THE POLITICAL ECONOMY OF SUBNATIONAL INDUSTRIAL PROMOTION IN INDIA AND MEXICO

BY

ERIC M. JEPSEN

B.A., Political Science, Texas Lutheran University, 1994
M.A., Political Science, The University of New Mexico, 1996

DISSERTATION

Submitted in Partial Fulfillment of the
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UMI Number: 3230833

Eric Michael Jepsen
Candidate

Department of Political Science
Department

This dissertation is approved, and it is acceptable in quality and form for publication on microfilm:

Approved by the Dissertation Committee:

Wendy L Hansen, Chairperson

Accepted: Amy B. Wohlert
Dean, Graduate School

JUL 25 2006
Date

Eric Michael Jepsen
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____________________, Chairperson

Kenneth M. Roberts

Karen L. Remmer

Accepted: Amy B. Wohlert
Dean, Graduate School

JUL 25 2006
Date

DEDICATION

To Kaiya.

In the words of the great American troubadour Debbie Boone,

"You light up my life."

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ABSTRACT

How have subnational governments in India and Mexico coped with their newfound economic policymaking responsibilities due to increased policy decentralization and market liberalization within the two countries? To gauge the relevant factors influencing policy choice across the Indian and Mexican states, my research examines the factors that are dictating subnational industrial policy choice within the two country cases. By utilizing both a large-n, statistical analysis of policy choice and a small-n, qualitative analysis, the dissertation seeks to explain subnational industrial promotion policies by testing propositions drawing from institutional and interest group explanations for policy choice. Individual chapters examine the level of industrial policymaking across all states in India and Mexico and seek to trace the processes underlying policy formation in the Mexican states of Aguascalientes, Queretaro, San Luis Potosi; and the Indian states of Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh. The dissertation seeks to inform the comparative political economy literature on economic development by examining the subnational level of analysis

within two large federal countries. The dissertation uses a dataset that was partially gathered during fieldwork in the two countries for the statistical analyses, and information from over 100 interviews for the qualitative study of policy choice and strategy.

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CHAPTER 1

INTRODUCTION

Across all regions of the world, the contemporary phenomenon of economic globalization is affecting the nature of governance and interstate relations. Whereas the relative levels of trade openness, imports, and exports have only recently surpassed the levels seen in the last great era of globalization in the late 19^{th} century and early 20^{th} century, this period of globalization has been a fundamentally different one in many ways. Of concern to this dissertation is the affect of globalization on municipal, state, and provincial governments around the world. These subnational governments are increasingly exposed to the global economy and have been forced to engage it in ways previously thought unthinkable. Whether it is local governments in South Africa that are developing there own intellectual property regulations or district water managers in India and Bolivia attempting to develop 50-year water policies to comply with aid agreements and requisition requests from multinational corporations, subnational governments interact to a greater degree than ever before with the global economy. While it is customary for the political science literature and for public policy analysis to focus on the nation-state "under globalization," much less attention has been paid to how subnational governments grapple with the constraints and opportunities in the globalizing world.

Over the last several generations of comparative politics scholarship, a number of crucial questions have continued to vex practioners within the field. Some of these key questions will be directly addressed by this dissertation. Specifically, how should governments best order their economic affairs in order to attract industry and develop their economies? And secondly, why have governments, over time and under different conditions chosen to pursue different development strategies? Comparative scholarship has usually addressed these questions at the inter-national level of analysis, with relatively few that examine the intra-national level. This dissertation will look for answers to these questions by utilizing a unique comparative research design that examines subnational economic policymaking in India and Mexico. The dissertation is distinctive in that it utilizes both quantitative and qualitative tools of inquiry within a cross-regional framework.

Method of Analysis

This dissertation employs a research design that uses quantitative and qualitative methods in order to explain patterns of subnational policymaking in India and Mexico. The particular research design that is utilized to explore subnational development policy parallels a "most different systems" design as defined by Przeworski and Teune (1970). In examining the same questions across two different national systems, I try to identify common causal patterns at the subnational level and thereby generate robust theoretical findings. The analysis of subnational policy focuses specifically on India and Mexico—two of the biggest nations and most important recipients of foreign investment in the developing world. India's annual average FDI and portfolio investment flows expanded more than eighteen-fold from 1991 to 2002, rising to $10.2 billion from $400 million. Non-agricultural sectors have received well over 80 percent of these monies. Similarly, Mexico has seen its FDI and portfolio investment flows increase from $3.6 billion in

1989 to over $25 billion by the late 1990s. These trends are likely to continue for the foreseeable future (EIU 2000; World Bank 1999).

India and Mexico are federal political systems with relatively large numbers of states, which offers opportunities for comparing policies across a large number of political units that are similarly situated with respect to the international system. Both also evince high levels of intra-national variation in industrial development. Yet the two countries differ significantly with respect to issues that might be expected to affect industrial policy, including historic patterns of federal-state governmental relations, mode of insertion into the international economy, and regional development contexts. Despite these differences, I argue that policies across the subnational level in the two countries vary similarly in response to hypothesized institutional and interest group conditions. The advantages of utilizing the subnational-level of analysis, across two states is that we can have more confidence in attempts to hold other factors constant, as all the states within India and Mexico face the same legal and political environment relative to their federal government. The design is such that there is a most-similar systems comparison that is nested within a most different systems comparison across India and Mexico. It has been argued that this type of research design, the incorporating the subnational level of analysis, is a fruitful type of inquiry (Snyder 2001), with this dissertation further advantaged by the inclusion of a cross-regional comparison.

The research was carried out in two countries using both qualitative and quantitative evidence. By nesting an in-depth qualitative analysis within a systematic quantitative analysis, one guards against the limitations of each research technique. This research design represents one of the more promising methods for social science research (King, Keohane, and Verba 1994; Rogowski 1995; Tarrow 1995).

The quantitative component of the research entails a statistical analysis of subnational industrial promotion and deregulatory policies using two large-n panel/time-series studies, with heavy reliance on budgetary, fiscal, and institutional data. In the case of India, I will test my hypotheses via a pooled, intra-country statistical analysis of the 25 Indian states from the federal economic reform in 1991 to 2003. Mexican subnational industrial promotion policies will be studied using a similar large-n panel/time-series analysis of 31 Mexican states from the mid-1980s period of liberalization and decentralizing reforms to 2003.

Drawing upon the cross-sectional time series analysis, I test my basic hypotheses about industrial promotion with a model that incorporates several key control variables into the model: economic distress, level of urbanization, level of development, and education level. Empirical findings in the U.S. literature (Feick 1992; Reese 1994) suggest that states undergoing short-term economic distress relative to other states spend more on industrial promotion programs. Distress is measured by subtracting the yearly unemployment rate for each state from the calculated national average. The U.S. literature has also found that more urbanized and more educated states tend to spend more on industrial promotion programs (Ambrosius 1989; Dye 1966, 1984; Elkins et al 1996; Plaut and Pluta 1983). I will operationalize these variables by incorporating measures of urbanization, GDP per capita, and literacy rates for each state in India and Mexico.

The second empirical component of the research is a small-n comparison of three states in each country that exhibit significant differences with respect to their institutional situation. Since the types of policy mixes pursued by individual states can only be partially examined on the basis of quantitative data, the small-n comparison is designed to take a deeper look at the role played by local institutions in the policymaking process. By utilizing this type of research strategy, I try to achieve a more in-depth understanding of the interaction between institutions and policy over time at the subnational level. This component of my research will resemble a most-similar research design strategy (Przeworski & Teune 1970). The dissertation holds constant the national political context for each case and investigates cases that have similar levels of development, allowing for the isolation of the causal effects of subnational political institutions and interest groups. Within each country, I have selected three states that are highly similar in terms of structural conditions and geographical location, but that differ significantly over the last decade in industrial policy orientation.

The qualitative portion of the research is designed to flesh out the analysis of subnational policy by examining aspects of local-level policy processes that lead to the distinct policy strategies. The qualitative research is thus designed to add to and supplement the quantitative analysis of the level of industrial promotional activities by examining more in depth the level of activities and by addressing questions about variation in types of industrial and deregulatory policy choices pursued at the subnational level. It is expected that the same set of institutional factors that affect the level of activity shape policy type.

Overview of the Dissertation

Chapter 2 details the theoretical framework employed by the dissertation. By looking at literature from three major subfields of political science—comparative politics, international political economy, and American politics—we gain insight from theory-building from different parts of the discipline. There has been an artificial divide between some of this literature, and this chapter will seek to build theoretical bridges in order to provide more leverage for our examination of subnational development policies in India and Mexico. Chapters 3 and 4 are devoted to the examination of the subnational Indian case. Chapter 3 utilizes a set of statistical models to investigate why state goverments in the country have been doing different things in the economic policymaking sphere. Chapter 4 is a qualitative, detail-rich exploration of subnational policy choice in three states within India from 1991 to 2003.

Similar to the previous two chapters, Chapters 5 and 6 examine the Mexican case at the subnational level. Chapter 5 uses similar statistical models to present evidence as to why Mexican states have adopted a diversity of economic development strategies over the last 20 years. Chapter 6 is a qualitative, in-depth exploration of subnational policy choice in three states within Mexico from 1988 to 2003. The conclusion in Chapter 7 synthesizes data garnered from both India and Mexico and places it in a larger comparative context. Both countries lend themselves to comparison with other federal and non-federal countries in terms of subnational economic policymaking. The broader conclusions drawn from the empirical chapters are that local level institutional variation and subnational interest group activity influence the content of industrial policy in the Indian and Mexican states.

And finally, there are numerous implications of these findings, as the evidence from India and Mexico suggests that future research should incorporate different ways of measuring and accounting for policy choices by subnational governments. Existing theory has limited explanatory power for telling us why states have been doing what they have been doing, and with the increasing importance of subnational governments in the sphere of economic policymaking, these limitations will become more apparent in the years ahead. As well, the innovative research design employed in this dissertation shows the clear advantages that can be obtained from cross-regional work, and that which employs both quantitative and qualitative analyses of empirical in comparative politics.

CHAPTER 2

THE POLITICAL ECONOMY OF SUBNATIONAL INDUSTRIAL PROMOTION IN INDIA AND MEXICO:

THEORETICAL PERSPECTIVES

Ascertaining the merits of competing economic development models across different regions and cases has been a focal point of study for comparativists and comparative political economists for the last 40 years. In addition, much literature in recent decades in the American politics subfield has examined competing explanations for different types of economic development activity employed by states and local governments in the U.S. Similarly, a key area of the international political economy literature has focused on the role of states in economic development. Much of this research focuses on the role of the nation-state in the context of competition within the global economy. All of these three expansive categories of the economic development literature, broadly defined, serve to guide this dissertation in its exploration of policy choice by the Indian and Mexican states in pursuit of economic growth and the attraction of new industry to their political localities. This chapter will examine the theoretical roots and competing explanations across the comparative political economy, international political economy, and U.S. politics literatures. In addition, there will also be a discussion of the theoretical foundations of the hypotheses to be investigated in subsequent chapters.

Theoretical Underpinnings

The dissertation evaluates the political economy of industrial promotion programs at the subnational level in India and Mexico. Much of the existing literature on the political economy of development places central emphasis on the role played by national governments in fostering new economic investment. Over the past several decades, however, market-oriented reforms in combination with administrative decentralization have increased the importance of subnational governments for promoting industrial development (Chaudhury 1993). To shed new light on these trends, the dissertation addresses two central questions about subnational industrial promotion policies in less developed and emerging market nations. First, what accounts for variation in the level of development activity by governments across subnational political units? Second, what factors account for variation in the types of industrial policies adopted by subnational governments to promote foreign investment and industrial development? In order to properly frame the research question, we must examine the competing claims in the literature that detail what governments have been doing in the increasingly competitive environment.

Comparative scholars devoted widespread attention to the political economy of development in the decades after World War II. Throughout the era, the state's involvement in the economy has been a crucial topic of the literature. Likewise, the need for countries to be protected from foreign competition was a major focus of theoretical interest and policymaking. Yet, over the past two and one-half decades there has emerged a new emphasis on the free market and integration into the world economy. The fundamental challenges for national governments have come to be defined largely in terms of maintaining macroeconomic stability, improving social conditions, increasing international competitiveness, and creating "strong" but "lean" institutions capable of effectively implementing government policy. The logic underpinning shifts in national development policy implied that governments should limit their economic role and refrain from "picking winners" in the marketplace Williamson 1990, 1994).

The Developmental State and the East Asian Model

The origin of the literature on the "developmental state" can be traced to the influential book *MITI and the Japanese Miracle* by Chalmers Johnson (1982) on the role of the Ministry of International Trade and Industry (MITI) in guiding Japanese economic policy. His assertion that the crucial position played by the state in the design and implementation of Japanese economic policy presented a direct challenge to the noninterventionist proclivities of governments in the West. Johnson's book and the literature that came as a result of positive and negative reactions to it provide a useful counterpoint to the neoliberal development model that has come to be the dominant economic development paradigm in the last 15 years. At a similar time Skocpol's *et al* (1985) work on "bringing the state back in" led a generation of scholars to reexamine the function of the state as it pertained to economic growth and development. Other roots of the model can be attributed to work stemming from Prebisch's (1950) early analysis of the limits of markets in the Latin American context in light of the need to protect infant industry and Gerschenkron's (1947) seminal exploration of the problems associated with state planning in the Soviet Union.

Other authors asserted that a similar level of state planning and coordination as in the Japanese case could be found in other countries in East Asia. Books and articles by Haggard (1991), Kohli (1999), and Woo-Cummings (1999) demonstrated the importance of the state bureaucracy in the South Korean case and its own economic "miracle."

Likewise, other authors pointed to the crucial role played by the Taiwanese state in that country's economic development and industrialization (Gold, 1984; Wade 1991, 1995.) As Woo-Cummings (1999) has noted, the major finding from this virtual cottage industry of development state writings was that what the development state came to represent was not one ideal type for the role of the state in economic policymaking, but instead a heterogeneous collection of writings and theory building that sought to incorporate government involvement in the economy back into the debates about differing models of economic development.[1]

An earlier work that attempted to bridge the gap between the East Asian literature on the developmentalist state and the Import Substitution Industrialization (ISI) literature on Latin America was the work by Gereffi (1990) and Wade (1990) in the edited volume by Gerrefi & Wyman (1990) which sought to explain the divergence in economic development patterns within the two regions by examining the role of governmental policies and domestic institutions, as well as social actors and cultural factors. Other important scholarship detailed the specific regional traits of the Latin American cases which came to be known as the *desarrollista* (still development though) states to differentiate them from the East Asian NICs (Maxfield 1990; Schneider 1997, 1999). Brazil and Mexico were states most often compared to the East Asian cases in order to understand the key cross-regional differences in developmental trajectories. Likewise, the work of Evans (1995) on embedded autonomy tried to identify crucial reasons as to why state intervention succeeds in some cases while failing in others. In his analysis of

[1] Woo-Cummings in her introductory chapter in The Developmental State (1999) has an expansive discussion of the history of the writings on the developmental state. Likewise Chalmers Johnson's (1999) chapter from the same edited volume serves as a broad and personal discussion of what his 1982 book inspired in the comparative political economy and East Asian literatures.

the computer industries in Brazil, India, and South Korea, Evans argues that institutional creation and adaptability for economic policymaking was the result of the particular ties that the state had with the private sector and the intervening social relationships.

Neoliberalism and the "Washington Consensus"

The first use of the term "Washington Consensus" in 1989 described the broad parameters of what at that time was the established conventional wisdom among development economists, international financial institutions like the World Bank, and a major portion of the Washington-based political establishment (Williamson 1990). In addition, as Williamson made clear in later writings, an important source for what Feinberg (1989) named the "universal convergence" around the ten crucial policy changes was the input from local development economists and government officials in the Latin American region (Williamson 2003). Articulated in the context of the debt crisis that gripped Latin America for much of the 1980s, it was set in direct opposition to the rising popularity in the literature of the applicability of the developmental state model to the region, and perhaps more importantly, the bankruptcy of the Import Substitution Industrialization (ISI) model in practice throughout much of the developing world. Although works by Bates (1981) de Soto (1989) were earlier, seminal critiques of state intervention and the negative consequences associated with high levels of state involvement in the economy. The original consensus detailed the ten reform areas that developing states should pursue in order to reorient their economies towards more reliance upon the private sector. These can be summarized as follows:

1. Budget deficits...small enough to be financed without recourse to the inflation tax.
2. Public expenditures redirected from politically sensitive areas that receive more resources than their economic return can justify...toward neglected

fields with high economic returns and the potential to improve income distribution, such as primary education and health, and infrastructure.

3. Tax reform...so as to broaden the tax base and cut marginal tax rates.
4. Financial liberalization, involving an ultimate objective of market-determined interest rates.
5. A unified exchange rate at a level sufficiently competitive to induce a rapid growth in nontraditional exports.
6. Quantitative trade restrictions to be rapidly replaced by tariffs, which would be progressively reduced until a uniform low rate in the range of 10 to 20 percent was achieved.
7. Abolition of barriers impeding the entry of foreign direct investment.
8. Privatization of state-owned enterprises.
9. Abolition of regulations that impede the entry of new firms or restrict competition.
10. The provision of secure property rights, especially to the informal sector. (Williamson, 2003; 324)

The contrast with the developmental state model is stark; there was a very small, defined role for the state to play and in most cases, reforms should seek to narrow the scope of the involvement of the state in the economy.

Later iterations of this development model have moved beyond what has been described as the "first-generation" reforms to those that suggest that more attention should be paid to the types of institutions that can regulate the elements of the Washington consensus. Specifically, the post-Washington Consensus consensus adds the following second order reforms to the original ten: strengthening corporate governance, increasing anti-corruption measures, providing flexible labor markets, abiding by WTO agreements, implementing developed world financial codes and standards, opening "prudently" the capital account, reforming exchange rate regimes, forming independent central banks, providing adequate social safety nets, and targeting poverty reduction (Naim 2000; Williamson 2003). By and large, these supplementary measures would soften some of the social pain associated with the original (still viable in their proponent's vision), and provide for a more complete reform package that would allow for economic growth and development.

In sum, this section examines the opposing ends of the theoretical literature on the proper role for the state in economic development. On one end of the continuum we have the neoliberal literature that suggests that the state should play a small role in guiding economic policy. On the other end we have the theoretical literature stemming from the developmental state school of thought which argues that a government can intervene, at certain times, for certain reasons, in guiding economic development. In later chapters we will see that this false divide in the national-level comparative political economy literature fails to properly address certain sets of developmental questions at the subnational level in India and Mexico.

The International Political Economy Perspective

While for the purposes of this analysis, we divide the discussion of political economy into the subfields of international political economy and comparative political economy, there is much scholarly overlap between the two. This section details the area of the literature that concerns itself with the role of the state in light of the pressures associated with economic globalization. Dating back to the work of Peter Katzenstein (1985) on the relative economic position of the small states of northern Europe in the context of a competitive global economy, scholars have attempted to paint increased trade exposure as either a constraining force or a helpful agent in terms of its effect on the relative policymaking space of governments.

Weiss (2003) provides a helpful typology of the recent literature on the subject of the role of government policy under globalization. Broadly categorized, the impact of globalization on state policymaking is either characterized as constraining or enabling. Proponents of the constraint school argue that the existence of mobile finance capital, large multinational corporations (MNCs), and the competitive pressures associated with the contest for economic development among nations, leaves little room for certain types of governmental policies. As discussed amply in the popular literature on globalization, Friedman (1999) posits that the "electronic herd" will put downward demands on governments as they "race to the bottom" in order to remain competitive with other countries. The political economic literature is rich with works that seek to paint a heavily constrained role for the state in the increasingly interdependent world. Many scholars argue that there has been a great decrease in the maneuverability of national governments (Cox 1997) and that private actors have become more powerful relative to the regulatory capabilities of states (Scholte 2000; Strange 1996). As the role of domestic and international capital looms larger, states will be forced to relinquish roles they once played in the pursuit of economic development (Rodrik 1997). Rosenau (1995, 2000) argues that the state is now just one of many actors playing a role in governance, whereas previously it had near absolute power.

