industrial policy is a prerequisite, but the *maintenance* of cooperative agency-firm ties continues to be politically contingent. First, incumbents may re-centralize control in the face of increasing political vulnerability *ex post*. Second, bureaucrats may themselves hide information about their effort levels and their performance from supervisors, politicians, and their constituents, thus contributing to “bureaucratic dysfunction” (McCubbins, Noll, and Weingast 1987). Horizontal embeddedness minimizes these costs by enfranchising a broader, cross-cutting policy constituency than is normally the case in strictly *vertical* forms of cooperation between bureaucratic agencies and firms. Clientelism can develop more easily *within* these vertical networks, while horizontal embeddedness produces the cross-agency monitoring that raises the costs of bureaucratic shirking. Horizontal embeddedness also raises the costs of intervention by politicians by creating alternative sources of political support through the expansion of the constituency of public agents and private clients involved in industrial policy making.⁸

The combination of delegative government and horizontal embeddedness emerges in cases where incumbents delegate authority and resources to political technocrats but are themselves exposed to incentives to divide the governance of economic policy among an array of different agencies rather than invest control in just one. Intergovernmental competition among states provides the strongest set of incentives. The work on “competitive federalism” in American politics holds that intergovernmental competition fosters innovation in public policy to attract consumer-voters and businesses (Dye 1990). These conflicts also create political inducements to attract federal funding lest other states acquire relatively larger shares. By creating an array of public agencies to design and implement industrial policy, incumbents can bolster their arguments for more resources from the central government with references to the immensity of the economic crisis and the related need to fund an expansive industrial policy structure. Given that industrial policy includes multiple tasks and policy skills ranging from areas as diverse as utility management to labor retraining, logistical exigencies produce additional incentives for subnational governments to create numerous and connected public agencies to satisfy firm-clients and consumer-voters. Where political incentives to delegate are present, such horizontally embedded structures will be more common than in cases in which populist elites are in command of subnational government. Under populist management, the incentives to centralize control over policy resources will override the inducements created by competitive federalism to decentralize. Elite polarization will continue to tip political institutions in directions that favor clientelistic exchange.

Thus far the argument for delegation is based on the cost-benefit calculations of *political executives*. Yet social actors, and particularly labor and business organizations, play a role in defining these governments as delegative or populist, and they help shape the configuration of horizontal embeddedness. The extent to which unions and business associations play a collaborative role in defining the industrial policy apparatus or maintain antagonistic positions greatly affects incumbents’ propensity to delegate. Moreover, the integration

Figure 2 Ideal Types of Inter-Agency Networks



of unions and business associations into the management of industrial policy will involve these organizations in the policy network defined by horizontal embeddedness. Like public sector agencies, these organizations will provide administrative resources and they will be constrained by the same cross-cutting oversight. The weakness of these social actors may still allow for delegation by minimizing the potential for social conflict, but the nature of horizontal embeddedness will be more state-directed as a result. Therefore, the causes of delegation and the identity of the relevant actors in horizontal embeddedness are partially defined by path dependent factors—the subnational history of state-society interactions.

Beyond the identity of the relevant actors, horizontal embeddedness varies according to the structure of inter-agency relations, and this is a function of whether these agencies are created under delegative or populist government. I summarize the dimensions of the variable as a four-fold typology differentiated by the degree of inter-agency frequency of contact and the degree to which agencies are organized hierarchically (symmetry) (Figure 2). The upper cells are the results of delegative governments that allow for a decentralized inter-agency structure. The lower cells represent the centralized inter-agency structure associated with populist governments without horizontal embeddedness.

The most developed form of horizontal embeddedness is located in the upper left-hand cell. This type is characterized by continuous contacts across agencies that are non-hierarchically related but are coordinated under a com-

mon development plan that specifies targeted sectors or regions and agency responsibilities. The plan establishes a framework for setting goals and timetables for joint action (high-level functions) and, in practice, requires the sharing of personnel and information as a routine matter. No single agency maintains supremacy over the others, although an inter-agency council on which all are represented might have priority-setting powers. This ideal type may be labeled a “plan-oriented” horizontal embeddedness.

The second form of horizontal embeddedness created by delegative government is the project-oriented type (upper right-hand cell). The agencies still coordinate high-level functions and oversee each other’s operations, but contact is less frequent than in the plan-oriented system.

Strategic planning is coordinated among the agencies but usually without an inter-agency council or a development plan supported by a ministry. Planning is done as project opportunities emerge. As in the plan-oriented variety, no agency is supreme or able to see a firm project through to completion without the involvement of the others. As the cases will demonstrate, project-oriented forms of horizontal embeddedness are more likely to exist when politicians have de-emphasized the creation of industrial development plans and have left these functions to the agencies under an extant set of priorities.

Populist governments do not produce horizontal embeddedness, but they do foster the development of two types of inter-agency relations that are evident in the cases. The lower left-hand cell represents the “hierarchical-functional” type in which inter-agency relations are highly centralized. A dominant planning agency will devolve operations to more specialized units, but each of these sub-agencies will have only low-level functional duties (e.g., distributing finance, building infrastructure, etc.) without the authority to participate in strategic planning. Strategic planning will most likely be defined by politicians with command over the dominant agency. Contacts are “continuous” but asymmetrical between the dominant agency and the sub-agencies. Hence few opportunities exist to generate feedback or produce checks on potential abuses of power at the top.

The lower right-hand cell of the table represents the “non-functional” type. Like the hierarchical-functional system, this type has the concentrated inter-agency structure favored by populist governments. But in addition to the problems of reduced checks on executive decisions, low levels of inter-agency contact generate high costs of hidden information. Bureaucratic dysfunction and clientelistic misappropriation of resources are maximized in this type.

This article compares the composite pattern of subnational industrial policy in Spain and Brazil. Both countries developed such patterns although they each had *national* economic and political experiences that might have produced a more uniform outcome. High levels of horizontal embeddedness became the basis for innovative industrial policy making in regions with delegative governments. Firms in these regions tend to report favorable and ongoing expectations regarding their cooperation with public agencies, but other indicators for “success” include the production and sustainability of external economies and the maintenance of development programs over time. Other regions without delegative governments and horizontal embeddedness failed to implement or

maintain industrial reforms in the face of changing market conditions. Both countries favor optimistic approaches to decentralization as they are each federal and have devolved significant economic authorities and resources to subnational government. The case selection also tests pessimistic approaches as the subnational politics of both countries contain significant degrees of clientelism. Yet composite patterns of policy making suggest that neither allocative efficiency nor clientelistic exchange are endemic in Spain and Brazil. The causes of these differences are endogenous to subnational politics.

II. Brazil

During the 1980s, Brazil enjoyed a transition to democracy that was punctuated by direct elections for governor in 1982, the first such contests since the coup of 1964. Driven by their interests to exploit the contradictions of a liberalizing military regime that maintained authoritarian control over the central state, the governors and the opposition municipal and federal representatives (also elected in 1982) moved to expand their local bases of support through patrimonial networks (Abrúcio 1998). The rise of the “politics of the governors” *before* citizens had the right to vote for a democratic executive in 1989 legitimized decentralization as a *democratic* process. This enhanced the influence of regional interests in the Constituent Assembly of 1987, which devolved significant fiscal authorities and resources to the governors (Souza 1997).⁹

This unprecedented decentralization, however, did not produce salutary allocative efficiencies throughout Brazil. The Brazilian states proved to be irresponsible in their levels of spending and borrowing, generating unsustainable debts. Between 1986 and 1995, state level expenditures increased 33 percent in real terms, and subnational debt composed most of the increase in domestic public debt (Dillinger and Webb 1998). Governors and other subnational “traditional elites” faced few incentives to sacrifice their control over these funds as federal bailouts and the lack of nationally imposed hard budget constraints allowed the governors to bolster their clientelistic political machines. Consequently, many scholars would conclude that the Brazilian states could only subvert national macroeconomic policy and undermine efforts to implement democratic accountability (e.g., Hagopian 1992).

In the next sections I demonstrate that the case of Minas Gerais challenges the pessimistic view by showing how the advent of delegative government and horizontal embeddedness can provide for continuing forms of cooperation between agencies and firms. Rio de Janeiro, which lacks these conditions, is more reflective of the pessimistic argument. Finally, a reconsideration of the well-studied case of Ceará suggests that my observations about Minas are more generalizable within Brazil.

