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State–Business Relations Beyond Growth: Bringing in Development

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December 2016

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Abstract

The signatories of the UN Sustainable Development Goals (SDGs) have called on a wide range of businesses 'to apply their creativity and innovation' to address sustainable development challenges. Yet the role of business in contributing to development depends profoundly on its interaction with the state. This paper asks how states and businesses interact in different contexts to shape development outcomes. A considerable literature has explored state–business relations in producing investment and growth, and the factors that make these relations effective. However, most of these studies either weakly reflect or fail to reflect: (a) the process of interactions and how these are shaped by, and at the same time shape, the power and interests of the actors involved; (b) different political and economic contexts; and (c) the implications of state–business relations beyond economic growth. The paper makes the case for analysing state–business relations beyond economic impacts, by considering the implications of these interactions for three defining challenges of the early twenty-first century – namely inequality, exclusion and environmental degradation. Through a review of four case studies from Chile, Tanzania, India and Ethiopia, the paper explores the actors, structures and processes of state–business relations, along with development outcomes achieved. We employ the concept of 'negotiation' as a metaphor to describe the ongoing interaction that is state–business relations, in order to move the frame of analysis towards a goal-oriented process and to highlight the importance of power and interests in relation to these goals. Building on the case studies, we suggest three ways forward to develop clearer models of state–business relations in development. These are: (1) understanding state–business relations in different institutional contexts, how they emerge and how they operate, and their implications for development outcomes; (2) identifying specific factors that shape the process of state–business relations; and (3) explaining developmental effectiveness of state–business relations, considering also trade-offs and contradictions between different development goals. The challenge of developing adequate frameworks for understanding constantly evolving state–business relations in development is large; but given renewed calls for states and businesses to work together for development, the issues identified here should expectably have a central place on the research agenda.

Abbreviations

ADLI	Agriculture Development-led Industrialisation (Ethiopian Government Strategy)
AILAA	Agricultural Investment Land Administration Agency (Ethiopia)
AISD	Agricultural Investment Support Directorate (Ethiopia)
APEC	Asia-Pacific Economic Cooperation
ASOEX	The Fruit Exporters Association of Chile
BRIC	Brazil, Russia, India and China
CGAP	Consultative Group to Assist the Poor
CME	coordinated market economy
CONUPIA	National Confederation for Medium, Small and Micro Industry, Service and Craftsmen of Chile
CORFO	Production Development Corporation of Chile
CPC	Confederation of Production and Commerce (Chile)
CPPDE	Private Council for Export Development (Chile)
CUT	Unitary Confederation of Labour (Chile)
DIRECON	General Directorate of International Economic Relations (Chile)
EHDA	Ethiopian Horticulture Development Agency
EHPEA	Ethiopian Horticulture Producer Exporters Association
EPRDF	Ethiopian People's Revolutionary Democratic Front
FAO	Food and Agriculture Organization
FDP	Forum for Productive Development (Chile)
GAIN	Global Alliance for Improved Nutrition
GDP	gross domestic product
IDS	Institute of Development Studies
IPPG	(Research Programme Consortium for) Improving Institutions for Pro-Poor Growth
LME	liberal market economy
MDG	Millennium Development Goal
MFI	microfinance institution
MFIN	Microfinance Institutions Network (India)
MITI	Ministry of International Trade and Industry (Japan)
NABARD	National Bank for Agriculture and Rural Development
NBFC	non-bank financial companies
NFFA	National Food Fortification Alliance (Tanzania)
NGO	non-governmental organisation
NNS	National Nutrition Strategy (Tanzania)
PMJDY	Pradhan Mantri Jan-Dhan Yojana (Prime Minister's Money Scheme, India)
PROFO	Development Project (implemented by CORFO in Chile)
RBI	Reserve Bank of India
SBR	state-business relation
SDG	Sustainable Development Goal
SHG	self-help group
SME	small and medium-sized enterprise
SNA	National Agricultural Association (Chile)
SOE	state-owned enterprise
SOFOFA	Society for Manufacturing Promotion (Chile)
SONAPESCA	National Society of Fishing (Chile)
SUN	Scaling Up Nutrition
TPP	Trans-Pacific Partnership
VoC	Varieties of Capitalism
WTO	World Trade Organization

1 Introduction

State–business relations are ubiquitous in market economies. For at least two and a half centuries the economic and societal implications of these relationships have been a concern of scholarship (see, for example, Smith 1976 [1776]). More recently, the success of East Asian ‘developmental states’ – notably South Korea and Taiwan – has been studied as a case of effective state–business relations acting as catalysts for economic growth and structural transformation (White and Wade 1984; Evans 1996). Similarly, recent studies conducted in Africa and Asia claim that close and effective state–business relations reduce policy uncertainty, that the rate of investment increases, and that they determine economic growth and structural transformation (Cali and Sen 2011; Cali *et al.* 2011; Qureshi and Te Velde 2013; Lemma and Te Velde 2015).

While much research is being done on state–business relations, the question of how state–business relations lead to broader development outcomes beyond growth, such as reductions in inequality and poverty, or the promotion of sustainable development, has received comparably limited attention. Moreover, the question of the effectiveness of these relations in producing development outcomes in different institutional contexts is still far from conclusively answered. Important research is seeking to uncover or prescribe ‘correct’ or ‘good’ state–business relations. Yet given the many ways in which the perceptions of the roles of states and businesses in development are evolving and the varied forms of interaction in different contexts, we find a significant research gap in taking stock of the state–business relations which exist in developing countries and a lack of frameworks for understanding them in relation to development outcomes. We seek to address, in a non-deterministic and non-prescriptive way, this central issue of contemporary political economy.

Not long ago, the signatories of the UN Sustainable Development Goals (SDGs)¹ called on a wide range of businesses – from micro-enterprises to cooperatives to multinationals – ‘to apply their creativity and innovation’ to address the sustainable development challenges of ending poverty and hunger and reducing inequality. At the same time, ‘governments are expected to take ownership and establish national frameworks for the achievement of the 17 Goals’.² With contemporary development thinking and practice increasingly emphasising the role of business (Humphrey *et al.* 2014), we see a major gap in how the relationship of business with the state is posited. Statements like ‘how business does business, and where it does business, will have a significant impact on whether the Sustainable Development Goals are achieved’³ appear to position business as an autonomous core actor in development. Yet how and where ‘business does business’ depends profoundly on its interaction with the state, which acts not only as a regulator or partner, but also at times as facilitator, co-conspirator or adversary – and often more than one of these roles simultaneously.

This Evidence Report therefore poses the question: *how do the state and business interact to shape development outcomes?* We hold the underlying premise that the interplay between states and businesses profoundly affects development outcomes, including and beyond growth, to be uncontroversial. While this interplay has been obscured in the heated debate over business-led or state-led models, where the private sector can be said to be a development actor, it is frequently responding to policy directions or incentives from the state, or using public finance. Where states engage in development activities, they very often act in cooperation with or through delegation of tasks to the private sector, or react to harms created by business activities. Given the centrality of state–business relations to

¹ <https://sustainabledevelopment.un.org/post2015/transformingourworld>

² www.un.org/sustainabledevelopment/development-agenda/

³ Helen Clark, speech at the [UN Private Sector Forum, 26 September 2015](#).

development, we argue that understanding these relations, how they are structured and how they work in practice is crucial.

These issues are broad and one challenge is to define the boundaries. Firstly, we are examining *contemporary* state–business relations (roughly the past 20 to 25 years), instead of a broader sweep of history. Secondly, we are interested in state–business relations in *developing countries* that are market economies (in the broader sense).⁴ Thirdly, we focus on interactions between states and businesses that shape (or seek to shape) *development*, meaning the deliberate promotion of developmental outcomes (we elaborate on developmental outcomes in Section 6).

Within these bounds, this report aims to provide an academically grounded analysis relevant for the policy community (and those who advise or have the ear of the policy community) of existing conceptualisations and some insightful cases of how state–business relations shape development outcomes. Our approach consists of two components: first, a review of theoretical and empirical literature, and second, an examination of four case studies. Our literature review takes into account the contributions of different disciplines (notably political science and sociology) to understanding state–business relations, drawing out different perspectives on the power and interests involved in state–business relations in market economies. In particular, we focus on the Developmental States literature and recent works on ‘effective’ state–business relations for development, as well as examining a number of broader theoretical approaches. The literature ultimately points us to the importance of formal and informal coordination institutions, the notion of state–business relations as reflecting a balance of power, the potential value of a non-prescriptive approach to studying state–business relations, and the need to better understand processes in addition to structures of state–business relations.

While the literature supports our conceptualisation of state–business relations, the case studies provide the details: who has been involved, what processes have been at work, and what outcomes have emerged. While primary data-based investigation was beyond the scope of this initial framing paper, researchers with rich and direct experience in a particular sector and country developed each case based on published sources. These are national studies from Chile, Ethiopia, India and Tanzania, while Box 5.1 also considers the international dimensions of state–business interactions through the examination of Chinese business in Africa. The large volume of evidence that emerged from the case studies was synthesised through an inductive reasoning process to interpret and structure the evidence. This synthesis captured emerging themes such as the interdependence of states and businesses, the fine line between collaboration and collusion, different forms or modalities of coordination, and the importance of ideas in shaping state–business relations. We are well aware of the limitations of these secondary cases, particularly in the investigation of processes in which interests, agendas and interactions are often hidden. Nevertheless, we believe that the evidence that emerges makes the case for the need for a better and more nuanced understanding of state–business relations in determining development outcomes in different institutional contexts, and provides a basis for future empirical work.

1.1 Key concepts

Many of the key concepts used in this report are contested, and while we don’t aim to resolve these debates, we outline below the particular ways these concepts are used here.

⁴ By ‘developing countries’ we exclude European, North American and high-income Asian countries. Chile, one of our case studies, is a borderline case; but the case study deals with a period in which it was still rapidly economically developing. By ‘market economies’ we only exclude the very few remaining centrally planned economies, such as North Korea and Cuba.

1.1.1 Development and development outcomes

Economic growth is at the centre of much of the current literature on state–business relations. However, we consider investment and economic growth as central but insufficient components of development. We therefore focus on three additional defining development challenges of the early twenty-first century: reducing inequalities, such that the benefits of growth and existing wealth more evenly contribute to improved livelihoods and wellbeing; building inclusive and secure societies, where citizens are protected against shocks and have a stake in governance; and accelerating sustainability through development pathways that address resource demands and limits (IDS 2015). There are also potential trade-offs, contradictions and complexities between the pursuit of these different development goals (for example, Schmidt *et al.* 2015; Waage *et al.* 2015). We expand on these aspects of development, which resonate with many of the UN SDGs, in Section 5.

1.1.2 State and business

Defining the *state* is extremely challenging, and we return to this in our literature review. In this report, the state generally refers to a collection of actors (both organisations and individuals) with the legal mandate to represent populations, ranging from various ministries and the civil servants and politicians who work in them, to regulatory agencies or quasi-autonomous bodies. In practice, it is often the constituent elements of the nation state that are meant, but state also consists of actors and agencies operating at different levels (local, sub-national, national).⁵ These actors have varying degrees of autonomy, and have their own interests, including attaining and maintaining power. In any case, our understanding of the state extends beyond mere government; rather, in the Weberian sense, it is the compulsory political organisation that remains even after various rulers, governments or administrations have come and gone (although they may profoundly shape it).

We acknowledge therefore that in discussing specific examples of relations between state actors and business, such as those described in the case studies, we are often discussing government– rather than state–business relations. However, for simplicity and for consistency with use in most other papers, we use the term state–business relations throughout.

As the literature review makes clear, business can be seen as synonymous with capital and the capitalist class; it can refer to individual firms or ‘businesses’, or to groups of businesses. In this review, ‘business’ refers to a diffuse collection of actors: business associations, multinational enterprises, small and medium-sized firms and individual entrepreneurs. These actors may operate in the formal or informal sector, range across agriculture, industry and services, and trade mostly domestically or operate across national borders. While all businesses are interested in profits, the profit orientation may be primary or, particularly in the case of social businesses, secondary.

1.1.3 Power

It is nigh impossible to discuss state–business relations without some reference to power. Yet the concept of *power* is extremely contested. For liberals, power is a force which controls (‘power over’) and which therefore requires checks and balances; whereas collectivists see power as constructive (‘power with’), a means of aggregating resources for the collective good (Moore 2005). Some treatments of power centre on specific episodes of coercion or collective action, while others focus on power as the outcome of social processes (Murdoch and Marsden 1994). Foucault’s conceptualisation is more dynamic. Power is a network of relations constantly in tension; a perpetual battle rather than a contract (Foucault 1991: 26–7). Power may also be understood primarily in terms of its different manifestations. Fuchs

⁵ In the present analysis, we do not include international or inter-governmental actors, and consider them rather as ‘other’ actors that influence state–business relations.

and Lederer (2007), for example, discuss the power of business in terms of instrumental power, focusing on the power and influence of business over other actors; structural power, which is determined by underlying economic structures and organisational procedures that allow businesses to set agendas before any interaction takes place; and the power of ideas and values that shape identity and perceptions of problems and potential solutions.

Our understanding of power is partly instrumental, based on the actors involved and the resources they command in order to satisfy their preferences or interests. It is also highly structural, based on the agenda-setting power of the actors involved. Power may be employed both in the struggle for domination (power over) and to work with others towards common goals (power with). Power is not fixed but is shaped through social processes and interactions – an aspect we come back to in the next section.

1.2 Overview

Setting the context, the next section presents our lens on state–business relations as a structured process of negotiation, which is then followed by an overview of key theoretical and empirical literature on state–business relations. Both sections explore the concepts of power and interests as they influence and are influenced by the ongoing process of state–business relations. Sections 4 and 5 present our case studies and our synthesis of the themes that emerge. The synthesis also explores how state–business relations have contributed to development outcomes, including economic development, reducing inequalities, building inclusive and secure societies and accelerating sustainability. We conclude by proposing key elements of future research on state–business relations and development outcomes.

2 State–business relations: a structured process of ‘negotiation’

As the review in the next section will show, how states and businesses interact and the implications for society is a recurrent theme in political, economic and sociological thought. This report considers a subset of state–business interactions: that of state–business *relations*. In other words, the interactions that we are interested in are not one-off, discreet or arbitrary, but rather complex engagements over a longer period of time. We examine these relations through a specific lens, *negotiation*, which allows for a non-deterministic and non-prescriptive analysis, providing scope to explore both structural features of negotiation, shaped by power and interests, and the processes through which they take place.

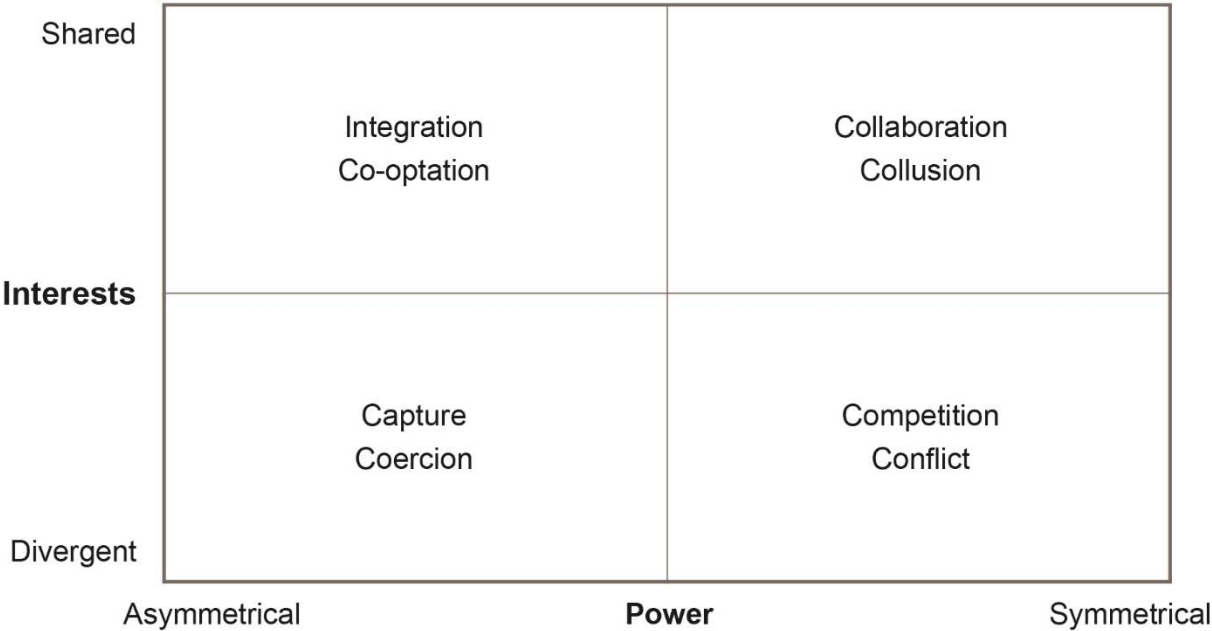
To clarify, we do not mean negotiation in the narrowly literal sense of different parties sitting around a table to ‘hammer out’ an agreement. These discreet events are only part of the broader and longer-term negotiation that goes on between states and businesses. In the wider sense, negotiation is an analytical metaphor that focuses our view on the various ways in which states and businesses interact in pursuit of their interests.

Our interest in negotiation is not unique. A number of other authors employ the concept. Evans (1995: 12) argues that developmental states engage business and society through ‘the continual negotiation and renegotiation of goals and policies’. States engage in negotiation with business and labour in search of compromises over economic reforms (Schmidt 2009). Weiss (1995: 612) highlights how states in successful late developing countries exercised ‘infrastructural, or negotiated, powers’ *vis-à-vis* business. Haggard (1997: 83) argues against painting state–business relations in terms of an autonomous state and a relatively passive private sector, seeing them as negotiations through which the government seeks political support, investment and information, while business seeks a predictable and stable business environment and relevant incentives. However, nowhere do we find the idea of state–business relations as negotiation properly deepened. We therefore outline negotiation as our analytical lens here.

2.1 Power and interests in negotiation

While the power of state or business actors in their ongoing negotiation is difficult to observe and define precisely, their relative power (symmetrical or asymmetrical) can provide useful insights (Crump 2015). This includes instrumental power derived from the resources that they possess, as well as the skill with which they employ these resources and their structural power to set the boundaries of the negotiation. Moving from power to interests, the interests of businesses could simply be defined as profits, while the interests of state actors could be defined as power. However, the exact preferences of specific business or state actors within negotiations are shaped by the types (for example, sector or function) and scale (for example, local, national, international) of their activities, their incentive structures and the institutional framework and network of relations in which they operate, and can be seen as relatively aligned or divergent. If we consider the possible combinations of power and interest alignment or divergence that may exist in the negotiation between business and the state, we find the four extreme scenarios represented in Figure 2.1.

Figure 2.1 State–business relations based on power and interests



Source: Authors' own.

On the right side of the diagram, states and businesses have more equal power:

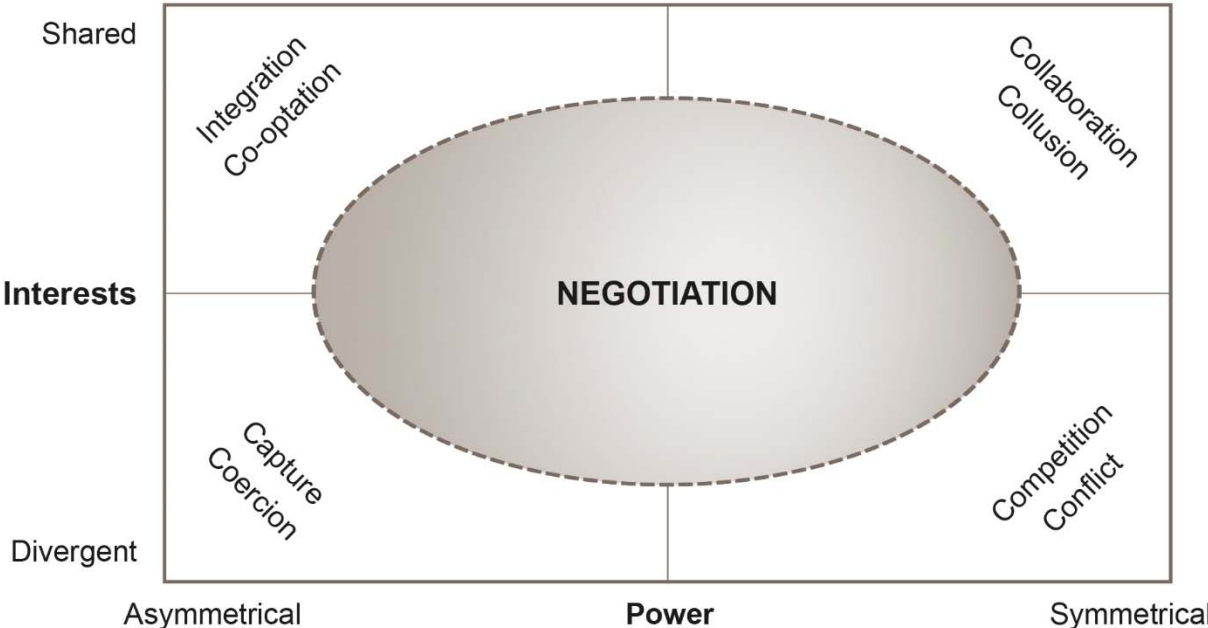
- At bottom right, similarly powerful actors with divergent interests are likely to engage in competition or conflict. In such a 'states versus markets' scenario, their irreconcilable goals lock the actors into entrenched competition for supremacy, with one seeking to dominate the negotiations at the expense of the other, but neither can succeed. Likely, both are weakened as a result.
- At top right, under conditions of equal power and shared interests, the state and business are likely to work closely together. This scenario highlights the 'constructive' face of power, which may be broadly benevolent or nefarious, manifesting as collaboration or collusion. Collaboration implies a beneficent confluence of interests, where state–business relations result in practical solution-seeking; collusion refers to the possibility that state and business actors may collaborate to the detriment of broader society.