The other contending perspective is articulated by numerous authors who suggest that globalization has instead provided an equal number of opportunities for governments. Garrett's (1998) important demonstrated that the global economy creates opportunities for governments as well as constraints. His argument that it is not necessarily the case that capital always fairs better relative to labor in the context of the globalization of markets, but that also pushed organized labor closer to certain parties within democracies, and been a real force for poverty alleviation under certain conditions. Weiss (1998, 2003) has argued that this increased interdependence does not necessarily imply a corresponding increase in competitive insecurity, but instead a possibility for policy innovation and initiative. Keohane and Nye (2000) have also posited that there are some degrees of freedom for countries based upon their underlying institutional character. Some literature on the developed world has found that openness does not necessarily lead to constrained policymaking, but that instead states can proactively engage globalization by targeting spending in ways that protect against the harsher effects of increased exposure to the global economy (Boix 1998; Quinn 1997). Likewise, other studies have demonstrated that the underlying institutional situation in a country explains more in the way of policymaking, and that enabling environments for protection can coexist with the competitive pressures (Swank 2001, 2003). Doner (2001, 2003) has argued that in the case of Thailand and its pattern of industrialization, the simple neoliberal/developmentalist divide does not address the underlying institutional diversity which affects the content of development policy.

In sum, there is a significant part of recent international political economy theory which allows space for policy innovation in the context of globalization. Specifically, the variety of economic decision-making institutions and patterns of state-business relations can serve to either exacerbate or lessen the impact of global market forces on the room for maneuverability for economic policymaking by states. While there has been a good deal written since the middle 1990s on the constraining nature of the global economy, a more recent, and theoretically richer literature has argued that organizational and institutional contexts mitigate the effects of globalization on national-level politics.

The United States Politics Perspective

Over the course of the last several decades, there has been much work that has analyzed the competition for investment at the subnational level in the United States. A sizable amount of research has demonstrated that American cities and states, within the context of greater global capital mobility, are in competition for investment with each other. Most of the research in this vein has concentrated on explaining the extraordinary variance in policies that exists across both the city and state unit of analysis. While American scholarship has evolved in sophistication and theory-building over the last 30 years, a large amount of it utilizes the earlier work of Paul Peterson as a touchstone for mapping state and municipal responses to intra-jurisdictional competition (Peterson 1981). His later work (Peterson 1995) would show that the era of competitive federalism was the result of the end of the period he called legislative federalism that should guide our understanding of state policymaking in the post-World War II time period, extending to the 1970s. In those decades, the logic controlling state behavior stemmed from the necessity of competing with each other through connections with their Congressional representatives in Washington DC. While the earlier era was not different in kind from the modern competitive federalist one, states and municipalities became much more active in later years because of the changing nature of federalism in the United States. States were increasingly responsible for revenue generation, making older federal-centric models of development less viable (Brace 2002).

Beginning with *City Limits*, Peterson's work on investment climates across subnational governments set the stage for further analysis by positing a demand-side notion of the setting of industrial policies by subnational political units. His innovative work suggested that businesses would base locational decisions on the relative amount of services provided by local governments as compared to the sum of taxes that the company would have to pay. This logic governing the demand side would force subnational governments to make policies that are attractive to business in order to lure new companies to their particular locality and also to keep those already there from moving on to another city or state. This basic collective action problem would lead states and cities to compete with each other by offering subsidies, tax abatements, sales tax holidays, and other financial inducements to encourage investment within their territory.

Over the last one and a half generations, this key insight spurred the creation of a large amount of American Politics research that examined the nature of the competitive environment across the U.S. states and sought to explain policy choice and efficacy. Existing literature has identified three main strategies that states can employ to foster economic development. First, subnational governments can attempt to control the regulatory policy environment. Saiz (2001) has characterized this as the generalist "locational" approach that attempts to lower the costs to business. These types of programs serve to lower the costs of production and generate incentives for new investment. This tactic might take the form of "right to work" laws, the streamlining of licensing and inspection processes (Plaut and Pluta 1983), or the removal of environmental or safety regulations that might discourage the entry of new investment (Leicht & Jenkins 1994).

As a second approach, U.S. states can try to attract new investment with targeted incentives for certain sectors in the economy. These types of promotional strategies were first identified by Sternberg (1987) and later refined by others in the comparative U.S. state literature (Saiz and Clarke 1999; Wolman & Spitzley 1996). Policies include the construction of physical and technological infrastructure or the promotion of human capital development (Fulton and Newman 1993; Licate 1993; Perry 1994; Rapp 1994; Saiz 2001; Saiz and Clarke 1999; Sbragia 1996). States can also adopt incentive approaches, including subsidies, and sectoral targeting incentives, to attract investment and improve their own economies relative to other states (Fosler 1988; Weber 1984).

Conveniently enough, the third type of subnational development strategy for the U.S. states has come to be called the "Third Wave" of economic development policymaking (Brace 2002). These types of strategies encompass entrepreneurial economic development approaches, which are more proactive than traditional state "promotional" expenditures. Third wave policies include those that create new types of institutional relationships to encourage investment (Clarke and Gaile 1998; Eisinger 1988; Saiz and Clarke 1999; Sherman, Wallace, and Pitnety 1995; Sternberg 1987). States adopting this tactic might focus on attracting investment in high-technology sectors or create a public-private partnership that functions as a state development and/or credit corporation (Saiz 2001).

Federalism and the Level of Analysis Question

Regardless of whether policy prescriptions for economic development have been statist or neoliberal, research has tended to focus on the national level in comparative politics outside of some of the case literatures like those from the U.S. and advanced industrial states like Germany. As a result, the growing diversity of development patterns at the subnational level has been overlooked within the political economy literatures. Scholars have assumed that the politics of creating programs to attract foreign investment and stimulate industrial growth revolve around national executives, legislatures, and bureaucracies rather than state or provincial governments. While some authors have realized the inadequacy of this line of reasoning (Echeverri-Gent 1999; Locke 1995; Montero 1997, 2001a; Weiner 2000), there has been little systematic and rigorous comparative analysis outside the U.S. context of subnational development policies.

With the global trend toward the decentralization of policy responsibilities, this research gap looks particularly problematic. The pressures for competitiveness in the global economy have caused an increase in the relative importance of international and local actors at the expense of national governments (Watts 1996). This "glocalization" (Courchene 1995) has resulted in increasing devolutionary pressures on national governments, especially within federal systems, and the emergence of subnational development policy as a major locus of innovation for industrial development (World Bank 1995, 1999). Hence, at the same time that national governments have come under intense international market pressure to reduce their economic roles, subnational states have maintained and even expanded their industrial promotion regimes (Montero 1997, 2001; Rodriguez 1998; Sinha 2003), creating a major disjunction between national and subnational policy trends. Largely hidden from view at the subnational level are an astounding and ever expanding array of subsidies, low-interest financing, tax credits, abatements, deferments and exemptions, subsidized employee training, and assistance with site selection and preparation (EIU 1997, 2000; Price Waterhouse 1996; World

Bank 1995, 1999). Equally evident are attempts to create "pro-business atmospheres," including lower taxes and minimal regulatory policies on the labor and environmental fronts (Plaut and Pluta 1983).

Given the tendency in the comparative literature to treat industrial promotion and deregulation as alternative rather than as potentially complementary dual strategies, these trends raise important and largely unanswered theoretical questions about the political economy of development. The literature on the developmental state provides insights into the political conditions that give rise to interventionist strategies of development. The more recent body of literature on market-oriented reform, on the other hand, addresses questions regarding strategies that favor deregulation. What has yet to be analyzed are the politics surrounding development strategies that combine deregulatory and promotional policies—precisely the kinds of policies that are undergirding development efforts at the subnational level across the international system.

Addressing this issue calls for a theoretical approach that bridges the two rather discrete and separate bodies of literature on the political economy of national development, taking us beyond the assumption industrial promotion strategies and deregulatory strategies are distinct policy choices at the federal-level. The evidence from the subnational level, however, suggests that governments pursue both types of development approaches, often in combination with one another, thus calling into question the adequacy of our understanding of the politics of development. Likewise, recent evidence would suggest that the international political economy literature which examines the constraints and opportunities of the global economy for policymaking, fails to incorporate the growing role of subnational governments in the process. Municipal, provincial, and state governments are increasingly responsible for policies designed to generate investment and growth, while the literature has largely treated these actors as secondary.

Theoretical Orientation and Working Hypotheses

While the objective of national economic policy is to promote aggregate employment, production, and purchasing power, the aim of state economic development is to create investment in a certain geographic location (Brace 1993). Individual state governments have little effect on larger macroeconomic issues, but they can provide incentives for businesses to invest in a particular location. These incentives are considered crucial for attracting investment and generating a multiplier effect that fosters job creation and the "rippling" of overall welfare gains. Hence it has long been recognized that U.S. state and local governments compete against each other for capital and investment (Peterson 1981). On an annual basis, state and local governments in the U.S. spend billions of dollars on development plans to attract and keep business (Saiz and Clarke 1999). Subnational governments in Germany exhibit the same pattern (Begg & Mayes 2000), as do the states in the cases of India and Mexico.

The critical questions that are raised by variations in subnational development efforts across subnational governments are thus twofold in nature. First, why are some states more active in the pursuit of investment than others? Second, why are there different state policies such as the standard "smokestack-chasing" promotional strategies and other policy approaches, including deregulation that states pursue?

Drawing upon both the comparative literature on national economic development and the U.S. literature on state economic development, my central theoretical explanation is that the type and level of subnational development activity reflect local-level institutional relationships. These relationships will allow us to differentiate "programmatically rich" from "programmatically lean" states (Elkins, Bingham, and Bowen, 1996), as well as to explain variation in the types of development activities undertaken by states, which are expected to vary significantly across the subnational level within the two countries.

The hypotheses that follow are designed to explore the impact of institutional conditions and interest group presence on subnational industrial policy in India by addressing questions about variation in both the *level* and *type* of industrial development policy activity across subnational political units within India and Mexico. The hypotheses draw from the broader comparative the U.S. politics political economic literatures. The research is organized around five hypotheses.

> ***H_1**: States that combine high levels of party competition with low levels of party fragmentation will engage in more vigorous economic development activity.*

> ***H_2**: States controlled by governments with more executive stability and less bureaucratic instability will have higher levels of economic development activity*

> ***H_{3a}**: States controlled by opposition parties not in power at the federal-level will engage in more vigorous economic development activity.*

> ***H_{3b}**: States controlled by regional parties will engage in more vigorous economic development activity.*

***H_4**: States with higher levels of industrialist interest group activity will engage in more vigorous development activity.*

***H_{5a}**: Higher levels of labor union activity will lead to higher levels of economic development activity.*

***H_{5b}**: Higher levels of labor union activity will lead to more active promotional than deregulatory effort.*

Hypothesis 1 is derived from the literature on the effects of political party competition on policy outputs. In those electorally competitive states, it is expected that in-party government officials will be more concerned with out-parties' abilities to convince voters that economic development is being mishandled, thereby influencing future control of the state government (Brace 1993; Elkins, *et al* 1996). Thus, party competition will stimulate more proactive economic development activity. In the same way, lower levels of party fragmentation leads to more vigorous economic development activity as governing parties are more likely to be held accountable for economic performance. Therefore, a two-party system will stimulate more aggressive development activity (Geddes 1994). Recent work (Kennedy 2004; Sinha 2003) suggests that stable, relatively competitive two-party systems are more likely to innovate in industrial development strategy.

According to Hypothesis 2, we will find states that have more stable policymaking environments will be more active in competing with other states in terms of subnational industrial promotion policies. Hypothesis 2 derives from literature which suggests that higher institutional capacity in the Indian and Mexican states is partly dependent on the consistency of the executive within the state (Rodriguez 1998; Sinha 2003). Likewise, work on the US states in the federal context asserts the consequence of the executive for state innovation in economic policy (Brace 1993). I expect that states with shorter tenure for chief ministers in India, and governors in Mexico will be less active on the industrial promotion front. Likewise, with more turnover in the Indian Administrative Services (IAS) in the Indian states, and increased frequency of churn in the administrative staffs of the key Mexican state economic ministries, there will be less well-defined economic development policy.

Hypotheses 3a and 3b derive from the literature on the differing incentives for actors from opposing parties across levels of government (Willis, Garman, & Haggard 1999, 2001). For hypothesis 3a, when the same party is in power nationally, subnational government officials are more inclined to attract resources from above and build support by means of political patronage. When an opposition party is in power, states will need to take more independent initiative in policymaking. We expect that when parties control the government of an Indian state that is different from the party in control in New Delhi, there will be higher levels of policy activity and faster movement towards a dual promotional/deregulatory strategy. Likewise, we expect that when a political party in control of a Mexican state is different from the administration in power in Mexico City, there will be more policy activity and a quicker movement towards the dual promotional and deregulatory economic development strategy. Hypothesis 3b predicts that states, when ruled by state/regional parties, will have higher levels of policy activity as compared to those states governed by national parties. Likewise, these regional party-ruled states will move more quickly toward a complimentary promotional and deregulatory economic development policy.

Hypothesis 4 draws from the comparative literature on business associations (Haggard, Maxfield, and Schneider, 1997) and the U.S. comparative state literature (Brace 2002; Newmark & Witco, 2005). It is expected that organized business associations foster non-particularistic industrial promotion policies by lobbying against direct firm-level aid programs and instead pushing for more diversified programs. In addition, higher levels of interest group activity lead to support for government deregulation and the removal of obstacles to investment. We expect that the Mexican and Indian states with higher rates of membership in the peak industrial associations will have higher levels of industrial promotion activities and move more quickly towards deregulatory-types of policies.

Hypotheses 5a and 5b are designed to explore variations in both the *levels* and the *types* of economic development activity or strategies pursued at the state level. Hypothesis 5a derives from the research on the impact of U.S. labor union activity on state-level policymaking (Saiz 1999) and the comparative literature on the role of labor in influencing state and local economic policies (Teitelbaum 2004). It is expected that more labor strikes will lead to increased economic development activity because of the union interest in and pressures for job creation (Elkins, et. al. 1996). In competing with other states, subnational governments confronting the pressures of an active union movement also have an interest in overcoming the tendency for firms to seek out locations with relatively weaker unions by becoming more active on the promotional policy front. T

Hypothesis 5b derives from work suggesting that active unions will be a strong veto point for deregulatory efforts (Nelson 1992; Teichman 1996; Zagha 1999). It is expected that higher levels of union strike activity will lead to less active deregulatory efforts because of the costs such efforts impose on organized labor. Thus higher levels of strike activity are expected to lead to greater reliance on promotional as distinct from deregulatory strategies of economic development. For both the Indian and Mexican states, we would expect a slower movement towards liberalizing the clearance process and streamlining the inspection regime.

These five hypotheses are designed to explore the impact of institutional interest group variation on policy choices made by the Indian and Mexican states over the course of the last 15 years. I expect that, in the quantitative and qualitative analyses herein contained, the answers to questions pertaining to why subnational governments in the two cases have been doing what they have been doing will be found in the interest group and institutional differences among states. The hypotheses discussed in this section will be able to be tested using both statistical and comparative case study approaches for India and Mexico. Because of the large amount of variance across the Indian and Mexican states, the four empirical chapters will allow for the drawing of causal inference with some degree of certainty because of the research design and variance on both the dependent and independent side.

Concluding Remarks

In summary, the dissertation will test hypotheses drawn from the comparative political economy, international political economy, and U.S. politics literatures and tests them at the subnational level in India and Mexico for the 1988-2003 time period. By examining the role of institutions and interest groups comparatively across the 31 states in Mexico and the 14 major states of India, the following chapters will argue that there is a need for a more sophisticated understanding of the causalities for why state governments have been doing what they have been doing, and that future literature must take into account the theoretically compelling results contained herein. In the chapters that follow I will frame my arguments with the five aforementioned groups of hypotheses in the comparative analysis of economic policymaking in the Indian and Mexican states. By incorporating research questions derived from three key areas of the political economy literature, and by examining six cases from two different countries, there will be a higher degree of confidence that we can ascribe to the findings based upon this methodological leverage.

CHAPTER 3

THE POLITICAL ECONOMY OF SUBNATIONAL INDUSTRIAL PROMOTION IN INDIA: 1991-2003

Introduction

Why have the recent gatherings of the World Economic Forum increasingly brought together representatives of state, provincial, and local governments rather than national governments?[2] Why have international financial institutions such as the World Bank, Asian Development Bank, and the Inter-American Development Bank begun channeling resources and loans away from central governments and towards governments at the subnational level?[3] Why have important segments of the international media increasingly covered the ramifications of subnational governmental policies on economic development as manifested by stories in *The Economist*, the *New York Times*, and the *Wall Street Journal*[4] And finally, why have global credit rating agencies like Standard & Poor's and Moody's increasingly devoted time and resources to appraising the credit-worthiness of state, provincial, and local governments the world over?[5]

The answers to these questions are all satisfied, in part, by noting the growing impact of subnational governments on economic development in recent years. Across all regions of the world, and especially in federal systems, international and domestic investors are forced to spend more time interacting with subnational government officials. Because of the dual movements towards economic liberalization and political

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[2] See http://www.weforum.org

[3] For examples of the trend, see: Asian Development Bank, *Country Assistance Plan for India*, 2000; Inter-American Development Bank, *Making Decentralization Work: A Background Paper for the Implementation of the Subnational Development Strategy*, April 2000; World Bank, *Assistance Program Evaluation for India, 2002.*

[4] There are a multitude of stories from recent years such as "New Map to the World."

[5] For instance, *Subnational Government: A Rating Agency Perspective*, Moody's Investor Service, July 1998 and Standard and Poor's, *Local and Regional Government Ratings Policy*, 2002.

decentralization in much of the developed and developing world, the rules of the game for business-state interaction now revolve around interactions that take place far from the national capitals of countries. Likewise, the alleviation of poverty, the agenda for primary education, and the drive for increased density of infrastructure are thought to be questions that will be resolved at the state and local levels of government.

Since the legislated end to the "permit-license *raj*" in the summer of 1991, states in India have been released to pursue investment free of much the central government's involvement that had existed during the previous four and one-half decades. Whereas in the years leading up to the reforms of the Narasimha Rao government, all investment location decisions were made *de facto* in New Delhi, the last 14 years have seen the *loci* of industrial investment policymaking switch to the state governments. Both domestic and foreign investors were quick to discover that the offices of consequence for gaining approval for and assistance with their projects no longer resided in the halls of the Planning Commission and the Finance Ministry in the capital, but now were in the corridors of state-level ministries in places like Ahmedabad (Gujarat), Bhopal (Madhya Pradesh), Hyderabad (Andhra Pradesh), and Lucknow (Uttar Pradesh.)

Some states jumped quickly out of the gate to gain advantage over their "competitors," while others trudged slowly through the initial years of the liberalization period. Whereas several states seized on the changed rules of the investment game to innovate in the policy arena to distance themselves economically from other states, a number of subnational governments did little, or drew up "paper-only" documents that did not gain attention from potential investors, let alone attract new investment.