Minas Gerais

The political elite of Minas Gerais has long epitomized the salience of clientelism in Brazil. At least one influential author has used the state to illustrate the persistence of the political oligarchy throughout the country (see

Hagopian 1996). The dominance of this elite was closely associated with Minas' economic development through industrial planning. The oligarchy built strategic alliances with national state-builders such as Getúlio Vargas during the 1930s and 40s and former governor of the state, Juscelino Kubitschek, in the 1950s, linking the *mineiro* elite's fate with the national development policies that were the centerpiece of these governments. When the military came to power in 1964, *mineiro* political leaders supported them in exchange for the placement of public firms in the state. By 1976, 57 percent of the largest 185 companies operating in Minas Gerais were public (Diniz 1981: 202).

The dominant position of "traditional elites" and the pivotal role played by advanced public industries such as mining and steel created a second political class linked to the public sector and technocratic *mineiro* development agencies, most notably the state utility company, Centrais Elétricas de Minas Gerais (CEMIG) (Gama de Andrade 1980; Tandler 1968). The military government accentuated the role of political technocrats within the economic bureaucracy but there was little conflict between the oligarchy and the political technocracy during the bureaucratic-authoritarian period (Hagopian 1996: 137). Consequently, the role of the political-technocrats in Minas' economic policy became more prominent as traditional leaders became concerned with diversifying the state's industrial development and reducing Minas' dependency on the more advanced industrialized states of the South and Southeast. By the 1960s it was also clear that national developmentalist policy was desirable but not sufficient to end Minas' dependency (Diniz 1986: 336).¹⁰

The state government's first efforts in industrial policy were implemented during the governorship of Magalhães Pinto (1961–1965), who set down plans for an array of developmental institutions and agencies modeled on CEMIG. Beginning with the creation of the Banco de Desenvolvimento de Minas Gerais (Bank of Development of Minas Gerais—BDMG) in 1962 as a credit agency to provide finance to small- and medium-sized firms, subsequent governments created other industrial policy agencies. Encouraged by a BDMG report in 1968 that laid out a blueprint for industrial planning, the governors empowered the Instituto de Desenvolvimento Industrial (Institute of Industrial Development—INDI) in 1967 to provide technical support to BDMG and CEMIG projects. In 1972 the state launched the Companhia de Distritos Industriais (Company of Industrial Districts—CDI) to assist in the planning of public infrastructure. Academic institutions such as the Fundação João Pinheiro (The João Pinheiro Foundation—FJP) and the Centro de Planejamento (Center of Planning—CEDEPLAR) of the economics department of the federal university of Minas Gerais supplied state planners with statistics and sectoral studies and recent graduates to work in the planning apparatus.

In contrast to the salience of the political technocracy, both *mineiro* business and labor organizations were weak. This gave the configuration of inter-agency ties a decidedly statist quality. *Mineiro* business, whose investments were deployed in agriculture and traditional industries or were dependent upon public investments in mining and steel, remained supine in the face of these new state initiatives (Hagopian 1996: 87). Lacking the strong immigrant experience that facilitated the emergence of an organized worker movement in São

Paulo, *mineiro* labor was also politically weak. The weakness of business and labor removed these actors as potential opponents. This condition enhanced the tradition of elite accommodation within the oligarchy and between it and the political technocracy. The political costs of delegation for Pinto and subsequent governors were thus low and horizontal embeddedness was confined to *state* agencies.

From their creation, the agencies were designed to work together on common projects and under the overarching direction of the state's development goals as set down in the 1968 BDMG diagnostic. This degree of plan-oriented horizontal embeddedness was reinforced through joint ownership of agencies such as INDI, which was governed by BDMG and CEMIG, and the routine circulation of technocrats among the agencies. Common academic ties through CEDEPLAR and FJP also facilitated communication and cooperation among the top political technocrats. Political and logistical concerns created additional incentives to form a horizontal network. The architects of the development agencies argued that the creation of a specialized and connected set of agencies would remedy Minas's economic problems and therefore justify the decentralization of additional federal resources and economic authorities to the state (Brito 1984).

Once in place, the agencies pursued the expansion of the capital goods and consumer durables sector in the state. Public investments in infrastructure, fiscal incentives, subsidized finance, and logistical support helped attract an array of multinational firms to Minas, most notably the Italian automaker, Fiat. By 1977 almost one-fourth of all FDI entering Brazil went to Minas, which enjoyed an industrial growth indicator far outpacing Brazil's "miracle" rates (Brant 1983: 322).

The 1980s saw a crisis in the *mineiro* system as the Latin American debt crisis caused a decline of public sector production, forcing hundreds of capital goods producers to divest. More serious was turnover in the governor's mansion. The first governor of the new democracy, Tancredo Neves, was more concerned with national politics as the candidate of the Party of the Brazilian Democratic Movement (PMDB), the largest opposition party in the presidential race of 1984. Breaks in the political oligarchy soon challenged the agencies. The 1986 gubernatorial elections empowered an outsider to Minas's political oligarchy: Newton Cardoso, a little known politician from Bahia. Faced with escalating opposition from traditional rivals, Cardoso pursued patrimonial economic policies to strengthen his political position. This led him to centralize his command over the development agencies.¹¹

Horizontal embeddedness, however, protected the agencies from becoming politicized. The continuation of frequent contact, common planning, and circulation of personnel kept lines of communication open, allowing political technocrats to mobilize business constituencies in their defense and creating opportunities for reforming the development mission under a subsequent delegative government. These common links raised the political costs of dismantling any one agency. For example, CEMIG's and BDMG's technocrats in INDI were defended by their mother agencies. Attacks on CEMIG were complicated by its role as both a power company and a partner in the development

network linked to INDI and its partner, the CDI. The agencies also cultivated political support in the business sector.¹²

The erosion of developmentalist planning caused the agencies to focus on more project-oriented strategies. A new BDMG-sponsored diagnostic of the *mineiro* economy in 1989 quickly became a vehicle for coordinating political technocrats under a new development mission. The election of Hélio Garcia, a member of the traditional elite, in 1991 created an opportunity for institutional change. Garcia empowered the political technocrats to reform the economic secretariats. In 1992, the political technocrats drafted new goals for *mineiro* industrial policy that were eventually published as the *Plano Mineiro de Desenvolvimento Integrado*—PMDI (the *Mineiro* Plan of Integrated Development) in 1995. Like the 1989 BDMG diagnostic, the new framework embraced the promotion of external economies as a means for diversifying the state's industry. It also recognized the fiscal limits of industrial policy and rejected the more costly developmentalist models used in the past. For example, the PMDI viewed auto parts as an area with high external economies and so it became a priority over previously protected sectors such as textiles. A new cross-agency "executive group," the Conselho de Industrialização (Council of Industrialization—COIND), coordinated the agencies on joint projects. The new structure facilitated joint planning while strengthening horizontal accountability.¹³

The creation and persistence of the *mineiro* agencies due to horizontal ties produced a series of synergistic linkages between the state and private firms. The most impressive of these cases involved the long history of ties between the agencies and the Italian multinational automaker, Fiat.¹⁴ Pushed by competitive forces in the global auto market, Fiat adopted a "just-in-time" (JIT) production system after 1988 to reduce dead time inventory costs and increase productivity. The company's ability to "globally source" JIT was limited by price fluctuations on imported units and content requirement laws mandating that end products contain 90 percent locally produced auto parts.¹⁵ The firm's Brazilian suppliers had little capital with which to import state-of-the-art machine tools, and they were limited by poor infrastructure and high finance costs. To create a JIT system, Fiat would need to have 100 total suppliers, instead of the 500 servicing the assembler in 1988, ready to produce parts mostly within Fiat's factory. The assembler would need help to get its suppliers to change, as most were members of monopolies or cartels that had a record of determining price and production on their own terms (Addis 1999: 151).

Mineiro agencies such as INDI and BDMG saw Fiat's strategy of convincing suppliers to relocate as consistent with their own strategy of improving the productivity of the auto parts sector. Fiat was well aware that the agencies shared mutual interests with the firm and both publicly announced cooperative "partnerships" (*parcerias*) involving a mix of state fiscal incentives and financial support.