The left side of the diagram represents situations with unequal power where 'power over' dominates; note that either states or businesses may have greater power:

- At bottom left, divergent interests and unequal power suggest relations in which either business elites overpower and capture the state apparatus, which they manage to employ to advance their interests at the expense of societal interests, or a strong state may overpower and effectively control businesses (coercion); an approximate example could be Venezuela's political economy in recent years.
- In the top-left corner, integration and co-optation suggest the interests of unequal actors aligning, with the weaker actor becoming incorporated into or led by the other. The more evident example of this would be the state leading business and integrating it into its agendas, as with 'state capitalism', or state-owned enterprise. But also business might effectively co-opt and integrate a compliant state (or agencies of the state), for instance if powerful corporations manage to control the policy agenda of a developing state which has no autonomy.

However, we suggest that these extremes are archetypal and in reality, they constitute exceptions rather than the rule. As illustrated in Figure 2.2, they are in the extreme corners of the matrix. In the realm between these extremes, actors' interests are different (although not 100 per cent incompatible), and each has some (but not necessarily equal) influence over outcomes.⁶ In this realm, negotiation is necessary because each actor requires something from the other to achieve its goals. Here, conflict is averted or resolved and some degree of cooperation is achieved (though whether this is 'collaboration' or 'collusion' is a point that will be taken up later). While conflictual/competitive, collaborative/collusive, coercive/capturing, or integrating/co-opting situations do exist – in many instances real state–business relations will contain some elements of each, and sit in the much less clear space in the 'middle'.

Figure 2.2 The realm of negotiation



Source: Authors' own.

2.2 Negotiation as process

Figure 2.2 is static. If our analysis stopped here, the lens of negotiation would be meaningless. We would need to understand state–business relations in any particular context as having a pre-determined outcome based on the relative power and interests of the actors involved. Yet we understand power as being shaped by, as well as shaping, social processes. Actors' orientations (their preferences and perceptions) too are shaped by the setting in which negotiation takes place and the ensuing exchange of ideas.⁷ Therefore, we need to consider analytically the *process* of negotiation alongside its structure. This view is in line with other theoretical approaches. It corresponds, for example, to that highlighted by Mayntz and Scharpf (1995) in their analysis of 'actor-centred institutionalism', in which structure and agency intermingle to shape political-economic outcomes and to elements of actor-network theory (Murdoch and Marsden 1994).

⁶ This theoretical space may be seen as pertaining to a specific issue (such as how to address malnutrition) or general issues (such as national development).

⁷ This premise stands in contrast to rational choice approaches that assume largely stable and fixed preferences.

In a review of negotiation theories performed for the Food and Agriculture Organization of the United Nations (FAO), Alfredson and Cungu (2008) identify five relevant theoretical approaches to negotiation, primarily drawn from business and management literatures:

- a *structural* approach, which explains negotiation as reflecting power structures between actors; outcomes can be predicted from actors' pre-existing power
- a *strategic* approach, which sees actors as rationally competitively bargaining, as in game-theoretic models
- a *behavioural* approach, which highlights the effect of individual negotiators, their personal characteristics and framing of the situation; for instance 'hard-liners' or 'altruists'
- a *concession-exchange* approach, in which negotiating parties make trade concessions for counter-concessions
- an *integrative* approach, which foregrounds the process of negotiation itself and the communication between the actors. In contrast to the other approaches, which presuppose a fixed 'pie' and rigid modalities, this emphasises the possibility of win-win outcomes created through collective problem-solving.

All five approaches may partly explain negotiations between state and business actors; however, the structural and strategic approaches are both very deterministic, the behavioural approach focuses too strongly (for our purposes) on negotiators' personal attributes, while the concession-exchange approach is rigid and formulaic. We would suggest that, for understanding state–business relations in development, the integrative approach best supports an analysis of the iterative 'games real actors play' (Scharpf 1997) under conditions of uncertainty and with interdependent preferences. As the case studies in Section 4 will show, negotiation between states and businesses is very often about seeking – successfully or not – ways forward towards 'win-win' outcomes through the discovery of the other's preferences, the building of trust and the identification of solutions (Lewicki *et al.* 2010: 125–43). There are, of course, well-known perils along the way: the good faith of one actor may be taken advantage of, negotiators may lose accountability to their constituency (as with 'cognitive capture' of regulators), or negotiation may be increasingly pursued for its own sake (Lewicki *et al.* 2010: 37). Moreover, adopting this integrative perspective says nothing about the impact of potential win-win solutions on broader society – they may be beneficial or detrimental to the actors outside the negotiation.

By seeing state–business relations through the lens of the 'structured process' of negotiation, we move the focus away from the four extreme corners of Figure 2.2 to shine a light on the process of negotiation in between, in which structural conditions are key factors, but not final determinants of, the state–business relations which shape development. If structure was all that mattered, negotiation itself would be meaningless, a foregone conclusion; but if only the process mattered, this would deny the ability of powerful and strongly interested actors to influence and shape both the scope of negotiation and the outcomes achieved. In the structured process of negotiation, states and businesses have power, interests and agency, and pursue (but do not necessarily attain) mutually acceptable ways forward, with implications for society more broadly.

3 Conceptualisation of state–business relations

The power and interests of state and business, and how they relate to one another, are the subjects of a vast array of literature. Already Adam Smith’s analyses actually went far beyond his famous idea of the ‘invisible hand’⁸ governing the economy, and with *laissez-faire* only part of the story. Smith in fact suggested that the state should steer business activity through selective taxation, and furthermore provide infrastructure, money, public services and even on occasion engage in public enterprise for revenue generation (Smith 1976 [1776]; Viner 1927).⁹ Marx’s writings also understood the modern state and capital as being in a dialectical and interdependent relationship with one another, shaped by the balance of class interests (Elster 1985: 400–28).¹⁰

Since then, very many authors and schools of thought have reflected on the nature of the state and business and their relation to one another. The aim of this review is to assess the state of play in the literature that deals with state–business relations in development, asking: how do power and interests shape state–business relations? Presented with a potentially vast literature to review, we focus on two particular streams of research: the literature on the ‘developmental state’, and more recent literature that analyses the ‘effectiveness’ of state–business relations in different countries. These offer key insights into the ways in which interactions are organised in different countries. But with their focus on the creation of institutions for coordination of business and state interests – effectively the bottom-left corner in Figure 2.1 – they do not address some questions around the structure (power and interests) and processes of negotiation. We therefore also draw on selected insights from broader theory to dig deeper into the nature of the state and business, the interests they may have and the powers at their disposal. We acknowledge that our review does not do justice to the full body of relevant scholarship. We have missed out literatures on private sector development, industrial policy and innovation studies, which consider how states can drive investment, growth and structural change. However, we believe our chosen scope is appropriate in the context of our question regarding how power and interests shape state–business relations and their implications for broader development outcomes.

3.1 Developmental states and embedded autonomy

The concept of the developmental state arose from the need to explain the economic growth of several East Asian countries – specifically Japan, South Korea and Taiwan – at phenomenal rates while diverging from both free-market and socialist planning growth strategies. Chalmers Johnson was the first to elaborate the concept¹¹ in *MITI and the Japanese Miracle: The growth of industrial policy, 1925–1975*. Johnson (1982: 17) stressed that ‘all states intervene in their economies’, and clarified that Japan was perhaps exemplary, but not unique. ‘In states that were late to industrialize, the state itself led the industrialization drive, that is, it took on *developmental* functions’ (Johnson 1982: 19). The state here acts as the organising force driving economic upgrading by national business.

⁸ Smith only employed this metaphor once in *The Wealth of Nations*, and not to illustrate the power of unfettered trade, but rather in a discussion of economic protectionism, as an illustration of how societal biases towards buying domestic goods benefited the national economy (see also, Kennedy 2009).

⁹ According to one of his foremost interpreters, Jacob Viner (1927: 231), Smith ‘was not a doctrinaire advocate of *laissez-faire*. He saw a wide and elastic range of activity for government, and he was prepared to extend it even farther if government [...] showed itself entitled to wider responsibilities’.

¹⁰ The young Marx evaluated the state as simply a capitalist apparatus (Marx and Engels 2004), but he later revised this to a more nuanced view of the state as an autonomous body that was variously tolerated, employed or ‘abdicated’ by collective business (capitalists). In Marx’ historical analysis in *Capital*, the state originally created the conditions for the emergence of modern capitalist economic relations (particularly Ch. 26 & 33 – Marx 1990: 873–77; 931–41).

¹¹ However, according to Evans (1989), researchers associated with the Institute of Development Studies were the first to dub Taiwan and South Korea ‘developmental states’, and hence coined the term (see also White and Wade 1984).

3.1.1 What is a developmental state?

Key to the success of any developmental state, Johnson (1982: 20–22) argued, was the existence of a powerful and talented economic bureaucracy leading business to contribute to the national industrialisation drive, much in line with Weber's (1978) notion of an effective bureaucracy as the key to rational exercise of authority. Johnson's subsequent writings (1999: 43) highlight the abstract nature of the developmental state model – not a Japanese or Asian specificity – and how it could be generalised. In its strong form, the developmental state concept (or hypothesis) contends that, in order to industrialise, any country requires a strong and capable state to lead the private sector with an industrial policy that enhances the nation's competitiveness. In its softer form, it suggests that an effective state with a rational plan can significantly accelerate economic development.¹²

Linda Weiss' (1995) study of Korea, Taiwan and Japan highlights that state 'strength' and bureaucratic 'autonomy' are not enough for a state to become developmental. Rather, developmental states possess bureaucracies that are strong and insulated from special interests, but not insular from the economy as a whole. Business and the state must relate to each other through 'governed interdependence'. The power of the state in successful late developers thus is not 'despotic', but rather, 'infrastructural'. Weiss suggests that four forms of governed interdependence are found in East Asian developmental states: 'disciplined support', where support for business comes attached to performance conditions; 'public risk absorption', where the state lowers the risk of establishing new or emerging industries; 'private-sector initiative in public policies', business shaping the state or colluding with it; and finally, 'public-private innovation alliances' around acquiring, developing, upgrading and diffusing technology (Weiss 1995: 607–11).

Evans (1995) refers to the same interrelationship of state and business as 'embedded autonomy'. Developmental states, he argues, have a bureaucratic apparatus which is autonomous as a coherent entity that remains separate from society, with its own meritocratic rules, but which is embedded 'in a concrete set of social ties that binds the state to society and provides institutionalized channels for the continual negotiation and renegotiation of goals and policies' (Evans 1995: 12). Evans suggests that in this way developmental states succeed at overcoming or 'fusing' what at first sight appears to be a contradiction between autonomy and embeddedness.

Embeddedness provides sources of intelligence and channels of implementation that enhance the competence of the state. Autonomy complements embeddedness, protecting the state from piecemeal capture, which would destroy the cohesiveness of the state itself and eventually undermine the coherence of its social interlocutors. The state's corporate coherence enhances the cohesiveness of external networks and helps groups that share its vision overcome their own collective action problems. Just as predatory states deliberately disorganize society, developmental states help organize it.
(Evans 1995: 248)

It has, however, been pointed out that bureaucratic structure alone cannot explain developmental states. Leftwich (2000: 167–68) underscores that a developmental state must demonstrate 'a determination and ability to stimulate, direct, shape and cooperate with the domestic private sector as well as arrange mutually acceptable deals with foreign interests'. The form of authority exercised in business may also matter.

¹² These ideas are older, harking back at least to German nineteenth-century economist Friedrich List, who contended that less advanced nations had to rely on the state to drive future development and catch up with advanced nations. List situated his ideas in a broader framework of 'national economics' (as opposed to Smith's liberal economics), arguing that Germany take a 'state-led' approach to push through the stages of economic development and catch up with Britain (List 1885/2011).

Some developmental state theorists point to crucial elements of ideology and state commitment. A state with a 'developmentalist' ideology is one whose main focus is improving its citizens' welfare through economic development, usually interpreted as high rates of accumulation and industrialisation. Castells (1992: 55) argues that such a state 'establishes as its principle of legitimacy its ability to promote sustained development, understanding by the steady high rates of economic growth'. It may succeed if this interest aligns with the interests of business to make profits; but the state must also have enough (though perhaps not too much) power to promote its strategy.

Laura Routley's (2012) review of the literature summarises the attributes of developmental states as: first, having a capable, autonomous but embedded bureaucracy; second, political leadership oriented towards development; third, a close and often symbiotic relationship between (at least some) state agencies and key industries; and fourth, successful policies which promote growth. She highlights that a truly developmental state must not only possess the capacity to perform developmental roles, but must also use it; elements which certainly can exist independently from one another. To paraphrase Routley, to be truly developmental, a state must show good bureaucracy, good leadership, good relationships and good policy, and direct these *in practice* towards economic development.

3.1.2 Confusions and limitations

Routley (2014), among others, has warned that the 'developmental state' may increasingly be used as a buzzword, particularly by politicians outside East Asia, losing its meaning as a fully-fledged model. Others have highlighted the divergence in discussions about the relative importance of different parts of the developmental state model (Evans 2011: 51; Booth 2015: 3), which could lead to the term being appropriated for very different state structures which are not developmental in nature, or at least have little in common with the original archetype. Conversely, some have also asked whether the concept may be tautological if the label 'developmental state' is applied *post-hoc* to any state that has successfully developed, rather than to states that show distinctive features (Mkandawire 2001).

Putzel (2002) highlights that the search for an East Asian developmental state model 'homogenised' the experiences of diverse nations, which may not have had a singular reason for success. Haggard (2004: 56) extends this criticism by arguing that 'the misguided effort to find a single institutional taproot' for East Asia's growth has led to a simplified understanding which does not account for regional variances. Hayashi (2010) contends that by focusing on the widely discussed East Asian examples, many lessons from other states (such as South-east Asian states) have often been ignored, although these countries and their development paths may be more relevant to current developing countries. Moreover, the focus on a few countries which enjoyed economic success often gives a rose-tinted view that obscures not only many failed cases, but also the social injustice and political repression which characterised post-war development in cases like South Korea and Taiwan, where the power and interests of state and business often superseded civil rights.

The developmental state concept has also been criticised for framing discussions around what 'works' for development too narrowly, around a few structural factors and explanations which neglect the history of a country or the context in which it found itself at the time its developmental state was 'active' (Woo-Cummings 1999: 2). It is argued that this focus on institutions misses the impact that politics and social processes can have on development. Institutions for coordination may well manage to address operational issues in a country's economy, but such coordination assumes that state and business have reasonably shared interests and a distribution of power that makes collaboration (rather than control or domination) likely. Leftwich (2010: 94) also highlights the importance of leaders, elites and coalitions exercising the 'right' sort of agency, which structure alone cannot explain.

3.2 Cross-country comparisons of formal and informal state–business relations

A body of literature has more recently emerged, which specifically deals with the effectiveness of ‘state–business relations’ in development, deepening the thesis that developmental state–business relations are characterised by ‘embedded autonomy’ or otherwise close and beneficent collaboration. This literature explicitly has sought to transfer and apply the lessons of East Asian developmental states to other regions. This ‘effective state–business relations’ literature highlights that close state–business relations reduce policy uncertainty, raising the rate of investment and bringing about economic growth and structural transformation (Cali and Sen 2011; Cali *et al.* 2011; Qureshi and Te Velde 2013; Lemma and Te Velde 2015). Coordination is a core theme – that is, the ability of state and business organisations to exchange information and align incentives, to reduce transaction costs and to lead to growth-oriented policy implementation.

3.2.1 Formal institutions and ‘good’ state–business relations

Much of this literature emerged from the Research Programme Consortium on Improving Institutions for Pro-Poor Growth (IPPG),¹³ which argued from an economic perspective that effective or ‘good’ state–business relations were those that addressed government, market and coordination failures and reduced policy uncertainty.

Good state-business relations are based on a benign collaboration between business and the state with positive mechanisms that enable *transparency*, ensure the likelihood of *reciprocity*; increase *credibility* of the state among the capitalists, and establish high levels of trust between public and private agents. They provide a transparent way of sharing information, lead to a more appropriate allocation of resources, remove unnecessary obstacles to doing business, and provide checks and balances on government intervention.

(Te Velde 2009: 5, emphasis in original)

In terms of evidence to support the suggestion that such state–business relations drive growth, researchers have conducted various cross-country quantitative comparisons and assembled case study evidence from individual countries. Sen and Te Velde (2009) scored 19 different sub-Saharan African countries according to the quality of their state–business relations, awarding higher scores to those that had:

- (i) greater private sector organisation *vis-à-vis* the public sector (the presence of umbrella business organisations/associations capable of lobbying the state)
- (ii) public sector organisation to support the private sector (the presence of an investment promotion agency)
- (iii) regularised interactions between government and the private sector (an institutionalised public–private dialogue taking place at regular intervals)
- (iv) mechanisms to avoid harmful collusion between the state and the private sector (having a competition policy).

They found that countries that had these characteristics witnessed higher economic output, since ‘improvements in formalised institutional relations between the state and the private sector increase economic growth in the African context’ (Sen and Te Velde 2009: 1,278). The composite score for ‘effective’ state–business relations was further refined and applied in subsequent studies (Cali and Sen 2011; Cali *et al.* 2011; Qureshi and Te Velde 2013). Cali and Sen (2011) and Cali *et al.* (2011: 1,543) set out to examine ‘the impact of effective state-business relations on economic growth’ in 15 Indian states. Applying the above measures

¹³ www.ippg.org.uk/

and standard growth regression methods, they concluded that the form of state–business relations significantly explained economic growth. Cali and Sen (2011: 1,543) added that more than any other conventional determinant of growth (such as geography or access to the sea), effective state–business relations explained differences in economic growth.

Qureshi and Te Velde (2013) approached the issue from a firm’s perspective, looking at whether effective state–business relations (understood in this case as firms’ membership of business associations and their perception of government quality) improved firm-level performance in seven sub-Saharan countries: Benin, Ethiopia, Madagascar, Malawi, Mauritius, South Africa and Zambia. They found that membership in a business association enhanced firm-level productivity by about 25 to 35 per cent (Qureshi and Te Velde 2013: 925), thanks, for instance, to associated firms having better access to information on regulations and to public goods. Overall, they suggested organised state–business relations improved a country’s investment climate and enhanced its labour productivity.

Lemma and Te Velde’s (2015) review of empirical studies in Asia and Africa confirmed that high scores on formal state–business relations measures were associated with higher economic growth and firm-level productivity. Many case studies also emphasise the importance of formal interactions between business associations and their public-sector counterparts. For example, studies from Ghana, Mauritius, South Africa and Zambia showed that formal consultative forums performed multiple functions, including enabling businesses to transparently influence government budget decisions (Te Velde and Leftwich 2010). Overall, there appears to be a trend towards greater formalisation of state–business relations in Africa, such as Presidential Investor’s Advisory Councils being set up to engage with business (Lemma and Te Velde 2015).