In this paper, I will argue that a cumulative understanding of why states behaved differently over the last 14 years in industrial promotion policies can best be achieved by examining the structural, electoral, and interest group factors operating at the subnational level within India. To uncover the underlying factors influencing the Indian states' strategies of industrial promotion, I will utilize state-wise time-series regression models of both the linear and logit varieties.

The case of India presents an ideal case by which to test the factors that account for the diversity of approaches residing at the subnational level. India, with a definitive starting point for reforms in the summer of 1991 that fostered new policy incentives for subnational governments, provides a fertile ground to test empirical findings from the comparative politics, international political economy, and United States politics literatures. The findings presented in this paper suggest that the Indian states exhibit a more complicated set of policy responses to a competitive environment than existing theory would predict. While existing literature by and large ignores the subnational level when speaking of economic reform, it also ignores the pluralistic strategies for development operating at the state and provincial level across countries. This research shows the necessity for moving beyond the "developmentalist-state versus deregulatory-state" debate and towards an acknowledgement of greater diversity in economic development strategies at the subnational-level throughout the world. The paper endeavors to show the institutional, structural, and interest group dynamics that account for this theoretical dissonance.

Prior Research

Comparative scholars devoted extensive attention to the political economy of development in the decades after World War II. Until the 1980s, central government involvement in the economy and protection from external competition were major *foci* of theoretical interest and standard instruments of public policy. Over the past two decades, however, there has emerged a new emphasis on the free market and integration into the world economy. The central challenges for national governments have thus come to be defined largely in terms of maintaining macroeconomic stability, improving social conditions, increasing international competitiveness, and creating "strong" but "lean" institutions that complement rather than replace the market.

Since the liberalizing reforms in the summer of 1991, much of the research on economic development in India focused on the changed rules of the game for both the public and private sectors. Yet twelve years after the reforms, many questions remain as to how these sectors are coping with the new regime. Following initial concerns about the durability of the reform project during the early 1990s, liberalization as a whole took firm root at both the national level and across the states. Research by Jenkins (2000) illustrates how democratic politics contributed to this acceptance and points towards the core reasons for the sustainability of the liberalization project. Saez (2002) argues that the economic reforms have altered the very nature of India's federal political system, with inter-jurisdictional competition for investment now the norm, instead of competition for development funds from the central government.

Nevertheless, the reform project has failed to progress quickly enough for some persons and groups. Various industrial associations like the Confederation of Indian

Industry and international financial institutions like the Asian Development Bank and World Bank continue to push for further liberalization at the center. Likewise, many of these same organizations and institutions now realize that much of the work to be done in terms of reforms is at the level of the Indian states. In fact, it is increasingly the view among scholars that the crucial element for understanding the liberalization story in India, and the focus of future research should rest at the subnational level (Jenkins 2000; Rudolph & Rudolph 2002; Wiener 2000.)

In recent years, a large body of scholarship has emerged showing the uneven response to the reforms in 1991 across the Indian states in terms of divergent growth rates. Other research points to the asymmetrical effect that the reforms have had on GDP growth and investment patterns across the states (Ahluwalia 2001; Ganguly 2002; Kurian 2002; Sachs, Bajpai & Ramiah 2001; Rao 2002; Singh & Srinivasan 2002.) In particular, states such as Gujarat and Maharashtra that were well positioned in terms of infrastructure, geography, and level of development at the start of the reforms, were able to capitalize on their newfound freedom to compete against other less well factor-endowed states. Moreover, as Ahluwalia (2001) points out, those states with better relative fiscal positions tend to attract more investment, which leads to higher growth rates. Sachs *et al* (2001) remain pessimistic about the chances for growth convergence among the Indian states. They predict that development will continue to be an urban and coastal state-led process. There are also new limitations on the spending capacities of the states. As Rao (2002) demonstrates, the concurrent declining fiscal position of the states puts great restrictions on their policy autonomy available to pursue economic development.

Despite the widespread acknowledgement that the states are now the focal point of the economic reform process in India, little research seeks to explain why states have been doing what they have been doing since 1991. While there is an expanding body of work that gauges the relative investment climates across the states (Dollar, Iarossi, & Mengiastae 2002; Venkatesan & Varma 1998; World Bank 199), numerous questions regarding state policy choices that influence such rankings have not been asked. What policies have the Indian states pursued for the last 12 years in search of industrial investment and growth? Why have particular states utilized differing policy mixes at different time?

The pivotal questions raised by variation in subnational development efforts in India and elsewhere are thus twofold in nature. First, why are some states more active in the pursuit of investment than others? Second, why are there different state policies such as the standard "smokestack-chasing" strategies and other policy approaches, including deregulation?

Existing literature has identified two main strategies that states can utilize to foster economic development. First, subnational governments can attempt to manipulate the regulatory policy environment. Approaches along this line serve to lower the costs of production and create incentives for new investment. This tactic might take the form of "right to work" laws, the streamlining of licensing and inspection processes (Doner and Hershberg 1999; Montero 2001a; Plaut and Pluta 1983), or the removal of environmental or safety regulations that might discourage the entry of new investment. The efficacy of this approach is a basic tenet of the neoliberal development model, which suggests that government regulations that hinder the entry of new firms, drive up the cost of production, or hamper competition should be abolished (Williamson 1990, 1994).

Second, subnational governments can attempt to attract new investment via promotional strategies as suggested by the literature on the developmental state (Evans 1995; Haggard 1991; Wade 1990) as well as the research on subnational politics in the U.S. (Saiz and Clarke 1999; Wolman & Spitzley 1996). Such strategies include the construction of physical and technological infrastructure or the promotion of human capital development (Fulton and Newman 1993; Licate 1994; Perry 1994; Rapp 1994; Saiz 2001; Saiz and Clarke 1999; Sbragia 1996). States can also adopt locational incentive approaches, including subsidies, and sectoral targeting incentives, to attract investment and improve their own economies relative to those other states (Fosler 1988; Weber 1984). Promotional strategies also encompass entrepreneurial economic development approaches, which can take the form of straightforward state "promotional" expenditures, as well as the creation of new institutional relationships to encourage investment (Clarke and Gaile 1998; Eisinger 1988; Saiz and Clarke 1999; Sherman, Wallace, and Pitnety 1995; Sternberg 1987). States adopting this approach might focus on attracting investment in high-technology sectors or create a public-private partnership that functions as a state development and/or credit corporation (Saiz 2001). These two strategies parallel those associated, respectively, with neoliberal and statist development models at the national level.

Drawing upon both the comparative literature on national economic development and the U.S. literature on state economic development, my central theoretical explanation is that the nature and level of subnational development activity reflect local-level institutional relationships and interest group activity. These relationships will allow us to differentiate "programmatically rich" from "programmatically lean" states (Elkins, Bingham, and Bowen, 1996), as well as to explain variation in the types of development activities undertaken by states, which are expected to vary significantly across the subnational level within India. These activities include the total expenditures made to expand the industrial sector within a particular state, as well as the type of industrial development strategy employed.

Hypotheses

The hypotheses that are tested in this chapter are designed to explore the impact of institutional conditions and interest group strength on subnational industrial policy in India by addressing questions about variation in both the *level* and *type* of development activity across subnational political units. As a first cut at evaluating the level of activity, I will assess the resources devoted to subnational development efforts on the basis of the governmental per capita level of revenue and capital expenditure on economic services in the industrial sector. And second, to explore variations in the types of development activity subnational governments pursue, I will examine the degree to which states pursued polices of the promotional and deregulatory varieties. As detailed in the dissertation's theoretical chapter, the models will be testing the role played by political party system type, the existence of out and regional parties, and the strength of industrial associations and labor unions within a state.

Statistical Models

In order to address the aforementioned complimentary research questions regarding levels and type of industrial promotion activity, I employ two distinct dependent variables. On the left side of the first model, I utilize state-wise budgetary spending data for the 14 major Indian States for the period 1990-2003.[6] Specifically, I use the monies spent each year across the 14 major states targeted towards industrial expansion divided by total revenue expenditure.[7] I use this dependent variable to test the hypotheses listed above regarding electoral structures and interest group activity influencing the level of promotional activity. For the second model, I have constructed a tri-partite, ordered dependent variable that captures the strategy a particular state pursues, ranging from the absence of an active industrial strategy to a promotional/deregulatory dual strategy in a particular year during 1991-2003.[8] I utilize this dependent variable to measure the impact of the same institutions and interest groups as above on the movement from the absence of a comprehensive strategy towards a dual strategy of industrial promotion.

Measuring Subnational Spending on Industrial Development

In the first model, the left side of the equation contains the variable that captures the resources that the Indian states' devote to industrial development in the post-reform

[6] These data originate from a World Bank dataset on subnational economic and budgetary data in India.
[7] This indicator is computed by taking Industrial Sector Economic Services Revenue Expenditure plus Economic Services Capital Expenditure divided by Total Revenue & Capital Expenditures. This results in values that range from .81% for Maharashtra in 2000, to 8.65% in Karnataka in 1991.
[8] The result is a variable that takes on values of "0," "1," and "2." The coding scheme is as follows: A state receives a "0" in a specific year when that state has neither implemented comprehensive sales tax subsidies for industry (promotional), nor put into practice a broad system for "clearing" the state-level permits necessary for opening an industry (deregulatory.) A state obtains a "1" when it has applied a plan of sales tax subsides to promote industry, but has not yet instigated a policy of streamlining the permit process. A state receives a "3" in a specific year when the state has employed both the promotional and deregulatory types of policies.

period. I examine data on industrial development spending for 14 states[9] in India between 1991 and 2003.[10] The model is formatted as a time-series cross-sectional (TSCS) data set that includes 13 annual observations for each of the 14 states within the sample. For the analysis, I take the recommendation of Beck and Katz (1996) and use OLS with panel corrected standard errors (PCSE.) I adopt this technique as there is the propensity for TSCS data to have problems with autocorrelation and heteroskedasticity.[11] Because of this tendency, the coefficients would be consistent, but the estimates of the standard errors may be of concern.

In addition, as Beck and Katz (1996) advise, I have lagged the dependent variable and included it on the independent side of the equation.[12] One is thus able to examine the influence of time within the panels of the model in question. I then use OLS to calculate the coefficients and use PCSE for the estimations of coefficients' standard errors. This method results in stricter thresholds of significance, thereby resulting in more confidence-inducing estimates. The regression model is as follows:

Industrial Sector Economic Services Revenue & Capital Expenditure/Total Revenue Expend.) = a_1 + b_1(Lagged Dependent)) + b_2(Level of Development) + b_3(Economic Distress) + b_4(Education Level) + b_5(Urbanization) + b_6(Union) + b_7(Industrial) + b_8(Party System) + b_9(Out Party)

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[9] The states included in the sample are Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Orissa, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh, and West Bengal.
[10] This includes both revenue expenditure and capital expenditure in the area of Economic Services in the sub-area of Industrial Development.
[11] Once the lagged dependent variable was included on the right side of the model, there were no remaining problems with autocorrelation. Beck and Katz (1996) state that this is appropriate when dealing with situations that have more panels than time periods.
[12] The model was also run as a GLS model, with the errors defined as AR1, which resulted in no significant impact upon outcomes.

Measuring Subnational Industrial Development Strategy

In the second model, the left side of the equation contains the variable that captures the type of strategy that the Indian states' employ to promote industrial development in the post-reform period. I examine data on industrial development strategy for 14 states in India between 1991 and 2003, and conduct the analysis by using an ordered logit model. For such models, recent apprehensions by Beck, Katz, and Tucker (1999) involve temporal dependence, given choices by the *same states* over time. The model is estimated using an ordered logit model with a time duration variable.[13] This is the most suitable procedure as it accounts for the powerful and expected temporal effects. Thus one can protect against capturing significance in the model that is due to duration dependence. In keeping with established practice, I do not report the coefficients and standard errors of the duration variable. This technique provides for the same accounting for time as the inclusion of cubic splines and both are suggested for inclusion in this type of model by Beck *et al* (1999.)

The regression model is given below:

Industrial Development Strategy (0, 1, 2) =

$a_1 + b_1$(Dependent Duration) + b_2(Level of Development) + b_3(Economic Distress) + b_4(Education Level) + b_5(Urbanization) + b_6(Union) + b_7(Industrial) + b_8(Party System) + b_9(Out Party)

Control Variables

Drawing upon the previous research, from the American politics and Comparative politics literature, I incorporate several key control variables into each of the models. The first control variable is **Economic Distress**. Economic distress is operationalized by

[13] The variable takes on the value of 0 for the first year of a new strategy, and then 1 is added for each additional year that the indicator remains at the same level.

using the yearly unemployment rate for each of the states. It has been shown in the U.S. literature (Feick 1992; Reese 1991; Sharp 1991) as well as the comparative literature (Montero 2001a) that states undergoing short-term economic distress relative to other states spend more on industrial promotion programs. Distress is measured by subtracting the yearly unemployment rate for each state from the calculated national average. Previous work also points to level of **Urbanization**, **Level of Development**, and **Education Level** as important factors which influence a state's capacity to invest in industrial promotion. These three concepts are incorporated as controls into the models. Empirical findings in the U.S. literature suggest that more urbanized, wealthier, and more educated states tend to spend more on industrial promotion programs (Ambrosius 1989; Dye 1966, 1984; Elkins *et al* 1996; Plaut and Pluta 1983), while similar findings have been confirmed in other federal states such as Brazil (Montero 2001) and Germany (Begg & Mayes 2000). I calculate **Urbanization** for the 14 states by utilizing the figures periodically released by the Census of India. **Level of Development** is derived from the annual Gross Domestic Product, per capita, for each state. And finally, I use the literacy rates for each of the states to measure **Education Level**. In addition to these variables, **Fiscal Condition** also is tabulated in order to assess the impact of subnational budgetary constraints on availability of resources to aid the industrial sector. This will be measured as the percentage of revenues above or below the expenditure level.

Independent Variables

Drawing upon the aforementioned hypotheses, the first of the independent variables is the **Party System** measure. This variable incorporates two distinct features ascribed to party systems. Recent research suggests that party competition will serve to stimulate more aggressive economic development activity. Correspondingly, lower levels of party fragmentation leads to more vigorous economic development activity as governing parties are more likely to be held accountable for economic performance. The assumption implicit in the hypothesis is that a competitive, two-party system will stimulate more aggressive development activity (Geddes 1994). This variable will be operationalized as the absolute value of the effective number of parties minus two [$|(N_s-2)|$] (Laakso & Taagepera 1979; Mainwaring & Scully 1995).[14] **Out Party** measures the dissimilar incentives facing policymakers across discrete levels of government. In short, a party or parties in control of a government in a state are more likely to be more active in promoting industry if they are not in the federal government coalition. This concept will be measured by a dummy variable, with '1' representing those cases in which the subnational government is controlled by a party or a coalition government is controlled by a party not in power at the federal level. **Union** captures the militancy and political strength of labor unions across the states. It is measured by tabulating yearly number of strikes and lockouts per capita, multiplied by the number of workers involved, multiplied by the length of the strike. The result is an indicator that represents person-hours per-capita, per year, "lost" to strikes and lockouts. **Industry** encapsulates the relative strength of national-level industrial associations across the states. This concept is measured by calculating the yearly roster of companies who are members of an industrial association for each state in India. Specifically, I rely on the membership database for

[14] The value is calculated as $N_s = 1/\Sigma p_i^2$, where N_s represents the effective number of parties measured by the number of seats and p_i is the proportional share of seats of the i-th party (Mainwaring & Scully 1995). When you have a party system with two perfectly balanced parties in terms of electoral competition, the value will be two, while the indicator will result in a score of zero. The indicator measures state political systems as a departure from this two-party, perfect competition model.

the Confederation of Indian Industry (CII) and the Federation of Indian Chambers of Commerce and Industry (FICCI).

Table 3-3-1 lists all the variables on the right side of the equations and the expected direction of influence on the dependent variables for each model.

Table 3-1: Control and Independent Variable Summary

Variable Name	**Expected Influence on Spending**	**Expected Influence on Movement toward Dual Strategy**
CONTROL		
Economic Distress	Positive	Positive
Urbanization	Positive	Positive
Level of Development	Positive	Positive
Education	Positive	Positive
Fiscal Condition	Positive	--
INDEPENDENT		
Party System	Negative	Negative
Out Party	Positive	Positive
Union	Positive	Negative
Industry	Positive	Positive

Empirical Findings

Subnational Spending on Industrial Development

The first model endeavors to explain the degree to which subnational governments in India devote resources to industrial development. In all cases, results stand up to diagnostic tests for outliers and heteroskedasticity.[15] Table 3-2 shows the results of the OLS regression for the two similar models[16]:

[15] Test for outliers included analyses of partial-regression leverage plots and Cook's Distance. With respect to heteroskedasticity, panel corrected standard errors are used.

[16] The first model is run without the Fiscal Condition model. The second model includes this independent variable. Only minor changes occur in the significance of the other independent variables which will be discussed in the text below.

TABLE 3-2: OLS Panel, Time-Series Regression, with PCSE, on Industrial Spending

Variable	Model 1 *Industrial Exp./ Total Exp.*	Model 2 *Industrial Exp./ Total Exp.*
Constant	1.79 (.90)	1.88 (.90)
Lag Dependent	5.25*** (.69)	4.89*** (.69)
Economic Distress	.15** (.07)	.17** (07)
Urbanization	.65*** (.21)	.81*** (.30)
Level of Development	-2.54*** (.95)	-2.36*** (.91)
Education	.26 (.31)	.25 (.30)
Fiscal Condition	--- ---	.15*** (.05)
Party System	-.25** (.11)	-.18* (.09)
Out Party	.40* (.23)	(.42)* (.22)
Union	-.68 (.54)	-.57 (.53)
Industry	.025 (.037)	.079** (.041)
	$R^2 = .71$ $N = 168$	$R^2 = .72$ $N = 168$

NOTE: ***Numbers in parentheses are panel corrected standard errors***

****p < .01, **p < .05, *p <.10*

The various measures for the control variables perform moderately well in the first model. As one would expect, the lagged dependent variable is a highly significant predictor of spending. The amount a state spends on industrial development in any given year, has great impact on the next year's level of spending. As predicted, the model shows that increased levels of economic distress leads to higher industrial development spending at the .05 level. Likewise, more urbanized states tend to devote more resources to industrial economic services in their yearly budgets at the .001 level of significance. Contrary to expectations, states with higher levels of development allocate *less* money for industrial development. The outcome parallels the findings regarding the issue of economic distress. The results suggest that, during the 1990's, the relatively underdeveloped Indian states spent additional funds in attempt to close the developmental gap with their richer neighbors. While in the predicted direction, the coefficients on the education level of the states were not significantly different from zero. This is most likely indicative of the wide variation in education across the states, with highly literate states such as Kerala and to a lesser extent Maharashtra not spending monies on industrial development during the decade. Equally, states with low levels of literacy such as Bihar and Uttar Pradesh spent more on industrial facilitation than expected using education level as a predictor.

We turn now to the findings from the model concerning the effects of the institutional and interest group variables on the level of industrial spending across the Indian states as anticipated. Party system type is a significant predictor of financial resources devoted to industrial development. Systems that approach the competitive, two-party ideal type are more likely to devote monies to industrial development at the .05 level, and less so those that begin to climb away on the scale of the measure. For instance, an increase in the mean-level of fracturing and concurrent decrease in competitiveness on the party system indicator (.986) to one standard deviation above the mean (1.94) decreases the priority of budgetary industrial spending by nearly 21%. A similar prospect holds for the "out party" indicator. Parties or coalitions of parties in power at the state-level and not at the federal-level devote more resources to industrial economic services spending. The coefficient for this indicator is significant at the .07 level. Differing from predictions, the coefficient for union strength is negative. While not quite statistically significant at conventional levels, the direction of the influence suggests a different logic underlying the relationship between union activity and budgetary priorities in the Indian states. It is likely indicative of governments responding to the visibility of the labor strikes by focusing on shorter-term solutions to the problem at hand, instead of devoting resources to projects and investments that might not result in additional industrial growth for many months or years down the road. In the first model, little influence is visible on the part of industrial associations upon state spending for industrial promotion.