A couple of examples of *parceria* illustrate the function of the agencies. In the case of Kadron, one of Fiat's chief exhaust system suppliers, Fiat's strategy and the activity of the agencies worked in tandem. In March 1993, Kadron initiated the first phase of a three step modernization program designed to

improve its evolving just-in-time links with Fiat. In April 1994, the firm completed construction of its new plant for the JIT construction of exhaust systems and catalytic converters. Total investment in the plant exceeded \$4 million and created 150 new jobs. Kadron received state tax incentives of over \$4 million for the initial stages of the firm's modernization and all of its investments since 1990 (a sum which was paid back in 1996). INDI provided technical and infrastructural support (e.g., telephone lines, energy, roads), which in the opinion of Luis F. S. Machado, Kadron's general manager, accelerated the firm's modernization at a rate that "exceeded expectations" (*INDI Informa* 1993: 3).

Another example of *parceria* involved INDI's program to supply ready-made sheet metal to Fiat. Before 1984, Fiat prepared steel plates internally at great cost. In that year, INDI officials organized a program to have Usiminas, then a national public steel firm, produce ready-made pieces of 300, 400, and 500 tons and make them available on timetables established by Fiat. By 1992 Usiminas was stamping body parts itself. Fiat officials note that the original partnership was made possible eight years before only because INDI officials were well-connected enough at Usiminas to implement the program. As a result, Fiat saved millions on inventory and transportation costs while Usiminas was guaranteed about \$100 million in sales every year with the Fiat deal.¹⁶

These and other efforts by the agencies were facilitated by close, communicative relations with Fiat and its suppliers, yet they continued throughout the 1990s as a new model of industrial policy only because the agencies themselves were horizontally integrated. Horizontal embeddedness, combined with the earlier advent of delegative government, preserved the *mineiro* industrial policy system and helped transform it from a developmentalist modality to a market-oriented one.

Additional Brazilian Cases

The experience of Minas's industrial policy might be considered an outlier within Brazil, but recent scholarship at the subnational level suggests that the politics of the delegative dilemma and horizontal embeddedness are salient features in determining "success" or "failure" across a range of policy areas. In this section I compare two additional subnational cases with the Minas experience, Rio de Janeiro and Ceará. The case of Rio demonstrates the importance of delegative government. Without it, multiple attempts to reverse the state's industrial decline were hindered by populist governors who misappropriated resources and left a non-functional form of industrial policy. The much-studied case of Ceará, on the other hand, confirms the importance of political delegation and horizontal embeddedness.

Rio de Janeiro. Unlike Minas, Rio de Janeiro's political class was never a coherent group. The state's urban politics from the late Old Republic period (the 1920s) to the "New Republic" democracy (1985–present) were dominated by rival "grand figures" (*figurões*)—populist leaders with personal followings (Conniff 1981). Even the state's opponents to authoritarianism in the 1970s and 80s remained divided within the PMDB. Factions linked to the urban political machine of Antônio de Pádua Chagas Freitas, leftists known as *autênticos*

(“authentic”) who challenged military rule and opposed Chagas Freitas’ own close ties to the generals, and independents or members of the political machine of ex-governor Ernâni do Amaral Peixoto (the so-called *amaralistas*), battled for control of state politics (Diniz 1982).

Having had his political rights restored in 1979, Leonel Brizola, a former governor of Rio Grande do Sul and federal deputy from Guanabara, returned from exile to Rio de Janeiro. Like Chagas Freitas, Brizola faced rival leaders within his party, the PTB, which reemerged after an electoral reform permitted a multi-party system in 1979. *Brizolismo* added yet another current to the vestiges of the old *chaguista*, *autêntico*, and *amaralista* cleavages that continued to reinforce incentives for political elites to cultivate patrimonial bases. Frequent party switching and the overall weakness of party labels facilitated populist-clientelistic coalitions. An indicator of this fragmentation is the fact that as many as 43 parties competed in the four major state races held between 1982 and 1994. Yet 21 of these disappeared after their first election (Schmitt 1997: 148).

Given deeply rooted traditions of populist government in state politics and an overarching high level of elite conflict, Rio’s development policy was manipulated for political purpose and left with a non-functional inter-agency structure. The latter was possible only through the concentration of political control over development agencies, which hindered any attempt to forge the horizontal ties that were crucial to industrial policy making in Minas Gerais. The most important example was the experience of the Companhia de Desenvolvimento Industrial of Rio de Janeiro (Company of Industrial Development—CODIN).

Like the *mineiro* agencies, CODIN was established in the 1970s to bolster Rio’s industrial development, which had declined steadily since the 1920s. However, political appointees left an anemic record that inspired little credibility in the eyes of business. Centralization of political control hindered the flow of information within CODIN and between the agency and its industrial districts and client firms. Current CODIN employees who worked for the agency during the 1980s report that politically appointed administrators in the Secretariats of Planning and Industry and Commerce seldom communicated with CODIN’s staff during the four gubernatorial administrations of Chagas, Brizola (two terms), or Wellington Moreira Franco.¹⁷ Centralized control also impeded communication with state and municipal utility companies. As a result, the horizontal ties that connected COIND, INDI, BDMG, CDI, and CEMIG in Minas Gerais failed to emerge in Rio.

Rio’s business class, which unlike workers, was well-organized by the Federation of Industries of the State of Rio de Janeiro (FIRJAN). But FIRJAN was poorly linked to the CODIN system. The business association participated in the operations of the Development Agency of Rio (AD-Rio), a public-private mixed society, which duplicated many of CODIN’s functions. Yet the *brizolistas* and their political enemies routinely used jobs in AD-Rio’s administration as patronage during the late 1980s and early 1990s. During this time technocrats exited the agency, leaving it as a marketing arm for FIRJAN. Thus the business class and the technocracy remained separated, working through two organizations that increasingly competed against each other.¹⁸

In the views of CODIN personnel and business leaders, these factors contributed to a history of project failures. An illustrative set of cases includes the uneven governance of CODIN's industrial districts. During its first few years of operation, CODIN sold none of its properties. During the late 1970s and early 1980s, the few firms that did purchase in the industrial districts at subsidized prices failed to develop their operations. In practice, the state government led by the *chaguistas* and later by Brizola employed CODIN to sell off large parcels of land at artificially low rates to political supporters but provided no follow-up.¹⁹ Motivated more by a desire to use industrial policy to garner support in areas heavily disputed by the *brizolistas*, Moreira Franco attempted to use CODIN's industrial districts as part of a populist campaign to capture the votes of informal sector workers.²⁰ CODIN's main industrial districts in fashion design, the production of optical equipment, footwear, and computers failed soon after they were launched. No new industrial activity was initiated in these areas and, in hindsight, private business in Rio tended to discount the state's industrial policy as "politically motivated."²¹

Ceará. Judith Tendler's study of "good government" in Ceará during the early to mid-1990's represents the most thorough study to date of subnational economic policy in Brazil. While it does not focus on political causes but on the developmental effects of innovative policy making, the Ceará story suggests that political delegation and horizontal embeddedness played important roles in making this a case of policy success.

Tendler notes how reformist governors, specifically Tasso Jereissati (1987–91 and 1995–present) and Ciro Gomes (1991–94), blocked parochial encroachments by political opponents by strengthening meritocracy in Ceará's civil service. She is silent on the motivations of these seemingly "good governors" and their political capacity, but a closer look reveals that the political class they led faced divided partisan opponents and was broadly supported by the electorate and important segments of business. Both "Tasso" and "Ciro" were among a political class of successful entrepreneurs who had since the 1970s become active in discussing the state's economic development as leaders of the most powerful business association in Ceará, the Cearense Industrial Center (CIC). Their rise to power after the 1986 elections followed the decomposition of the formerly hegemonic, pro-military party and in-fighting among the three military "coronels" (César Cals, Aduino Bezerra, and Virgílio Távara) who had previously controlled state government through an extensive clientelistic network. The reformist coalition of the PMDB and leftist parties almost gained a majority in the state assembly, but succeeded in unseating mayors loyal to the coronels in both Fortaleza, the capital, and the interior. Faced with remaining political opposition in the state legislature including growing dissension within the PMDB, Jereissati and the reformers joined the Brazilian Social Democratic Party (PSDB) in 1989 and retained the governorship in 1990 and 1994 with first-turn wins and with increasing popular majorities during the 1990s. Declining electoral volatility in the state assembly, an increasing incidence of straight-ticket voting for federal and state office, the absence of ideological cleavages in the electorate or the political class, and a growing sense among voters of "pro-government" and "opposition" lines gave

Ceará an unusually coherent party system during the early to mid-1990s (Moraes Filho 1997). These trends empowered Ciro Gomes' reformist administration, which enjoyed a majority in the state legislature beginning in 1992. With clear, supportive electoral signals, the backing of the state's business organizations and public opinion, and the absence of labor opposition or relatively severe social conflict, the reformist governors could expect to retain power. As with the Pinto and subsequent gubernatorial administrations in Minas during the 1960s and 1970s and then later the 1990s, these conditions created the political security the *cearense* reformers needed to restructure the public apparatus as an "inducer of new investments" (Gondim 1997: 369-370).