These findings, produced as part of the IPPG Consortium, suggest that economic growth depends on the extent to which states’ and businesses’ interests are aggregated and formally negotiated (IPPG 2010). However, some doubts have also recently been raised over the importance of centralised formal organisations in maintaining ‘good’ state–business relations. For instance, drawing on survey data from 171 local firms in Kenya, Tanzania and Zambia, Charles *et al.* (2015) explored how these firms engaged with the government. They found that a significant number of firms (as high as 50 per cent in Kenya) did not participate in business associations, and when they did, they tended to go with more than one association, splitting and weakening their voices and engagement with governments. These results resonate with Taylor’s (2012) suggestion that statistical measures may overstate the roles of business associations.

3.2.2 Beyond formal institutions

While the policy recommendations have naturally included supporting business associations, investment climate reforms, investment facilitation, public–private dialogue mechanisms and the creation of special economic zones (Sen 2015), much of what really lies behind ‘good’ state–business relations may not be formal or measurable. It is acknowledged that formal institutions are not easily put in place, and that informal state–business relations might be a stepping stone towards formalisation. Researchers from the Centre for the Future State¹⁴ addressed these issues based on case study analyses from countries such as Brazil, China, Egypt, Indonesia and Vietnam, placing a much greater emphasis on informal rather than formal institutions. Abdel-Latif and Schmitz (2009), for example, found that informal relationships (social networks with common social roots and professional backgrounds) facilitated effective public–private relationships that played a role in raising investment and economic growth in Egypt.

¹⁴ www2.ids.ac.uk/futurestate/

In understanding how to achieve effective interactions of state and business, Unsworth and Moore (2010) even suggest that Weber's (1978) ideal of a depersonalised and purely meritocratic bureaucracy may have been taken 'too far':

Informal arrangements and personalised relationships can also be part of the solution, with potential to contribute over the longer term to more inclusive, rules-based arrangements. Elements of 'public authority' – the provision of collective goods – can be created outside the state, for example when trust between businesspeople substitutes for legal enforcement of contracts. They can also be created through informal collaboration between public and private actors. (Unsworth and Moore 2010: 8)

One conclusion from the Centre for the Future State is that state–business relations reflect a balance of power between different interests, which may be formally or informally negotiated. Bargaining between groups that hold political/military power (but need revenue, finance and investment) and those who hold economic power (who need order, security, infrastructure and predictability) is fundamental both to political settlements and for strategies for investment and growth. While the authors are sensitive to the risk of crony-capitalism, they emphasise the importance of examining how state–business relations work *in practice*, rather than condemning all informal relationships as collusion. At the same time, they note an interplay between formal and informal, and suggest that while informal institutions can be of great importance for short-term growth, sustaining growth requires more rules-based governance (Unsworth 2010).

To appraise these recent literatures: they have provided valuable demonstrations of how state–business relations matter for growth, and have clearly shown the importance of formal arrangements that allow states and business to engage one another, as well as asking whether informal arrangements may stand in for (or help foster) formal ones. However, both literatures have dealt with development outcomes primarily in the form of economic growth, even where specified as 'pro-poor growth', rather than through a wider lens, and still tend towards an emphasis either primarily or ideally on formal interactions and institutions.

3.3 Theoretical perspectives on the political economy of state and business

This deeper look into the theoretical literature from political economy and sociology deepens the questions around power and interests that shape state–business relations. What power and interests does the state have, what power and interests does business have, and what relationship exists (or should exist) between the state and other economic actors in capitalist or market economies?

3.3.1 Varieties of Capitalism

One literature that theorises the relations of businesses with each other explains different 'Varieties of Capitalism' (VoC).¹⁵ Its core hypothesis is that national economies diverge in important ways because institutional arrangements in different spheres of the economy only make sense when they fit together. Both businesses and states have an interest in institutional coherence, since 'institutions within a successful economy are mutually reinforcing, balanced, and complementing' (Nölke and Vliegenhart 2009: 672).

Hall and Soskice (2001) originally proposed two types of capitalist economies: liberal market economies (LMEs) – typified by the United States and the United Kingdom – and coordinated

¹⁵ The VoC literature has focused primarily on selected rich countries. It emerged in part as a reaction to popular notions about an inevitable global convergence towards market liberalism in the aftermath of the Cold War (Fukuyama 1992; Friedman 1999), and sought to explain the persistent differences in how successful capitalist economies are organised.

market economies (CMEs) – typified by Germany, Japan and Sweden. In LMEs, the activities of economic actors are coordinated mainly through market institutions, creating an economy organised through competition and formal contracting; in CMEs, strategic and longer-term network-based interaction between firms and other actors plays a greater role. The VoC typology has since been expanded extensively (and contestedly), but for us the framework of analysis is of far greater interest than the number of different varieties. The logic of VoC analysis may best be understood by focusing on the two original varieties (LME and CME).

While in VoC thinking the key unit of analysis is the economy of nation states, the key explanatory unit is in fact the firm and its relations (Hancké 2009: 8). Firms must enter into relationships with a range of other actors (in order to produce and sell goods or services), and therefore they encounter a number of different coordination problems. These can be resolved in either liberal/market-based ways or in coordinated/non-market ways:

- Industrial relations – how firms coordinate bargaining over wages and working conditions. Wage negotiations in LMEs to take place more often at the firm rather than sector, industrial or national levels, which is where they occur in CMEs (due to stronger trade unions).
- Vocational training and education – how firms secure a suitable workforce, and how workers decide on investing in skills. LME workers tend to have more general, transferable skills, allowing them to switch jobs more easily, while in CMEs workers have more specific skills tailored to an employer or industry.
- Corporate governance – how firms are financed and controlled. LME firms are funded more through share investments, and therefore pay attention to their capital market valuation, while in CMEs, firms have access to more patient capital thanks to dense networks which link them to investors or banks; this allows them to invest in longer-term projects based on incremental innovation.
- Inter-firm relations – how firms coordinate with suppliers and buyers. In LMEs, relationships between firms are based on markets and spot contracts, while in CMEs, relationships are more based on longer-term partnerships that encourage technology transfer.¹⁶
- Employee relationships – how firms elicit employees' cooperation and ensure their competency. In LMEs, firms rely on employees' transferable skills and shorter contracts (hiring and firing), while in CMEs, firms foster specific skills and have longer-term employment contracts and stronger workforce representation in decision-making.

The key explanation for these differences is that arrangements for solving one coordination problem will be congruent with certain arrangements for another. For instance, a firm with longer-term, patient capital will have a greater interest in entering into longer-term contracts with more specialised employees, and will engage in longer-term arrangements with buyers and suppliers – which again strengthens the case for longer-term capital, and so on. These complementarities, Hall and Soskice argue, explain why entire countries come to have distinct *varieties* of capitalism. The 'comparative institutional advantage' of certain arrangements then leads nations to specialise in producing certain goods and services, and to follow different trajectories of innovation – radical innovation in LMEs, incremental in CMEs.

Strikingly absent from this explanation is the state, however, as Schmidt (2009) points out. In her call for 'bringing the state back in yet again', she argues that a third distinct variety should

¹⁶ In LMEs, technology and knowledge transfers happen more often through transfer (poaching) of personnel.

be recognised: state-influenced market economies,¹⁷ such as France, Italy, Spain, Korea and Taiwan (which includes two countries understood as developmental states). But also, Schmidt points out that in all varieties of capitalism the state has power over the institutional arrangements that the VoC framework generally derives from firms' interests and interactions. The state matters in four key ways:

- it constitutes a *setting* in which economic actors act (the nation state and its borders)
- the *polity* of the state (its form, for instance centralised or dispersed/federal) affects the economy
- the state makes economic *policy* (substantive political activity: *faire, laissez-faire*, etc.)
- the state is *politics* (an arena of discourse over the practicalities and principles of how the economy works).

Thus, the VoC literature offers poignant insights into why countries may not only have very different business–business relations, but also very different state–business relations. These depend on the way the state structurally acts as a setting and is constituted, but also which interests are reflected in the policy processes of the state and how the power of state politics shapes business.

Given its origins in explaining the political economy of successful (i.e. rich) capitalist countries, some caution may be advised in taking cues from the VoC framework for our analysis. But the proposition of 'institutional comparative advantage' is very compelling and focuses our attention onto how state–business relations may not only be shaped by institutions, but also may create institutional settings which either reduce firms' coordination problems (through creating coherent institutions) or exacerbate them (through institutions that contradict each other). For instance, while a developing country's government may have a logical interest in fostering specialist skills development and stable labour relationships, this might fail to create growth or employment if the main employers are footloose firms that operate on short-term inter-firm contracts and are financed by impatient capital. State–business relations, the VoC literature suggests, shape institutional coherence.

3.3.2 State authority

Bob Jessop (2001) summarises half a century of theorising about the state, and concludes it to be 'an emergent, partial and unstable system that is interdependent with other systems in a complex social order' (Jessop 2001: 166–67). The power of states under capitalism is far from absolute, and their interests are indeterminate and interdepend with others'. The review concludes with five themes which offer highly valuable pointers for us: firstly, to pay attention to the heterogeneity of different states; secondly, that states have differing capacity which shapes how they can negotiate with businesses; thirdly, globalisation has seen some businesses truly 'go global', while states have generally retained a national jurisdiction; fourthly, the changing scale of politics means that important interactions between state and business now also happen at the supra-national level; fifth, many regulatory and political factors shaping business fall into a grey area of 'governance', characterised by neither government hierarchy nor market anarchy. Yet while such a contextualisation of the state is important, it draws attention away from its unique authority. Weber (1978: 54) famously defined the state as that body which possessed the '*monopoly* of the *legitimate* use of physical force' to enforce its order,¹⁸ and in his oeuvre on the relationships between economy and society he placed a key focus on the state. Yet while Weber never systematically

¹⁷ These are characterised by a strong role of the state in shaping the economy – in a positive or a hindering manner – for instance, by shaping industrial relations or orchestrating reforms and adjustments to promote economic competitiveness. In such economies, it is the state rather than the interactions of firms that determines the shape of (for instance) employer–union relations, corporate finance or firms' skills regimes.

¹⁸ While this is the defining feature of the state, it by no means suggests violence to be the sole or most common method of statecraft for Weber.

clarified the relationship between state and economy,¹⁹ his thinking about the different types of authority, and his theorisation of modern state bureaucracies have proven to be lasting influences particularly on normative analyses of state–business relations.

Weber (1978: 216–45) argued there were three types of ‘legitimate’ authority: *rational*, or legally justified; *traditional* (i.e. it has always been done this way); and *charismatic*, built on devotion to individual leaders. Rational authority was central to modernity, Weber (1978: 224) contended, because capitalist production has an ‘urgent need for stable, strict, intensive and calculable administration’, and bureaucratic administration is key to the exercise of rational authority. He highlighted that rational-legal authority was the quintessential modern form of administration for nation-states and business organisations alike, being predictable and goal-rational, unlike charismatic and traditional rule.²⁰ A rational bureaucracy, in Weber’s (1978: 220–1) definition, is characterised by a well-defined hierarchy, meritocratic recruitment, professionalism (career administrators), and decisions being bound by clearly defined rules (the decision-makers have little effectively to decide).

Evans and Rauch (1999) found that the ‘Weberianness’ of states (operationalised in their case only as meritocratic recruitment and predictable long-term career rewards) is indeed an important, empirically measurable determinant of countries’ GDP growth. Drawing on Weber’s theories, the quality of bureaucracies – their ability to effectively translate government decisions into action – is an important factor in shaping state–business relations. Not only do Weberian states have more ability to exert power, but also a predictable, meritocratic state apparatus is likely a far better partner (or master) for business than a poorly functioning bureaucracy.

3.3.3 Business authority

Lindblom (1977) also refers to state hierarchy and authority. He points out that even in authoritarian states there are rarely times when one leader at the apex of a pyramid exerts power in a linear fashion down the hierarchy; in reality, multiple branches of government influence decisions, often with specialised authorities or personnel that cut across them. In market systems, power is further dispersed since states cannot, for example, mandate investment. In these systems, business is also an ‘authority’ that makes choices around technology, the organisation and structure of work and markets, and resource allocation. Public affairs (decisions that affect society) are in practice determined by two sets of authorities – state and business – which both have power and both pursue their own interests. As a result of this interdependence, ‘mutual adjustment among authorities’ is required in which each actor uses means such as exchange, persuasion and favours to influence the other, as in a process of negotiation. ‘Collaboration and deference’ between these authorities is therefore at the heart of politics (Lindblom 1977: 175).

While Lindblom’s analysis explains forcefully why state–business relations matter, Haggard *et al.* (1997) contend that this structural power of capital in market economies is not the whole story. While all capitalists may share some interests, such as the protection of private property or policies that encourage investment, on many (if not most) issues, there are divergent interests, for instance between sectors or between firms (exporters versus importers) in one sector. Table 3.1 outlines five ways in which, following Haggard *et al.* (1997), business and its relations with states are conceptualised. It shows how the different

¹⁹ In fact, his few direct statements on the matter may even be misleading. In his exploration of how political bodies are funded, for instance, Weber argued that revenue-raising (taxation) was the *key* connection between the state and business (Weber 1978: 194).

²⁰ Charismatic and traditional authority continue to exist, however, and may play a very important role in shaping state–business relations. Some stories of successful national late capitalist development, for instance, hinge on the charismatic authority of ‘father of the nation’ figures, such as Lee Kwan Yew in Singapore. While traditional authority is likely to hinder development and change, nonetheless some resource-rich traditionalist monarchies have also grown rapidly.

levels of aggregation or disaggregation of ‘business’ matter in shaping (and analysing) its relations with the state. The table begins with the most aggregated viewpoints.

Table 3.1 Theories of business

Business as ‘capital’	<ul style="list-style-type: none"> • All businesses share the same interests. • Capital ‘votes twice’: through lobbying, and deciding on investment. • The structural power of capital constrains the state; however, this can be positive where it constrains a predatory state.
Business as ‘sector’	<ul style="list-style-type: none"> • Sector composition and representation in the political system affect state–business relations. • Business sectors share common interests; however, the free-rider problem means that businesses do not necessarily act collectively. • Contending interests of different sectors constrain the state.
Business as ‘firm’	<ul style="list-style-type: none"> • Firm size (concentration) and diversity (conglomeration) matter. • Multi-sector conglomerates have diverse interests and may support changing policy priorities. • Ownership and how firms acquire capital (family, foreign, shareholder) may also be important.
Business as ‘association’	<ul style="list-style-type: none"> • Business associations matter: if a small number of businesses with large economic weight organise, their power is great. • Associations can be rent-seeking but ‘encompassing multi-sectoral associations’ can limit pursuit of particularistic interests.
Business (and government) as ‘network’	<ul style="list-style-type: none"> • Embedded autonomy and the developmental state. • Networks between business and government can represent clientelism. • Repeated interaction leads to trust and cooperation, but no guarantee of ‘good’ policy. • Sanctions ensure compliance (avoiding free-rider problems).

Source: Authors’ own, based on Haggard *et al.* (1997: 38–57).

The perspectives of Lindblom and Haggard *et al.* serve as a reminder that, in market economies, an analysis of state–business relations which focuses only on state authority and its capacity to coordinate and influence business misses the interactions which mediate states’ and businesses’ power and their interests. Business must also be understood as an ‘authority’ in the sense of having the power to make decisions that affect the public. Yet neither business nor the state is monolithic, and an ongoing process of mutual adjustment, or negotiation, shaped by how their interests are aggregated, leads to policy outcomes.

3.3.4 State–business relations and the balance of power

With both state and business exercising authority, state–business relations appear as a terrain of contestation over who shapes the economy and its trajectory. This point is made strongly by Mariana Mazzucato (2013), whose thesis of an ‘entrepreneurial state’ as the core driver of innovation (in the United States) points to the interdependence and power struggles in state–business relations. While government spending fuelled America’s economic leadership through breakthrough technologies, for instance in digital innovation (among other things through research funds, incentives and technology transfers), the state has been unsuccessful at negotiating for its share of the subsequent spoils.

The question of relative state–business power in shaping innovation (as part of economic development) harks back to Joseph Schumpeter’s (2003 [1942]) foregrounding of the figure of the entrepreneur as the driver of ‘creative destruction’. Schumpeter believed – much like Marx – that capital tended over time to centralise into trusts and monopolies, and therefore gradually the heroic, dynamic type of entrepreneurs who had shaped earlier stages of capitalist development would be disempowered by technocratic corporate and state

bureaucracies. However, as Alexander Ebner (2009) shows, Schumpeter noted the state could play a key role in economic development through facilitating entrepreneurship, and even sometimes act entrepreneurially itself – as Mazzucato has elucidated – to overcome collective action problems in innovation and to encourage innovation and technology adoption via selective financing (Ebner 2009: 373–5).²¹ But Schumpeter feared this would come at the expense of private sector entrepreneurship, with a more powerful state stifling the interests of businessmen.

Marx broadly regarded the state as a manager of the class balance under capitalism (Elster 1985: 426), a notion fleshed out by many theorists including Antonio Gramsci. Gramsci's writings suggest states and businesses are interdependent and pursue their aims through a combination of coercion and consent, strongly suggestive of an ongoing process of negotiation between entities with power and interests. A Gramscian reading of different economic formations – such as Fordism, developmentalism and neoliberalism, as well as different national development models²² – suggests these to be temporary historical compromises between different forces in society, which take the shape of distinct state–business relations. Gramsci warned against misreading the state as an autonomous steering entity (Gramsci *et al.* 1998: 243–5), and referred to this 'fetishism' as 'statolatry' (Gramsci *et al.* 1988: 237–8); a fallacy which, interestingly, both neoliberal and state-led theories of development fall for when they assume state and business can be separated.

Another key line of thought suggestive of state–business relations as power balances comes from Karl Polanyi, whose idea of social embeddedness has gained considerable traction in political economy. Polanyi's embeddedness notion goes beyond the more familiar idea of market transactions requiring trust, mutual understanding and legal enforcement (Block 2001: xxiv), and rather suggests market relations to be necessarily embedded in (that is: subordinated to) society itself. The key way in which market relations are embedded in the modern age is through the policies of the state, which (often haphazardly) works to counteract the constant interest of businesses in marketing everything as commodities; which, if it were achieved, Polanyi (2001: 3) says would risk 'annihilating the human and natural substance of society'. This perspective suggests that the state and the economic elites (business) cannot ever fully overpower one another – if they did, the results for capital accumulation and society would be disastrous. Rather, states and businesses stand in a complex dialectical relationship of conflict over power and co-dependency for power. In a Polanyian reading, state–business relations may then be seen as negotiating the political balance needed to reconcile economic change with the protection of the social foundations of the economy.

3.4 Some conclusions from the literature

Much more could be said about the vast literature on the relationships between the state and business and how they affect development. For practical reasons, we have focused this review narrowly on the developmental states literature and recent work that highlights some characteristics and effects of 'effective' state–business relations, as well as a snapshot of key theoretical perspectives on the political economy of state and business. In a broader review in future we may hope also to capture further insights from literatures that were beyond the scope here.

What can we learn from the reviewed literatures? First, the developmental states and 'effective state–business relations' literature highlights the importance of institutions for coordination of policy with business objectives – 'embedded autonomy', 'infrastructural

²¹ Ebner (2009: 385) suggests the East Asian 'miracle' was a case of a Schumpeterian 'entrepreneurial state... carrying out the entrepreneurial function of introducing novelty'.

²² Gramsci deals specifically at length with Fordism; developmentalism and neoliberalism came after his time.

power', etc. There is a strong emphasis on coordination through formal institutions (and some informal ones), and formal institutions explain some growth successes. At the same time, the notion of the developmental state risks increasingly becoming a buzzword if apolitical notions of coordination or collaboration eclipse questions about power and interests. Several of our case studies show how formal institutions matter but are often not enough to explain outcomes.

Second, state–business relations reflect or embody a balance of power between different interests, as many contributions highlight, be this between state and business authority (Weber, Lindblom), entrepreneurs and government (Schumpeter, Mazzucato), or capital and labour (Gramsci, Polanyi). States and businesses may be weaker or stronger, but there are unresolved questions around how their interests are aggregated, and which (or whose) interests are reflected in state–business relations. Neither the state nor business is a monolith ('statolatry', business as 'capital'), and they themselves must be unpacked.

Third, the diversity of existing state–business relations cautions against the idea that 'good' state–business relations can be implanted from one context to another, as does the notion of coherence between institutional spheres, which the VoC literature introduces. Furthermore, viewing development outcomes more broadly than economic growth calls into question what kind of state–business relations may qualify as 'good' at all. This lends credence to our focus on non-prescriptively evaluating state–business relations in this report.