In the second model predicting spending, with the inclusion of the fiscal situation as an independent variable, the results are consistent with those of the first model across the independent variables, with one major exception. The results illustrate that economically distressed and urbanized states spend more on industrial economic services than their counterparts. In addition, as in the first model, economically developed states spend less on industrial promotion than their relatively underdeveloped neighbors. Non-competitive and fractured party systems lead to less industrial spending. States governed by parties not in power at the national level tend to devote more monies to industrial development. As stated above, the second model includes a fiscal situation variable which measures the fiscal deficit/surplus of a state in any given year. At the .01 level, the profligate states tend to spend more money on industrial economic services. As expected, states in India have borrowed money from the center and taken out external loans to finance industrial sector expansion. This finding is consistent with other scholarship (Kurian 1999; Rao 2000, 2002) showing that some of the Indian states spent far beyond their revenues on several line items in their budgets. One would expect that this situation is changing in the early years of the 21st century as the central government is beginning to impose harder budget constraints. However, the unexpected result in the second model is that with the inclusion of the fiscal condition control variable, larger industrial association membership leads to reduced spending. The possible explanation emerges from recent work which suggests that industrial groups are increasingly lobbying state governments for deregulatory actions and not pressuring the governments for increased economic services spending, which leads to poor fiscal circumstances. We will be able to address this puzzle directly in the logit model below.

Subnational Industrial Development Strategy

The second model predicting type of activity ventures to explicate the speed with which subnational governments in India move from no industrial development strategy, to a promotional strategy, and finally to a complementary promotional/deregulatory strategy. Table 3-3 shows the results of the ordered Logit regression[17]:

[17] Different specifications of the models were also tested: the model on strategy was split into separate logits for both tax subsidy time promotion and single-window clearance deregulation. In the ordered logit model the Union variable was significant and in the positive direction. Likewise, in the separated logit models for both promotion and deregulation, the Union variable had a significant positive influence on both promotion and deregulation. In both the ordered and regular logit models, higher levels of Union strike activity led to a quicker move toward promotional strategy and the dual promotional-deregulatory strategy.

TABLE 3-3: Ordered Logit Panel, Time-Series Regression on Industrial Strategy, with Duration Count Variable

Variable	**Model 1** *Industrial Dev. Strategy*	*Change in Odds (w/ 1 S.D. change)*
Economic Distress	-.51 (.97)	-18.8.0%
Urbanization	.80* (.47)	87.6%
Level of Development	-.17 (.23)	-5.3%
Education	.52* (.21)	89.8%
Party System	-.13 (.22)	-14.2%
Out Party	.42** (.13)	54.5%
Union	-.15** (.069)	-42.3%
Industry	.19** (.09)	71.6%
Cutpoint (1) *Cutpoint (2)*	4.67 (1.50) 7.21 (1.60)	--- ---
	Log Like = -116.06 *N = 168*	

NOTE: ***Numbers in parentheses are standard errors***

****p < .01, **p < .05, *p <.10*

Ordered logit analysis generates coefficients that signify the effect of every independent variable clear of all other included independent variables, as well as standard errors coupled with these coefficients that permit hypothesis testing. While logit analysis does not allow a direct interpretation of the coefficients, the change in odds provides a way to gauge the impact of the independent variables. Exponentiating the coefficient estimated for an independent variable generates the factor by which a one standard-deviation increase in the independent variable increases, on average and without the effects of other variables, the odds of the ordered dependent variable taking on its next-greater value. For a particular independent variable, with all others held to their mean, we see in the right column the percentage chance that a state in India, in a given year, will move up the ladder from no industrial promotion policy, to one of a promotional nature, and finally to the dual promotional-deregulatory type of policy set.

Among the control variables, level of economic distress, urbanization level, and education level are all in the expected direction. While the impact of level of economic distress upon the movement towards a more progressive industrial strategy is not significant, there is still an 89.8% greater chance that a state suffering from unemployment rates 4.2% higher than the national average will move up the strategy ladder with all other variables constant at their means. Similarly, level of education and urbanization level have odds percentages of 89.8% and 87.6% respectively and are both significant at the .10% level. Similar to the finding in the OLS model on industrial spending, the impact of level of development on the industrial strategy of states is minimal and has a small negative effect.

The most interesting findings in the Logit model are that the interest group measures are highly significant and in the expected direction. In addition, the institutional measures hold up reasonably well and appear to have a moderate to high degree of influence on subnational industrial strategy. The party system variable is in the expected direction, but is not significant. A change in the measure from the mean to a score of 1.97 results in an increased chance of 14.2% for a movement to the next higher industrial strategy category. As expected, parties in power or heading coalitions at the state-level and not at the federal level are more likely to pursue more progressive industrial strategies. There is a 54.5% greater likelihood for a subnational government to pursue such polices when headed by a party not involved with the national government in New Delhi.

The estimate of the effect of labor militancy is significant at the .05 level and in the expected negative direction. Thus, an increase in person-hours per million people lost to strikes or lockouts in a particular state to 51,456 results in a 42% decrease in the chance that the particular state will move up the industrial strategy ladder. Similarly, as expected, a one standard-deviation increase in per capita industrial association membership in a state, with all other variables held constant, increases by 71.6% the chance that the state will pursue a more progressive industrial policy in a given year. In sum, a fractured and non-competitive party system decreases the likelihood that a state will pursue a more diverse industrial strategy. In contrast, having a state controlled by an "out party" strongly increases the chance of a more diverse strategy. And finally, while labor militancy strongly inhibits the movement towards a varied industrial policy, higher degrees of industrial association influence increases the chance of such policies.

Conclusions

Most prior research has repeatedly focused on the national-level of analysis when discussing economic reform and industrial promotion, while ignoring the role that state, provincial, and local governments play in the globalizing marketplace. This article has attempted to redress these shortcomings in the political economy literature by looking at the subnational unit of analysis in two key federal countries. By taking as its theoretical point of departure the literatures on federalism, economic development, and U.S. politics, this article suggests and tests a different perspective, which suggests subnational governments pursue a multitude of policies that are considered exclusive in the national-level literatures. These findings are important in four ways. First, it is apparent that the structures of electoral institutions and interest group activity across the Indian states have a significant impact on subnational economic development policy. As demonstrated by the empirical results, the type of party system and what parties are in control relative to the center greatly affect the amount of resources these states devote to industrial spending. Likewise, these institutional variables also greatly influence the types of industrial development strategies that states pursue. Second, it is clear that the comparative political economy literature has underspecified the connection between industrial policy and subnational variables. To the extent that it has focused attention on the national level of analysis instead of the subnational, a good deal of information has been disregarded. This paper presents evidence suggesting that there has been a diversity of levels and types of subnational industrial policies since the reforms in India in the summer of 1991. This diversity of policy responses is much greater than what the established literature would have predicted. Thirdly, these results have clear implications for policymakers and scholars in light of the current waves of decentralization and economic liberalization sweeping the globe. This study provides key information as to what the implications might be for the subnational governments in a country undergoing such reforms, and the probable institutional and interest group influences on the different options that states have in pursuing industrial development. Finally, and most importantly, these findings show that the mutually exclusive divide of "deregulatory-state" and "developmental-state" as seen in the comparative political economy literature does not apply at the subnational level. States can be seen to be pursing a diversity of strategies including those which utilize both of these strategies. Across the states of India and Mexico, the pursuit of economic development and the corresponding state strategies does not fit into the theoretical framework that currently exists and the national level in the comparative political economy literatures.

CHAPTER 4

INDUSTRIAL PROMOTION IN ANDHRA PRADESH, MADHYA PRADESH, AND UTTAR PRADESH – IN-DEPTH SMALL-N ANALYSIS

"In other countries even municipalities are honing their strategies for investment. It is therefore entirely appropriate that in India state governments have begun to play a major role in pulling in the money they need to help finance their development. Most of our bigger states have populations that are equal to those of some European countries and are considerably less developed. Our needs are so great that have to attract huge investment both nationally and globally to be able to provide employment for all these people and raise their living standards… In the past few years, state governments have begun competing with each other in this regard and that is healthy for the country as a whole." --N. Chandrababu Naidu, Chief Minister of Andhra Pradesh (Naidu 2000)

Introduction

Over the weekend of January 10-12, 2004 the third annual Non-Resident Indian (NRI) and People-of-Indian Origin (PIO) conference was held on the grounds of the *Vigyan Bhavan* in New Delhi, India. Over 1,000 important and successful NRI's and PIO's were in attendance from every corner of the globe. The national Bharatiya Janata Party (BJP) government sponsored the conference, in part, with the hope of luring successful Indians from numerous sectors abroad into investing money in the economy of India. Even as many of the major states had official delegations present at the conference, most decided not to attend. Why did some state governments send delegations while others did not? As has been the case with other situations such as this, some state governments in India have been more active than others in the pursuit of industrial investment in the post-1991 era. While it is impossible to judge a government's policymaking priorities on the basis of one decision, there are multiple examples of opportunities for industrial promotion that are not taken. However, when one examines a 14- year period for the states, in multiple policymaking arenas, a pattern of behavior arises. This chapter seeks to explain this variance in activity across state governments in India in terms of the promotion of the industrial sector in the post-1991 reform environment.

Since the legislated end to the "permit-license *raj*" in the summer of 1991, states in India have been released to pursue investment free of much the central government involvement that had existed during the previous four and one-half decades. Whereas all investment location decisions were made *de facto* in New Delhi, in the years leading up to the reforms of the Narasimha Rao government, the last 12 years have seen the *loci* of industrial investment policymaking switch to the state governments. Both domestic and foreign investors were quick to discover that the offices of consequence for gaining approval for and assistance with their projects no longer resided in the halls of the Planning Commission in the capital, but now were in the corridors of state-level ministries in places like Ahmedabad (Gujarat), Bhopal (Madhya Pradesh), Hyderabad (Andhra Pradesh), and Lucknow (Uttar Pradesh.)

Some states jumped quickly out of the gate to gain advantage over their "competitors," while others trudged slowly through the initial years of the liberalization period. Whereas several states seized on the changed rules of the investment game to innovate in the policy arena and distance themselves economically from other states, a number of subnational governments did little, or drew up "paper-only" documents that did not gain attention from potential investors, let alone attract new investment.

In this chapter, I will argue that a cumulative understanding of why states behaved differently over the last 14 years in industrial promotion policies can best be achieved by examining the institutional and interest group factors operating at the subnational level within India. To uncover the underlying factors influencing the Indian states' strategies of industrial promotion, I will examine three Indian states and their subnational industrial policymaking over the course of the post-reform era.

India presents an ideal case to test the factors that account for the diversity of approaches residing at the subnational level. With a definitive starting point for reforms in the summer of 1991 that fostered new incentives for subnational governments, India provides a fertile ground to test empirical findings from the comparative politics, international political economy, and United States politics literatures. The information presented in this chapter suggests that the Indian states exhibit a more complicated set of policy responses to a competitive environment than existing theory would predict. Neither national policies nor global market pressures determine policies at the state level, local politics make a difference. The chapter endeavors to show the institutional and interest group dynamics that account for this theoretical dissonance.

Prior Research

Comparative politics scholars devoted extensive attention to the political economy of development in the decades after World War II. Until the 1980s, central government involvement in the economy and protection from external competition were major *foci* of theoretical interest and standard instruments of public policy. Over the past two decades, however, there has emerged a new emphasis on the free market and integration into the world economy. The central challenges for national governments have thus come to be defined largely in terms of maintaining macroeconomic stability, improving social conditions, increasing international competitiveness, and creating "strong" but "lean" institutions that complement rather than replace the market. The logic underpinning shifts in national development policy implied that governments should limit their economic role and refrain from "picking winners" in the marketplace (Williamson 1990, 1993).

Since the liberalizing reforms in the summer of 1991, much of the research on economic development in India focused on the changed rules of the game for both the public and private sectors. Yet fifteen years after the reforms, many questions remain as to how these sectors are coping with the new regime. Following initial concerns about the durability of the reform project during the early 1990s, liberalization as a whole took firm root at both the national level and across the states. Authors such as Rob Jenkins (2004) have suggested that we need more Indian inter-state comparative studies on policymaking and economic reform and that there has been a failure at theory-testing in light of the crucial reforms in 1991.

Other research by Jenkins (1999) illustrates how democratic politics contributed to the broad acceptance of the reform project at the center. He points towards the core reasons for the sustainability of the liberalization project as being the political choice of the market liberalizers at the center to undercut political resistance to economic change by making many key reform issues part of the domain of the states. Then, reform would come via states competing with each other, allowing the resistance to be spread out across the whole country. Similarly, Saez (2002) argues that the economic reforms have altered the very nature of India's federal political system, with inter-jurisdictional competition for development funds now the norm. Whereas in the past competition existed between states in New Delhi, now there is a much greater impact of state policymaking on the chance to differentiate one state from another.

Nevertheless, the reform project has failed to progress quickly enough for some groups. Various industrial associations like the Confederation of Indian Industry and international financial institutions like the Asian Development Bank and World Bank continue to push for further liberalization at the center. Likewise, many of these same organizations and institutions now realize that much of the work to be done on reform is at the level of the Indian states. In fact, it is increasingly the view among scholars that the crucial element for understanding the liberalization story in India, and the focus of future research should rest at the subnational level (Jenkins 1999; Rudolph & Rudolph 2002; Wiener 1999.)

In recent years, a large body of scholarship has emerged showing the uneven effects of the reforms in 1991 across the Indian states in terms of divergent growth rates. Other research points to the asymmetrical effect that the reforms have had on GDP growth and investment patterns across the states (Ahluwalia 2001; Ganguly 2002; Kurian 2002; Sachs, Bajpai & Ramiah 2001; Rao 2002a; Singh & Srinivasan 2002.) In particular, states such as Gujarat and Maharashtra that were well positioned in terms of infrastructure, geography, and level of development at the start of the reforms were able to capitalize on their newfound freedom to compete against other, less well factor-endowed states. These structural explanations have had limited success in explaining the movement of states relative to each other in terms of their industrial policymaking.

Moreover, as Ahluwalia (2001) points out, those states with better relative fiscal positions tend to attract more investment, which leads to higher growth rates. Sachs *et al* (2001) remain pessimistic about the chances for growth convergence among the Indian states. They predict that development will continue to be an urban and coastal state-led process. There are also new limitations on the spending capacities of the states. As Rao (2002b) demonstrates, the concurrent declining fiscal position of the states puts great restrictions on their policy autonomy available to pursue economic development. This decline in position is mostly due to the implementation of "hard budget constraints" which has seen the federal government lessen the degree to which it will bail out profligate states.

Despite the widespread acknowledgement that the states are now the focal point of the economic reform process in India, little research seeks to explain why states have been doing what they have been doing since 1991. While there is an expanding body of work that gauges the relative investment climates across the states (Dollar, Iarossi, & Mengiastae 2002; Venkatesan & Varma 1998; World Bank 2002), numerous questions regarding state policy choices that influence such rankings have not been asked. What policies have the Indian states pursued for the last 12 years in search of industrial investment and growth? Why have particular states utilized differing policy mixes at different times? And finally, why are some states more aggressive in their search for industrial investment than others?

Recent work by Sinha (2004) offers answers to these types of questions by looking at the institutional capacities of Indian states in order to understand differing outcomes of economic policymaking. Specifically, she examines the development of institutional capacity in West Bengal and Gujarat to provide an explanation for why some states have performed better than others in the post-1991 environment. Other work by Sinha (2002) examines institution-creation and frameworks for crafting development strategies. Work by Baru (1999), on the other hand, suggests the need to examine the importance of regional capitalists. By examining district-specific industrialist activity across Andhra Pradesh, Maharashtra, and Gujarat, and Tamil Nadu, we are given a different perspective on how we should look at coalitions for reform in the context of a large, federal state such as India.

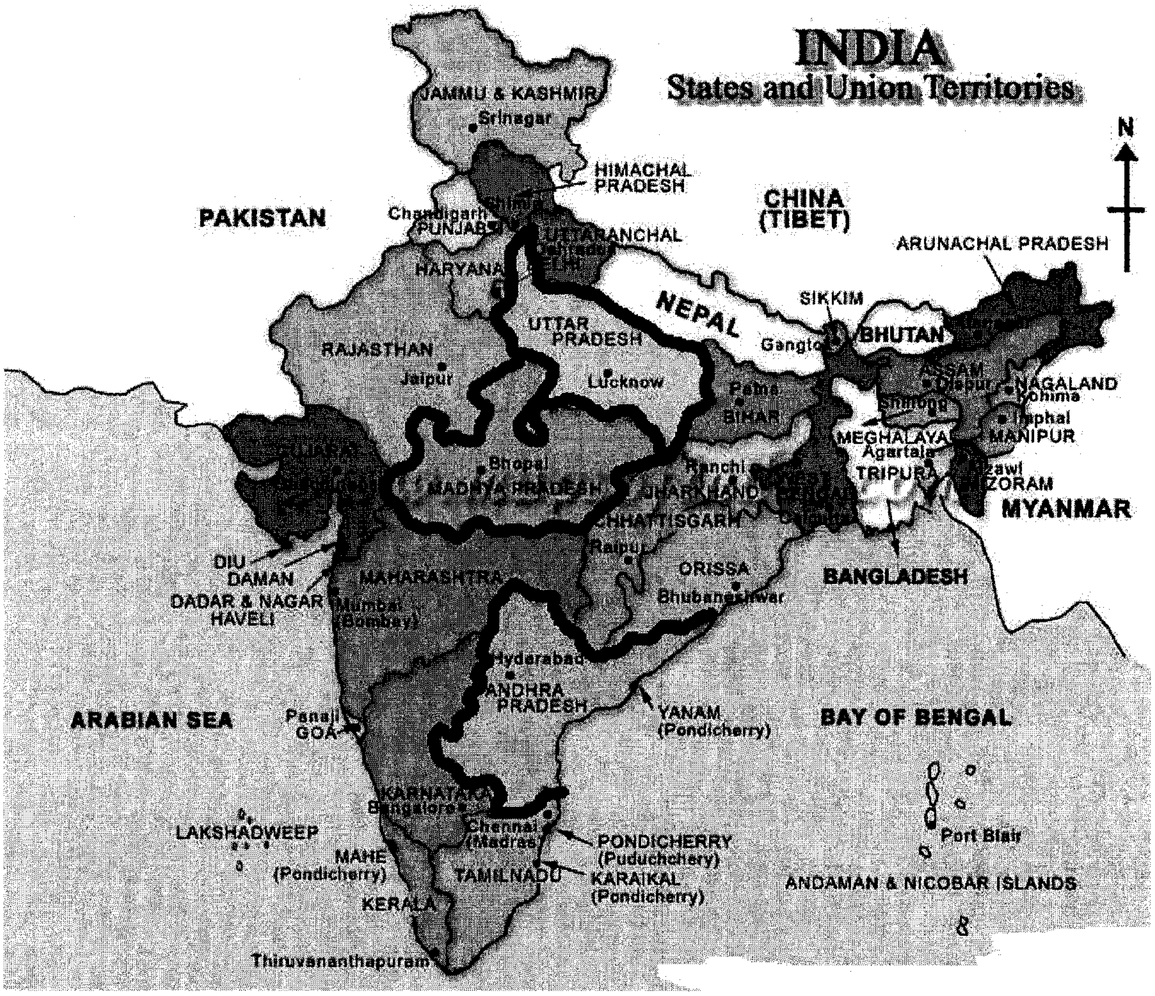
Kennedy (2004) examines the states of Andhra Pradesh and Tamil Nadu and tests the meta-theories that Jenkins (2004) posited as the dominant theories in the study of subnational economic development in India. The first of these theories is the expectation that richer states are the ones doing the reforming in the post-1991 era. And the second is the finding that poorer states will reform in an attempt to "signal" domestic and foreign investors as to their "sincerity" about, and commitment to, the reform agenda. Kennedy, in the examination of her two cases, finds that the "reform packaging" in each state is dissimilar because of differences in political party system structure and strategic signaling intensions.