Tendler's analysis of four policy areas—preventive health, emergency employment, agricultural extension, and public procurement for small firms—emphasizes merit-based recruitment into the civil service, self-motivated public servants, official publicity, and close cross-monitoring by suppliers and recipients of public goods as key independent variables. But her cases are also explicit about the development of horizontal ties linking public agencies, private clients, producer associations, and neighborhoods in enhancing the effects of publicity, monitoring, and program follow-through. Her fourth policy area—procurement policies for small firms—most closely approximates the policies analyzed in my own study. Tendler notes that two agencies—the state Department of Industry and Commerce (SIC) and a semipublic technical-assistance agency, the Brazilian Small Enterprise Assistance Service (SEBRAE)—spread-headed the creation of an industrial district of small furniture producers in the remote town of São João do Aruaru (SJA) during the 1990s. The story highlights the close connections linking SIC and SEBRAE, particularly the fact that more than 70 percent of the latter's funding came from SIC and that the two agencies worked in tandem to secure public contracts and supply technical assistance to the small producers in SJA. These horizontal ties extended to the agencies' role in fostering the formation of small firm associations in SJA to bid for state contracts. The agency-association networks not only proved successful in garnering state contracts and upgrading production to fulfill them but also provided political protection from the opposition of displaced competitors and politicians "representing" them. As Tendler notes:

The purchasing agencies first contracted with SIC for the goods or services. SIC then made a second contract with SEBRAE to provide technical assistance to the small firms, paying SEBRAE a 5 percent commission to purchase the goods or services from an association of small firms, artisans, or building tradesmen located near each other. Key to the good results of these arrangements, SEBRAE would not contract individually with small firms. It instead sought out existing small-firm associations or encouraged and helped groups of potential suppliers located in one place to organize an association...they [SIC and SEBRAE] also encouraged the associations to become a counter-lobby to the hitherto more powerful displaced firms, as well as to lobby in favor of tax exemptions for small firms. For every round of opposition from the previous suppliers, SIC and SEBRAE mobilized a wave of presidents of local small-firm associations to pressure the governor to preserve the program or to extend it to their towns (Tendler 1997: 116, 130).

Official publicity enhanced the constituency-building effects of horizontal ties. Horizontal ties also limited the costs of hidden information by promoting cross-monitoring, which included feedback from neighborhood associations and producer groups. Both the organizational attributes Tendler describes among the agencies in Ceará and the effects of these ties on small firm productivity and the political maintenance of the policy network highlight the central qualities of horizontal embeddedness: information flows were symmetrical and frequent, cross-monitoring prevented bureaucratic dysfunction, and agency interconnections reinforced sources of political support. Unlike Minas's inter-agency system, the configuration of horizontal embeddedness in Ceará included business and semi-public actors as well as government agencies.

The "success" of industrial policy, here defined as the continuation of agency-firm coordination of policy, hinged in the Brazilian cases on the advent of delegative government and the subsequent development of horizontal embeddedness. Industrial policies in Minas Gerais and Ceará benefited from these elements while Rio's projects stagnated due to the absence of these factors. The next sections provide further evidence for the argument in a completely different national setting: Spain.

III. Spain

Following Francisco Franco's death in 1975, Spain underwent a transition to democracy that was punctuated by nationalist calls for the construction of a decentralized state. The transition itself encouraged Catalonia and the Basque Country to reclaim fiscal, cultural, and political authorities instituted in "statutes of autonomy" during the Second Republic and later abrogated by the dictator in the 1930s (Carr and Fusi 1981). The Basque separatist group, Basque Homeland and Freedom (Euskadi ta Askatasuna—ETA), pressed the nationalist cause violently while nationalist parties pursued negotiations with the two main parties of the transition, Adolfo Suárez' ruling centrist Union of the Democratic Center (UCD) and Felipe González' Socialist Party (Partido Socialista Obrero Español—PSOE). With the "regional question" hanging like a Sword of Damocles over the democratic transition, national political party elites prepared constitutional rules in 1977-78 that envisioned a decentralized state called the *Estado de las Autonomías* (state of the autonomies).

The 1978 constitution and subsequent distributional claims by nationalist and non-nationalist regions produced an asymmetrical and open-ended federalism. The new constitution created two routes to regional "autonomy"—the "fast track" and the "slow track." "Fast track" regions, which included the nationalist regions of the Basque Country, Catalonia, and Galicia plus Andalusia due to its economic underdevelopment, achieved autonomy almost immediately and received greater degrees of revenue shares, intergovernmental transfers, and corresponding spending duties.²² All other regions governed by a "slow track" achieved autonomy by 1983 but their secondary status created incentives to continue pressing for extensions of their authorities to tax and spend. Periodic negotiation of each statute of autonomy gave the regions a venue for their lobbying efforts. Economic problems, particularly high annual

rates of unemployment (over 20 percent), provided incentives to allocate increasing levels of subnational spending into the restructuring of heavy industries, labor retraining, and the promotion of small- and medium-sized firms. In the first 12 years of the *Estado de las Autonomías* the central government went from administering 90 percent of public spending to 65 percent, while the regions increased their share to 25 percent (Curbelo 1994: 7). In terms of policy making, the regions went from administering 30 percent of all laws and 15 percent of all decrees to promulgating 85 percent of all laws and over two-thirds of all decrees by 1991 (Agranoff 1996: 388–389).

While the degree of decentralization in Spain was significant, no uniform pattern of allocative efficiency emerged throughout the country. The open-ended constitutional framework and differing subnational capacities produced a composite pattern in which some regions maintained industrial policies that were coordinated between agencies and firms while others encouraged populism and highly centralized reforms.

Asturias

As a region long dependent on declining public steel and mining industries, Asturias experienced economic change during the 1980s and 90s that produced points of common political interest across the Asturian political elite. In order to answer the claims of the region's powerful unions, which remained fragmented sectorally and organizationally, the regional government, led during most of the 1980s by the Socialist party, forged broad political support for making national and European Union resources available to Asturias. But the management of these resources was driven by regional government interests in diversifying the local economy. Enjoying a stable majority in the regional parliament (*Junta*), the Socialists constructed an apparatus of technocratic development agencies. Once the Asturian development agencies were constructed, they built horizontal ties that preserved them through subsequent Socialist governments that became more vulnerable to rival parties. The governance of industrial policy in the Asturian case therefore follows a similar pattern to that of Minas Gerais, although the focus of industrial policy, which became the promotion of small- and medium-sized firms and not so much the development of externalities in a multinational sector, was different. The configuration of horizontal embeddedness in Asturias, given the region's legacy of strong unions, involved workers' organizations more extensively in the administration of the agencies than was possible in Minas.

In May 1983, the Asturian PSOE won an absolute majority in the *Junta*. The new *Junta* gave the PSOE 26 of 45 seats; the center-right *Alianza Popular* (forerunner of the *Partido Popular*—PP) and its coalition partners held 14 seats, with the remaining five falling under the control of the Communists. Important municipal governments also went to the Socialists, including the key industrial areas of Oviedo, Langreo, Avilés, Gijón, Siero, and Mieres.

Although it was not necessary to forge strong cross-party alliances, Asturian politicians still agreed on the basic principles of Asturian autonomy and the need to react to the national "reconversion" (downsizing) of public industries

that became a focus of González' economic policy. All of the regional parties backed the Socialist (the Unión General de Trabajadores or General Union of Workers—UGT) and Communist unions (Comisiones Obreras or Worker Commissions—CCOO) in their opposition to labor downsizing at the major public steel firm (ENSIDESA) in the critical reconversion years of 1984 and 1985. Politicians from these parties participated in union protest activities and the Asturian government mediated negotiations among central state actors and sectoral business and labor groups, including those designed to delay downsizing at the public mining firm, HUNOSA.