Fourth, much of the literature focuses on the structures (or institutions) of state–business relations, and says less about the process. As we said in Section 2, process and agency are important, too, for understanding how state–business relations shape developmental outcomes in practice. This is clearly an issue more for in-depth case studies rather than grand theory, and one which we seek to reflect more strongly in our case studies in Section 4, each of which traces the processes in specific episodes of change.

4 Four case studies of state–business relations

4.1 Introduction

Four case studies underpin our exploration of state–business relations in development, and our synthesis of common themes and lessons (Section 5). Our full case studies appear in the annexes, while this section presents a summary as follows:

- Case 1: Export-oriented growth and democratic transition in Chile
- Case 2: Food fortification and the nutrition agenda in Tanzania
- Case 3: The creation of a financial inclusion sector in India
- Case 4: Private commercial farms and public land in Ethiopia

As summarised in Table 4.1, these four cases cover a considerable breadth of state–business relations in developing, emerging and middle-income economies, representing episodes of recent change. They showcase state–business relations in a range of economic and social development policy areas.

Table 4.1 Characteristics of the case studies

	Case 1: Chile	Case 2: Tanzania	Case 3: India	Case 4: Ethiopia
Economic and political system ²³	Democratic (post-dictatorship); liberal market economy	Multi-party democracy (recent); mostly market economy	Mass democracy, clientelist; market-oriented with state role in parts of economy	Single-party dominated state; mixed economy
Level of economic development	Upper-middle/high income	Low income	Lower-middle income (BRIC)	Low income
Timeline	1990 to 2006	2009 to present	mid-1980s to present	2001 to present
Public policy goal	Export-oriented growth	Combating malnutrition via food fortification	Creation of a more ‘inclusive’ financial system	Economic growth and development; structural change in agriculture

4.2 Case study 1: Export-oriented growth and democratic transition in Chile

This case study examines two sets of state–business relations that contributed to Chile’s high rate of export-oriented growth and increasing trade openness following the return to democracy in the 1990s. While this was a period when relations were uneasy and trust between the government and business was low, a mutual fear of instability – economic and political – opened the door to dialogue.

In the first set of interactions, DIRECON, Chile’s government trade agency, engaged business, particularly the peak manufacturing association, SOFOFA, and labour, in trade policy fora and other processes through which they received briefings and provided advice on trade negotiations. While initially business and labour participated in the same processes, their significantly differing interests led to increasingly ineffective engagement and ultimately a shift to labour and business being consulted separately. The net result of these interactions was to create shared knowledge, preferences and technical expertise between business and state representatives, as well as personal relationships of trust. Labour, on the other hand, saw its influence wane. In the second set of interactions, CORFO, Chile’s economic

²³ Based on authors’ own assessments of the economic and political system.

development agency, coordinated the upgrading of groups of agro-industry firms, particularly small and medium enterprises (SMEs). Through these processes, CORFO supported sectors to reorganise production, improve standards and upgrade productive capabilities, leading to improved export competitiveness. At the same time, these changes saw a shift to more seasonal and non-unionised jobs in the countryside and a loss of landholdings for rural smallholders.

Overall, the outcomes of these state–business relations in Chile include a more competitive and outward-looking economy, with a number of new free trade agreements signed and exports growing from 23 per cent of GDP in the early 1980s to 42 per cent by 2006. However, the marginalisation of labour – and later also environmental groups – compared to the close state–business relations has opened the way for measures (dispute settlement rules) that could weaken labour and environmental regulation. The quality of jobs and livelihoods in the countryside has also been negatively impacted.

Please refer to Annex A for the full case study.

4.3 Case study 2: Food fortification and the nutrition agenda in Tanzania

This case study examines a state-led multi-stakeholder strategy, where the government in Tanzania sought to leverage private sector resources and skills to achieve a public policy goal: enhancing the nutrition of the general population. However, the interactions excluded a key class of actors and created an outcome that missed its mark.

The government sought to reduce undernutrition via the establishment of the Food Fortification Action Plan, among other initiatives, which set regulations to require the food industry in Tanzania to fortify all flour (wheat and maize) and locally processed edible oil. From the outset, the Fortification Plan was encouraged by international aid donors (particularly the World Bank) and designed through a multi-stakeholder process with multiple ministries, international donor agencies and large-scale domestic manufacturing firms. It was championed by the President and aligned with high-level (national and international) political support for the nutrition agenda. While these negotiations managed successfully to leverage the organised wheat flour industry's resources and engage larger firms to fortify their products, the outcomes for the population were mixed, as the diffuse maize sector, comprised of SMEs, is non-compliant. While improvements in micronutrient fortification of some staple foods was achieved, these fail to reach the urban and rural poor who consume maize flour produced by these small mills.

The 'multi-sector strategy' had *de facto* excluded small-scale millers and small farmers, as the agenda was set by the ruling party, international agencies and large businesses. The idea of fortification with industrially produced nutrients was supported by international donors, but pushed the nutrition agenda in a direction where the interests of the state aligned with a few large domestic manufacturers (wheat producers), rather than with the vast majority of small enterprises (maize producers) who produce most of the food which reaches poor communities. Had small food producers been brought to the table, or had the nutrition agenda not been set to focus so strongly on industrial food fortification, the aim of improving access to nutritious food would possibly have been pursued more effectively. In this case, the results achieved were enhanced business reputations for larger firms in the private sector, increased expenditure on the government side, but little or no impact for the poor and the informal sector.

Please refer to Annex B for the full case study.

4.4 Case study 3: The creation of a financial inclusion sector in India

This case study examines the drive for financial inclusion in India, first through self-help groups (SHGs), then microfinance institutions (MFIs), and recently, state-driven mass banking programmes. SHGs are semi-formal organisations of women, assembled to collectively access formal banking services; they emerged in the 1980s and have been supported by state governments and parastatal organisations. Commercial MFIs emerged in the early 2000s and grew rapidly, thanks to supportive policies, deregulation, a singular policy focus on credit, and financial support received from commercial banks, state governments and investors. Since 2011, the Indian central government has launched several mass banking initiatives to bring about universal financial service coverage, working particularly through large public banks to extend accounts, insurance services, debit cards, and overdrafts.

The state in India, working with and through business actors (in different constellations), has thus consistently since the 1980s worked to increase market-based financial access for poor people; a case of state activism. However, state–business relations also showed interdependence, with the state needing capital from the financial sector to pursue its social policy goals, and the financial sector in turn seeking permissive regulation, policy support and public sector funding. The requisite interactions were largely built on informal elite networks and a shared broad consensus that financial expansion and hands-off regulation were necessary. For many years, the Reserve Bank of India was a key broker in these interactions, and only recently central government has asserted more regulatory authority through forceful initiatives to speed up financial inclusion. The shared vision that financial access should bring modernity and pro-poor growth was a key factor in facilitating the (shape-shifting but consistent) collaborations of state and business actors.

The results of these efforts have included a massive growth of micro-lending in India – from US\$500m (2005) to US\$5.5bn (2010) – a deeper reach by banks and other formal finance institutions, and tens of millions of new accounts (although many remain dormant). But also, a lack of evidence persists that financial access has ameliorated poverty in India, and there have been major episodes of social unrest and economic insecurity linked to microfinance.

Please refer to Annex C for the full case study.

4.5 Case study 4: Private commercial farms and public land in Ethiopia

This case study explores state–business relations in a two-pronged farm commercialisation strategy in Ethiopia since the turn of the century: cut flowers, and large-scale food and biofuel crops farming. Emulating the ‘developmental state’ approach, the Ethiopian government exerted an active role, creating formal institutions and using these to enlist business; the idea of ‘developmentalism’ proving malleable enough to accommodate an agriculture-based (rather than industry-based) economic development programme. These efforts formed part of longer-term strategy to transform what was largely subsistence agriculture through commercialisation for national economic growth and development.

State activism and business diplomacy were directed mainly at international businesses, and negotiations focused on subsidised access to state-controlled land and various tax incentives in exchange for business investment, technology and expertise to produce growth and development. Key players in the cut flower sector were the Ethiopian Horticulture Producer Exporters Association (EHPEA) on the business side and its public counterpart, the Ethiopian Horticulture Development Agency (EHDA). While large commercial farms were facilitated by the Agricultural Investment Land Administration Agency (AILAA), businesses

did not have a formal agency through which to interact with the government. Government and businesses negotiated agreements individually or through their representative bodies on land leases and investment. Moreover, indigenous communities, national and international non-governmental organisations, and research organisations contested the policy and its execution and shaped and reshaped state–business relations.

State–business relations over commercial farming in Ethiopia produced a vibrant cut flower sector of more than 100 farms, which generated in excess of 50,000 jobs and US\$1bn in export revenue. The jobs created were especially for women and in urban and peri-urban areas with acute employment challenges. On the other hand, many of the 400-plus large-scale farms licenced to produce food and biofuel crops for export either did not start or started at a much smaller scale than planned, hence vast areas of land remained unutilised. In some places the farms displaced communities and rendered them landless, and have been accused of contributing to deforestation.

Please refer to Annex D for the full case study.

5 Synthesis of the case studies

5.1 Case overview: state–business relations at the centre

While the cases highlight the diversity of state–business relations, this section synthesises the evidence to reveal common themes and draw preliminary lessons. In different ways these case studies overturn conventional wisdom about the business or state forces at work in particular areas of development. What at first sight appears to be a business-led initiative often turns out to be one strongly shaped by the state. In other cases, where the state is typically seen as leading, it may actually be following. Chile, for example, is hardly known as a stereotypical developmental state. If anything, given its recent economic history as a neoliberal poster-child, a minimalistic ‘hands-off’ state engagement with business may be expected. However, state–business relations in Chile were marked by a strong coordinative form of engagement. The case of food fortification in Tanzania is one where, in an almost model ‘multi-sector strategy’, the state sought to leverage private sector resources and skills to achieve a public policy goal. However, to the extent that the state–business relations here may be understood as negotiations, they excluded a key class of actors and created a negotiated outcome that missed its mark. At first sight, the creation of a private commercial agricultural export sector in Ethiopia comes with all the hallmarks of the developmental state: a strong government exerting active control over the development agenda, creating formal institutions, and using these to enlist organised business into longer-term strategies for national economic growth. But the case’s details expose that the developmental state can be as much an aspirational idea as a reality, especially where weak state–business relationships fail to drive investment.

5.2 Main themes and features of the four cases

This section draws out the main features of state–business relations as they developed in our four cases. We start with three cross-cutting themes. The first is a clear interdependence between business and state actors – the need for joint action or an exchange of resources – acting as a catalyst for negotiation and cooperation. However, whether the nature of the cooperation so achieved should be understood as collaboration or collusion remains an outstanding question. The second relates to the negotiation process; which in our cases evolved as either involving a network of actors in an ongoing policy dialogue, or a more direct *quid pro quo* exchange in response to policy priorities. The third is the reflection that not only power and interests shape negotiations, but also ideas and ideologies. We also present three insights or features of state–business relations that are reflected in a number of the cases: the issue of which actors were included (or excluded) from the negotiation, the role of international actors and multi-level governance networks, and the ongoing relevance of informal institutions.

5.2.1 Interdependence as a catalyst for negotiation

All four cases are firmly situated in the realm of negotiation at the core of Figure 2.2; mostly towards the top right quadrant. While the cases contain elements or aspects of the other quadrants, none drifted into open conflict, domination or control. None of the negotiations broke down completely. Nor were there clear cases of ‘capture’ or ‘control’ by one party over the other. In Tanzania, for example, while the government directly mandated change (fortification) through regulation, this policy was based on an agenda set through a multi-stakeholder process involving the ruling party, international agencies and large businesses.

Table 5.1 Synthesis summary of the case studies

	Case 1: Export-oriented growth and democratic transition in Chile	Case 2: Food fortification and the nutrition agenda in Tanzania	Case 3: Creation of a financial inclusion sector in India	Case 4: Private commercial farms and public land in Ethiopia
Core state and business actors	State: Key agencies from the Ministries of Economy and Foreign Affairs (CORFO, DIRECON) Business: Peak industry association (SOFOFA), clusters of SMEs in agriculture Others: Labour	State: President, Ministries of Health, Agriculture, Trade, regulator (TFDA) Business: large food processors Others: Donors (e.g. World Bank, USAID), UN agencies	State: Central executive, Central Bank (RBI), public banks, state governments, specialist bank (NABARD) Business: commercial banks, microfinance institutions, financial investors Others: semi-formal associations (SHGs)	State: Key agency under the Ministry of Agriculture and Rural Development (AILAAA); and an autonomous government body (EHDA) Business: Sectoral association for horticulture (EHPEA), large firms, especially from diaspora
Structure of state–business interaction	Corporatist. Sectoral <i>peak association</i> and <i>powerful state agency</i> engaged to negotiate trade policy. <i>Clusters</i> of 8 to 15 SMEs in agriculture supported by highly <i>specialised agency</i> to invest in upgrading.	<i>Food fortification policy platform</i> with multiple <i>ministries, international donor agencies</i> and <i>large-scale domestic firms</i> . <i>President</i> champions the initiative.	<i>Informal elite relationships</i> with <i>consensus</i> between political and business elite on need for financial expansion. <i>State seeks capital</i> to pursue social policy goals; <i>business seeks permissive regulation, policy support and funding</i> .	State agencies court firms and steer private investment; central agencies <i>trade land access in return for capital and expertise</i> .
Process of state–business interaction?	<i>Structured, routinised and repeated</i> interactions, supported by <i>informal relationships</i> with interchange of staff led to trade policy network. <i>Coordination</i> of SMEs to <i>overcome collective action problem</i> .	<i>Multi-stakeholder process</i> . Government offers incentives and support <i>to facilitate</i> private sector investment to achieve a public policy goal, encouraged by international donors.	<i>State activism</i> . State policy directives set ‘national mission’ for financial inclusion; with policy support, direct state action and hands-off regulation.	<i>State activism and diplomacy</i> directed at international business. Indigenous communities, NGOs and research organisations contested policy and its execution, and shaped and reshaped domestic state–business relations.
Influential ideas and ideologies	Shared state–business interest in maintaining economic and political stability; common policy positions develop over time.	High-level political support for nutrition agenda.	Financial inclusion as a means to achieve modernity and pro-poor growth.	State seeks to emulate ‘developmental states’ by transforming agriculture through commercialisation, growth and development.

Box 5.1 The role of the state and business in China's engagement in Africa

In line with much of the literature, our four case studies analyse state–business relations predominately at the national level. However, state–business relations are also multi-layered. Here we explore how state–business relations in China influence investment in Africa; a familiar story that is much more complicated than is generally recognised. Certainly, the role the Chinese state and its 'state capitalism' plays in Africa's development is contentious; opinion is divided between those who see China's role as rapacious, even colonial, with asymmetrical and unstable relations (Clinton 2011; Fisher 2011), and those who see China as a developmental role model of partnership and mutual benefit (Renard 2011; Diaw and Lessoua 2013; Gu and Carty 2014). The reality is that China's overseas investment by state-owned enterprises (SOEs) is multi-layered and complex (Gu and Schiere 2011; Bräutigam and Zhang 2013; Chintu and Williamson 2013). Chinese businesses are flexible, pragmatic, less risk-averse and with longer horizons than northern counterparts (Chintu and Williamson 2013); state–business relations within China are diverse and disaggregated, operating at provincial as well as national levels; while relations between Chinese businesses and African states are mostly informal and uncoordinated.

Core actors in China's economic development experience

The private sector is the new driving force of the Chinese economy. The renaissance of Chinese manufacturing, creation of a major service sector, including financial and banking industries, an intensification in the operations of megalithic SOEs in the energy, mineral and agribusiness industries, and the emergence of business associations are key features. State–business relations within China work through patterns of informal or indirect influence, for example through the opening up of party membership to successful private business leaders. Notable too, is the growing importance of Chambers of Commerce in policy advocacy, fulfilling party-state needs for liaison with private business, and acting as important intermediaries for promoting trade and, latterly, China's policy of encouraging enterprises to 'go out' to overseas markets.

Role of the Chinese state towards Chinese business in Africa

The Chinese state's role *vis-à-vis* business in Africa is substantial; but is contextual rather than directive. Change is driven by actual business practices, within the context of overall strategic state control. The government's policy framework provides the context, authority and legitimacy for Chinese firms to go to Africa, based on the 'Africa Policy' and the 'Going-global' policy. A key challenge, however, is a perceived gap between state policy formulation and implementation; that is, between the publicly stated national goals of China and the African states, and the actual competitive realities of business practices facing Chinese firms in Africa (Gu 2009, 2011; Bräutigam and Zhang 2013). While the Chinese state has a strong, dedicated, interlocking institutional network of agencies at home to support firms 'going out' to Africa, the principal sources of information are frequently friends, networking introductions and businesses' own research and trading experiences. These are only then followed by central government, embassies and local Chinese community networks in Africa, and finally Chinese local government or other local firms (Gu and Carty 2014; Gu *et al.* 2016).

Conclusion

There is a pressing need to better understand China's engagement in Africa, shifting the focus beyond the central state. Chinese firms (state-owned and private) play a key role; operating principally to their own commercial priorities; notwithstanding government and party ownerships, policies and strictures. Processes are informal, unplanned, negotiated, decentralised, uncoordinated and diversified. All embed 'the state', but in different ways and to varying degrees, adding to the complexity of explaining state–business–state relations between China and Africa.

Our cases demonstrate an interdependence between business and state actors, leading them to negotiate common solutions or to exchange resources (financial resources, as well as information, skills, expertise and support), based on a degree of balanced – though not equal – power and shared objectives. In Chile, for example, CORFO wanted to change the behaviour of small agro-processing businesses in order to achieve growth objectives, while business sought resources and state support to invest in upgrading. In India, the state needed capital to pursue social policy goals, and enabled (variously) microfinance and mass banking initiatives, while bringing the poor to the financial market, initially through self-help groups. In Ethiopia, the government aimed at attracting capital, technology and expertise, as well as creating jobs, expanding food production and reducing poverty, while business sought land and a supportive policy environment.

If most of the cases sit towards the bottom left corner of the matrix, are these negotiated settlements best described as ‘collaboration’ or ‘collusion’? Both terms suggest cooperation between actors for mutual benefit; however, in collusion this benefit comes at the detriment of other actors, who do not have the same opportunities to participate or otherwise secure outcomes in their favour. Collaboration and collusion are therefore distinguished by the process (who has the opportunities to participate or have their interests represented?) and the outcome (who is affected, who benefits?).

Process conditions to address participation and representation suggested by our review of the literature include mechanisms that enable transparency, accountability of negotiators to their constituency, effective competition policy and the presence of a Weberian bureaucracy insulated from particular interests. Yet defining non-collusive interactions based on these factors sets an unrealistically high bar that (for many reasons) is unlikely to be met in many developing countries, and cannot easily be manufactured. To quote Rodrik (2013: 31), only slightly out of context, such prescriptions would essentially suggest, ‘if you want to become rich, you need to look like rich countries’. Rodrik’s prescription for growth advocates instead heterodox ‘second-best’ strategies. More analysis is needed of the types of second-best strategies that work in different contexts to foster collaborative rather than collusive state–business relations. The second factor that distinguishes collusion from collaboration is outcomes, and who benefits from state–business relations. We come back to outcomes in the next section.

5.2.2 Negotiation processes

We identify two broad types of (sometimes overlapping) processes at play in the four cases of state–business relations:

Integrative or networked negotiation: Some of the cases reflect Haggard *et al.*’s (1997) category of ‘business and government as a network’. Through repeat interactions, these networks of business and state actors coordinate; share information and technical expertise; develop collective learning and consensus about preferences; and negotiate shared policy proposals over time. In Chile’s trade policy network, for example, although relationships started on shaky ground, they were consolidated through the process of trade negotiations. In India, the push for financial inclusion involved elite actors with a common vision of a modern and broad-based financial sector, although based on different underlying interests. The state saw more equitable financial access as a palliative for social inequality, while business interests focused on acquiring new clients. The importance of networked policy dialogue and agenda setting suggests paying closer attention to ‘who knows whom’, and where and how they interact, in studying state–business relations. But the notion of networked interaction should not distract from issues of relative power. Box 5.1 points to information flow and collaboration as part of a competition for dominance as ‘networked hierarchy’ (Lin and Milhaupt 2013) which in China means that success in business leads to rewards in the political realm and vice versa.