The pivotal questions raised by variation in subnational development efforts in India and elsewhere are thus twofold in nature. First, why are some states more active in the pursuit of investment than others? Second, why are there different state policies such as the standard "smokestack-chasing" promotional strategies adopted by some states and the market-oriented policy approaches, including deregulation, favored by others?

Methodology and Case Selection

This chapter explores the impact of institutional and interest group influences upon subnational industrial policy in India. The states of Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh were selected because they all have similar structural conditions and have had levels of economic development and economic growth below the national average in the time period leading up to the 1991 economic reforms. Similarly, all three states have population bases and predominant industrial and economic structures in landlocked areas. Because of the sheer population size of the Indian states, it is difficult to choose cases that are identical on all parameters. Yet there is a reasonable degree of structural, geographic, and demographic similarity across the three states. Figure 4-1 shows the locations of the three cases.

<u>Figure 4-1</u>: Map of India with Cases Highlighted



Likewise, there is good variance on those institutional and interest group factors that can be expected to influence different types of politics and policy orientations.

The information presented here is from archival research, survey data, and over 70 interviews (including those with persons in the three aforementioned states and New Delhi.) The three states are all states that are included in the classification of the 15 *major* states of India. These major states contain well over 95% of the republic's population and represent over 97% of the republic's economic activity. As seen in Table

4-1, all three states have relatively large populations and they have the fourth, sixth, and first highest populations respectively.

Table 4- 1: Basic Information about Cases

	Andhra Pradesh	**Madhya Pradesh**	**Uttar Pradesh**
Population (2001)	76 million	60 million	166 million
GDP PC (2001)	10,437 rupees	8,718 rupees	7,148 rupees
Literacy Rate (2001)	61.1%	64.1%	57.36%
Urbanization (2001)	27.1%	26.7%	20.8%

The three states also have similar GDP per capita figures, literacy rates, and levels of urbanization. None of the states can be considered outliers on basic socioeconomic measures and they were all clustered together on most economic and socioeconomic factors at the time of the disbanding of the *license-permit raj* in 1991.

Evidence from the Three Case Studies—the Dependent Side

For the purposes of this chapter, we need to establish the differences among the three cases when it comes to economic policymaking since the summer of 1991. Evidence suggests that the three case studies have a high degree of variance in pursuit of a reform agenda from 1991 to 2003. Specifically, this section will make clear that Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh can be differentiated on a continuum of reform that looks at both promotional policies and deregulatory policies. In addition, there will be a discussion of the process of inter-state competition between the cases which looks at industrial subsidies, state marketing, permit clearance procedures, infrastructure priority, and Special Economic Zone (SEZ) policies.

At the beginning of the reform period, in 1991 all three of the cases were bunched together at the lower end on lists of states with policies favorable to the private sector and new investors. While Madhya Pradesh and Uttar Pradesh have been part of the list of "BIMARU"[18] states in the Hindi-belt with poor growth rates and general unfavorable ratings in the eyes of the private sector, Andhra Pradesh, at the beginning of the 1990s, was in a similarly poor position to take advantage of the new competitive economic reality. Andhra was, for the most part, overshadowed by its more competitive neighbors of Maharashtra and Tamil Nadu, and was far down most lists of attractive industrial locations immediately after the 1991 reforms.

A variety of independent bodies have produced studies in the post-1991 era to gauge the relative extent of policy reform across the Indian states. The first of these, a study carried out by the Indian daily newspaper *Business Today* had the three cases ranked near the bottom of the 26 Indian states in 1995: Madhya Pradesh, #21; Andhra Pradesh, #22; and Uttar Pradesh, #24. Six years later, the states had the following rankings: Andhra Pradesh, #3; Madhya Pradesh, #17; and Uttar Pradesh, #24. What accounts for the rapid rise of the Andhra case while the other two cases stayed near the bottom of the rankings? A joint World Bank and Confederation of Indian Industry study[19] from January 2002 ranked Andhra Pradesh as having a "good investment climate" and Uttar Pradesh as having a "poor investment climate." Recent yearly studies by the Federation of Indian Chambers of Commerce and India have surveyed investors to rank the states of India according to their "investment reputations." Studies from the last three

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[18] BIMARU, spelled from the beginning letters of the Hindi-belt states of Bihar, Madhya Pradesh, Rajasthan, and Uttar Pradesh is a clever play on the Hindi word for "sick"—with the meaning that in recent decades these four states and consistently underperformed the all-India average for economic growth and development.

[19] Madhya Pradesh was not included in this study.

years have Andhra in the third position, with Madhya Pradesh 7th, and Uttar Pradesh 11th among the 13 "large" states that were survey. Likewise, a recent study by Laveesh Bhandari and Bibek Debroy ranks the Indian states by measuring the degree of "economic freedom" in the twenty largest states. Andhra Pradesh is ranked number two, Madhya Pradesh number nine, and Uttar Pradesh number thirteen. What accounts for Andhra skipping from the lower tiers of most rankings in the early 1990s to near the top fourteen years later? Why has Madhya Pradesh risen on most lists to near the middle of the pack in terms of economic freedom and reform? Why has Uttar Pradesh remained in the bottom tier in most of the rankings? This chapter argues that it is the aforementioned institutional and interest group factors which have influenced policymaking within the three states and underlie the rankings of the three states on measures of business climate and investment potential.

On the promotional side, the three case studies can be ranked according to their promotional activities such as targeting subsidies to attract industry and the marketing of the state to potential investors inside India and outside the country. Table 4-2 summarizes the industrial promotional activities of the three states:

Table 4-2: Promotional Activities from 1991 to 2003

	Andhra Pradesh	Madhya Pradesh	Uttar Pradesh
Promotional:			
Subsidy Initiation speed	Average	Early	Average
Subsidy Level	Average	High	High
State Marketing	High	Average	Average

Madhya Pradesh was among the first states to offer comprehensive packages of industrial subsidies in the earlier part of the decade. The state also attempted to compete with surrounding states by offering higher levels of sales tax subsidies and site preparation subsidies for new investors. By comparison, Andhra Pradesh and Uttar Pradesh were comparatively average for an Indian state in proffering a subsidy regime in their industrial procedures policies. Whereas Madhya began offering sales tax subsidies and other subsidized industrial inducements in 1992, Andhra Pradesh and Uttar Pradesh offered comparable subsidies only in 1994. Likewise, while Andhra Pradesh and Uttar Pradesh deemphasized the importance of the subsidy regimes in their industrial plans of 1997 and 1998, the state of Madhya Pradesh continued to push forward with an increasing number of subsidies through 1999.[20]

There is also clear difference between the states on priority given to the marketing of the state during the post-reform era. Andhra Pradesh placed a much higher priority on attending domestic and international conferences in the attempts to lure new investors to the state. Andhra Pradesh was the first state to send delegations to the World Economic Forum in Davos during the 1990s and had a whole office devoted to marketing the state as an investment destination by the end of 1995. Conversely, Madhya Pradesh and Uttar Pradesh placed a much lower priority on the marketing of the state externally during the time period. Offices in the two cases were not set up until 1996 in Madhya Pradesh and 1998 in Uttar Pradesh to promote the states to possible investors. Similarly, the construction of "Hi-Tec City" outside of Hyderabad in Andhra Pradesh in the mid-1990s was undertaken with the belief on the part of state policymakers that there needed to be a focal point as the center of the campaign to market the state externally. This made

[20] "Industrial Policy" state plans for Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh.

Andhra one of the first states to publicly advertise the state as a possible destination for technology and computer firms, with a delegation traveling to San Jose, California in 1996 to drum up business connections for the state.

The three cases can also be ranked according to the priority given to deregulatory economic policy activity as seen in Table 4-3:

Table 4-3: Deregulatory Activities from 1991 to 2003

	Andhra Pradesh	Madhya Pradesh	Uttar Pradesh
Deregulatory:			
Single-Window speed	Fast	Medium	Low
Infrastructure Priority	High	Medium	Medium
SEZ's Priority	Medium	High	High

Whereas Andhra Pradesh was the first state to prioritize the development of a new policy for the "clearing" of new industrial permits in 1997, Madhya Pradesh and Uttar Pradesh took much longer in implementing a similar set of policy changes. The clearance process, and the corresponding difficulty of setting up a new business due to the necessity of visiting a multitude of offices around the state in order to gain approval for a new industry, has been cited most often as the biggest barrier to investment in the Indian states.[21]

The single-window clearance mechanism seeks to redress the problems caused by bureaucratic inefficiency by setting maximum allotted times for an investigation into the merits of a sought permit, and by designating one institution (the single-window) as the "go-to" location for finding out information on the clearance process. Before these types

[21] Much of the 2002 CII/World Bank study explores questions of the "clearance raj" and the differences among states in "clearing" permits for new investment.

of reforms, there would be upwards of 55 approvals needed to begin construction of a new manufacturing plant, with delays often resulting in the process lasting over a year. As an investor in Uttar Pradesh stated: "We began the process in 1993 to open here in Kanpur. We opened in 1995. Why did it take so long? The clearances needed to open. Before it was a *license permit raj,* and then it became a *clearance raj.* We needed numerous prior approvals from the boiler inspector, from numerous labor inspectors, from the electricity board... all located in different offices, sometimes different cities..."[22] With the implementation of a single-window clearance mechanism, states sought to lower the amount of time associated with the setting up of a new business to a small number of months.

The three cases can also be ranked in terms of priority given to deregulating infrastructure and the development of Special Economic Zones (SEZs.) Andhra Pradesh was a leader in prioritizing the privatization of infrastructure during the reform era as well. Independent studies of the highway and energy sectors gave Andhra comparatively high scores on reforms in these areas (Debroy 2004). Madhya Pradesh and Uttar Pradesh lagged behind Andhra in each of these areas and this was reflected in their composite scores in several studies.[23] The availability of high quality infrastructure has been consistently cited as a primary concern among the Indian business community.[24]

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[22] CEO, NeoMagic Corporation, Interview with Author, Lucknow, 11 November 2002.
[23] Citation, energy studies and infrastructure
[24] World Bank study (CITE) and FICCI surveys (CITE)

Evidence from the Three Case Studies—the Independent Side

This section explores the recent economic policymaking of the three case studies in light of causal variables that stem from the hypotheses discussed in a previous section. The following table summarizes the independent variables:

Table 4-4: Causal Variables from 1991 to 2003

	Andhra Pradesh	**Madhya Pradesh**	**Uttar Pradesh**
Institutional:			
Party Fragmentation	Low	Low	High
Number of Parties	2.11	2.27	3.59
Party Competition	High	High	High
Out Party	Both	Both	Both
State Party	Yes	No	No
Bureaucratic Turnover	Low	Low	High
Number of Governments	3	3	10
Interest Group:			
Business Assoc. Density	High	Medium	Low
Labor Strikes	High	Low	Low

This section will begin with a study of electoral competition and party systems, followed by an analysis of executive stability and administrative services transfers. Next, there is an examination of the evidence as it concerns "out parties" and regional parties. And finally, we will look at the marshaled evidence as it concerns the relative influence of industrial associations and labor union activities.

Electoral competition and party systems in the three states

There is a long body of work which suggests that differing levels of electoral competition prompt governments to innovate in different ways based upon the particular electoral logic at play. Subnational India provides a good mix of supply-side electoral situations that allows us to examine the underlying context of industrial promotion across the states. Following from the discussion of the specific cases examined in this chapter, we begin by examining the evidence from three Indian states. The cases of Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh provide us with clear differences in terms of electoral competition, effective number of parties, and party system fragmentation in the reform period. For the time period from 1990 to 2003, we have three or more electoral cycles in each case, providing a good mix of possibilities in each case on the independent side for explaining policy choice by the respective state governments. The following table provides a brief overview of the party systems and number of state assembly election cycles in each state:

Table 4-5: Party System independent variables

	Andhra Pradesh	Madhya Pradesh	Uttar Pradesh
Party System Fragmentation	Low	Low	High
Effective Number of Parties	2.11	2.27	3.59
Assembly Elections[25]	3	3	5

[25] Elections within each of the three states took place as follows: For Andhra Pradesh, elections in 1989, 1994, and 1999; for Madhya Pradesh, elections in 1990, 1993, and 1998; and for Uttar Pradesh, elections in 1989, 1991, 1993, 1996, and 2002.

As seen in Table 4-5, the breakdown on the number of elections ranged from five in Uttar Pradesh to three in both Andhra Pradesh and Madhya Pradesh. Over the course of the 14 year time period under discussion, we have some variability on party system fragmentation across the three cases. In Andhra Pradesh and Madhya Pradesh there are relatively low levels of party fragmentation, while in Uttar Pradesh there is a higher degree of party system fragmentation. During interviews, investors commented often on the impact of party competition on industrial promotion policies. As one stated regarding the Andhra case: "Looking at the cycles of party elections here in AP, we have seen the benefits of a recently stabilized party system." [26] In the case of Andhra, with the rise of the Telugu Desam Party (TDP) in the 1980s and 1990s, there developed a party system that was effectively comprised of two parties for the duration of the post-reform period. The TDP is a Andhra-based party that articulates state-level interests and thus induced the Indian National Congress (INC) to compete on those terms, providing a stimulus to policy innovation. As seen in the following table, the TDP and INC received over 77% of votes in each of the three elections.

Table 4-6: Percentage of Votes in Andhra Assembly elections

	TDP	**INC**	**Other Parties and Independents**
1989	36.6%	47.1	18.3
1994	44.1%	33.9	22.0
1999	43.9%	40.6	15.5

[26] Top 10 Indian IT company CEO, 1998 investor in Andhra Pradesh, Interview by author, Hyderabad, 6 February 2003.

An INC assembly member during the 1990s commented that "As a party we were able to frame ourselves in opposition to the TDP.... And contrast our positions on attracting investment during the campaigns."[27] The INC campaigned in the 1999 elections with an economic plank of opposing much of Chandrababu Naidu's and the TDP's reform agenda by arguing that the Naidu administration opposed the interests of the urban and rural poor. At the same time, party members had to reassure members of the business elite, past investors, and potential investors that the INC, if victorious, would continue on the reform path.

This set of industrial promotion policies would be less forthrightly pro-business than what had been the case during Naidu's first term, but industrial association members acknowledged that the INC recognized the potential longer-term benefits for the state due to some of the government's policies. As an executive officer in the Confederation of Indian Industry stated, "We had formal and informal discussions with higherups in the Congress about what would be the relationship if they won the elections. It was told to us that we could expect a certain degree of continuance in the reform policies."[28] There was less room to maneuver because of the competitive nature of the party system in the state. Specifically, the stability afforded by what industrialists and politicians referred to as the "2-party system," created an environment whereby there was a supportive role played by the state's electoral competition for what were perceived as "pro-growth" policies. A representative for a company that invested in the state in 2000 remarks on what the thinking was on the decision to invest in the period leading up to the 1999 AP assembly elections: "There was much rhetoric on the part of the INC to the effect of seeming to

[27] Greater Hyderabad district AP assembly member, interview with author, Hyderabad, 29 January 2003.
[28] Executive Manager, CII, interview with author, Hyderabad, 26 January 2003.

scare business and the chance of undoing some of what Naidu had been doing in the state. But we made the calculated risk based upon talking to members of the IAS [Indian Administrative Services] and people in the industrial ministry that we could expect continued support…"[29]

Overall, the case of Andhra provides much support for the hypothesized relationship between the party system and the propensity for higher levels of industrial promotion policies and continuity of policy regimes. From the beginnings of the TDP policy "revolution" beginning after the 1994 elections, and on until the events of the early 21st century, the relatively stable and unfractured party system in Andhra provided electoral incentives for policy innovation and a strong measure of policy consistency for investors and potential investors. The competition to curry favor with the organized business community was an implicit concern of both parties, aside from any inflammatory rhetoric that might come from individual party members.

The case of Madhya Pradesh contrasts slightly with the Andhra case. While both states had a low level of party fragmentation and an effective number of parties approaching two, in Madhya Pradesh, the dominance of one particular party during the time period and the lack of a post 1991 reform break with policy subsets led to a lesser amount of policy innovation and industrial promotion. While Andhra's two-party system is comprised of one national party and one state party, in the case of Madhya Pradesh, both main political parties, the BJP and the INC are national parties. Unlike the Andhra case, the logic underlying inter-state competition took longer to affect Madhya Pradesh because of the higher degree of involvement and coordination with the national party offices in New Delhi. As argued by a member of the Madhya Pradesh planning

[29] Operating officer for US-based IT firm, Interview with Author, Hyderabad, 10 February 2003,

commission: "We faced a much different dynamic here. We had two parties competing in our state for control that mirrored those battling at the national-level in the reform period. It took us longer than others to have a period of 'Madhya-first' as an organizing principle for the elections..."[30]

[30] MSPIDC, Industrial minister, Interview with author, Bhopal, 11 January 2003.

TABLE 4-7: Percentage of Votes in Madhya Pradesh Assembly elections

	BJP	INC	Other Parties and Independents
1990	39.1%	33.4	27.5
1993	38.8%	40.7	20.5
1998	39.3%	40.6	20.1

As seen in Table 4-7, the BJP and INC captured from 72% to 80% of the vote during the assembly elections of the 1990s. The government headed by the INC and Chief Minister Digvijay Singh starting in 1993 through 2003 made a variety of reforms a key part of its governing agenda. Unlike in Andhra, however, the focus was on local governance reforms, education, and community health programs. While the government implemented a series of business attraction policies in the mid-1990s, many came to be known as "paper-only reforms," with little in the way of regulatory changes sought by potential investors and the business community. As a senior official in the Singh administration declared with some candor: "We have been very concerned with good governance issues and programs that we could call pro-poor especially in the lead-up to the 1998 elections. We played the subsidy game with other states in the mid-1990s.... but in the end the BJP did not play up the infrastructure and industrial attraction problems until the 2004 elections... We did not, in hindsight, do as much as we could.... [Chief Minister] Diggy was more concerned with capturing the rural vote and business was a secondary concern."[31] Unlike the electoral dynamic in Andhra that had a national party

[31] Director, MPSIDC, Interview with author, Bhopal, 3 January 2003.

forced to address the concerns of the business community because of policy dynamism coming from a state party, in Madhya Pradesh, the competition for investment took a back seat at the beginning of the 1990s to other political concerns. In other words, the state experienced electoral mobilization linked to national political dynamics with little impetus to mobilize on the basis of state-level interest or policy differences. While the solidifying structure of the two-party system fostered policy competition as expected by the hypotheses, the total effect was much less due to the important distinction of *which two parties were competing*—and how this influences the content of policies. We will now turn to Uttar Pradesh, which represents a party system at the other end of the continuum regarding fragmentation and the effective number of parties.