Regional business associations—the Federation of Asturian Business (FADE) and the Chamber of Commerce—had little impact on the composition of the regional governments' or the unions' strategies. Neither business association represented the most important industries in Asturias, the public firms and the multinationals. Since FADE and the chamber represented mostly small- and medium-sized firms, they could play only a minor role in the composition of regional policy. At the same time they had nothing to gain from opposing initiatives proposed by the regional government. As the priority of regional policy became diversifying the local economy and favoring programs for small firms, the business associations became more integrated into the administration of industrial policy (Gutiérrez 1994: 956).

More than any other factor, the stable position of Socialist incumbents, and primarily Pedro de Silva who served as the regional PSOE president from 1983 until 1990, allowed the regional government to construct an industrial policy that went beyond the unions' focus on the "reconversion" of the steel and mining firms. Based on prior experiences with development policy, key members of the Asturian PSOE and the political technocracy advocated an industrial policy that would *reduce* the region's dependence upon the public sector. While the PSOE held its absolute majority in the *Junta*, this development mission and the agencies created to implement it, thrived and produced a horizontal embeddedness governed by regional development plans. After the PSOE lost its absolute majority, and even after it lost control of the regional government to the center-right Partido Popular (PP) in 1995, horizontal embeddedness allowed the agencies to stay the course on industrial restructuring, and even innovate under a more project-based pattern of policy making.

As Asturias's economic problems worsened and other regions competed for shares of national and EU resources, the regional government justified the further devolution of authority over economic policy by pointing to an array of development agencies run by the government of the Principado. Among the most important were the Instituto de Fomento Regional (Institute of Regional Promotion—IFR) created in 1983, the Servicio de Asesoramiento y Promoción Empresarial (Service of Assistance and Entrepreneurial Promotion—SAYPE) initiated in 1988 and the Sociedad Regional de Promoción (Regional Society of Promotion—SRP) created in 1984.

The thinking of these agencies was conditioned by key political technocrats in the Chancelleries of Economy and Industry and the Asturian statistical and research agency, Sociedad Asturiana de Estudios Económicos e Industriales

(Asturian Society of Economic and Industrial Studies—SADEI), which had been developing the groundwork for an Asturian industrial policy for several years prior to the transition to democracy. Rosa Corujedo, one of these key political technocrats, had earlier championed the creation of regional mechanisms to develop the Asturian economy in the 1970s. As a chief researcher for SADEI during the late 1960s and 1970s, Corujedo had participated in a series of studies of the Asturian economy that argued for an administrative decentralization of economic policy among other alternative development strategies. Reflecting on the experience, Corujedo would argue that SADEI and its staff had been motivated by the foreseeable decline of mining and steel and the failure of national planning to deal with these problems.²³ Consequently, these studies pioneered an advocacy for devolving planning functions to local administrations years before the “state of the autonomies” would become a reality.

Like the *mineiro* BDMG diagnostic of 1989 and the PMDI, the Asturian development plans and the earlier SADEI studies upon which they were based argued for a “market-oriented” industrial policy—one that would prepare the region’s firms for more competitive domestic and foreign markets. Given both the poor performance of the national public sector and the region’s reliance on mining and steel, the plans emphasized the need to “diversify” the region’s industrial and service sectors through externalities that would increase employment and break Asturias’ traditional dependencies. They emphasized in particular the need to make small- and medium-sized firms in particular more productive by enhancing their access to finance, information, and skilled labor.

IFR, SAYPE, and SRP increasingly took on more tasks and coordinated their efforts to maximize their resources. The agencies evaluated firm proposals for national and regional subsidies and venture capital; they supplied technical and investment information, and they funneled national infrastructural programs to areas of the region considered critical to the Asturian economy. The Asturian development policy apparatus matured during the course of the 1980s, both in terms of size, range of activities, and institutional complexity. The IFR and SAYPE both implemented an increasing array of financing programs for small- and medium-sized firms. In addition, IFR developed infrastructural, technological, and retraining programs. SRP, a venture capital society that fell under IFR’s administration, attracted some large noteworthy investments such as Thyssen (elevators) and DuPont (chemicals) to the region.

The placement of the agencies in Asturias’s only “technology park” in Llanera, just off the highway linking Gijón, Avilés, and Oviedo, facilitated their coordination. The park would become the headquarters for all three agencies and other organizational spin-offs. Numerous interviews with staff emphasize that the physical proximity of the agencies greatly enhanced the efficiency of administering joint projects. Both SAYPE and SRP were placed inside the IFR’s main building, and that center was surrounded by more specialized working groups located in separate buildings. Under these circumstances the agencies increasingly worked as one, emphasizing joint planning and encouraging daily meetings among agency directors.²⁴

After the agencies were able to develop a high level of horizontal embeddedness, their political fortunes changed. By 1990, the unions, diminishing and limited campaign against national reconversion policy caused splits within the regional PSOE. Competition among politicians representing steel and mining areas for control over limited resources meant to soften the social effects of "reconversion" made Silva's embrace of "reindustrialization" efforts politically more complicated and facilitated his retirement from regional politics in 1991.²⁵ Silva's successors played to either mining or steel labor interests to control the party. The Socialists' fortunes worsened when the leftist Izquierda Unida (IU) abandoned the PSOE in the Junta, opening the way to the rise of the PP's Sérgio Marqués to the regional presidency in May 1995.

With regional politics so divided and distracted away from the "reindustrialization" mission of the agencies during the post-Silva governments, the industrial policy system between 1991 and 1993 tended to focus on project support but no new ideas for promoting industrial productivity. The agencies continued to function and were soon able to bootstrap additional resources for new industrial policies. The continuity and innovation of the Asturian development agencies was due to the fact that the political technocracy first created under the Silva administration continued to evolve under more populist, successor governments. Chief technocrats, such as Nieves Carasco, one of Silva's main stewards of industrial policy, circulated from executive positions in the Chancellery of Industry to agency directorates. This preserved key sources of experience from the previous period of activity.²⁶ This experienced core of political technocrats utilized existing close contacts among IFR, SAYPE, the chancelleries and other agencies to refocus industrial policy on the promotion of small- and medium-sized firms. In part, the new focus emerged from the experience these officials had with the problems of promoting large public and foreign investments in a secondary region with poor infrastructure. They agreed based on experience and the fact that national outlays for regional industrial policy were finite that the promotion of small- and medium-sized firms was the most feasible function for the development agencies.²⁷

In 1994, the agencies, and the IFR and SAYPE in particular, resuscitated their resources and functions with an ambitious *Plan de Apoyo a las PYMES 1994-96* (Support Plan for Small- and Medium-Sized Firms 1994-96). The improvement in the agencies' activities was possible only because new sources of political support appeared. By this time, the unions and the Asturian technocracy first assembled during the Silva government, were agreed on the priorities of regional industrial policy. Yet the unions were slow to come to this point. They viewed the work of the agencies through the lens of the industrial restructuring. The unions argued that "reindustrialization" efforts were too long-term and insufficient to matter. But as union efforts to slow or stop industrial restructuring proved ineffective, labor became more open to the regional government's strategy of promoting small- and medium-sized firms as a mechanism for preserving and increasing employment.²⁸ Union representatives were invited to sit on the Board of Directors of the IFR and attended the board meetings of other agencies. FADE took a similar position. The changing configuration of horizontal ties to involve the unions and business in the

administration of key agencies provided political protection from any attempts by the post-Silva governments to disassemble or manipulate the economic technocracy.

The measures of the IFR's and SAYPE's effectiveness are both general and specific. General figures for the performance of the IFR's financial programs show that between 1988 and 1997, 172 firm projects were rejected, 339 were approved and half of these had been completed by 1998, an indicator typical of projects for small firms. The average firm project received a subsidy equal to 24 percent of the firm's initial investment. Approved projects generated \$1.5 billion in new investments, created 5,121 new jobs and maintained 11,508 old jobs (IFR 1998: 73). In 1991, SAYPE approved 364 small- and medium-sized firm projects, which generated \$75 million in new investments and 1,332 jobs. By 1998, SAYPE was organizing over 1,000 such projects per year and generating an average of \$210 million in investment and 1,927 jobs per annum (SAYPE, various years).