Policy-directed concession-exchange: While some of the cases reflect networked relations between business and state, in others, coordination is achieved through a focused concession-exchange negotiation of resources. In the case of cut flower farming in Ethiopia, government and business negotiated an agreement through their representative bodies on land leases and investment. The government aimed at attracting capital, technology and expertise, in support of transforming agriculture through commercialisation. The cut flower sector successfully pressed for a five-year sector strategy, access to land and credit, and coordination of transportation for export. In Chile, CORFO catalysed a process to work with businesses to improve quality and competitiveness, and used special instruments (PROFOs) to incentivise business cooperation within a geographically based association. The risks here are principal-agent problems where the desired outcome (for example, investment) that represents the goal driving the negotiation is not achieved. The incidences of land speculation in Ethiopia are a case in point. These processes reveal that much of ‘how business does business, and where it does business’ – to paraphrase Helen Clark’s quotation from page 1 – is shaped also by negotiations with the state over the implementation of policy.

5.2.3 Ideas matter

Several of the cases suggest that understanding state–business interactions based only on power, interests and processes misses part of the story. Ideas and ideologies also matter. In India, the state’s focus on financial inclusion was partly a reflection of elite actors’ ideas of modernity and social inclusion. In Ethiopia, the idea of developmentalism and emulating successful ‘developmental states’ shaped state–business relations. This vision and narrative fit with Ethiopia’s strong state, and proved malleable enough to accommodate an agriculture-based (rather than industry-based) economic development programme.

Although ideas alone cannot explain or create functional state–business relations, we would suggest that they have very powerful effects in being able to move relations along the vertical axis in the matrix (Figure 2.2). A positive example: the case of Chile illustrates how what, structurally, should have been a relationship of conflict (given the fairly equal power but divergent interests between the nascent democratic regime and the country’s conservative business elites) instead led to stable negotiations. Given the country’s recent history, the idea of maintaining economic and therefore political stability above all else was important, as were smaller, more practical ideas, such as the ‘room next door’ institution which kept business representatives connected to policy discussions. Over time, through the emergence of trust and a shared interest in competitiveness, state–business relations in Chile moved gradually closer to true collaboration. The case of Tanzania, meanwhile, suggests the idea that fortification with industrially produced nutrients, which was supported by international donors, pushed negotiations in a direction where the interests of the state aligned with large domestic manufacturers, rather than the majority of small enterprises that produce the food that reaches poor communities.

5.2.4 Other features: international actors, informal institutions, engaging the right actors

There are three other striking insights that cut across more than one case and provide pointers for further research and analysis of state–business relations:

- In countries that were unable to mobilise sufficient domestic resources, notably Ethiopia and Tanzania, **international actors and multi-level governance networks** affect domestic state–business relations. In Tanzania, where approximately one-third of government spending was financed by donor funds, international donors were a key actor; while in Ethiopia, the government brought international and diaspora investors to the table through diplomatic missions in major capital cities. This is also a key message from Box 5.1, in which ‘going global’ by Chinese agri-business has

been shaped by national and provincial authorities in China. Understanding state–business relations means also analysing the impact of international actors including donors, diasporas, international advisers and NGOs. State–business relations, if they ever were, are no longer just domestic affairs.

- It is obvious, yet important, to point out that successful outcomes of state–business relations require *engaging the right actors* for given policy objectives. The Tanzania case, for example, raises the question of why the negotiation focused on large businesses involved in wheat fortification, when it should have been apparent that these businesses were not involved in the markets of the poorest. Clearly, negotiations with large companies within a concentrated sector is less costly and complex than attempting to engage a very diffuse sector of micro- and small-scale millers. Yet working with the actors that have the right tools for the challenge is paramount. While much of the literature emphasises business associations as key contributors to effective state–business relations, associations can also be rent-seeking, and doubts have arisen as to whether the role of associations is overstated. The question for research is how state–business relations should be understood and analysed in relation to small firms that nevertheless hold the key to policy objectives.
- *An analysis of informal institutions is needed.* Earlier studies of state–business relations have acknowledged the importance of informal institutions. These include not only extra- formal networks, but also shared cultural-cognitive and normative frames, which relates to the power of ideas (above). However, despite acknowledging the relevance of the informal, methodological challenges have meant that quantitative studies tend to focus only on formal institutions. Case study approaches, while better at taking into account informal institutions, see these mostly as stepping stones to more formal structures. Our cases suggest that informal institutions continue to be important and more pervasive than has generally been recognised. For example, the Chile case shows how repeated formal interactions can generate informal and personalised relationships of trust, loyalty and friendship, which matter even when they are embedded in formal structures.

5.3 Development outcomes

The aim of our work is not simply to analyse state–business relations in developing countries, but to build understanding of how these relations impact development. While the literature highlights that repeated interactions between business and the state can lead to trust and cooperation, cooperation is no guarantee that good policy and development will result. While some existing studies also correlate interactions with development outcomes, these focus overwhelmingly on economic development and aspects such as investment, trade and growth. We, too, look at these elements. However, growth is not enough for development if the benefits are severely unequal or are achieved at the expense of actors who lack the opportunity to secure outcomes in their favour. Such state–business relations may be better understood as collusive than collaborative.

There are different ways in which broader development outcomes could be assessed, in terms of food security or job creation, for example, or in relation to the SDGs – areas that we see as fruitful for future investigation. However, we have chosen to frame our current analysis in terms of three ‘defining challenges and transformations’ articulated by the Institute of Development Studies as being at the heart of the present agenda of global development²⁴ (IDS 2015). These are: to reduce inequalities, to accelerate sustainability, and to build more inclusive and secure societies (as explained in Box 5.2). They encompass different dimensions of development – including social, economic, environmental and political –

²⁴ *Global* development highlights the universality of these challenges and transformations; not only are they challenges which require contributory action from actors around the world, but also the relevant transformations need to be achieved in all countries, not merely those usually identified as ‘developing’.

instead of reducing development to any singular outcome. Considering these transformations supports an analysis of state–business relations that deals with more than the economic implications of business. Their qualitative, broad, interpretive nature opens the space to consider outcomes beyond what the current numerical case data would support, since many of these outcomes are still emergent and uncertain, rather than fully demonstrated, at this stage.

Box 5.2 Development outcomes defined

Economic development. Economic development is often simplistically understood as growth of output. More broadly, it refers to a structural change in a country’s economy, connected to technological and social progress, sectoral upgrading and productivity growth, often measured in terms of economic growth and an increase in average material wellbeing (World Bank 2004).

Reducing inequalities. Inequality has risen markedly in recent decades globally. Recognition is growing that action is needed, particularly by the state, to avoid the harms of inequality. Inequalities are associated with lower wellbeing for the vast majority, vulnerability to shocks, unequal voice and power, and violence and conflict (IDS 2015: 8). Reducing inequalities means not just reducing economic disparities themselves, but also countering the civic/political and social inequalities which are produced by, and in turn reproduce, economic ones (Justino and Moore 2015).

Accelerating sustainability. Recent social and economic advances have come at increasing cost to the environment and climate, from the local to the global level. Accelerating sustainability amounts to reducing those costs and ideally reversing the trend. Technological, social and economic solutions for the transition to a sustainable use of resources are sought by different actors in the public, private and civic sectors (IDS 2015: 9).

Building more inclusive and secure societies. Inclusion is related to inequalities, but here the focus is more on access to and participation in economic and political spaces and processes. Security refers not only to averting conflict and violence, but also to protection from threats and environmental, economic, political and social shocks (IDS 2015: 10). State–business relations can shape inclusion and security directly, where they are addressed to relevant issues, but indirectly in creating socio-economic conditions that are more or less conducive to inclusive and secure societies.

In Table 5.2 we explore the available information on the development impacts of state–business relations in our case studies. We can, in some areas, link state–business relations directly to outcomes. In Tanzania, for instance, the process of state–business negotiation was directly linked to improvements in micronutrient fortification of staple foods; however these failed to reach the urban and rural poor. Had different actors been involved, by bringing small food producers to the table, or had the nutrition agenda not been set to focus so strongly on food fortification, the aim of improving access to nutritious food would have been pursued differently, and possibly more effectively. In Chile, the process of state–business negotiation between CORFO and associations of SMEs improved coordination in the sector, contributing to export competitiveness and significant export growth, and the creation of rural jobs in the process. However, these were non-unionised seasonal jobs, which arguably leave workers in a precarious situation; vulnerable, for example, to volatility in the external market. In other areas, it is difficult to attribute outcomes to the processes observed, such as environmental outcomes in Tanzania and India. This area warrants further exploration.

The picture that emerges from Table 5.2 is twofold. In the economic domain that has been the traditional focus of analysis for work on state–business relations, our findings point to the positive outcomes that state–business relations can help to achieve. Our two cases in this area (Chile and Ethiopia) both demonstrated economic development resulting at least in part from an ongoing negotiation between the state and business. However, viewed with our somewhat wider lens, the trade-offs become apparent. These include casualisation of labour (Chile), exclusion of small-scale farmers (Chile and Ethiopia), and land conflicts (Ethiopia).

Negative environmental impacts are another outcome, although these are disputed in the case of Ethiopia. At one level, these trade-offs are unsurprising or not particularly unique to cases where state–business relations strongly matter. Changes generally create winners and losers. However, to judge the impact of state–business relations, we need to understand the degree to which those not involved in the negotiation reap benefits or suffer losses.

Table 5.2 Mapping developmental outcomes in the four case studies

	Case 1: Export-oriented growth and democratic transition in Chile	Case 2: Food fortification and the nutrition agenda in Tanzania	Case 3: The creation of a financial inclusion sector in India	Case 4: Private commercial farms and public land in Ethiopia
Economic development	<ul style="list-style-type: none"> Exports grew from 10 per cent of GDP (1980s) to 35 per cent (late 1990s). Chile achieved high-income status. 	<i>Unclear</i>	<ul style="list-style-type: none"> Micro-lending grew from US\$500m (2005) to US\$5.5bn (2010). Banks deepened their reach. 	<ul style="list-style-type: none"> More than 100 flower farms set up; more than 50,000 employed. More than US\$1bn export revenue generated.
Building more inclusive and secure societies	<ul style="list-style-type: none"> Rapid growth supported economic and political stability. Pluralist policymaking declined due to exclusion of labour and (later) environmental groups. 	<ul style="list-style-type: none"> The ‘multi-sector strategy’ excluded <i>de facto</i> small-scale millers and small farmers. The agenda was set by the ruling party, international agencies and large businesses. 	<ul style="list-style-type: none"> Financial inclusion, with a particular focus on women and rural areas. More than 18m bank accounts opened in one week (2014). Episodes of social unrest and heightened economic insecurity linked to microfinance. 	<ul style="list-style-type: none"> Land allocation is exclusionary and has made some communities landless or displaced.
Accelerating sustainability	<ul style="list-style-type: none"> Water and air pollution from mining and pulp and paper production. Depletion of fish stocks. 	<i>Unclear</i>	<i>Unclear</i>	<ul style="list-style-type: none"> Disputed – e.g. natural environment being adversely affected because of deforestation.
Reducing inequalities	<ul style="list-style-type: none"> Smaller firms were able to access export opportunities. Small landholders were marginalised. Jobs were created, though seasonal and non-unionised. 	<ul style="list-style-type: none"> Rich/poor inequalities in access to nutrient-rich foods were not reduced, and may have been exacerbated. 	<ul style="list-style-type: none"> Impact studies do not show a reduction of poverty among microfinance clients. 	<ul style="list-style-type: none"> Jobs created, especially for women and especially in urban and peri-urban areas where employment challenges are high.

On the other hand, in the cases where social policy was the target, notably nutrition and financial inclusion, the picture is more mixed or negative. The elite bargain in Tanzania did not improve nutritional outcomes for the poorest, despite that ostensibly having been the policy goal. In India, the goal of financial inclusion was achieved in large measure; however, many bank accounts remain unused, and impact studies have failed to confirm that this inclusion has led to poverty reduction. These findings seem to confirm suspicions that state–business relations in the social sphere may benefit business more than society. However, at this stage, we must be cautious about drawing this conclusion.

We do not claim that the outcomes identified in these four cases are representative of the nature of state–business relations more generally, and we acknowledge that information gaps in the context of this secondary case analysis mean that we have not been able to explore outcomes in sufficient detail. But we do believe that our analysis makes a clear case for the need to understand how different structures and processes of state–business relations, particularly in the context of non-Weberian bureaucracies and imperfect institutions, impact development.

6 Conclusion and research agenda on state–business negotiations

The interplay between states and businesses profoundly affects development outcomes, including and going beyond growth. We suggest that many of the important interactions between states and businesses consist of what we refer to as ‘negotiation’; our four case studies focus on such interactions, which do not fit easily into any of the standard ‘boxes’ of conflict, collaboration, capture or co-optation. We look at Chile’s transition to democracy and export-oriented growth, combating malnutrition in Tanzania, creating financial inclusion in India and agricultural commercialisation in Ethiopia. As we see from the cases, there is often a marked *interdependence* between state and business actors that is the catalyst for negotiation; but to the extent that states and business do engage one another constructively, it is hard to say where *collaboration* ends or *collusion* begins. We identify two recurring patterns of *negotiation processes* in our cases, namely networked negotiation and policy-directed concession-exchange. The analysis also showcases the *power of ideas* and ideologies at shaping and reshaping state–business relations over time.

6.1 Towards a research agenda

The question of how states and businesses interact and the implications for society is a recurrent theme in political, economic and sociological thought. Recent literature on state–business relations has clearly posited ‘effective’ state–business relations as key contributors to economic growth and structural change. Moreover, it has suggested institutions that support policy coordination are important ingredients of effectiveness. However, this literature raises as many questions as it answers. It remains unclear whether ‘good’ coordinating institutions can really be transplanted from one context to another; how states’ and businesses’ interests are best aggregated; how formal institutions interact with informal ones; and finally, but crucially, how state–business relations impact broader development outcomes beyond economic growth.

Further study of state–business relations within the realm of negotiation can help to illuminate key issues. To begin with, business and state *actors* are not homogenous, each representing a diffuse collection of actors; which necessitates recognising a diversity of power and interests, and how they can be aggregated and expressed. Different businesses will share some interests, but will also be in competition or conflict in other areas, and similarly, different government ministries may have shared or competing interests. The characteristics and strategies of negotiators (statesmen, business leaders, key bodies within organisations) are also determining factors. While actors act in what they understand to be their self-*interest*, which determines the degree of alignment or divergence of objectives that must be negotiated, we aim for a more dynamic analysis of interests that recognises how they are shaped by ideas and influenced by the negotiation process itself. Meanwhile, understanding *power* in state–business relations means exploring both ‘power over’ and ‘power with’ others as actors strive towards their goals. The power used may be instrumental, derived from the resources which actors possess, as well as the skill with which they use them. But it also importantly includes the more hidden, agenda-setting or structural power which frames the boundaries of the negotiable and determines what is on or off the table in the pursuit of development.

Vast challenges to understanding state–business relations remain, particularly in light of the vision embedded in the SDGs that states and businesses will work together for development. Building on the work above, we would suggest three complementary ways forward to be:

1. **Developing clearer models of state–business relations in different institutional environments.** Our case analysis identified different processes of formal and informal state–business relations; some more networked and others more directive, with a variety of state, business, labour and civil society actors involved. What are the different types of state–business relations, how do they work, how can we explain their emergence and their implications for different development outcomes? The literature review discussed different approaches to typologising institutional arrangements in different countries, such as types of developmental state, or Varieties of Capitalism. Ongoing research is developing these further, while asking critical questions about how (and how well) these typologies may work (for example, Schneider 2009; Routley 2012; Witt and Redding 2013). We seek to build on this emerging analysis to develop better comparative frameworks for understanding the processes and structural factors that constitute state–business relations. This work should be tailored specifically to developing countries, and focus on the *relational* element rather than focusing on either the state or business as the driving force. A further challenge – and opportunity – moreover lies in accounting for the transnational dimension (Unsworth 2010; Jenkins 2013), which often plays a greater role in the state–business relations of developing countries given the influence of international business and international donors.
2. **Identifying key factors that shape state–business relations and their development outcomes.** Closely connected to an effort at developing models (or typologies) is the question of which variables, components or elements of state–business relations matter most. Our research has pointed to a number of factors that shape state–business relations, including the actors, power and interests; it also suggests additional intervening variables, including institutions, linkages between states or businesses and international actors, policy leadership and the role of policy networks, and ideas and ideologies. This work may be deepened and connected to recent variable-based research on developmental states, industrial policy and economic growth (for example, Lemma and Te Velde 2015; Sen 2015), while broadening the perspective to include outcomes beyond growth.
3. **Explaining developmental effectiveness of state–business relations.** What makes state–business relations ‘effective’ for development? Most current literature focuses on economic performance, identifying formal institutions such as investment promotion agencies and business associations, and proposing a ‘theory of change’ in which these features contribute to intermediate outcomes for economic growth such as information sharing, the building of trust and credibility, and fostering collective action to remove obstacles to investment. However, one important question is what are the features that contribute to state–business relations that are effective in achieving broader development outcomes, and based on what theory of change? Are these features different in different institutional contexts? Specifically, one might focus on the developmental outcomes encapsulated in the SDGs, or in relation to broader challenges such as inequality, sustainability, inclusion and security, as we have suggested in this paper. This would help to illuminate more clearly also any trade-offs, contradictions and complexities between pursuing different development goals (for example, Schmidt *et al.* 2015; Waage *et al.* 2015).

The challenge of developing adequate frameworks for understanding evolving state–business relations in development is large; but given renewed calls for states and businesses to work together for development, the issues identified here should expectably have a central place on the research agenda. Tackling these questions will entail engaging in partnerships that go beyond the usual disciplinary boundaries. Thus far, it has often been economics that has studied state–business relations, but political economy, sociology, anthropology and others can offer vital and unexpected insights. This will especially be the case wherever the aim is to cast a wider view onto developmental outcomes and the role that state–business relations play in driving them.

Annex A – Case study: Export-oriented growth and democratic transition in Chile

This case study examines the state–business relations that have shaped core features of Chile’s economy during the country’s return to democracy in the 1990s. While Chile is characterised by a strong, disciplined and stable party system and a diverse array of interest groups, the (big) business–government relationship has been closer and more extensive than the government’s relationship with other interest groups. For much of the country’s history, business leaders had moved in and out of top government jobs, including cabinet posts. While these relations were disrupted by President Allende’s socialist government (1970–73), and the military coup and economic restructuring initiated by General Pinochet (1973–90), as early as 1982 business was again working closely with government on economic policymaking. Although the practice of appointing business leaders to government positions ended after the return to democracy in 1990, an ongoing negotiation between government and industry continues to be at the heart of economic policymaking. This closeness has not necessarily implied malfeasance. Despite a recent series of corruption scandals related to corporate financing for political parties, overall the country has long been characterised by low levels of corruption.²⁵ However, policymaking is inevitably most influenced by the perspectives and priorities of those who have the greatest access to it.

The result of Chile’s economic policymaking since 1980 has been to create an outward-looking economy based on copper and other mineral resources, fishing and fish processing, foodstuffs, iron and steel, wood and wood products, transport equipment, cement and textiles. After recovering from extreme crisis in 1982 when it fell more than 13 per cent, Chile’s GDP recovered, growing at an average of 6.4 per cent per year during the 1990s. Exports rose from 23 per cent of GDP in 1980 to 30 per cent of GDP by the end of the 1990s and 42 per cent of GDP by 2006.²⁶ Sixty-six per cent of exports were carried out through preferential trade agreements with the USA, the European Free Trade Association and several Asia-Pacific Economic Cooperation (APEC) countries. By the end of 2006, Chile had signed trade agreements with more than 50 countries, which represent 83 per cent of global trade (Ferraro and Stumpo 2010).

Despite this ‘economic miracle’, there are losers from the economic policies of recent decades, notably import-competing industries and rural smallholders (Kurtz 2001). While agro-industry created jobs in the countryside, these were seasonal and not unionised. Since 1990, redistribution has countered the worst effects, with poverty falling from 40 per cent in 1990 to 15 per cent in 2010. However, Chile is also one of the most unequal countries in the world. While inequality has also fallen – from a Gini coefficient of 57.3 in 1990 to 50.5 in 2013 – the middle class remains small and inequality stubbornly high.