The state of Uttar Pradesh had 5 legislative assembly elections during the time period under discussion. As seen in table 4-7, Uttar Pradesh had 3.59 effective number of parties. And, to add to the disruptive effects on policy clarity, the same parties did not poll well during the five elections. Table 4-8 shows the breakdown of parties and the percentage of votes for the five elections:

Table 4-8: Percentage of Votes in Uttar Pradesh Assembly elections

	BJP	INC	JD	BSP	JP	SP	Other
1989	11.6%	27.9	29.7	9.4	.74	x	20.1
1991	31.5%	17.3	18.8	9.4	12.5	x	10.5
1993	33.3%	15.1	12.3	11.1	.52	18.0	9.7
1996	32.5%	8.4	2.6	19.6	.13	21.8	15.0
2002	20.1%	9.0	x	23.1	x	25.4	22.4

Over the duration of the subnational reform period in India, Uttar Pradesh had a highly fractured political party system. While it was a highly competitive party system, with four different parties heading the government during the decade and a half, policy coherency suffered greatly due to the highly unstable electoral results. And, as will be discussed in the next section, there was also the concomitant problem associated with executive turnover and emergency rule from the central government. As one industrial association official noted: "To be honest, we had a situation for much of the 1990s where we could not count on a policy that was told to us being around by the following week. We would receive commitments from the new governments about working with us on needed reforms, but soon enough a new round of electioneering and campaigns was under way… at times it felt like we never got out of campaign mode in UP…"[32] Subsidy regimes were pulled before they were fully implemented and there was little movement on the single-window clearance program until the latter part of 2003. In the words of an industrialist from Kanpur: "We would receive information and policy papers from

[32] Head of regional industrial association, Interview with Author, Lucknow, 21 December 2002.

officials in the ministries. But we rarely saw implementation, because by the time it was ready to be used, the program had been pulled because the new government wanted their own stamp on anything done. While things were more stable in NOIDA and surroundings, the rest of UP never saw the benefits from any of this…."[33]

All told, the impact of party system fragmentation and competition was great on industrial policymaking within the three states. In Andhra Pradesh, with a relatively stable two party system with a state party versus a national party, much more innovation and stability in the industrial promotion regime was evident. In Madhya Pradesh, with a stable two party system with two national parties, there was a great deal of internal consistency to policies, but the developmental priorities for the state were more targeted at the education and health sectors. There was less consequential industrial policy innovation than in Andhra. The final case, Uttar Pradesh, had a competitive but highly fragmented political party system throughout the time period of 1990-2003. This electoral instability led to problems with program implementation and caused a high degree of concern in the private sector and the organized business community in the state. In all three cases, the party system directly influenced levels and types of industrial promotion policies. In the next section we turn to the related issue of executive stability and administrative transfers.

Executive Stability and the "Transfer Raj"

Another significant set of factors altering the parameters of Indian subnational industrial policy from 1990 to 2003 is the tenure of chief ministers across the states and the rate of transfers in the Indian Administrative Services (IAS). When a new

[33] US IT sector subsidiary Official, Interview with author, Kanpur, 3 December 2002.

government comes to power in one of the Indian states, there is usually a high number of transfers within the IAS cadres. Because IAS officers are assigned to a particular state, they are appointed to a position within the state bureaucracy by the chief minister of the ruling government. In cases where the control of the state changes hands from one party to another, there is usually a high degree of changeover within the bureaucracy in the months immediately following the governmental transition. In addition to the turnover in chief ministers due to normal electoral politics, they can also be changed because of intervention by the central government in Delhi and because of changes in the leadership of the party or coalition of parties in control of the state. The Union Minister of State Personnel Vasundhara Raje Scindia, in an interview with the *Indian Express* newspaper, commented on administrative changes in the states:

> "...Ours is a federal structure in which the command and control over an all-India officer posted in a state rests with the state government. The system works something like this: As the cadre controlling authority, we at the Centre are responsible for the appointment, disciplining, and dismissal of officers belonging to the all-India services. For everything else, the power rests with the state government... The Centre has no legal right to intervene in the decisions a state government may take on postings and transfers."

Other research has argued that executive stability impacts the rates of program implementation (Sinha 2002) and policy cohesiveness (Jenkins 2004). In situations where there is a high degree of turnover in policymaking and administrative teams, policy coherence suffers. Similarly, the variability of mandated bureaucratic transfers by a particular chief minister in a state impacts industrial policymaking and institution-building. Banik's (2001) work on the IAS stability and tenure differences and the resultant effects on performance capabilities suggests that the existence of a "transfer raj" would influence economic policymaking at the state level in the three cases. The underlying political logic was that administrative transfers were necessary for a new government to "seize" control of the bureaucracy and show state workers that there were new lines of political control from the state capital.

Table 4-9 shows the number of chief ministers in each state, and the frequency of administrative transfers within the state during the tenure of each chief minister:

Table 4-9: Chief Ministers, Tenure in Office, and IAS Transfers

State	Minister/Exec.	Party	Tenure	Months	Transfers	Trans/mo.
Andhra Pradesh	N. Reddy	INC	12/90—10/92	23	253	**11.0**
	K. Reddy	INC	10/92—12/94	27	262	**9.7**
	N. Rao	TDP	12/94—9/95	10	156	**15.6**
	C. Naidu	TDP	9/95—5/04	104	1123	**10.8**
Madhya Pradesh	S. Patwa	BJP	5/90—12/92	31	425	**13.7**
	Admin. Rule	na	12/92—12/93	12	103	**8.6**
	D. Singh	INC	12/93—12/2003	120	1128	**9.4**
Uttar Pradesh	M. Yadav	JD	12/89—6/91	18	493	**27.4**
	K. Singh	BJP	6/91—12/92	18	521	**28.9**
	Admin Rule	na	12/92—12/93	12	297	**24.8**
	M. Yadav	JD	12-93—6/95	18	814	**45.2**
	M. Mayawati	BSP	6/95—10/95	5	501	**100.2**
	Admin Rule	na	10/95—3/97	17	1037	**61.0**
	M. Mayawati	BSP	3/97—9/97	6	1350	**225.0**
	K. Singh	BJP	9/97—11/99	27	822	**30.4**
	R. Prakash	BJP	11/99—10/00	11	488	**44.4**
	R. Singh	BJP	10/00—3/02	17	771	**45.4**
	Admin Rule	na	3/02—5/02	2	77	**38.5**
	M. Mayawati	BSP	5/02—8/03	15	1200	**80.0**

Sources: IAS "Report on State Cadre Transfers," unpublished, 2004.

As Table 4-9 demonstrates, the average tenure of the executive varies greatly across the three cases. In the case of Andhra Pradesh, the mean term of rule was 41 months. For Madhya Pradesh, the average period was 54 months. For Uttar Pradesh, the average tenure was 14 months. This divergence in executive longevity influenced industrial policymaking in each state to differing degrees, with Andhra Pradesh and Madhya Pradesh more likely to have program administrators around long enough to shepherd policies from design to implementation. Likewise, there is a significant difference in the volume of bureaucratic transfers within the state cadres of the Indian Administrative Services (IAS). Table 4-9's right-most column contains calculations for the average number of administrative transfers for each state, for each administration, per month of office-holding. The differences are stark among the three states and across the time periods within states. Whereas the average number of transfers was 11.8 per month in Andhra Pradesh, 10.6 for Madhya Pradesh, and there were 62.6 transfers per month from 1990 to 2003 in Uttar Pradesh. The consequence of such extreme administrative turnover was great on the effectiveness of economic policymaking.

In the case of Andhra Pradesh, the longevity of the second TDP government of Chandrababu Naidu led to a relatively stable body of IAS officers in the higher ranges of the economic development ministries. This consistency over time and across offices had a significant impact on the relations between the state government, potential investors, and the organized business community. Key positions were held by officers who developed longstanding relationships with members of the private sector. As the director of a large industrial chamber in Andhra Pradesh remarked: "We have had great stability here in Andhra... The team in charge of attracting new IT investment in the state has been in place for several years. We have a good relationship with them. I can pick up the phone and discuss matters with them. It has been a big advantage for our member industries."[34] The stability in the officer cadre in Andhra Pradesh was extremely beneficial in coordinating subsidy programs put in place to attract new investment.[35] Information was relatively easy to obtain and the specific parameters of programs could be negotiated with a core group operating within the Andhra Pradesh Development Council. This type of environment largely parallels what Peter Evans (1995) has called "embedded autonomy" in East Asia a generation ago.

In the case of Madhya Pradesh, there was also a high degree of internal consistency in the membership of the IAS officers in the industrial promotion offices within the state. Although as discussed elsewhere, there was less of a focus on the attraction of large-scale investment for much of the 1990s, companies that did invest in the state during the time period cited the reliability of policies and government interactions thanks in large part to the stability of the staffs of the state government. Internal investment site documents for a large-scale manufacturing plant cited this as an important factor in considering the location of Indore in Madhya Pradesh for their investment.[36] The administration of Digvijay Singh, which governed Madhya Pradesh from 1993 to 2003 had a monthly IAS reassignment ratio of less than 10 officers per month allowing for a large amount of regularity of interactions over the decade. While Banik (2001) and Potter (1998) have voiced concerns about such longevity in posts and

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[34] State Representative for the CII, Interview with Author, Hyderabad, 22 February 2003.

[35] In interview with numerous recent investors in the state, the consistency and regularity of their working relationships with members of the AP IAS was cited as a crucial factor in their decisions to locate in the state.

[36] The author was allowed to view an internal 1999 "Site Selection" document that has a pointed discussion of the reliability of state-private sector interactions based upon their discussions with representatives of other companies within the state.

the possible problems associated with such long tenures in IAS assignments, in the case of Madhya Pradesh, there was much praise in the private sector for the quality and training of persons occupying key posts in the Singh government.

The case of Uttar Pradesh is much different in the quantity of IAS transfers for the duration of the post-1991 reform era. While the other two states had monthly transfer ratios in the high single digits or low double digits, over the course of the 14 year period in Uttar Pradesh the number of transfers reached these levels of bureaucratic changes *per day*. In fact, during two of the Mayawati administrations in 1995 and 1997, there were over 100 and 200 transfers, respectively, per month among the IAS civil servants. In one key position that coordinates investment and regulatory control over the Greater NOIDA economic development zone in the far western part of the state (proximate to New Delhi), there were 21 Administrative CEOs between 1995 and 2002. In one episode in late 1997, there were three CEOs in a three-week time span.

Events like these caused much policy confusion that many business leaders named as a great concern for retaining industry and attracting new investors to the state. As the head of a large industrial chamber relayed to the author: "There were times when we would call a civil officer about a problem with a regulatory issue and the movement towards the new clearance procedure for an industry. Our phone calls would not be returned and when we would call again, we would find out that the official in question had been transferred the previous day to a district tax post in another part of the state."[37] With the competition for investment among states becoming even more pronounced over the course of the 1990s, many investors and private sector officials became very concerned about governmental regulatory and oversight issues. As one company official

[37] Director, large Industrial Association, Interview with Author, Lucknow, 26 December 2002.

stated: "It felt as if people were not in their offices long enough to do any good… We would meet the new clearance official at a reception on a Thursday, and by the following week there was a new person in the office… They had been recently transferred from a tax collector position in a rural district and did not know the first thing about the policies of the state government concerning investment targeting."[38] The "transfer raj" in Uttar Pradesh created many problems for the state in attempting to compete with other states for investment.

Overall, the impact of executive change and IAS transfers in the three case studies presents clear evidence of problems associated with a lack of transparency and continuity or predictability in the bureaucratic regulation of the private sector. States such as Andhra Pradesh and Madhya Pradesh, with relatively little civil servant movement and more regular patterns of executive control, were better positioned to attract industry and investment because they had clearer rules of the game. States such as Uttar Pradesh had a more difficult time because of governmental turnover and extremely high levels of IAS reassignments. The hypothesized relationship between executive instability and policy coherence is largely confirmed in these case studies.

Out Parties, Regional Parties and the Federal dynamic

The different composition of political party control across the states and levels of government affected Indian subnational economic policymaking from 1990 to 2003. Specifically, a variety of parties and coalitions of parties controlling the federal government, and others in power at the subnational level over the years, results in expectations for which dynamics will result in more activist state governments in

[38] CEO, large manufacturing firm, Interview with Author, Kanpur, 20 December 2002.

industrial policy. It is expected that those states that are governed by an "out party"—one not in power at the center--or by a "regional party"[39]—a non-national party will be more likely to be active on the industrial promotion front and the movement toward a dual strategy that includes deregulation. Those states governed by a party in power at the center are expected to move more slowly in industrial policy innovation. Table 4-10 shows a matrix of political party control at the federal and state levels in India:

[39] For the sake of our discussion here, we will include as regional parties a party that exists in only that particular state.

Table 4-10: Matrix of Party Control, 1990-2003

Year	Federal[40]	Andhra Pradesh[41]	Madhya Pradesh[42]	Uttar Pradesh[43]
1990	JD	INC	BJP	JD
1991	JD/INC	INC	BJP	JD/BJP
1992	INC	INC	BJP/*AR*	BJP/*AR*
1993	INC	INC	*AR*/INC	*AR*/JD
1994	INC	INC/TDP	INC	JD
1995	INC	TDP	INC	JD/BSP/*AR*
1996	INC/BJP/JD	TDP	INC	*AR*
1997	JD	TDP	INC	*AR*/BSP/BJP
1998	BJP	TDP	INC	BJP
1999	BJP	TDP	INC	BJP
2000	BJP	TDP	INC	BJP
2001	BJP	TDP	INC	BJP
2002	BJP	TDP	INC	BJP/*AR*/BSP
2003	BJP	TDP	INC	BSP

[40] On June 21' 1991 the government went from control of the Janata Dal to the Congress party. On May 16' 1996 the government went from control by the Congress party to the Bharatiya Janata Party. Later in the year, on June 1' 1996, the Janata Dal took over from the BJP.
[41] On December 12, 1994 the TDP government took over from the Congress government.
[42] There was Administrative Rule in the state from Dec. 16, 1992 until December 6, 1993.
[43] For the years of 1991, 1992, 1993, 1995, 1997, and 2002, Uttar Pradesh had multiple parties in power over the course of year and/or a period of administrative rule in addition to a ruling party in the state assembly.

As we can see from the table, the three case studies provide nice variance on the independent variable of out parties and regional parties. The lightly shaded squares denote years where there was an out party. The squares shaded a slightly darker hue signify those years when there was a regional party in power during that year in the state.

In Andhra, there were two distinct periods of cross-level party dynamics. With the exception of 1990—the last year before the federal economic reforms of the summer of 1991—the first half of the decade is noteworthy for having an "in party" controlling the government. The latter part of the decade is a different story, however. A very clear increase in policy activity in Andhra Pradesh, beginning in 1995, fits with our expectations about the impact of a state controlled by a regional party on industrial policy. During the 9 years that Chandrababu Naidu ruled the state, Andhra Pradesh was consistently rated as one of the most reform-oriented states.

While many have argued that this was a person-specific causal mechanism (Kennedy 2004; Rudolph & Rudolph 2001), this research suggests that there was a very basic institutional difference because of the nature of the variations in party control across levels of government. The TDP cannot be categorized as a pure "out-party" because of its crucial role in supporting the BJP coalition when it was in power in the latter part of the 1990s and early 2000s. The existence of a regional party-led government for the time period pushed the state in the reform direction. As a higher up Naidu administration official recounted: "We were in a very good position. We were able to play up our Andhra roots, and place ourselves in opposition to the national parties. This was also the case for our policy differentiation. We had more space to maneuver because of our position in the centre."[44] Naidu himself was forthcoming in his autobiography from 2000:

> "The Telugu Desam is a regional party with a national outlook.... The first fundamental departure... is to recognize that the end of politics is governance, not mere ruling. ...the second is our belief that the politics of populism can be replaced by the politics of development. The latter too can be made to pay electoral dividends.

The TDP sought to develop economically through policy intervention, as they were severed from national patronage because the very nature of their existence as a regional party.

There are three distinct periods of cross-level party differences in Madhya Pradesh. There is the first out-party era from 1990 to 1992, followed by in-party rule from 1993 to 1996, and then the second out-party era from 1997 to 2003. There is some degree of support for the hypothesized relationship based upon what transpired in the state during the post-reform period. While the INC party government that held power in the state from 1993 to 2003 was a roughly in the middle of the Indian states on the reform front, there was recognition within the Singh administration that the rules of the game were different after the non-INC coalitions took power in New Delhi in 1996. In the words of one governmental official: "We soon realized that we had to alter our development strategy after Congress fell out of rule in the capital. We did not have a good relationship with the new government and found ourselves in a situation where we had to do things for ourselves if we wanted changes to take place."[45]

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[44] Senior IAS Officer, Class 1, Interview with Author, Hyderabad, 12 February 2003.
[45] Madhya Pradesh development official, 1994—2001, Interview with Author, Bhopal, 26 January 2003.

It is during this time period that the Madhya Pradesh government commissioned a study to examine an overhaul of the subsidy regime for attracting new business. After the results came back showing that there was little measurable return on the lost money due to decreased state income from sales taxes, the government overhauled the system to make the subsidy system less generous.[46] The state then chose to prioritize infrastructure expenditures and decided to study the implications of liberalizing the inspection regime with the hope of attracting new investment. Several officials cited the change in governments at the center as an impetus for altering the state strategy for attracting new investment.

As for Uttar Pradesh, the ability to draw causal inference from changes in party control at the center and in the state is more difficult. As with the previous discussions about party fragmentation, executive turnover, and the "transfer raj," the existence and changeover of "out parties" in Uttar Pradesh happened at a dizzying pace. For some years, there were two or three changes in relative party control in the state vis-à-vis changes in coalitions in power at the center. Many private sector officials expressed some degree of bewilderment about how unsteady the politics were in the state during 1992-2003 era. As one industrial chamber official spoke of it: "It was a bit like a multi-dimensional chess game. There were not clear lines of influence from the center… and with the rapid rise and fall of parties within the state, industrial policy clarity was nonexistent for much of the decade."[47]

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[46] The author was allowed to look over the internal document in the offices of a state official on the 27th of January, 2003.
[47] Director, Confederation of Indian Industry, Lucknow Office, Interview with Author, Lucknow, 5 December 2002.

Overall, there is some degree of support for the hypothesized relationship between the nature of "out party" and regional party influence on industrial promotion policies in the three case studies. A state like Andhra Pradesh with the multi-year rule of the TDP regional party certainly caused the states industrial policy to be more progressive in comparison with other states. Although the TDP was a critical member of the center coalition for much of the time, its existence as a state-based party allowed it to operate outside the normal patronage system flowing from the corridors of power in New Delhi, and instead the TDP was forced to innovate programmatically in light of state electoral concerns. In Madhya Pradesh we also gain some confirmation for the expectation that in times of the state's rule by an out party would be periods of progressive policy formulation, but the level of activity was somewhat lessened by a different strategic choice due to the nature of political contestation in the state. And finally, in Uttar Pradesh, because of the high degree of instability in the "out party" indicator for the state, it is more difficult to comfortably express a causal linkage between out parties and industrial policy. Nonetheless, the general instability in the party control variable at both the state and federal levels played a significant role in what we have seen as a general lack of policy cohesion for much of the decade in Uttar Pradesh.

Coalitions for Reform: Organized Business and State Governments

This section explores the nature of the relationship between formal business sector associations and subnational industrial policymaking in the three cases. As hypothesized, we expect that there would be a positive relationship between the density of industrial association membership in a state and higher levels of subsidies for new external investments in the particular state. Likewise, we expect that there is a positive relationship between density of membership and speed with witch a state moves toward a more progressive promotional and deregulatory strategy. Table 4-11 shows the yearly breakdown, state-wise, of total medium- and large-sector business participation in the two pan-India, peak industrial associations—the Confederation of Indian Industry (CII) and the Federation of Indian Chambers of Commerce and Industry (FICCI).