These global figures for IFR and SAYPE performance do not reveal the true effectiveness of these policies. In order to analyze the performance of the agencies, particularly their monitoring and follow-through functions, I conducted a small-N study of small- and medium-sized firms in various sectors. The firms contacted in this study were chosen randomly from numerous directories of Asturian enterprises that had initiated projects with the development agencies. With only the most general information about the nature of the selected projects but without any prior knowledge about the outcome of these projects, I arranged for interviews with the managers of these firms to acquire details about their contacts with the Asturian agencies.

Based on interview data, I found that frequency of contact and a combination of financial and logistical aid contributed to improvements in productivity. Eight of the eleven firms in the sample reported that agency-directed projects were crucial to improvements in the quality of production and/or employment. The lack of finance for small- and medium-sized firms was most frequently cited as the problem the agencies helped these firms overcome. All of the selected firms reported that they considered agency personnel who had contact with them to be highly professional and knowledgeable about the operations and demands of their industry. Nine of the eleven selected firms reported that they viewed the activities of the agencies, and particularly the IFR, as positive for the Asturian economy and they noted that they would employ the agencies in the future. That number included three firms that previously reported few substantive effects from past agency activities on production or employment. The two remaining firms had no answer to the question. These numbers are demonstrative of more than an overall satisfaction with the performance of the agencies; they are indicative of a more diffuse confidence in agency mechanisms and their availability over time.

As in Minas Gerais, delegative government in the Asturian case laid the foundation for the development of a decentralized and horizontally coordinated inter-agency industrial policy structure. Horizontal embeddedness preserved and fostered innovation in the work of the industrial policy network.

Additional Spanish Cases

As with the Brazilian cases, I find that the experience of Asturias is no outlier within Spain. The advent of delegative government and the development of horizontal embeddedness are crucial to the creation and continuation of cooperation between public agencies and firms. I pursue this point here with a brief examination of the Andalusian and Valencian cases.

Andalusia. Andalusia's experience with industrial policy contrasts with the Asturian case. As one of the least industrialized regions of Spain, Andalusia had a political leadership that, during and after the transition to democracy, argued that it had the possibility of redressing its economic backwardness. Their reasoning, however, was shaped by a contentious political context in which rival socialist, center-right, and leftist parties competed for control over the regional government. These conditions created incentives for the Socialists to use populism more extensively in Andalusia than was needed early on in Asturias. In 1982, the PSOE succeeded in using populism to gain an absolute majority in the regional parliament. More than a populist campaign, the PSOE used state resources to cultivate a constituency among workers and business; tactics that included clientelistic exchange. The Socialists continually relied on these tactics as they faced threats from opposition parties, labor unrest sparked by rising unemployment, and the antagonism of Andalusia's most powerful business association. In contrast to Asturias, labor unions were not integrated into a horizontally embedded industrial policy system. The unions were targeted as "outside" constituencies of politicians, not as contributors to the administration of policy. The major business association not only remained outside the system but also maintained antagonistic relations with industrial policy agencies. Consequently, PSOE leaders centralized their control over the region's development agencies and manipulated their resources and staff to buttress the party's political base. The result was a hierarchical-functional horizontal embeddedness in which finance and other goods were distributed by industrial policy agencies that had dwindling command over the process or goals of strategic planning.

The pattern of populist government began with the first regional elections of the democratic transition in 1977. The PSOE faced an independent socialist party, the Partido Socialista de Andalucía (Andalusian Socialist Party—PSA), which campaigned successfully on a nationalist message that Andalusians were "economically oppressed" by Spain's richer regions. The PSOE won a majority by the barest of margins in 1977 and again in 1979 as the PSA's message played to the party's base. The PSOE, led by Rafael Escudero, responded by co-opting its rival's campaign.

Populism allowed for the creation of an industrial policy apparatus, but it would come to be highly centralized. The region's chief development agency, the Instituto de Promoción Industrial de Andalucía (Andalusian Institute of Industrial Promotion—IPIA), was created in 1983 with the expressed intent to redress "economic oppression." Under the direction of Julio Rodríguez, a technocratic former economist for the Bank of Spain and Andalusia's first autonomous Chancellor of the Economy, IPIA and its associated holding company,

the Sociedad para la Promoción y Reconversión Económica de Andalucía (Andalusian Economic Promotion and Reconversion Society—SOPREA), recruited professional economists, administrators, and engineers and cultivated ties with consulting firms and banks as if it were a private agency. Yet the agency's initiatives were hampered by its arms-length ties with Escudero and the latter's penchant for populism. Rodríguez and IPIA's first Director General, Ricardo Sánchez de la Morena, struggled to justify the agency's role under the PSOE's "economic oppression" campaign.

IPIA's dependency on the PSOE's political support was exacerbated by the fact that the agency was unable to cultivate horizontal associations with other agencies or economic actors in the region. SOPREA remained a dependency of IPIA, just as vulnerable to political intervention as the mother agency itself. Both became targets of criticism by the powerful Confederación de Empresarios de Andalucía (Confederation of Andalusian Business—CEA), Andalusia's chief entrepreneurial association. CEA sought to be the region's chief representative of business and it saw IPIA as a competitor in this regard. Escudero, for his part, only increased the CEA leadership's sense of encirclement by refusing to negotiate with the business association as the exclusive representative of Andalusian firms. Not surprisingly, CEA was no ally of the regional PSOE, which it campaigned intensively against during the crucial election of 1982.

The PSOE also faced intense opposition to its economic policies in the regional parliament. Among the most noteworthy critics of Socialist policy was Julio Anguita, the head of the Izquierda Unida Convocatoria (and the future head of the Izquierda Unida national party). The Alianza Popular (AP) (the predecessor to the center-right Partido Popular), also did not hesitate to attack the regional PSOE's large industrial policy budgets by citing dozens of cases of wasted public resources in failing firms.²⁹ Andalusian nationalist parties and the Seville municipal government under nationalist control routinely attacked the regional Socialist leadership and its industrial policy. In practice, these criticisms were intended primarily to cut into the PSOE's absolute majority in the regional parliament. Over time, such opposition had an eroding effect on the Socialist's grip on power. Opposition parties, particularly the PP and IU, made sizable electoral gains during the late 1980s and early 1990s, eventually breaking the PSOE's absolute majority in 1994.

Yet perhaps the most serious threat to the PSOE's position came from the unions. Unlike Asturias, where the regional government was able to avoid open conflicts with labor and business, the PSOE-led regional government in Andalusia faced continuing labor criticism. Comisiones Obreras openly rejected negotiations proposed by Escudero's successor, José Rodríguez de la Borbolla. The Andalusian PSOE's decision to follow the lead of the national party and back a "moratorium" on direct negotiations with the UGT pushed that confederation closer to CCOO's position in the region during 1989 and afterwards.³⁰ The regional PSOE's leadership, however, preferred not to discount union support. The Socialists sought to keep workers in their electoral base by appealing to the unions' view that public investments in industry were necessary to begin a "genuine process of industrialization." This made exploit-

ing the populist message of “economic oppression” to shore up union support a centerpiece of Andalusian politics.

Faced with significant levels of elite conflict with the CEA, nationalists who retained control of the municipal government of Seville, and increasing labor union strife, Rodríguez de la Borbolla and his successor, Manuel Chaves, relied increasingly on the use of ambitious industrialization projects, particularly those involving large investments by foreign firms, to protect the party’s political base of workers.

First, the development apparatus was centralized further after IPIA and SOPREA were fused into the Instituto de Fomento de Andalucía (Andalusian Institute of Promotion—IFA). As a result, the IFA became a de facto holding company for the regional government’s expanding list of public firms and joint ventures, making it particularly attractive to regional politicians as a source of patronage appointments and resources to business and labor supporters. By 1993, IFA owned completely or in part 61 firms and was investing over \$100 million per year in its going concerns. These IFA investments represented a concentration of public resources in a small number of large firms. About 99 percent of Andalusian firms, which are small- and medium-sized operations, were left out of the IFA’s demiurge activities. This indicated a wholesale lack of planning and a focus on short-term political concerns, in contrast to the way industrial policy fostered long-term externalities and local diversification in Minas and Asturias.