Core actors

Business

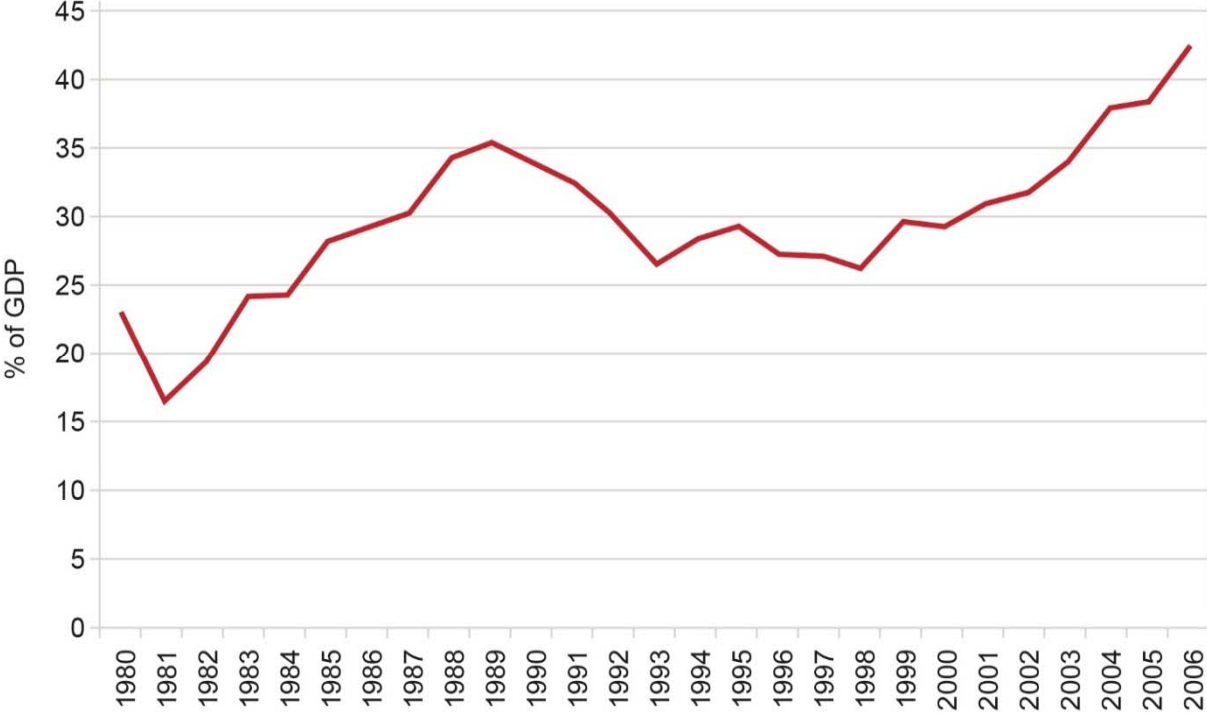
Chile has a highly concentrated business sector, with a number of large conglomerates with diversified holdings either internationally (concentrated in core sectors) or domestically (by acquiring firms in different sectors). At the other end of the scale, in 2004 18.2 per cent of companies were SMEs. Business is represented by strong and longstanding industry bodies including the peak association, the Confederation of Production and Commerce (CPC),

²⁵ Chile ranks 23rd out of 168 countries on the Transparency International Corruptions Perception Index, for example www.transparency.org/country/#CHL

²⁶ Based on World Bank data.

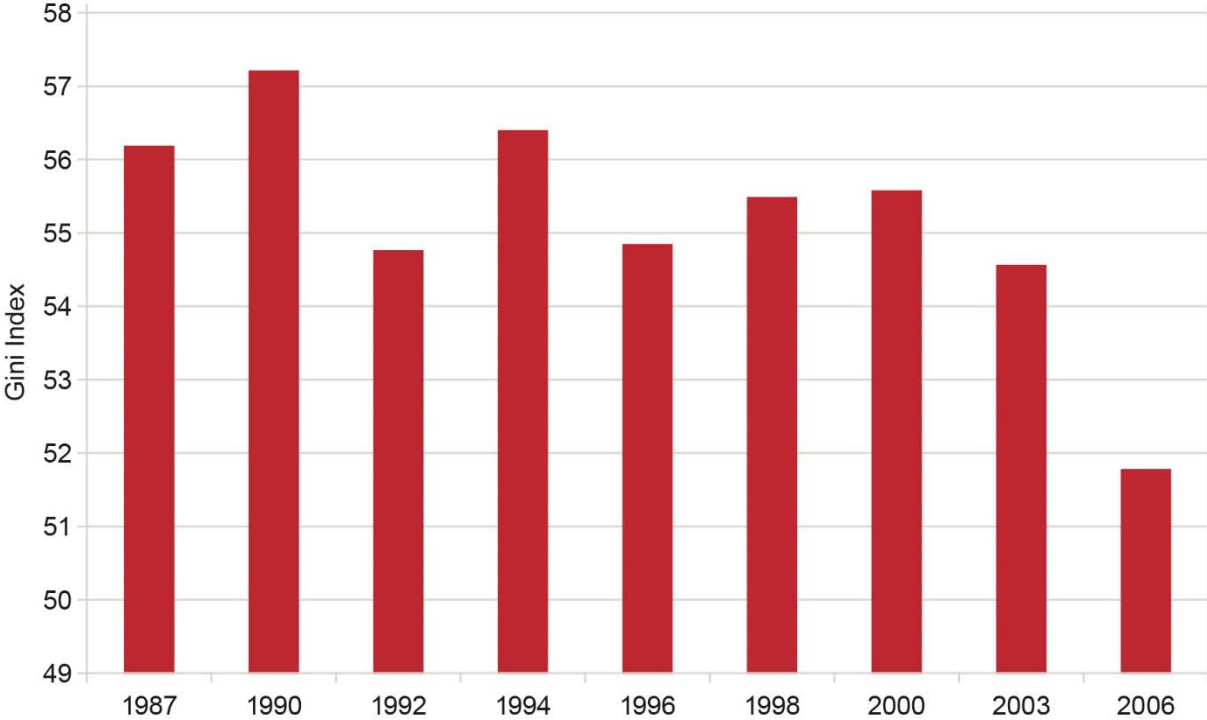
established in 1934. The CPC includes six powerful sector peak organisations, including the National Agricultural Association (SNA) and the Society for Manufacturing Promotion (SOFOFA). The National Confederation for Medium, Small and Micro Industry, Service and Craftsmen of Chile (CONUPIA) represents SMEs nationally.

Figure A1 Exports as a percentage of GDP in Chile 1980–2006



Source: Authors' own, based on World Bank Indicators.

Figure A2 Gini index for Chile



Source: Authors' own, based on World Bank Indicators.

SOFOFA represents industrial interests in Chile. With 2,500 corporate affiliates, 36 sector association affiliates, and eight regional affiliates, SOFOFA members control more than 80 per cent of Chile's industrial capital and account for 30 per cent of GDP.²⁷ In the 1990s, a number of export-oriented producer associations were created and included in SOFOFA, representing food manufacturers (Chilealimentos), fruit exporters (ASOEX) and fishing (SONAPESCA). These developments increased SOFOFA's power base in agriculture relative to the SNA (Bull 2008).

State

Since Chile's democratic transition in 1990, the country has predominately been governed by the Concertación de Partidos por la Democracia (Concertación), a coalition of centre-left parties initially formed to campaign for the return to democracy. This case study is concerned primarily with the first three Concertación administrations of Patricio Aylwin (Christian Democrat 1990–94), Eduardo Frei Ruiz-Tagle (Christian Democrat 1994–2000) and Ricardo Lagos (Socialist 2000–06). Aylwin and Frei in particular won very strong mandates to govern, and were focused on maintaining the stability of the democratic transition. In addition, two state agencies, CORFO and DIRECON, are particularly relevant to the case studies.

The Production Development Corporation of Chile (CORFO) was created in 1939 as an autonomous agency to support the country's economic development by improving the technological capacity of (particularly) agriculture, fisheries and forestry. The agency selects its own technical personnel on the basis of merit, and is governed by a board headed by the Ministry of the Economy and composed of representatives of the private sector and relevant government ministries. It does not have significant resources of its own, but works closely with external partners: intermediary agents, financial institutions, investment funds, universities and technology centres, collaborations which enhance the agency's knowledge and expertise (Nelson 2007; Ferraro and Stumpo 2010; Rivas 2012).

The General Directorate of International Economic Relations (DIRECON) was set up in 1979, and is part of the Ministry of Foreign Affairs. It is seen as a highly competent and relatively powerful agency in the area of trade and foreign economic policymaking, and as a counterweight to the powerful Central Bank and the Economy Ministry (Faust 2004). DIRECON officials form a key part of Chile's trade negotiating team, and lead the engagement with business over trade policy development.

Other

Chile's democracy is traditionally corporatist, giving the peak labour association (as well as business) a formal role in policymaking. While organised labour was significantly weakened under the Pinochet dictatorship, the return to democracy saw labour, represented by the Unitary Confederation of Labour (CUT), restored to this formal role in policy negotiations.

State–business relations and Chile's export orientation

Upon Chile's return to democracy in 1990, there were substantial fears that the country could slip back into the economic crisis and inflationary shocks of earlier decades. Therefore, the majority of the elite, regardless of ideology, supported maintaining the key features of Pinochet's pro-market reforms including macroeconomic stability, export-orientation, and a business-friendly investment climate. Patricio Aylwin's campaign explicitly committed to continuation of these reforms (Armijo and Fauber 2002). The commitment to this economic model was important to the developing relations between the Aylwin regime and the business sector. At first these relations were uneasy; business had been (and some still were) strong supporters of the dictatorship. However, business scepticism was overcome,

²⁷ www.sofofa.cl/english/sofofa2004.htm#3

due in part to pre-existing social contacts between business leaders and representatives of the Christian Democrats (Bull 2008), and in part to the government's commitment to maintaining the economic model that business favoured. A mutual fear of instability – economic or political – opened the door to dialogue, despite mistrust between the parties.

The core features of Chile's economy shaped by state–business relations include:

- high levels of growth in non-traditional exports, driven by government support for coordination and upgrading in these sectors;
- the rapid negotiation of more than 50 free trade agreements.

Growth in non-traditional exports

Pinochet's reforms had liberalised trade and created the potential for export expansion. However, not all sectors had the capacity to export. Prior to 1980, Chile's agro-industry, which later became a major exporter, was dominated by domestic firms using small-scale, second-hand equipment and discard-quality raw materials. Under the Aylwin and Frei administrations, export success was heavily supported by state intervention led by CORFO, which assumed a new role in promoting the reorganisation of these firms. These efforts built on similar programmes first implemented under the Pinochet regime.²⁸

Among CORFO's policy instruments was the 'Development Project', known as a PROFO,²⁹ initiated in 1993. It sought to identify new ways to organise production, improve standards and upgrade productive capabilities in order to improve competitiveness, especially of SMEs. The goal was to move away from competitiveness based on low wages, and towards competitiveness based on productive capabilities (Perez-Aleman 2000). Support was given to groups of companies or associations. These newly created associations consisted of generally 8 to 15 firms in the same sector and vicinity, producing similar or complementary products. They were expected to develop a collective business strategy and a new, more skilled and competitive business association. CORFO provided finance and a group manager to support associations to develop and implement a joint plan. By 1997, there were 306 PROFOs in Chile, with 3,400 SMEs involved (Perez-Aleman 2000; Ferraro and Stumpo 2010).

The nature of the collaboration between CORFO and these new associations of SMEs stands in contrast to the traditional role of industry associations, oriented towards defending the particular interests of segments of the business community. CORFO facilitated the new associations in order to reorient the sector towards export through better coordination, diffusion of knowledge and promotion of collective learning (Perez-Aleman 2000). Working through small associations with a broad membership also made it less likely for CORFO to be captured by any one individual or group (Nelson 2007). In this way, CORFO managed to catalyse a process to identify how best to improve the quality and competitiveness of Chile's exports (Perez-Aleman 2000). Effectively, this state–business relation functioned to overcome a collective action problem, in that individual SMEs were unlikely to achieve competitiveness through their own investment – the whole sector needed to change. This does not imply that CORFO had superior knowledge of what best to do in order to achieve upgrading, however. Rather CORFO catalysed a process with business to identify how best to improve the quality and competitiveness of Chile's exports (Perez-Aleman 2000).

²⁸ In 1975, the Pinochet government created PROCHILE, an agency to support alliances of agro-industrial firms and assist them in entering export markets.

²⁹ PROFOs built on policies that had already been implemented by PROCHILE (the Export Promotion Bureau of Chile) under the Pinochet government.

Free trade agreements

As Chile transitioned back to democracy, numerous bodies were set up to bring business and labour into trade policymaking under DIRECON. Labour was represented by the CUT, while SOFOFA played a strong role in coordinating and representing business interests. SOFOFA's role was bolstered as they hired a former director of DIRECON with long experience in trade negotiations, as well as an expert on the WTO, also from DIRECON. These appointments established SOFOFA's trade expertise and created important links with the ministry leading trade negotiations. Formal bodies were established involving business and (in some cases) labour in trade policy, including the Bilateral Council for Trade and Investment and the tripartite Forum for Productive Development (FDP), both focused on issues of competitiveness and trade. Business and labour were also invited to participate in trade negotiations through the institution of the 'room next door', in which business and labour representatives literally followed the negotiations in a room beside the main proceedings, receiving briefings and providing advice (Bull 2008).

However, due to significantly different interests that were hard to reconcile, it became ineffective to try to bring business and labour together in one single grouping. The FDP was closed down, for example, and its functions replaced by the Public-Private Council for Export Development (CPPDE), which was closely tied to SOFOFA and excluded labour representation. Similarly, the 'room next door' process broke down as labour was torn between a desire to exert influence and a total rejection of free trade. Business and labour ended up in different 'rooms next door' to avoid the conflicting interests holding up negotiations. While engagement continued, each group was consulted separately (Bull 2008).

As a result of these processes, a close network and a high degree of consensus in terms of trade policy priorities developed between public officials, led by DIRECON, and business, led by SOFOFA. This created predictability, facilitated effective negotiations and helped secure support for trade agreements at home. This trade policy network emerged through repeated interactions between business and the state, in bodies such as the CPPDE and in the series of intensive negotiations that Chile carried out with big trading blocs like the USA, Europe, Mercosur and Asia. Over time, these relations created a shared knowledge and technical expertise, as well as a general consensus about preferences, priorities and benefits of free trade policies. They also created personal relationships of trust, and even loyalty and friendship, that were embedded in these formal institutions (Bull 2008).

While not all business was united in supporting Chile's approach to trade liberalisation,³⁰ the business sector is by far the most active and influential non-state actor in Chile's trade negotiations (Herreros 2010). Although both the Aylwin and Frei administrations aimed to re-establish labour participation in policy deliberations, labour was effectively excluded from the close state–business network that emerged. A similar picture arises in relation to the environment. Chile's growth in export industries have resulted in significant levels of pollution and environmental damage, including water and air pollution from mining and pulp and paper production, and the depletion of fish stocks. While Chile's economic opening came at a time when no environmental management policies were in place and the environmental movement was not strong, more recently, environmental groups in Chile have protested new trade negotiations on the Trans-Pacific Partnership (TPP). They particularly highlight how the TPP would open the way for measures (dispute settlement rules) that would allow investors to sue governments and demand compensation if regulations, on the environment or labour, for example, are enacted that are deemed to violate free trade and damage their profitability (Fortin 2014, 2015). While government engagement with civil society on such issues has

³⁰ The SNA had taken a protectionist stance in early trade negotiations, and during the negotiations with MERCOSUR even chose to stay out of the negotiations completely and to protest outside. However, eventually the SNA's anti-free trade position weakened (Bull 2008).

increased in recent years, these tend to be limited to bilateral consultations and briefings by government officials and are unlikely to have the same influence as the close policy network between business and the state.

Conclusions – implications

This case study highlights the role of certain types of state–business relations in contributing to Chile’s successful development of export-oriented trade in non-traditional sectors. Overall, these relations were based on a productive interaction between business and the state, rather than one characterised by rent-seeking. They supported the country to maintain political and economic stability, upgrade agribusiness and grow non-traditional exports in this sector, and to negotiate trade agreements with more than 50 countries. At the same time, and particularly in relation to Chile’s trade policy network, the boundaries between public and private functions were blurred while social sectors were marginalised. The net result of strong state–business relations has therefore been to build a more competitive and outward-looking economy, but to weaken efforts to build more inclusive policymaking, opening the way for measures that threaten to undermine environmental and labour regulation.

Annex B – Case study: Food fortification and the nutrition agenda in Tanzania

Tanzania has a population of around 50 million people. Its economy has enjoyed a real gross domestic product (GDP) strong and steady growth rate average of 7 per cent in the last ten years. The main drivers of growth recently have been several fast-growing sectors, such as construction, transport and financial services (World Bank 2016). Agriculture remains a key sector of Tanzania's economy, as it accounts for 45 per cent of GDP and is the source of livelihood for more than three quarters of the population. However, Tanzania's agriculture remains small-scale, undercapitalised and labour-intensive (Cooksey 2012). Tanzania's political system has been democratic with multi-party elections since 1995. Political decision-making is highly centralised but complicated by vested interests among cliques within the ruling party. This allows little room for the inclusion of views from outside high-ranking political circles (Anyimadu 2016). In addition, Tanzania is one of the largest recipients of international aid in sub-Saharan Africa. From 2007 to 2011, approximately one third of government spending was financed by donor funds (Anyimadu 2016).

Despite this steady economic growth, Tanzania still faces a major undernutrition problem, with one of the world's highest rates of chronic undernutrition in children – 42 per cent of children under five are stunted and 30 per cent of women are deficient in iron (NBS and ICF Macro 2011). Regardless, evidence shows that economic growth is not sufficient to reduce undernutrition (Bhutta *et al.* 2008; Headey 2012). The problem is particularly acute among people living in rural areas and lower income groups. In the last ten years, with high-level support from the Tanzanian central government, nutrition has become a national policy priority. The Government of Tanzania established the National Nutrition Strategy (NNS) (2009–2015), with a core element being the Food Fortification Action Plan, initiated by the National Food Fortification Alliance (see below) to increase the supply of foods rich in micronutrients in the country (Ministry of Health and Social Welfare 2011). In addition, from the outset, the Prime Minister's Office of Tanzania provided support for the nutrition agenda.

Tanzania's push to reduce undernutrition was aligned with a strong international commitment to tackle malnutrition, with multi-stakeholder initiatives such as the Scaling Up Nutrition (SUN) movement, initiated in 2010 or the establishment of organisations, like the Global Alliance for Improved Nutrition (GAIN) (Hoddinott *et al.* 2015), with a strong focus on reducing undernutrition by engaging the private sector. In this context, the Government of Tanzania became one of the first members of the SUN movement in 2011, and a focus country of USAID's Feed the Future initiative – a multi-year, multi-country programme focused on targeting global hunger and food security.

This case study focuses on the government efforts to incentivise and engage the private sector to reach a social goal, increase nutrition intake by the population, through the Food Fortification Action Plan, which required the food industry in Tanzania to fortify all wheat flour, maize flour and edible oil. Food fortification is seen as a cost-effective strategy to reduce prevalence of micronutrient deficiencies, and aimed to reduce stunting by 15 per cent by 2015. The case study will focus on and analyse the coordinative and facilitative state–business negotiation to leverage the wheat and maize flour industry resources and engage them to fortify their products, with the aim of reducing undernutrition. These relations had mixed outcomes for the population.

Core actors

The Tanzania Food and Drugs Authority (TFDA) is the government's organisation responsible for delivering quality assurance and quality control by the private sector. The TFDA has offices representing each geographical area of Tanzania (seven in total), five outside and two in Dar es Salaam.

Large flour processors in Tanzania control 94 per cent of the *wheat flour* market, which is very concentrated. Bakhresa and Azania Mohamed Enterprises, both Tanzanian companies, are among the three largest wheat processors in the country. Bakhresa is also a key player in Eastern, Central and Southern sub-Saharan Africa. In contrast, the *maize flour* market is very diffuse, where ten firms control 5 per cent of the market, and is dominated by *the informal sector and small millers*.

The National Food Fortification Alliance (NFFA), created in 2003, is a multi-stakeholder platform that served as the forum where the public sector and industry discussed the regulations to be implemented as the Food Fortification Action Plan was developed and adopted by the government in 2009.

- Government members: Ministry of Health and Social Welfare, Ministry of Industries and Trade, Ministry of Agriculture and Food Security (now Ministry of Agriculture, Livestock and Fisheries), Tanzania Bureau of Standards, Tanzania Food and Drugs Authority, Tanzania Food and Nutrition Center, Small Industries Development Organisation.
- Private sector includes a range of large local companies, such as: Power Foods (blended cereal products), Tropical Foods (processed fruits and vegetables), Bakhresa, Azania Mohamed Enterprises, Tanzania Chamber of Commerce, Industries and Agriculture, food manufacturers, processors, and Consumer Association.
- Civil society, academia and international donors, including: Sokoine University of Agriculture; International Health Food Association; Helen Keller International; and UNICEF, WFP, World Bank.