Table 4-11: Industrial Association Membership and Per Capita, 1990-2003

Year	Andhra Pradesh		Madhya Pradesh		Uttar Pradesh	
	Total	*Per Cap*	*Total*	*Per Cap*	*Total*	*Per Cap*
1990	158	2.44	76	1.18	76	0.56
1991	163	2.46	77	1.17	80	0.58
1992	171	2.54	79	1.17	87	0.61
1993	175	2.56	81	1.18	95	0.65
1994	180	2.59	85	1.21	98	0.66
1995	191	2.70	89	1.23	103	0.67
1996	197	2.74	97	1.32	105	0.67
1997	200	2.75	100	1.33	107	0.67
1998	200	2.72	100	1.30	108	0.66
1999	205	2.76	101	1.29	108	0.65
2000	207	2.75	101	1.27	109	0.64
2001	211	2.76	107	1.29	111	0.66
2002	217	2.78	108	1.28	114	0.67
2003	222	2.80	111	1.29	116	0.67

As seen in the table, there is a large degree of variability in the density of business association membership across the states and across the 14-year time period under discussion. In all three cases there is an absolute growth in the number of participating medium- and large-sector companies within the two umbrella industrial associations. Over the course of the 1990-2003 era, absolute membership levels increased by 141%, 145%, and 153%, respectively, in Andhra Pradesh, Madhya Pradesh, and Uttar Pradesh. There is a larger difference among the states, however, when we look at these gross level measurements as per capita figures. The density of membership in the peak industrial associations in Andhra grew from 2.44 large and medium sector companies per million people in 1990 to a ratio of 2.80 by the end of 2003. These relatively high levels contrast strongly with the results from our other states. The "medium" state on the dependent side, among the three cases, Madhya Pradesh had per capita ratios of 1.18 growing to 1.29 over the course of the era. And finally, the slow moving state on the industrial policy front, Uttar Pradesh, had low measurements on the business density indicator in comparison. Starting with a ratio of .56 in 1990, the per capita membership only reached a .67 level by the end of 2003. These figures suggest at least tentative confirmation for the hypothesized casual relationship between policymaking activities of states and the density of industrial association membership.

For the case of Andhra Pradesh, business association officials were for the most part quite satisfied with the level of coordination and consultation that took place between the state government and the formal private sector. As the managing director of an industrial chamber said: "Starting in 1997 we had regular contact with the Naidu administration... In comparison to other states that I have worked in and what I hear from officials in other states, we had a higher degree of interaction with persons on the development staff of the government."[48] Beginning with the implementation ofthe Andhra Pradesh Industrial Policy of 1994, the state government held formal meetings with the private sector to garner feedback on what could be done to attract more industry.

This higher level of official consultation was done much earlier than was the situation in the two other case studies. What began as consultations on subsidy regimes became a regularized set of interactions through a governmental institution by the name of the AP State Business Council. These regular meetings were instrumental in altering some aspects of the *Vision 2020* document that the government produced in January 1999

[48] Managing Director, CII, Interview with Author, Hyderabad, 2 March 2003.

that charted the plan for the state's development for the following two decades. As a 1996 investor in the state described it: "Almost immediately after our investment in the state, we would receive regular calls from the Council asking us to participate in the strategy meetings.... It was here that I and others brought up the inspection raj issue and I think that is why the government attempted to implement the single-window clearance system in advance of other states..."[49]

For the cases of Madhya Pradesh, there were lower levels of official state and organized business association interaction during the time period. While there was informal consultation on issues relating to the business environment in the state, it was not until 2001 that the state government formed an institution that would meet semi-regularly to have discussions between the industrial development wing of the state government and members of the organized business community. One industrialist voiced an opinion on why this was the case: "There did not seem to be a real concern with Digvijay Singh and some of the industrial officials with what we thought about development in the state. I think that they were so focused on a Kerala-model of development that attracting industry and the competition with other states was not as important." [50] In fact it was not until after the release of a report on the industrial incentive regime in the state done by the New Delhi-based "National Insitute of Public Finance and Policy" headed by the noted economist Indira Rajaraman[51], that the government invited business leaders to a roundtable discussion of what could be done to compete with neighboring states for investment.

[49] Pharmaceuticals Industrialist, Interview with Author, Hyderabad, 27 February 2003.
[50] Invest C, Manufactured Household products, Interview with Author, Bhopal, 28 January 2003.
[51] "Fiscal Industrial Incentives of the Government of Madhya Pradesh: Costs and Benefits" (Rajaraman et al 1999)

As for Uttar Pradesh, there was not any formalized state and private sector institution for interaction for the duration of the 1990-2003 time period. Although several were planned by different administrations during the 1990s, none met more than once because of the related instability in the executive and the rapid movement of IAS officers from position to position in the bureaucracy. In fact, the PHD Chamber of Industry in Uttar Pradesh held informational retreats for bureaucrats to demonstrate to the officers how the state could move beyond "the red tape associated with locational decisions."[52] While attendance was high, the meetings seemed to affect little change in the state. As one industrialist from NOIDA spoke about it: "We simply could not have had an institution like that because of the extreme uncertainty around who would even attend the meetings. We would have liked to influence policy but there were no ways to do so."[53] The comparative lack of formal channels for interaction as well as relatively low levels of industrial association membership, in combination with factors discussed before, resulted in some slower movement by the state in addressing key business concerns like the inspection regime and the clearance system.

In sum, there is some degree of support from the case studies for the hypothesized influence of the formal industrial sector pressuring subnational governments for policy changes. Although there is some caution that must be expressed when attempting to look at the exact causal mechanism. There is the potential competing explanation which would ascribe the levels of business involvement in policy and density of membership as being a *result* of the actions of a state government on industrial policy. Clearly, there is

[52] Utilizing the terminology from official UP documents in the mid-1990s, the Chamber sought to establish a working relationship with the key governmental officials who would be in charge of changing industrial promotion policies for the state.
[53] Investor Q, Interview with Author, New Delhi, 28 November 2002.

at minimum the existence of a feedback loop between policy and business organization and involvement, but there is some amount of support for the expectation that states with higher density and more channels for institutionalized state and private sector interaction will be those states that moved more quickly on the reform front in the post 1991 environment in the Indian states.

Labor Union Activity and State Reputations

The final of the hypothesized influences on state industrial policy is the effect of organized labor union activity on subnational industrial policymaking. Specifically, we would expect that higher levels of union activity to cause states to become more active in terms of promotional activities, but less likely to pursue deregulatory strategies. Table 4-12 gives the state-wise distribution of person-hours lost to industrial strikes and lockouts from 1990 to 2003. Also included are the per capita figures for the same years and three cases:

TABLE 4-12: Industrial Strikes/Lockouts Person-days Lost and Per Capita

Year	Andhra Pradesh		Madhya Pradesh		Uttar Pradesh	
	Total	*Per Cap*	*Total*	*Per Cap*	*Total*	*Per Cap*
1990	3,422,206	52,855	211,628	3,302	1,267,653	9,409
1991	2,759,295	41,810	105,068	1,602	1,019,367	7,397
1992	2,546,361	37,924	39,017	581	858,512	6,086
1993	2,001,853	29,332	153,031	2,230	836,454	5,790
1994	3,129,093	45,108	319,516	4,551	571,292	3,861
1995	4,136,013	58,660	96,955	1,349	516,969	3,412
1996	2,138,193	29,835	380,201	5,173	683,913	4,408
1997	1,357,354	18,690	108,367	1,445	1,009,906	6,376
1998	5,972,937	81,338	161,822	2,119	824,336	5,103
1999	1,370,136	18,449	399,770	5,141	628,706	3,812
2000	4,384,675	58,375	620,935	7,843	1,776,436	10,537
2001	2,654,821	35,056	403,854	6,687	873,995	5,263
2002	1,465,320	19,131	533,632	7,221	1,221,945	6,701
2003	1,778,393	22,434	488,221	6,256	925,843	5,459

As seen in the table, the three case studies have quite dissimilar amounts of industrial strike and lockout activity. Whereas Andhra Pradesh has 18 to 81 thousand person-hours lost per million people, Madhya Pradesh and Uttar Pradesh have much lower ratios. For these two states, the averages are in the low single-digit thousands of person-hours lost on a per capita basis in the states. These data include only those strike and lockouts in the industrial sector of the economy, and do not include those from the service, agricultural, or public sectors.

Across the three case studies, numerous state governmental officials expressed concern with the labor activity issue in terms of its impact on the state's reputation for labor peace and stability. The stability factor was seen as a crucial aspect of what potential investors might look at in discussing options for the location of an investment. Internal documents seen by the author from two site location studies both examined the "labor situation" across the states in light of strike activity and recent history of private sector/labor union interactions.[54]

Andhra Pradesh has a long history as a state with a high degree of labor militancy. With its long history of communist party strength through the 1960s, there has been a fairly activist labor movement in the state in the decades since the start of the declining electoral fortunes of the two main communist parties. In interviews with foreign and domestic industrialists in the state, concerns with labor militancy were not a big issue. As one business official spoke of the situations: "We don't really have a problem here in Andhra. The levels of strikes are higher than some other states, but nowhere near what they are in West Bengal and Kerala. Those are states with poor reputations. It is not a concern here in Andhra."[55] There was near unanimity among governmental officials and IAS officers that the labor situation and the relatively high levels of strikes and lockouts did not affect industrial policymaking to any great extent. The expectation would be that a case like Andhra Pradesh, with a labor militancy level far higher than the average for all of India, would be slower on the movement toward a dual promotional/deregulatory strategy—and this is not the case.

Unlike Andhra, Madhya Pradesh and Uttar Pradesh have much lower levels of labor militancy as compared to the all-India average. Contrary to expectations, this did

[54] One of the site survey documents, from Proctor & Gamble was dated March, 1996. The other site survey document, from a large British conglomerate was from January, 2000. Both documents discussed many issues of concern when deciding among states for investment including quality of the labor pool, proximity of the labor pool, and relative "militancy" of labor in each of the states.
[55] Investor 1996 C, Interview with Author, Hyderabad, 11 March 2003.

not seem to foster a creative environment for more proactive industrial policies in the two states. As one Madhya Pradesh governmental official stated: "We very seldomly get asked about this by potential investors. Mostly they want to know about other things: water, infrastructure, subsidies, various regulations.... How educated and trained the workforce is also tops on lists."[56] Likewise, officials in the state government of Uttar Pradesh discounted the extent to which the relatively pliant labor force influenced state economic policymaking. As an economist based in New Delhi described it: "If the low levels of union strike activity was affecting policymaking in states like UP, we would expect that the government would be much more active than it has been. This issue has been overshadowed by the other factors causing the disorganization among the economic planners in the government"[57]

In sum, the impact of labor strength and militancy on economic policymaking across the three cases seems to be somewhat negligible. While our expectations would be that in a state like Andhra Pradesh that the higher incidence of industrial strikes and lockouts would dampen the level of industrial promotion policies and decrease the speed of reforms, this was not the case in the post-1991 subnational reform era. Conversely, in states with low levels of labor union militancy like Madhya Pradesh and Uttar Pradesh in the reform era we would expect higher amounts of industrial policy activity and a quicker pace on the movement towards a dual promotional/deregulatory strategy. As seen in the analysis above, this was not the case. When taken together, the evidence presented suggests that this factor was overwhelmed by other influences on the ability for state governments to make industrial policy. Perhaps in a more stable political environment in

[56] Industrial Services Officer, Interview with Author, Hyderabad, 12 March 2003.
[57] Bibek Debroy, Rajiv Gandhi Foundation, Interview with Author, New Delhi, 12 November 2002.

Uttar Pradesh, economic policy officials could have capitalized on their comparative advantage in labor stability. But due to the chaotic politics of the state from 1991 to 2003, any possible benefit was cancelled out by executive instability and party system fragmentation. Likewise, in a fast reforming state like Andhra Pradesh, the disadvantage coming from higher levels of labor militancy did not appear to play a large role in slowing down deregulatory-oriented polices because of other supporting factors discussed in previous sections.

Conclusions

This chapter presents information from three case studies of states in India. The data portray an environment of competition among state governments in India that stems from the national-level economic reforms instituted in the summer of 2001. By examining a fast-reforming state such as Andhra Pradesh, an average-reforming state such as Madhya Pradesh, and a laggard-reforming state such as Uttar Pradesh, all with similar structural characteristics, we can delineate the underlying institutional and interest group causal mechanisms that have affected economic policymaking in the three states.

Party system fragmentation and competition has been shown to affect the content of policy in each of the three states. Competitive, non-fractured party systems such what has existed in Andhra Pradesh tend to produce policy environments more supportive of progressive industrial policymaking. Conversely, states such as Uttar Pradesh with high amounts of executive instability and administrative transfers, have less coherent economic policymaking because poor coordination between the public and private sectors. In addition, states headed by an "out party" or a regional party tend to act more differently than states governed by a party that is power at the center. Out parties tend to move more quickly on economic reforms and regional parties tend to move much more quickly because of the nature of their relationship with the center in a federal system such as India's. Labor union militancy has some effect on policymaking in the three states, with high-incidence-of-strike states like Andhra Pradesh concerned about reputational issues in the eyes of investors, although this factor is much less important than the institutional differences across states. And finally, the caliber of government-private sector relationships is of great importance in affecting economic policymaking by state governments. Higher levels of institutionalized interaction, coupled with stable government staffs, result in policies more popular with the private sector.

CHAPTER 5

THE POLITICAL ECONOMY OF SUBNATIONAL INDUSTRIAL PROMOTION IN MEXICO: 1993-2003

Introduction

Why do a number of state governments in Mexico have fully staffed trade offices in places like Tokyo, Houston, and Brussels? Why do some states send delegations to trade conferences around the world touting the advantages that their state has to offer to potential investors? And conversely, why do several states only have skeletal staffs working on economic development issues even within there own state? Why have other states failed to reform their states' laws to cut the red tape involved in the start-up of a business and thereby increase the likelihood that a new industry might seek to open operations within the state's territory? To uncover the answers to these questions, I will examine the last 15 years of economic development policy by subnational governments across Mexico. This chapter seeks to find the underlying causes for the diversity of state behaviour in recent years by testing theoretically-informed hypotheses utilizing several panel-time series statistical models.

Beginning with political decentralization measures initiated by the Miguel de la Madrid administration in the mid-1980s, and continuing with further political decentralization that took place during the Salinas and Zedillo *sexenios*, state governments in Mexico have become responsible for a greater array of policy areas. At the same time, the country also embarked upon an alternate development path upon its entry into the General Agreement on Tariffs and Trade (GATT) protocol in the mid 1980s. The movement towards greater liberalization of the Mexican economy has continued, in fits and starts, for much of the last 20 years. The resultant effect for subnational governments in the country has been that officeholders and bureaucrats within the halls of state ministries in Chiapas, Chihuahua, and Puebla face many different policy constraints and options than they did a generation ago. As economic liberalization in the country has increased the need for state's to respond to competitive pressures both within the country and from the external world, they have had to take on a greater amount of policymaking responsibilities in the social, development, and education areas of governance. The question becomes, "Why have states in Mexico done what they have done since the country's movement towards political decentralization and economic liberalization?"

The case of Mexico provides an ideal case by which to test existing theory that has been generated from a variety of sections of the comparative and U.S. political economy literatures. Mexico, with its dual movement toward political and economic liberalization during the latter part of the 1980s and on into the1990s led to an increasingly competitive environment for states that were seeking to expand their economies and diversify the industry located in their state. The findings in this chapter suggest that subnational governments in Mexico have behaved in a more complicated fashion than what we would expect based upon the national-level comparative political economy literature, and that existing theory on subnational Mexico has not been tested on the prevalence of different industrial policy regimes within the country.

In this chapter, I will argue that subnational governments in Mexico have responded in a variety of ways to these new constraints and pressures. I posit that while controlling for general economic, geographical, and sociopolitical traits of the Mexican states, that institutional variance and interest group influence will determine what subnattional governmental policymaking. Specifically, the type of political party system, the amount of executive stability, and the content of state-federal party relations, along with business associational and labor union strength can explain industrial policy across subnational Mexico from 1993 to 2003.

Prior Research

The comparative political economy literature has been a vital part of the subfield for the last several generations of scholarship. The focus of much of the work on development in the early part of the time period was centered on the proper role that the state should play in regulating decisions about investment, demand, and supply. More recently, with the shift in favor of orthodox economics, there has been a greater emphasis on how the state can minimize its impact on the market and foster an environment that allows for more transparency and marketization of the economy. The central government should focus on macroeconomic stability, while letting the private sector play a greater role. Much writing since Williamson's (1990) important work on the Washington Consensus has focused on the proper role to be played by the state to allow for economic and social development.

Until recently, most comparative political economy literature examined the role played by national-level governments in the development process. Unfortunately, this bias has neglected the richness of the empirical evidence that exists when one drops down a level of analysis. There has been very little scholarship that examines the remarkable diversity and quantity of economic policymaking that is now taking place at the subnational level. Municipalities, provinces, and states around the world are increasingly involved in the regulation of many aspects of the global economy. While there is a large amount of theoretically-informed work that examines the national context to the development question, there is a shortage of works that looks at the effects of local politics on local economic decision-making. In recent years, several scholars have noted this problem in the literature (Echeverri-Gent 1999; Locke 1995; Montero 2002; Snyder 2001; Weiner 1999; Wibbels 2001, 2002), but there remains a severe shortage of quality work that examines the political economy of subnational economic policy.

The demands placed on subnational governments to be competitive in the global economy have caused an increase in the comparative significance of both international and local actors at the expense of national governments (Watts 1996). What has been termed "glocalization" (Courchene 1995) by some has caused devolutionary pressures on national governments, especially within federal systems, and the emergence of subnational development policies as major location of innovation for industrial development (World Bank 2002, 2005). While national governments have come under intense international market pressure to reduce their economic roles, subnational states have maintained and even expanded their industrial promotion regimes around the world (Montero 1997, 2001a; Rodriguez 1998; 2003), calling attention to a major gap between national and subnational policy trends. Subnational governments currently offer an astounding and ever expanding array of subsidies, low-interest financing, tax credits, abatements, deferments and exemptions, subsidized employee training, and assistance with site selection and preparation (*EIU* 1997, 1998, 1999; Price Waterhouse 1995, 1996, 1999; World Bank 1995, 1998, 2000). Likewise, governments have endeavored to craft "pro-business atmospheres," including lower taxes and minimal regulatory policies on the labor and environmental fronts (World Bank 2002).

Because of the propensity in the development literature to treat industrial promotion and deregulation as alternative rather than as potentially complementary dual strategies, these trends raise important and largely unanswered theoretical questions about the political economy of development. The literature on the developmental state provides insights into the political conditions that give rise to interventionist strategies of development. The more recent body of literature on market-oriented reform, on the other hand, addresses questions regarding strategies that favor deregulation. What has yet to be analyzed are the politics surrounding development strategies that combine deregulatory and promotional policies—precisely the kinds of policies that are undergirding development efforts at the subnational level across the international system. Addressing this issue calls for a theoretical approach that bridges the two rather discrete and separate bodies of literature on the political economy of national development, taking us beyond the assumption that industrial promotion and deregulation are distinct policy choices at the federal-level. The evidence from the subnational level, however, suggests that governments pursue both types of development approaches, often in combination with one another, thus calling into question the adequacy of our understanding of the politics of development.