The extraordinary intervention in the market contemplated by Andalusian leaders underscored the Socialists’ model for maintaining control of the regional government. Rodríguez de la Borbolla attempted to institutionalize Escudero’s older populist politics into a pact-making process called *vertebración social* (meaning: to provide a social backbone to policy) that was designed to attract the support of the region’s major political and economic interests. For the regional technocracy *vertebración social* meant nothing less than more direct political control over the management of industrial policy. The IFA would continue to be operated by political technocrats, but these figures would cease to have the power to shape regional industrial policy as had Rodríguez and Morena, who abandoned the agency shortly afterwards. Political interests injected themselves into Andalusian industrial policy to an unprecedented degree, leading to numerous cases of corruption and nepotism in the 1987–95 period.³¹ The weakening of the Andalusian technocracy’s control over the IFA and the agency’s lack of horizontal ties allowed politicians on the IFA’s administrative council to use agency resources to advance their own political interest, particularly concerning failing firms. One IFA technocrat estimated that at least one in every four projects is created entirely for a political purpose by politicians on the council. While only 25 percent, these tend to be the most costly projects.³²

Consequently, the economic effects of IFA activities are mixed. By 1989, three of the IFA’s five major public firms were running heavy deficits. Between May 1993 and August 1994, the Andalusian government invested over \$269 million of the regional budget to save 13 nonviable firms.³³ This amount surpassed the total for all of the IFA’s other industrial promotion programs in

agriculture, industry, and services in 1993 and represented 83 percent of total industrial investment in Andalusia for the same year.³⁴ Although economically inefficient, such distribution was politically profitable for the Socialists. Chaves and the PSOE, after losing their absolute majority in June 1994 and despite sweeping victories by the PP in most of Spain's other regions, survived a challenge from the PP in 1995 and remained in power.

Valencia. As in Minas, Asturias, and Ceará, "success" in Valencia's industrial policy has depended upon the advent of delegative government and the development of horizontal embeddedness. A reformist leadership led by Joan Lerma of the Valencian PSOE (PSPV-PSOE) pursued a regional industrial policy during the years they held power from 1983-1995. Like Silva and the Asturian PSOE, Lerma and the PSPV-PSOE were motivated by the autonomy process and early experiences with the industrial "reconversion" before they assumed office. After the public steel works at Sagunto were targeted for a complete phaseout in 1981, the PSPV-PSOE and the Valencian UCD negotiated the broad outlines of a regional economic policy as a way of defending Valencian autonomy. Cross-party support for the creation of a regional development apparatus was institutionalized in the regional statute of autonomy in 1982. The agreements stressed the need to develop new ways of promoting innovation in small- and medium-sized firm "clusters" located throughout Valencia. Once in power with an overwhelming majority in 1983, the PSPV-PSOE initiated its plans for the creation of regional technology institutes as part of its larger campaign to take full advantage of the economic development clauses built into the statute of autonomy. Lerma and his chancellor of industry, Segundo Bru, took the lead on these projects as an extension of nationally subsidized efforts to relocate downsized Sagunto workers. These policies were politically significant as they would consolidate the first major "reconversion" reforms in Spain and create a strong justification for decentralizing development policy to the Valencian government.

As in Asturias, the precedent of the reconversion created common interests between regional government, business, and labor, but government played the coordinating role in assembling an alternative to reconversion policy. The Sagunto experience fostered close relations between the PSPV-PSOE and the region's business associations and labor unions, and Lerma used these to create a series of accords with Valencian business, UGT and CCOO on public employment, retraining, and reindustrialization policies. The major business associations participated in the organization of the region's technology institutes, thereby creating a set of ongoing working relationships in diverse sectors with state agencies. More fundamentally and in comparison with the successful Brazilian cases of Minas and Ceará, the PSPV-PSOE enjoyed low levels of social conflict. This granted Lerma the political security to map out a reindustrialization strategy for the long-term.

The Valencian industrial policy network emerged around the activities of IMPIVA (the Institute for Small and Medium-sized Firms), which was created in 1984.³⁵ IMPIVA coordinates its actions with regional technology institutes and business and innovation centers located near local clusters. Each cluster is represented by a not-for-profit private business association that works closely

with the agencies. Representatives from the regional government (through IMPIVA), the Ministry of Industry, local business associations, and the unions sit on the governing bodies of the technology institutes. The result is a horizontally integrated industrial policy network that works to foster and reinforce cooperation among small- and medium-sized producers in ceramics, footwear, textiles, plastics, and other sectors through the provision of public goods in infrastructure and technical support.

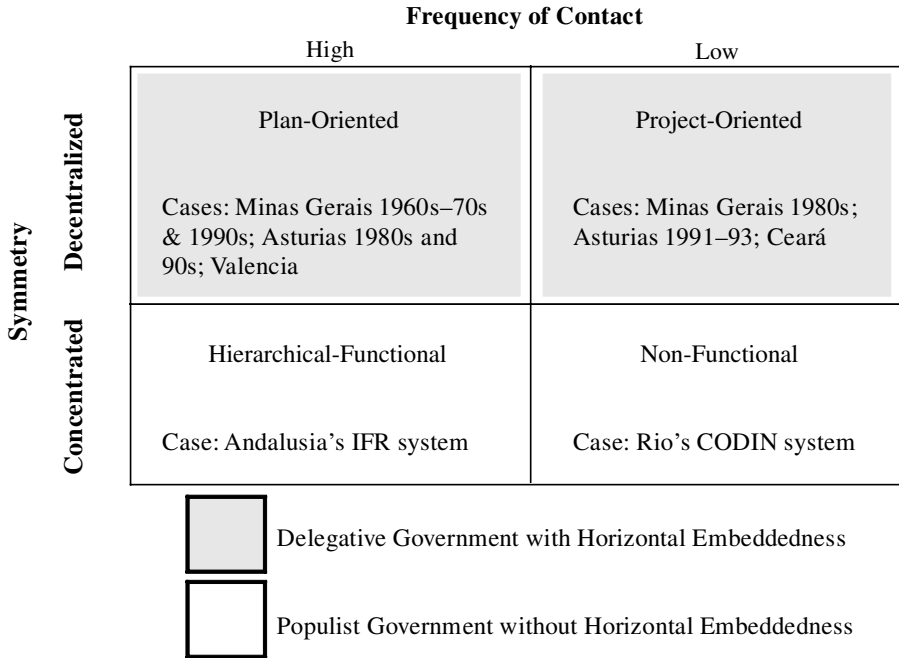
The organization and function of the Valencian technology institutes has been well studied by Spanish and internationally well-known scholars of business such as Michael Porter (1990). Even without venturing into the details, a review of this scholarship reveals that the salient characteristics associated with the success of IMPIVA and local institutes in promoting the coordination of small firm clusters are symmetric and frequent transfers of information and finance linking public agencies, universities, the institutes, business associations, and labor unions (Rico 1992: 123–135). These characteristics have fostered appreciable levels of policy feedback and facilitated policy experimentation (Más 1995; Espina Montero 1994: 149–172). Horizontal ties have also enhanced accountability in the use of public resources. The result has been high levels of business confidence in the performance of the IMPIVA system, an outcome that has continued beyond the end of the PSPV-PSOE mandate in 1995.

IV. Conclusions

National models are inappropriate to the study of composite patterns of industrial policy making in decentralized states. While optimistic accounts of decentralization have provided important case studies of “success stories” of subnational policy making, they have been unable to explain many other cases of failure due to political obstacles highlighted by pessimists. The pessimists have tended to make endemic arguments that obscure the political contingencies of elite conflict and bureaucratic structure that accompany successful cases of policy reform and implementation. Moreover, they have ignored the ways in which a variety of configurations of inter-agency and state-society cooperation foster effective forms of state intervention in subnational economies.