International donors that support the establishment of the food fortification agenda, such as the *World Bank*, are central to the development of the Food Fortification Action Plan, providing funds and technical support. Support also came from *GAIN*, an international organisation launched in 2002 to tackle malnutrition. *GAIN* established a 'Premix'³¹ Hub' in Dar es Salaam in 2011, to supply food manufacturers with the required premix, ensuring an affordable and good quality supply.

State–business relations shaping the nutrition agenda in Tanzania

Tanzania's efforts to reduce undernutrition have been highly dependent on international aid since the beginning. Tanzania's NNS was actively supported by other donors – almost US\$76.7m from the US, as part of their Feed the Future programme and the New Alliance for Food Security and Nutrition, US\$2m from the World Bank and US\$2.69m from the Government of Japan (Bleggi 2014). Donors are increasingly calling for private sector involvement in national nutrition systems. Tanzania has been a pioneer in the region in introducing a strong role for the private sector within the NNS.

The focus of this case is on the coordinative and positive state–business relations that led to the creation of the Food Fortification Action Plan and its implementation, as well as a brief analysis of its mixed results. This case study shows how the state drove the relations by seeking, successfully, to leverage private sector resources and skills, with the aim of,

³¹ Mix of nutrients added to the flour in order for it to be fortified.

unsuccessfully, achieving the social goal of reducing undernutrition by increasing nutritious food products in the markets. Also, these relations are influenced by international donors, shaping how government expenditure is allocated, what the final policies will look like and who will benefit from them.

State–business relations on the Food Fortification Action Plan

The NFFA, established in 2003, attracted strong support from development partners. After six years of meetings, the NFFA, on May 2009, supported by two consultants from the World Bank, started developing the Food Fortification Action Plan. It included an overview of malnutrition in Tanzania, a cost-benefit analysis for the government and the private sector of the introduction of a food fortification strategy in the country, and a roadmap ‘to make food fortification a reality in Tanzania’ (World Bank 2009). The plan was presented to a High-Level Forum in September 2009, including representatives from the central government, key international donors (World Bank, World Food Programme), and other stakeholders, such as private sector or civil society organisations. They decided that:

A concerted effort is needed by all stakeholders to implement the Food Fortification Action Plan and get started on food fortification in Tanzania. An important outcome of this meeting should be the endorsement of the action plan by stakeholders, and a consensus on the essential next steps and the timetable for moving forward quickly with this essential intervention.

(The Chief Medical Officer, as chair, on behalf of the Permanent Secretary, Prime Minister’s Office, quoted in World Bank 2009)

This shows how, from the outset, the nutrition agenda in Tanzania was encouraged strongly by international aid donors. Another example came when the World Bank threatened to remove the US\$2m donation if the Food Fortification Plan was not enforced on time, so in 2011 the Minister of Health and Social Welfare signed the national regulation and the enforcement started in May 2013 (Bleggi 2014).

The Plan was set to be implemented by the private sector, with support from the government and international donors. It passed legislation that makes it compulsory for all food processors in Tanzania to fortify wheat and maize flour and edible oil. It, implicitly, was mandating the private sector to deliver a social objective (reduce undernutrition by producing fortified flour products with micronutrients), incentivising them to comply with the regulations by enforcing the law, supporting them to acquire the premix and providing technical assistance to learn how to fortify. The logic underlying mandatory fortification is that by creating an even playing field through regulation, government can simplify the constraints that businesses face to deliver nutritious food. Also, the cost of food fortification is assumed to be very low for the companies, particularly given government support.

To ensure the implementation of the new regulations, the government gave incentives to companies to support them to comply, such as a tax exemption for imported premix to support the acquisition of the premix and the dossifiers.³² Also, GAIN established a ‘Premix Hub’ in Dar es Salaam, to give local food producers access to affordable and high-quality premix in a cost-effective way. It is easily accessible to large manufacturers located near Dar es Salaam. Finally, support from former President Kikwete helped attract the attention of industry decision-makers, and the NFFA advocated for the industry to adopt and sustain the new food-fortification practices.

³² A ‘dossier’ is the dispenser installed on the mill to ensure correct rate of premix is added to the flour.

Who can comply with the legislation? Who benefits from it?

Overall, achieving effective fortification within large industry and a concentrated sector is less costly and complex than for a very diffuse sector. Often, for the government it is easier to support large-scale manufacturers to enable them to easily adapt to the new legislations, at reduced costs. However, micro and small millers will not be able to comply with the legislation, as these imply a costly and complex process for them. In Tanzania the food market is divided between the large-scale, industrial manufacturing that produces wheat flour; and the micro- or small-scale processing plants, that produce maize flour. Furthermore, in Tanzania it is small enterprises, not large industries that provide products for the majority of the rural and urban poor (see Table B1). Both Bakhresa and Azania produced maize flour, but discontinued after the mandatory fortification policy started.

Table B1 Market characteristics in Tanzania

Flour type	Type of company	Degree of concentration	Target population	Complying with fortification
Wheat flour	Large food processor	Concentrated – two firms control 94%	Urban middle and high income	Yes
Maize flour	Micro and small mills	Diffuse – ten firms control 5%	Rural and urban poor	No

Source: Adapted from Robinson and Nyagaya (2014).

By 2015, six of the major companies were already fortifying their wheat products and complying with the legislation. As an example of industry's support for this agenda, and the good relations between the government and the industry, President Kikwete announced the start of the fortification campaign from the main wheat flour factory of the country, Bakhresa's Buguruni Flour Mill (Bakhresa Group 2013). In addition, Bakhresa was the first company to start fortifying its products (Robinson *et al.* 2014).

In spite of this success, available evidence suggests that the poor do not buy their products from any of these companies. Poor people consume maize flour, and most of it (80 per cent) is processed by micro and small mills (Trevor and Wilson 2015). Maize flour is also a key ingredient for complementary foods, consumed by 70 per cent of breastfed infants and 80 per cent of non-breastfed infants between the ages of six and 23 months. Lack of proper complementary feeding is one of the major causes of undernutrition in the country (Temu *et al.* 2014). As of 2015, there was no evidence that maize flour was being fortified.

Small millers cannot access the premix itself, as GAIN's facility is not accessible to them. Furthermore, the current Tanzanian regulation system is too complex for SMEs – pushing them potentially out of the markets (from registration to fortification), as only a handful of small maize millers are registered with the Tanzanian regulatory agencies, the TFDA and the Tanzania Bureau of Standards (Temu *et al.* 2014). As of today, the government has not managed to enforce the regulations in the informal markets, and the TFDA (enforcement body) is not able to fulfil their role, as they are short on staff and equipment³³ (Robinson and Nyagaya 2014).

A USAID programme, Tuboreshe Chakula (2011–15), with a budget of US\$22m, aimed to upgrade SMEs and facilitate fortification for maize flour with very little success. It worked with more than 700 SMEs across three regions (Dodoma, Manyara, Morogoro), and as of early 2014, none of the enterprises participating had been able to undertake fortification. According to the assessment of project managers, small enterprises will not fortify unless

³³ The TFDA is expected to monitor as many as 1,000 or 2,000 maize flour millers, with only four offices outside Dar es Salaam and one regional office with two inspectors.

there is higher demand for the fortified products or strict enforcement (Robinson and Pittore 2015).

Although several businesses are making products fortified with micronutrients, these target middle and higher income consumers who are willing and able to pay a higher price. It has been observed that the larger firms are selling their products at high prices, offsetting their costs by marketing their products as premium quality brands – helping them differentiate from the informal sector and sell to middle-higher income consumers (Maestre *et al.* 2014). Furthermore, as shown above, an excess in regulation can end up driving small and micro-processors out of business, as they try to comply with the new legislation and upgrade their facilities to the required standards. It is clear that small businesses are crucial in reducing undernutrition among Tanzania's poorest communities. In Tanzania, the majority of the complementary foods in rural areas are made from unfortified cereals and do not provide enough energy or micronutrients (Temu *et al.* 2014). Even for large companies it is difficult to compete with cheaper, unfortified products made by small businesses, given the high distribution costs for rural areas.

Conclusions – implications

This case shows that while state–business relations can be coordinative and positive, the final goal of the government may fail. The risk is that by excluding certain voices from the discussions and the policy design, the final outcome – while well intentioned – will result in unintended consequences for the targeted population. This is a case where the state, influenced and supported by international donors, sought to leverage private sector resources and skills to achieve a social objective. While the relations were successful, the state policy succeeded in fortifying wheat flour but failed in reaching poor consumers with it, hence not achieving its public policy goal overall. In this case, it ended up resulting in increased sales and business reputations for the private sector, an increased expenditure on the government side, and little or undesired consequences for the poor and the informal sector.

Annex C – Case study: The creation of a financial inclusion sector in India

Financial inclusion is widely celebrated as a private sector initiative for inclusive development (for example, Accenture and CARE 2016; Ehrbeck 2014). But in reality it is more complex, with both private and public sector organisations negotiating and shaping different approaches for connecting poor and marginalised people to financial services. Financial inclusion efforts in India have sought to turn the poor into viable clients for the financial system, aiming for them to borrow at lower interest rates, accumulate capital through savings and more recently, use digital payment services.

Since the colonial age, first the British and then Indian administrations sought to expand access to finance, hoping to alleviate inequality and rural–urban divisions (Turnell 2005; Teki and Mishra 2012). Financial services, particularly credit, were long used (or abused) as a form of social policy. India’s rapid economic growth since liberalisation has been extremely unequal, focused on urban centres and the export-oriented service sector (which accounts for 8 per cent of GDP and 30 per cent of exports); and the IT and business services sector in particular (Hyvonen and Wang 2012). However, two thirds of India’s population live in rural areas, as do 86 per cent of the country’s poor (Alkire *et al.* 2014). Agriculture still employs half of the nation’s workforce, and accounts for a (declining) share of only 18 per cent of output (World Bank Indicators). Farmers and unskilled labourers find themselves increasingly superfluous to the expanding high-skilled urban economy (Taylor 2011).

Given this economic structure, Indian development strategy is generally negotiated between (mostly) higher-class politicians and urban business elites. These state–business elites view a more ‘inclusive’ financial system for all Indians as a remedy for rural underdevelopment, poverty and lack of opportunity that comes at low cost to the state and without redistribution. Beyond creating an ‘enabling environment’, the state has actively shaped the agenda for the private sector’s engagement. As with food fortification in Tanzania (see above), this entailed the state pursuing social policy goals through the activities of certain kinds of business.

Core programmes and evolution of microfinance in India³⁴

Since the 1980s, three sets of initiatives have been particularly important: self-help groups (SHGs), microfinance (through MFIs), and recent mass banking initiatives. Thanks to large commercial MFIs, India is now (with Bangladesh) the global heartland of financial inclusion, accounting for 42 per cent of the world’s microfinance borrowers.³⁵ But India has also spawned some of the most notable episodes of harm and deviance in financial inclusion.

Self-help groups (SHGs)

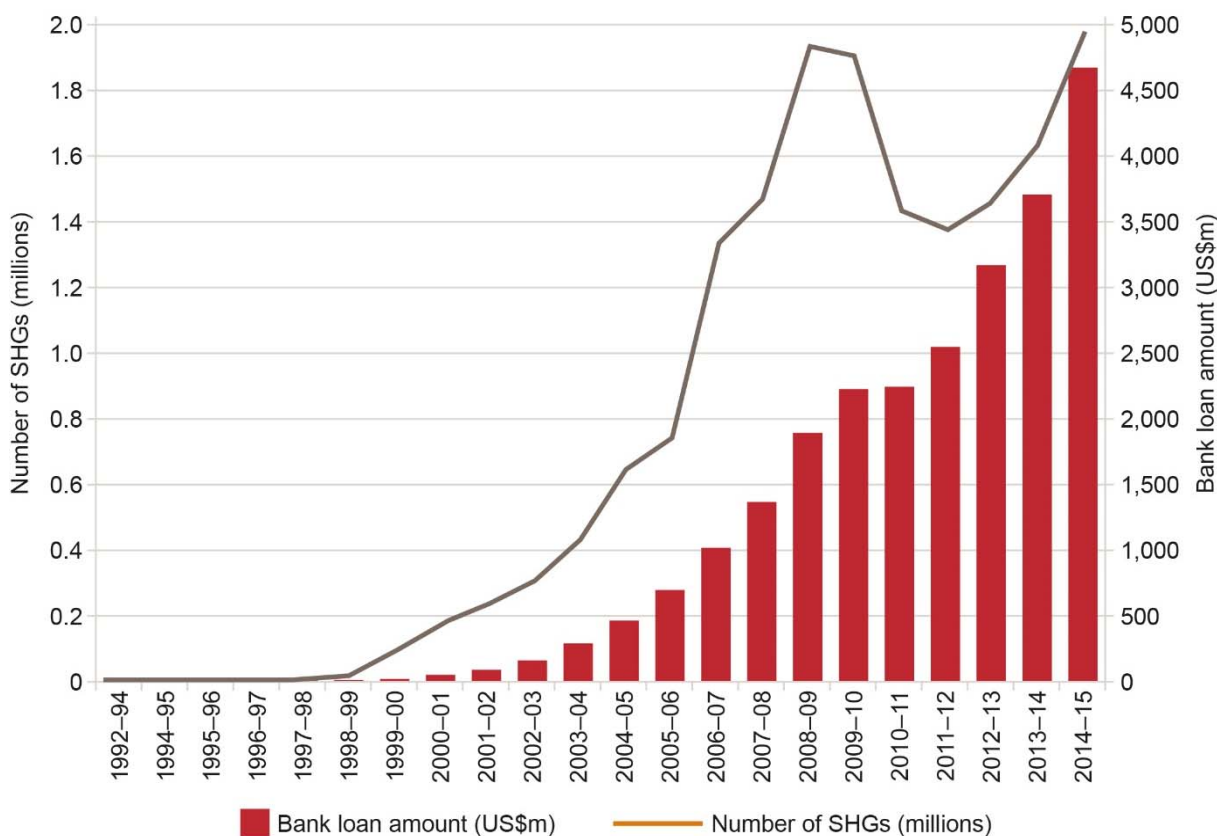
SHGs organise women into groups large enough to access formal financial services at reasonable cost to the service provider (banks). By aggregating their individual savings into a single account and their credit needs into a single loan, SHGs lower the transaction costs (Christen *et al.* 2005). They started in Southern India, with Myrada (a parastatal agency that had managed mostly rural cooperatives) and the National Bank for Agriculture and Rural Development (NABARD) collaborating to support, organise and expand rural groups and link them to banks for loans. They obtained support from the World Bank and several Indian state governments.

³⁴ To ease readability, many facts and figures presented here are not referenced in detail; see Mader (2015: 160–94) for references.

³⁵ As registered by the database MIXMarket (www.themix.org/mixmarket/countries-regions/india, 22 June 2016).

SHG formation and bank linkages began in the 1980s and rapidly accelerated in the 2000s, particularly in four states in the south (Andhra Pradesh, Tamil Nadu, Kerala and Karnataka). By the late 2000s, around 15 million SHGs, each comprising 10 to 15 women, had been linked with banks, borrowing around US\$4.5bn in 2014/15; see Figure C1.

Figure C1 Growth of the SHG–bank linkage



Source: Adapted from Sa-Dhan (2015: 73).

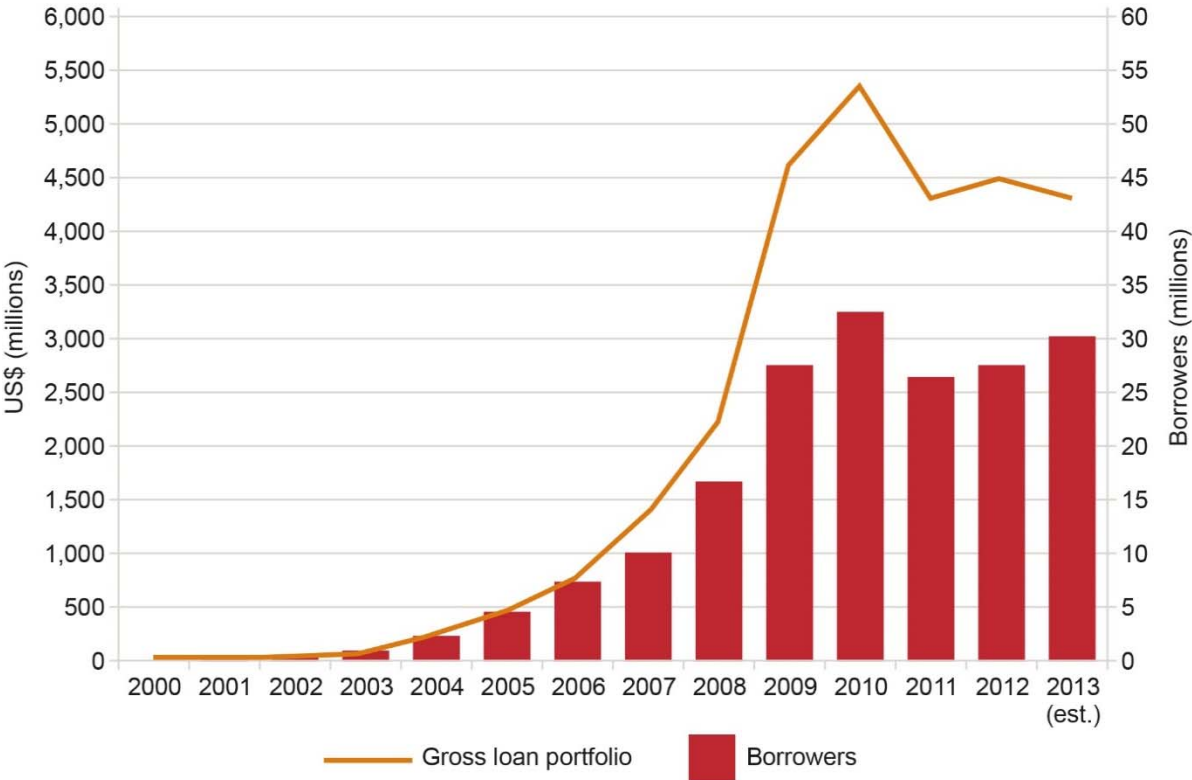
Microfinance institutions (MFIs)

MFIs emerged amid the Indian NGO community in the late 1990s, with support from NABARD and the Reserve Bank of India (RBI), and were promoted as a means to obtain even lower transaction costs than through SHGs. They also worked through assembling borrowers into groups, but without forming independent entities with internal governance structures (like SHGs).

MFIs worked strategically to bring domestic and international investor capital directly into lending to the poor, which led to a ‘gold rush’ among investors attracted to Indian MFIs’ extraordinarily high profitability (Wichterich 2012). They focused almost exclusively on credit. The growth was further encouraged by the government’s supportive but hands-off approach; it left microfinance unregulated. The government further incentivised investments in MFIs by declaring microfinance a ‘Priority Sector’ (more below).

MFI growth was focused on the same states as SHGs, and often targeted the same groups, in a practice criticised as ‘poaching’ of borrower groups. By 2009, nearly one third of all MFI credit was located in Andhra Pradesh. MFIs grew rapidly from the early 2000s and expanded their lending by 61 to 106 per cent each year in the second half of the decade (see Figure C2), until in 2010 over-indebtedness and borrower revolts precipitated a repayment crisis and snap regulation in Andhra Pradesh.

Figure C2 Lending done by MFIs in India



Source: Adapted from Mixmarket.org.

Mass banking initiatives

Recently, large government-led financial initiatives have sought to advance financial inclusion via the mainstream financial system, shifting the focus away from SHGs and MFIs. In 2011, the United Progressive Alliance government in Delhi launched a campaign called Swabhimaan to bring formal banking to everyone.

This was revamped by incoming Prime Minister Narendra Modi in 2014 with Pradhan Mantri Jan-Dhan Yojana (PMJDY – ‘Prime Minister’s People’s Money Scheme’), which focuses on making it easier for individuals to open bank accounts, access insurance benefits, get debit cards and gain overdraft facilities of up to 5,000 Rupees (Sa-Dhan 2015: 1). One key change was that while the ‘Swabhimaan scheme [...] focused on villages, the PMJDY focuses on households, thereby covering both urban and rural areas’ (Awasthi 2015: 338). PMJDY, the ‘largest financial inclusion scheme in the world’, aims for universal no-frills bank account coverage, working mainly through the public banks sector but also private banks (Nair and Tankha 2015: xiii). The opening of more than 18 million new bank accounts in the first week was recorded in the Guinness Book of World Records.³⁶

Financial inclusion in India: state activism and state–business interdependence

The evolution of financial inclusion programming in India can be read as sequential negotiations between an activist state and an often more reactive business side (specifically,

³⁶ www.guinnessworldrecords.com/news/2015/1/india-makes-financial-world-record-as-millions-open-new-bank-accounts.

owners of financial capital) about where capital goes, to whom and at what price, and thus ultimately the terms on which business contributes towards social policy.³⁷

The state has actively pushed financial inclusion, albeit until recently more through ad hoc measures and policies – such as SHG and MFI promotion – than through explicit strategies. Only in India's 11th and 12th Five Year Plans (2008; 2013) did 'inclusive growth' and 'financial inclusion' come to feature prominently (Arun and Kamath 2015: 275). But different governments and levels of government have at least since the early 1990s used sticks and carrots – such as subsidies, legal obligations and public banking – to entice the financial sector to do more business with poor and rural populations. As Rao and Anand (cited in Arun and Kamath 2015: 276) say, 'the idea of financial inclusion had existed in essence, albeit, without the nomenclature, even before the [2008–2013] reforms'.

The central government's Priority Sector regulation, originally introduced in 1972 and expanded throughout the 1970s and 1980s, has also massively encouraged the push for financial inclusion. It stipulates that banks in India must allocate at least 40 per cent of their net credit (32 per cent for foreign banks) at preferential rates to certain targets, among which are agriculture, small businesses, infrastructure, self-employed persons, education, housing, microcredit and disadvantaged social groups. Priority Sector rules, a salient feature of India's financial system, have long been a sticking point in negotiations between financial actors and the state, particularly due to the costs they entail for banks (Nathan Associates 2013). Banks thus warmly welcomed microfinance and financial inclusion as counting towards Priority Sector targets, because of the reliable and easy returns that could be earned relative to other areas. Indian banks became keenly involved in financial inclusion particularly through loans to MFIs (Chen *et al.* 2010), but could also meet their targets by subscribing to bond issues from NABARD, which channelled capital onward to MFIs or into the SHG system. MFIs in turn have consistently lobbied to retain 'Priority' status, because it ensured access to abundant cheap capital (Mader 2013).

There is no single key forum of interaction or policy dialogue between the state and other actors over financial inclusion in India. A key broker in negotiations about how financial inclusion is to work, however, has been the RBI, which has increasingly pushed for a *bank-led* model for achieving financial inclusion, through no-frills accounts, correspondent banking, new branches and relaxation of norms. This comes after many years of support for SHGs and microfinance; in 2000, for example, the RBI freed all MFIs registered as for-profit non-bank financial companies (NBFC) from key regulations, including minimum capital or liquidity requirements, on the condition that they refrain from deposit-taking. This state support for MFIs led to the rapid expansion of commercial *credit-driven* microfinance in the 2000s.

Contrasting with the heavy-handedness of Priority Sector rules, until recently the Indian central government has pursued a decidedly hands-off approach to regulating financial inclusion itself. Instead of regulating microfinance, for instance, successive governments emphasised MFIs' self-regulation, use of industry standards and voluntary codes of conduct. These rules were developed by industry representative bodies such as the Microfinance Institutions Network (MFIN) and Sa-Dhan, often at the behest of government (Rozas and Sinha 2010). The representative bodies, meanwhile, have resisted attempts to regulate MFIs and insisted on the sector's capacity to self-regulate, even in the face of multiple crises culminating in 2010 (Arunachalam 2011; Mader 2013).

Only in its recent massive drive for universal financial access (programmes such as Swabhimaan and PMJDY) has the state again clearly taken the legislative initiative, albeit to actively push or enforce (not contain) financial expansion. The PMJDY Mission Document

³⁷ Whether financial inclusion is actually effective, ineffective, or harmful is another question (see, for instance, Mader 2015, 2016).

describes the initiative as a ‘national mission’ encompassing different stakeholders, including central government departments, the RBI, banks and bank associations, NABARD, and regional and local governments and banking committees (Gol 2014: 34–44). PMJDY depends on the compliance of the banking sector, but it is unclear what, apart from sheer legal stipulation, incentivises banks to offer accounts and services to the poor. The consequences of denying service or other instructions are unclear. A notice published by the Ministry of Finance announced:

This is to inform all concerned that if anyone wishes to open an account under PMJDY, he/she may visit to the nearest bank’s Branch / Bank Mitrs [agent office] and can open his/her account... if anyone is facing any problem/difficulty in opening of bank accounts, he/she may write to Mission Office, PMJDY or can register his/her grievance/complaint online on our website pmjdy.gov.in (write to us) or call at the numbers listed below.³⁸

PMJDY is effectively financial inclusion by decree, but without transparent enforcement. This may nonetheless work, because India’s financial sector remains strongly state-dominated (Shimizu 2010).³⁹ Public sector banks account for more than two thirds of all banking sector assets (down from more than 90 per cent in 1980). Likely because of the more direct capacity for government control, the vast majority of the PMJDY roll-out has gone ahead through public sector banks and (also government-led) regional rural banks.

Table C1 Official statistics, PMJDY accounts opened by 10 August 2016

	Rural accounts (millions)	Urban accounts (millions)	Total (millions)	Balance in accounts (INR billion)	% zero-balance accounts
Public sector banks	104.5	80.22	180.68	330.6	24.47
Regional rural banks	30.52	5.8	40.9	71.4	21.05
Private banks	5.2	3.3	8.4	152.4	36.47
Total	140.49	90.13	230.62	417.2	24.31

Note: 1 billion INR = approximately US\$15m.
 Source: Adapted from <http://pmjdy.gov.in/account>.

Despite the government’s reports of success, claiming that 230 million accounts have been opened in less than two years (see Table C1), the situation on the ground remains opaque. For instance, several Indian states have claimed 100 per cent coverage of households with bank accounts, but investigations for *The Hindu* newspaper revealed poor people faced serious difficulties when opening bank accounts; bank employees, business correspondents and households often were even unaware of the scheme (Venkatesan 2015). In mid-2015, CGAP (the World Bank’s microfinance agency) reported that bank correspondents and banks were making a loss on PMJDY-related activities (Bakshi *et al.* 2015). In short, while the government is now driving financial inclusion and is reporting successes, the actual progress is uncertain.

Conclusions – implications

India is today widely recognised as a global leader in financial inclusion, boasting rapid expansion of access to services. Its pathway of financial inclusion shows a protracted process of interdependent negotiation between the state and business (the financial sector),

³⁸ Downloaded from: www.pmjdy.gov.in/, 12 August 2016
³⁹ This should not be taken to suggest that the sector is static or statist. Due to the promotion of competition and market discipline, public and private sector banks in India show little difference in terms of earnings performance, efficiency and soundness (Shimizu 2010).

in which the state had an interest in deploying financial access as a palliative for social inequality, and financial business actors had an interest in acquiring new clients. These objectives may be either aligned or in conflict, depending on the conditions, as the spectacular episodes of both expansion and breakdown of financial inclusion initiatives show. The implementation of SHG, MFI and mass banking initiatives represent different negotiated outcomes of how financial development in India is to proceed. Overall, the case demonstrates how such initiatives which are commonly associated with 'business' approaches to poverty reduction often in fact reflect public policy choices that shape state–business relations. In this case, the state engaged in 'pro-market activism', pursuing social policy through expanding the reach of (financial) business.

Annex D – Case study: Private commercial farms and public land in Ethiopia

With just over 100 million people, Ethiopia is the second most populous country in Africa, second to Nigeria. Its government is a federal parliamentary republic, with nine self-governing regions and two city administrations. Following the fall of the communist regime in 1991, the government has been ruled by the Ethiopian People's Revolutionary Democratic Front (EPRDF).

The communist regime (aka Derg)⁴⁰ (1974–91) nationalised land and large-scale manufacturing and service industries. It left a diminutive formal private sector, with a large informal sector running alongside. Shortly after 1991, the EPRDF-led government implemented a series of policies to develop the private sector. It opened up sectors reserved for the state to the private sector but retained ownership of land and the provision of key services like power and infrastructure (FDRE 1995; Ayele 2003). It also introduced market-oriented policies and strategies. In the 2000s, it embraced the 'developmental state' approach, and went on to play an even more active role in the economy. It envisioned reaching middle-income status by 2025, reducing poverty along the way and attaining major development goals (Rahmato 2014).

Implementation of a series of strategies such as Agriculture Development-led Industrialisation (ADLI) and the recently concluded Growth and Transformation Plan (FDRE 2010) led Ethiopia to register a 10.9 per cent average annual economic growth over 2004–2015, and reduce poverty levels from 39 to 22.2 per cent, meeting many of the Millennium Development Goals. With 40 per cent of GDP, agriculture accounts for the lion's share of exports and employs at least three in four Ethiopians (World Bank 2016). As food security remained Ethiopia's goal, the government provided smallholders with improved inputs such as seeds and irrigation and promoted non-farm rural employment. ADLI had a limited export orientation, and participation of the private sector in agriculture was likewise limited. Consequently, Ethiopian agriculture remained dominated by smallholder farmers operating on two hectares or fewer. It also remained rain-fed, low-input and low-output.

The government's drive towards commercial farming came around 2001, as it moved to attract foreign capital into agriculture and catalyse a rural transformation from subsistence to commercial farming. The strategy was two-pronged: first in the cut flower sector, and second in large-scale commercial farming. The latter focused on three areas: export-oriented food crops including rice and maize; biofuel crops including palm oil and castor beans; and industrial crops, notably sugar cane and cotton⁴¹ (Rahmato 2014; FDRE 2010).

This case study focuses on this sustained growth period since the turn of the century, and explores state–business relations in the emerging private commercial farm sector. In these particular relations, the government aimed to increase domestic and foreign investment to promote growth, employment, etc. In return for business engagement in its programmes, it provided fiscal and non-fiscal incentives including subsidised access to land. Business, for its part, had various aims, including the creation of a competitive environment for business, and the reduction of risk of failure of business. Overall, the case study shows that while government-driven strategy led to some success, it also encountered problems around land use and from adverse effects on the livelihoods of communities.

⁴⁰ Derg (or dergue) is an Amharic term that refers to a military committee or council that ruled Ethiopia from 1974 to 1987.

⁴¹ Most cotton and sugar cane farms are government-run and are not covered in this case study.

State–business relations in the private commercial farm sector

Core actors⁴²

(a) The Ethiopian Horticulture Producer Exporters Association (EHPEA)⁴³ – The aim is to promote the competitiveness of the Ethiopian horticulture sector within the global market while at the same time addressing members' common concerns in production and marketing. At its start in 2002, the association had five members; by 2014 it had 94 member producers and exporters, covering 80 per cent of all flower farmers and exporters.

(b) The Ethiopian Horticulture Development Agency (EHDA) – Founded in 2008 to provide strategic support to the industry, facilitating global markets and building the capacity of investors in areas such as cold chain management and logistics. It aims to see Ethiopia as a prime choice in the international horticulture export market by 2025.⁴⁴

(c) The Agricultural Investment Land Administration Agency (AILAA) – Formerly known as the Agricultural Investment Support Directorate (AISD), created under the Ministry of Agriculture and Rural Development in 2009. It coordinates and provides technical and administrative support to investors. It is a 'one-stop shop' for land acquisition, including identification and delineation of potential agricultural investment areas.⁴⁵

Processes and events

Historically, business and EPRDF-led government relations have been fractious and shrouded in mistrust (SIDA 2004; Mihretu and Tolina 2015). Part of the business community perceives that it has not been fairly treated, suggesting that a few (often party-affiliated) have been favoured. Apart from symbolic 'consultation' processes, business also felt that it did not sufficiently contribute to policymaking, including on business registration and licencing procedures. The government questioned the ability of businesses to contribute to its policies and strategies. However, a formal dialogue between state and business was initiated in 2002 with the start of the Public-Private Consultative Forum (SIDA 2004). Although the Forum brought together the then Ministry of Industry and Trade and the Ethiopian Chamber of Commerce and Sectoral Associations, open and critical review of policies did not start until 2010. Since then the Forum successfully facilitated dialogue between the state and business, leading to improved customs procedures, business licencing and registration processes (Mihretu and Tolina 2015).

Turning to state–business relations in the commercial farm sector following its strategy on commercial farming, the government took a series of measures to engage with business. First, it created EDHA and AILAA (and its predecessor AISD) and strengthened other related agencies executing the policy. The Ethiopian Investment Authority (now Commission) and agencies such as the Ethiopian Revenue and Customs were reorganised to meet the needs of business. Second, the government actively courted international and domestic investors to engage in commercial farming (Keeley *et al.* 2014). Executive members of the federal and regional governments, and relevant agencies, held a series of conferences with business to introduce the policy and tax-based incentives and to discuss issues related to land access. Information on business opportunities was passed to potential investors. The government also conducted a coordinated and sustained business diplomacy effort aimed at international business. A Business Diplomacy Directorate was set up within the Ministry of Foreign Affairs. Diplomatic missions in major capital cities, where a large contingent of Ethiopian diaspora

⁴² Many state and non-state actors – indigenous communities, NGOs, researchers, etc. – also influenced both policy and execution.

⁴³ See: www.ehpea.org/

⁴⁴ See: www.ehda.gov.et/web/guest/home

⁴⁵ See: www.moa.gov.et/en_GB/agricultural-investment-directorate

and potential investors are based, were targeted. High-level government officials (including the president and prime minister) paid visits to target countries and met with respective government and business representatives. They also held side meetings with business leaders at the UN Summit and Davos events.

Businesses too, individually and collectively, engaged with the government. For example, a meeting between the late Ethiopian Prime Minister Meles Zenawi and Pierre Castel, founder and president of the Castel Group and BGI International, led to the successful establishment of the Castel Winery business in Ethiopia.⁴⁶ The cut flower sector, represented by EHPEA, successfully lobbied the government to develop a five-year sector strategy and provide access to land and credit, as well as coordinating with Ethiopian Airlines to ship flowers to European markets. Investors in large farms, however, did not have a formal association nor did they approach the government in an organised fashion.

The political economy of state ownership of land and the land ‘market’

The main arena of state–business interaction in Ethiopia is concerned with access to land. Because of their great importance to the livelihoods of a large segment of the population, access to and use of land have been contested for generations. Since 1991, EPRDF have argued that private ownership of land dispossesses the peasants of land and leads to urban unemployment (Rahmato 2014; Ayele 2003). Following this, in the 1995 constitution land was retained under the ownership of the state. Furthermore, constitutional power over the acquisition and transfer of land was placed under the regional governments (FRDE 1995).

Today, land is only transferred by lease, as sale is prohibited by law, and the sole supplier of land is the state. Land leasing involves a long bureaucratic process, and altering the order of applications has been a common practice, allowing certain businesses to jump the queue by quasi-legal or illegal means. However, in 2009, responding to investors’ complaints about the complexity of obtaining land, the Federal Government set up a ‘land bank’, administered under AILAA, to transfer land of 5,000 hectares or more (Rahmato 2014). Different factors enter into land lease negotiations: location, quality and size of land, duration of lease period, and other conditions of use. In theory, land leasing can be done by auction in an open and transparent manner; however, as details about the land in question are often unknown, the government leases land through negotiations. Lease deals were made at what many regarded as ‘giveaway prices’ – around US\$2/ha/year for 25 to 45 years (Oakland Institute 2011).⁴⁷ But investors still complain about the time it takes to process lease deals – according to a UNDP study, these took an average of a year, unless speeded up by payments to officials, which typically reduced the time to 232 days (UNDP 2013).

The emerging private commercial farms

The government aimed to attract capital, technology and expertise, and create jobs, expand food production and reduce poverty. But what did the policy on private commercial farming and state–business relations produce? Evidence on the number and size of farms, employment, production etc. are hard to come by; the brief below mainly refers to numbers of farms.

The ideal location for cut flower farms is high-altitude, flat land with a cool climate. The sector also needs to be close to reasonably well-developed infrastructure to access domestic and international markets, and near urban centres with high potential labour force. Such factors

⁴⁶ See details here: www.investethiopia.gov.et/stories/success-stories.

⁴⁷ Oakland Institute (2011) showed land lease rates in Ethiopia ranged from US\$1.25–40 per ha/year whereas the African average ranged US\$350–800 per ha/year.

led cut flower farms to be set up in pre-urban areas, particularly close to Addis Ababa (Rahmato 2014; Oqubay 2015). From five farms involved in the production and export of cut flowers in 2003, the sector grew to about 100 in 2014. Exports also grew from three tons in 2003/04 to more than 50,000 tons in 2011/12, generating close to US\$1bn in export earnings. However, farm sizes are small, often under 500 hectares, but labour-intensive. From 2007 to 2012, the sector's employment doubled from 25,000 to 50,484; 70 per cent of these employees were female (Oqubay 2015; Gebreeyesus and Lizuka 2010).

Oqubay (2015) singled out 'state activism' and 'industrial policy' as key success factors in the cut flower sector. For him, government commitment (or political will) led to the development of a strategy for the sector; on the positive interplay between businesses and the state, he noted the industry 'picked the state' and the state 'picked the firms'. Nonetheless, business – notably its association – played an equally crucial role in promoting competition among members while at the same time putting members' common concerns to the government. The foreign direct investment (FDI) that was attracted to Ethiopia – the single-minded joint business–state focus on export, development of performance standards, etc. – was also a key explanation of the birth and subsequent success of the sector. In a nutshell, success was a product of effective state–business relations.

Large-scale commercial farms, on the other hand, emerged during the post 2007–08 food price and supply crisis when, according to Rahmato (2014:26), the government wanted to benefit from opportunities opened up by the crisis. Food volatility and price rises drove businesses and food importing countries to look for secured food sources overseas. Investors came mainly from emerging economies, notably India, the Middle East and the diaspora.

Deininger and Byerlee (2011) estimate that around 406 large-scale commercial farmlands were leased, occupying approximately 1.19 million hectares (although Rahmato (2014) mentions 3 million to 3.5 million hectares). Significant land leases were taken out, particularly in sparsely populated regions such as Benisgangul-Gumz and Gambella. Eight leases were for more than 25,000 hectares; one was more than 100,000 hectares. Many commented that these large farms were 'unmanageable' and adversely affected pastoralists and semi-pastoralists (Keeley *et al.* 2014). Estimates show that no more than a third of leased farms (and far fewer in terms of area) have become operational.⁴⁸ It has also been reported that land is being used for speculative purposes (Keeley *et al.* 2014).

The question remains: why was the 'state activism' that worked for cut flowers ineffective in the case of large-scale commercial farms? Studies are limited, but the emerging evidence is startling: large-scale commercial farming was conceived to produce export crops. However, neither capital nor knowledge and expertise came in as expected. Some farms became too large to manage, and weak land governance and regulation meant that new owners obtained deals for speculative purposes (Rahmato 2014; Oakland Institute 2011). The Oakland Institute (*ibid.*) in particular has consistently called it a 'land-grabbing' policy which threatened communities, wildlife and the broader environment. Its research details a list of unmet goals, including no improvement in food security, forest lands being cleared or burned, and wildlife habitat lost. Finally, unlike in the cut flower sector, large-scale farmers did not have a collective voice to put their predicaments to the government. In effect, weak state–business relations contributed to what is emerging as failed large-scale commercial farming.

Conclusions – implications

Two turning points in Ethiopia's recent past, namely changes in government in 1974 and 1991, fundamentally changed the climate for business: the former stifled business, while the

⁴⁸ See: <https://ig.ft.com/sites/land-rush-investment/ethiopia/>

latter allowed it to perform, but with some restrictions. Moreover, the state decided whom to support and where, and which products and markets. By virtue of its power over resources, the state determined the prices of critical inputs such as land, and leased it at subsidised rates in exchange for new capital, knowledge and expertise.

The government's formal acceptance of business as a partner in growth and development efforts was the starting point for positive state–business relations. Where interactions were sustained and collaborated through EHPEA (the business association) and competition within business was maintained, more success was registered. Preliminary evidence also suggested that state promotion of, and engagement with, large commercial investors was not overly successful. The few farms that were set up adversely affected the livelihoods of indigenous communities, forest land and wildlife. What the government promoted as 'transformational' for Ethiopian agriculture has been seriously contested, particularly by rights groups, as 'land-grabbing'.

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