In Minas Gerais, Asturias, Ceará, and Valencia, the advent of delegative government and horizontal embeddedness provided sufficient conditions for the *creation* and *maintenance* of systems of public-private cooperation in industrial policy making. While the goals, mechanisms, and economic effects of these policies ranged from the creation of externalities (Minas Gerais), to the promotion of small- and medium-sized firms (Asturias, Ceará) and innovation within firm “clusters” (Valencia), each relied on synergistic ties between public agencies and firms that would have been unlikely without political delegation and the development of horizontal embeddedness. In Andalusia, populist government created a hierarchical industrial policy system that proved wasteful in the appropriation of resources. In Rio de Janeiro, populist government manipulated the state’s anemic industrial policies and left the system non-functional. In both cases of “failure,” clientelistic exchange hindered the creation

Figure 3 Distribution of the Cases



of plan- or project-based horizontal embeddedness. Figure 3 summarizes the distribution of the case studies along the dimensions of the two independent variables. The comparisons suggest that the political context of incumbents’ decisions to delegate or centralize management of economic policy and the structure of the technocracy explain the composite pattern of subnational industrial policy making in Brazil and Spain.

Distinct patterns of state-society collaboration played a role in determining the degree of social conflict facing incumbents and the available range of choices for defining the configuration of horizontal embeddedness. Where labor (Asturias) and business (Ceará, Valencia, and Asturias) could be integrated into horizontal embedded ties, or were too weak to present a challenge to the industrial policy (Minas Gerais), delegative governments were able to produce either plan- or project-oriented policies. Significant opposition by these social actors and their exclusion from the industrial policy system in Andalusia and Rio de Janeiro reinforced the populist tendencies of the political class and the centralization of the policy-making apparatus.

As the research program on “decentralization” proceeds in different policy areas, new opportunities will emerge for assessing the way that factors endogenous to subnational politics affect decision-making and policy outcomes. Highlighting the limits of both optimistic and pessimistic endemic theories and focusing on the interests of politicians and the institutions of subnational policy-making are crucial first steps to “deepening” the “first wave” studies of decentralization.

Notes

I would like to thank Robert R. Kaufman, Scott Martin, Judith Tendler, William C. Smith, the editors, and two anonymous reviewers for providing comments on earlier drafts of this article. A previous draft was presented at the Third Meeting of the International Working Group on Subnational Economic Governance in Latin America and Southern Europe, San Juan, Puerto Rico, August 26-28, 2000.

1. Studies of transnational production and capital mobility have emphasized the eroding capacity of both central and subnational states to exert leverage over global firms and other investors. See Thomas (1997); Stallings (1995). Furthermore, studies of "adjustment" to global constraints have tended to assume that national governments are the only relevant stewards of policy change. See Haggard and Kaufman (1992).
2. The logic of allocative efficiency is based on the assumption that local units have better information than central planners. Competition among subnational units contributes to *distributive* efficiency by parceling out goods and services according to inter-regional preferences. This approach is most associated with the work of Charles Tiebout in the 1950s, but it is also a core principle of contemporary work on fiscal federalism. See López Murphy (1995).
3. This view is supported through case studies of subnational clientelism and inter-governmental conflicts and their effects on economic adjustment. See Samuels (1998); Treisman (1999).
4. This is a salient argument in the new political economy on industrial policy. See Evans (1995); Ostrom (1997); Tender (1997).
5. For additional analysis of the production function described here, see Ostrom (1997).
6. In the exposition of the argument I use the term "agencies" to describe mostly decision-making units of the public economic bureaucracy. But as the empirical cases in Spain will demonstrate, unions and business organizations can also play a policy-making role in partnership with public agencies. Since the argument emphasizes the inter-relations among these actors and not their organizational attributes, I subsume the role of unions and business associations in decision-making as "agencies."
7. This is true of the recent series of studies of subnational "success stories" such as Tendler (1997); Evans (1997); Locke (1995).
8. On the role of constituency "alarms" see McCubbins and Schwartz (1984).
9. After figuring for revenue sharing and transfers, in 1974, the national state disposed of 50.2 percent of all revenue, the states 36.2 percent, and the municipalities 13.6 percent. By 1988, the national state disposed of 33.4 percent of revenue while the states boosted their share to 50.7 percent and the municipalities to 15.9 percent.
10. State government documents illustrated the interest in creating a *mineiro* industry policy. See the proceedings for the First Latin American Meeting of the Financial Institutions of Development in BDMG (1964).
11. As Paulo Valladares, former president of BDMG and INDI recalls, "Cardoso had been in the opposition for a long time. He created a party of opposition in the state...Cardoso wanted to centralize power, not to decentralize it...So Cardoso did not really try to destroy the agencies, he tried to centralize power and that was inconsistent with empowering the agencies" (author interview, June 18, 1996, Belo Horizonte).
12. One example is how José Alencar, then-president of the state business association, Fiemg, convinced the governor in closed-door audiences, to remove a political appointee to head the BDMG in 1988. Confidential interview with BDMG officials, June 1996, Belo Horizonte, Minas Gerais.
13. BDMG has proved unwilling to approve technically and financially deficient projects. Author interview with Carlos Maurício C. Ferreira, Special Advisor to the Secretary of State for Industry and Commerce, June 12, 1996, Belo Horizonte, Minas Gerais.
14. I explore agency-firm ties in this case in greater length elsewhere. See Montero (2001).
15. Instability in Brazilian exchange rates and periodic surges in import duties convinced Fiat that it could not rely on imports to source JIT production (Addis 1999: 221).
16. Author interview with José Eduardo de Lima Pereira, Director of External Relations, FIAT, April 4, 1995, Betim, Minas Gerais.

17. Author interviews with CODIN staff, May 1996 and July 1999.
18. Author interview with Carlos Alberto Monteiro Rego, Economic Development Director, IPLAN-Rio (Institute of Planning, Municipality of Rio de Janeiro), June 5, 1996, Rio de Janeiro.
19. One independent study done in the 1980s concluded that the state lacked adequate public agencies for coordinating industrial policy with firms. The study specifically contrasted Rio's poor performance with the experience of Minas Gerais. See Magalhães (1983: 38).
20. Author interview with former CODIN president during the Moreira Franco and second Brizola governments, Jorge Fernandes da Cunha Filho, August 2, 1999, Rio de Janeiro, RJ.
21. Author interview with Charles Rossi, Chief of the Department of Industrial Promotion and New Investments, FIRJAN, May 29, 1996, Rio de Janeiro, RJ.
22. For a thorough review of shared and exclusive powers, see Agranoff and Gallarín (1997).
23. Author interview, May 31, 1995, Oviedo, Asturias.
24. Author interviews with SRP, IFR, and SAYPE staff (June and July 1994 and 1995); Encarna Rodríguez Cañes, Chancellery of Economy and Planning, July 26, 1994, Oviedo Asturias; José Manuel Suárez, Metallurgical Federation, UGT, March 26, 1996, Madrid.
25. Author interview, June 26, 1995, Gijón, Asturias.
26. In Carasco's case, she continued as Director of Industry until 1993 when she became Director of the Instituto Tecnológico de Materiales (Technical Institute of Materials), a public technological institute for the metallurgical industry in Asturias (author interview, June 28, 1995, Technology Park of Asturias, Llanera, Asturias).
27. Author interviews with María José Suárez Puente, IFR, July 26, 1994, Llanera, Asturias; Nieves Carasco, Director of Industry (1988-93), June 28, 1995, Llanera, Asturias; and Rodríguez Cañes.
28. Author interviews with Manuel Suárez (UGT); Dario Díaz, CCOO, June 27, 1995, Oviedo, Asturias; Suárez Puente, and Carasco. Also see the language in the agreement affirmed by both UGT and CCOO in January 1994 in Principado de Asturias (1994).
29. See comments by the national president of the AP, Antonio Hernández Mancha, in *El País* May 2, 1988.
30. See comments by UGT and CCOO leaders in *El País* February 23, 1989 and March 9, 1989.
31. One prominent case is that of Jaime Montaner, the Chancellor of Economy under Chaves. Montaner was well connected to a number of regional savings banks (Cajas de Ahorros) and often used these personal associations to extract favorable loans for business associates. The worst charges linked Montaner to a scheme that channeled kickbacks to the PSOE from financial deals involving sales of industrial plots (see *El Mundo* April 26, 1995).
32. IFA interviews, April 1996, Seville, Andalusia.
33. See *El País* August 19, 1994.
34. Calculated from ESECA (1994: 103) and IEA (1995: 81).
35. Between 1985-1994, IMPIVA consumed over 71 percent of all funds for industrial promotion in Valencia. See Más (1995).

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