While the objective of national economic policy is to promote aggregate employment, production, and purchasing power, the aim of state economic development is to create investment in a certain geographic location (Doner and Hershberg 1999). Individual state governments cannot have much effect on larger macroeconomic and market conditions, but they can provide incentives for businesses to invest in a particular location. These incentives are considered crucial for attracting investment and generating a multiplier effect that fosters job creation and the "rippling" of overall welfare gains. In the last decade, as well, there has been a growing segment of the Mexican politics literature which drops down a level of analysis to the subnational level and scrutinizes politics and policymaking across and within the 31 Mexican federal states. The previous scarcity of scholarship is in part due to the, historically, very centralized Mexican political system. Unfortunately, this has meant a shortage of scholarship that examines policymaking and politics at the subnational level within the country. However, recent literature analyzes the changed state of intra-governmental relations within the country (Rodriquez & Ward1999a, 1999b, 1999c) which depicted the underlying governance issues facing Mexico within the context of the post-decentralization policy environment.

Political decentralization and fiscal decentralization have become stronger within Mexico from the late 1980s until the end of the 1990s. Due to this, previously under-analyzed institutions and the politics surrounding them, now play a more dynamic role in policymaking. With the arrival of the time period described variously as "new federalism" (Ward & Rodriguez 1999), and "competitive federalism" (Bruhn 2001), came the need to understand what was happening at the subnational-level in Mexico and to provide theoretically-based explanations for variance across the regions and states within the country. Snyder (2001) in his analysis of subnational dynamics of the post-liberalization environment in the coffee sector provides us with a thorough analysis that looks at intra-state variation in what he terms the politics of "re-regulation." As the federal government withdrew from certain aspects of its longstanding regulatory role, state governments were forced to pick up the regulatory slack, with dramatically different results across different states in southern Mexico. Scholarship by Beer (2003; 2004) finds that the increased electoral competition occurring in many of the Mexican states fostered a new calculus for understanding the role subnational actors beginning in the 1990s. Specifically, the changing role of state legislatures and governors as the political system opened up in response to increased competition, to varying degrees, across the Mexican states. Legislators became more active and started to assume their constitutional roles within the states, while governors carved out wider policy areas with which they could attempt to build electoral coalitions.

On the economic side, recent scholarship demonstrates the vital rule played by the nuances of the federal system for resource allocation in Mexico (Diaz-Cayeros 2004), and the diversity of poverty alleviation schemes that have cropped up in the *neofederalismo* era (Diaz-Cayeros 2003.) Tamayo (2000; 2002) has argued that comparative advantage due to labor market conditions has played a large role in determining industrial locational decisions, while the incentives provided by states have had mixed results in terms of attracting industry. Hiskey (2005) showed that there was a wide divergence of experience across the Mexican states in terms of their recovery from the 1995 economic crisis, with those states further along in terms of open, competitive electoral systems more likely to weather the crisis better and recover faster than those less open. Rothstein (2005) demonstrates that by utilizing a commodity chain approach, we can begin to understand the policymaking objectives of a set of state officials in Guanajuato as they attempt to lure automobile industry to the state by focusing on a sector-wide target and garnering comparative advantage relative to other states by moving down a producer-driven model of industrial policy.

By generating hypotheses that draw from both the comparative literature on national economic development and the U.S. literature on state economic development, this chapter's fundamental theoretical expectation is that the nature and level of subnational development activity reflect local-level institutional relationships and interest group activity. These relationships will allow us to differentiate "programmatically rich" from "programmatically lean" states (Elkins, Bingham, and Bowen, 1996), as well as to explain variation in the types of development activities undertaken by states, which are expected to vary significantly across the subnational level within Mexico. This will take the form of an examination of the factors causing state governments to spend what they spend across the country over the last ten years and an assessment of the factors causing state behavior on the promotional and deregulatory policy fronts.

Hypotheses and Theoretical Considerations

As discussed in Chapter 2, the dissertation's hypotheses are designed to explore the effect of institutional conditions and interest group strength on subnational industrial policy in Mexico by addressing questions about variation in both the level and type of development activity across subnational political units. To examine the relative amount and nature of economic policy across the Mexican states, I will appraise the resources devoted to subnational development efforts on the basis of each states yearly spending on their Office on Economic Development. And second, to survey variations in the types of development activity subnational governments pursue, I will examine the degree to which the each state, through time, articulated promotional and deregulatory policies in their economic development plans.

In the first model, the left side of the equation contains the variable that captures the resources that the Mexican states' devote to industrial development in the post-reform period. I examine data on spending for the economic development offices for 31 states in Mexico between 1993 and 2003. The model is formatted as a time-series cross-sectional (TSCS) data set that includes 9 annual observations for each of the 31 states within the sample. For the analysis, I take the recommendation of Beck and Katz (1996) and use OLS with panel corrected standard errors (PCSE.) I adopt this technique as there is the propensity for TSCS data to have problems with autocorrelation and heteroskedasticity.[58] Because of this tendency, the coefficients would be consistent, but the estimates of the standard errors may be of concern.

In addition, as Beck and Katz (1996) advise, I have lagged the dependent variable and included it on the independent side of the equation.[59] One is thus able to examine the influence of time within the panels of the model in question. I then use OLS to calculate the coefficients and use PCSE for the estimations of coefficients' standard errors. This method results in stricter thresholds of significance, thereby resulting in more confidence-inducing estimates. The regression model is as follows:

Spending on Subnational Industrial Promotion Office =

a_1 + b_1(Lagged Dependent)) + b_2(Level of Development) + b_3(Economic Distress) + b_4(Education Level) + b_5(Urbanization) + b_6(Trade) + b_7(Party System) + b_8(Out Party) +b_9(Non-PRI Gov.) + b_{10}(Executive Stability) + b_{11}(Union) + b_{12}(Industry)

In the second model, the left side of the equation contains the variable that captures the type of strategy that the Mexican states' employ to promote industrial

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[58] Once the lagged dependent variable was included on the right side of the model, there were no remaining problems with autocorrelation. Beck and Katz (1996) suggest that this is appropriate when dealing with situations that have more panels than time periods.

[59] The model was also run as a GLS model, with the errors defined as AR1, which resulted in no significant impact upon outcomes.

development in the post-reform period. I examine data on industrial development strategy for 31 states in Mexico between 1993 and 2003, and conduct the analysis by using an ordered logit model. For such models, recent apprehensions by Beck, Katz, and Tucker (1999) involve temporal dependence, given choices by the *same states* over time. The model is estimated using an ordered logit model with a time duration variable.[60] This is the most suitable procedure as it accounts for the powerful and expected temporal effects. Thus one can protect against capturing significance in the model that is due to duration dependence. In keeping with established practice, I do not report the coefficients and standard errors of the duration variable. This technique provides for the same accounting for time as the inclusion of cubic splines and both are suggested for inclusion in this type of model by Beck *et al* (1999.)

The regression model is given below:

Industrial Development Strategy (0, 1, 2) =

a_1 + b_1(Lagged Dependent)) + b_2(Level of Development) + b_3(Economic Distress) + b_4(Education Level) + b_5(Urbanization) + b_6(Trade) + b_7(Party System) + b_8(Out Party) +b_9(Non-PRI Gov.) + b_{10}(Executive Stability) + b_{11}(Union) + b_{12}(Industry)

Control Variables

Drawing upon the previous research, from the American politics and Comparative politics literature, I incorporate several key control variables into each of the models. The first control variable is **Economic Distress**. Economic distress is operationalized by using the yearly unemployment rate for each of the states. It has been shown in the U.S. literature (Feick 1992; Reese 1991; Sharp 1991) as well as the comparative literature

[60] The variable takes on the value of 0 for the first year of a new strategy, and then 1 is added for each additional year that the indicator remains at the same level.

(Montero 2001a) that states undergoing short-term economic distress relative to other states spend more on industrial promotion programs. Distress is measured by subtracting the yearly unemployment rate for each state from the national average. Previous work also points to level of **Urbanization**, **Level of Development**, and **Education Level** as important factors which influence a state's capacity to invest in industrial promotion. These three concepts are incorporated as controls into the models. Empirical findings in the U.S. literature suggest that more urbanized, wealthier, and more educated states tend to spend more on industrial promotion programs (Ambrosius 1989; Dye 1966, 1984; Elkins *et al* 1996; Plaut and Pluta 1983), while similar findings have been confirmed in other federal states such as Brazil (Montero 2001) and Germany (Begg & Mayes 2000). I calculate **Urbanization** for the 14 states by utilizing the figures released by the Census of Mexico. **Level of Development** is derived from the annual Gross Domestic Product, per capita, for each state. I use the literacy rates for each of the states to measure **Education Level**. In addition to these variables, **Trade** measures the amount that each state exports outside of Mexico. It is expected that those states that are more tied to the global economy will be more likely to exhibit promotional and deregulatory policy behaviors.

Independent Variables

Drawing upon the aforementioned hypotheses, the first of the independent variables is the **Party System** measure. This variable incorporates two distinct features ascribed to party systems. Recent research suggests that party competition will serve to stimulate more aggressive economic development activity. Correspondingly, lower levels of party fragmentation leads to more vigorous economic development activity as governing parties are more likely to be held accountable for economic performance. The assumption implicit in the hypothesis is that a competitive, two-party system will stimulate more aggressive development activity (Geddes 1994). This variable will be operationalized as the absolute value of the effective number of parties minus two [$|(N_s-2)|$] (Laakso & Taagepera 1979; Mainwaring & Scully 1995).[61] **Out Party** measures the dissimilar incentives facing policymakers across discrete levels of government. In short, a party or parties in control of a government in a state are more likely to be more active in promoting industry if they are not in the federal government coalition. This concept will be measured by a dummy variable, with '1' representing those cases in which the subnational government is controlled by a party or a coalition government is controlled by a party not in power at the federal level. **Non-PRI** measures whether a state has had a non PRI governor or a non-PRI dominated state assembly. This will be measured as a dummy variable, with 0 representing continued PRI dominance up to and including that year, while 1 will be given for a year in which a state has *or has had* a non-PRI governor or state assembly plurality. **Executive** measures the tenure of the state's previous governor's tenure. A state governed by an executive whose previous tenant served out the full five years will have a 6 for that state-year. But if the previous governor served less than six years, than the state-year will have the appropriate number assigned based upon that tenure—and be given a 1 to a 5. **Union** captures the militancy and political strength of labor unions across the states. It is measured by tabulating yearly number of industrial strikes per capita. **Industry** encapsulates the relative strength of national-level industrial associations across the states. This concept is measured by calculating the

[61] The value is calculated as $N_s = 1/\Sigma p_i^2$, where N_s represents the effective number of parties measured by the number of seats and p_i is the proportional share of seats of the i-th party (Mainwaring & Scully 1995). When you have a party system with two perfectly balanced parties in terms of electoral competition, the value will be two, while the indicator will result in a score of zero. The indicator measures state political systems as a departure from this two-party, perfect competition model.

number of independent trade associations that exist within the state. Table 5-1 lists all the variables on the right side of the equations and the expected direction of influence on the dependent variables for each model.

Table 5-1: Control and Independent Variable Summary

Variable Name	**Expected Influence on Spending**	**Expected Influence on Movement toward Dual Strategy**
CONTROL		
Economic Distress	Positive	Positive
Urbanization	Positive	Positive
Development	Positive	Positive
Education	Positive	Positive
Trade	Positive	Positive
INDEPENDENT		
Party System	Negative	Negative
Out Party	Positive	Positive
Non-PRI	Positive	Positive
Executive	Positive	Positive
Union	Positive	Negative
Industry	Positive	Positive

Empirical Findings

The first model seeks to explain the degree to which subnational governments in Mexico devote resources to industrial development by way of budgetary allocations for the state's Office on Economic Development[62]. In all cases, results stand up to diagnostic tests for outliers and heteroskedasticity.[63] Table 2 shows the results of the OLS regression for the model:

[62] Alternate specifications of the model were tested to determine the appropriateness of the ordered logit models for the testing of the hypotheses. For each of the strategies, a separate logit regression was run to determine which factors led a state to utilize either a promotional or a dual strategy. In the case of the Union variable, which was not significant on the ordered logit model, it was likely not close to significance on either of the separate normal logit models. Union strike activity seems to play no role in pushing a state up the ladder of reform on the promotional front and the deregulatory front.

[63] Test for outliers included analyses of partial-regression leverage plots and Cook's Distance. With respect to heteroskedasticity, panel corrected standard errors are used.

Table 5-2: Panel, Time-Series Regression on Economic Development Spending

Variable	**Model 1** *Spending*
Constant	2.23 (1.11)
Lag Dependent	3.79*** (.77)
Economic Distress	.55 (.45)
Urbanization	1.11** (.42)
Level of Development	1.90 (.67)***
Education	.44 (.38)
Trade	1.66 (.51)***
Party System	-.18** (.07)
Out Party	.41 (.38)
Non-PRI	.88** (.41)
Executive	.71* (.45)
Union	-.22 (.20)
Industry	.58* (.35)
	$R^2 = .78$ $N = 279$

NOTE: Numbers in parentheses are panel corrected standard errors

****$p < .01$, **$p < .05$, *$p < .10$

The control variables seem to influence the amount of spending to a mixed degree. As we would expect, the lagged dependent variable which captures the previous year's spending is highly significant and a strong predictor of what a state spends in a given year. Conversely, the relative level of unemployment in a state does not seem to impact the dependent variable in any systemic way. This is probably due to the high levels of structural unemployment in Mexico, with many rural, southern states having high unemployment but relatively undeveloped industrial and manufacturing sectors. On the other hand, states which are more urbanized do devote more resources to their offices on economic development at the .05 level. In addition, as predicted, those states with higher per capita gross state production spend more on economic development. Those states that are better off tend to spend monies to increase investment and expand the economy due to greater availability of resources. Education level as measured by illiteracy rates does not seem to matter, but this variable is also correlated with level of development to a degree suitable for inclusion in the model, but high enough that it is likely drained of any of its explanatory power. And finally, for the control variables, the level of foreign trade is a statistically significant predictor of spending on the office of economic development at the .001 level. This likely reflects the high-trade states of the north and the *maquila* belt devoting more resources to industrial promotion.

The results for the institutional and interest group variables are mixed. Party system type is a significant predictor of spending. Those states that approach a perfectly competitive, two-party system are more likely to devote resources to their states' industrial promotion efforts at the .05 level. Conversely, the out party indicator does not have any meaningful influence on the level of spending. This is likely due to the negative overall impact by many PRD governed states in the period leading up to 2000, and the reversal of categories for of many of the states after Vicente Fox won the presidency in 2000. However, the measure of non-PRI states is significant at the .05 level. Therefore, states that have once had a turnover in power in the governorship or largest party in the state's assembly, then go on to devote more resources to their offices on economic development. Interestingly, the measure of executive stability is significant at the .08 level. Those states that have had executives with shorter tenure are apt to spend less on industrial promotion. The results for the interest group variables are underwhelming, although states with higher densities of industrial group membership do spend more of their budget on their offices of economic development. The level of strike activity across the states had no impact on spending, which is likely due to the general trend downward in labor strikes in many states throughout the north and central regions of the country.

The second model attempts to predict industrial strategy for the 31 states during the 1993 to 2003 time period in Mexico. The dependent variable is an ordered categorical variable which takes on the value of "no appreciable" development strategy, a "promotional strategy," and finally to a dual promotional/deregulatory strategy.

Table 5-3: Ordered Logit Panel, Time-Series Regression on Industrial Strategy, with Duration Count Variable

Variable	**Model 2** *Industrial Dev. Strategy*	**Model 2** *Change in Odds (w/ 1 S.D. change)*
Economic Distress	.27 (.22)	11.3%
Urbanization	.55** (.30)	20.7%
Level of Development	.69* (.41)	51.3%
Education	.19 (.17)	7.7%
Trade	.44 (.18)	10.8%
Party System	-22* (.14)	-31.3
Out Party	.18 (.16)	18.7%
Non-PRI	.65*** (.25)	29.5%
Executive	.16* (.09)	11.1%
Union	-.11 (.07)	22.8%
Industry	.14 (.10)	65.3%
Cutpoint (1) *Cutpoint (2)*	*2.24 (1.08)* *4.41 (1.27)*	
	Log Like = -212.37 *N = 279*	

NOTE: Numbers in parentheses are standard errors
****$p < .01$, **$p < .05$, *$p < .10$*

Ordered logit models generate coefficients that test that significance of each of the independent variables separate from each of the other independent variables. Hypothesis is possible because the statistical model reports the standard errors in addition to the coefficients. Unlike the previous OLS time-series model, however, one cannot directly gauge the impact of each variable based upon its coefficient. For this purpose, the ordered logit model results can be used to calculate the odds ratios—or change in odds—for each independent variable. By exponentiating the coefficient estimated for an independent variable generates the factor in which a one-standard deviation increase in the independent variable amplifies, on average and without the effects of the other independent variables, the odds that the ordered dependent variable will take on the next greater value.[64] For an independent variable, with all others that are held to their mean, the final column gives the percent chance that a Mexican state in a particular year will move up the categories from no appreciable industrial policy to a subsidy-oriented policy, and then from a subsidy-oriented policy to a dual promotional-deregulatory set of policies.

For the control variables, we have mixed results across the table of five controlling, independent variables. Economic Distress seems to play no statistically significant role in affecting a state's policy behavior. However, Urbanization is a significant predictor for industrial strategy in the Mexican states. As a state increases its level of urbanization by one standard deviation with all other variables held constant, there is a 20.7% greater chance that it will move up the ladder of policy choice during the time period. Similarly, a state's level of development measured by GDP per capita is

[64] Of the dependent variable moving up a category from 0 to 1, or 1 to 2 as this analysis models industrial strategy for the 31 Mexican states for each year.

significant at the .01 level and will influence policy with an odds ratio of 51.3%. The two final control variables of Education level and Trade openness do not have a statistically significant effect on state policy and moving up to another category toward the dual promotional and deregulatory type of strategy.

Three of the theoretical independent variables are significant, while the remaining four fall short of conventional thresholds of significance. States which have less competitive, multi-party electoral systems are less likely by an odds percentage ratio of 31.3% to move up another category towards a dual strategy. On the other hand, those states that have been controlled by the PRI either in the governor's office or in the state's legislative assembly are 29.5% more likely to move up into the next higher ordered category of economic policy. This variable is highly significant at the .01 level. In addition, those states which have had greater executive stability are more likely, at the .10 level of significance, to move to the next category with an odds ratio percentage of 11.1%. Conversely, the theoretical independent variables measuring out parties and the interest group strength did not significantly alter a state's policy in a given year, although the union strike variable is just under the .10 level of significance and slows down the categorical movement by 22.8%.

Conclusions

While much previous research has focused on the national-level when investigating the causal mechanisms at work for Mexican economic policy, the under analyzed subnational level demonstrates that there is a diversity of industrial programs and policies taking place when one drops down a level of analysis. This chapter has demonstrated, by way of the utilization of a pair of time-series statistical models on state behavior in 31 Mexican states, that institutional and interest group factors partially account for the diversity of economic policymaking at the subnational level in the country.

This chapter makes evident that institutional and interest group factors do influence subnational industrial promotion policies in the 31 Mexican states for the 1993-2003 era. The three most influential factors are all institutional variables. Specifically, states with party systems that approach the two-party, competitive ideal type are more likely to spend a higher percentage of funds on industrial funds than those that are more fractured and less competitive. As well, more competitive, less fractured party systems were more likely to implement a dual promotional/deregulatory industrial policy framework during the decade of competitive industrial policymaking in Mexico. Another important factor on both the level and type of policy is the seemingly special characteristic of state governments that have a history of non-PRI rule in their states. They are more likely to spend more on industrial promotion and also more likely to implement policies fitting with the dual promotional and deregulatory type of strategy. As well, executive stability appears to play a role in the policymaking behavior of the Mexican states. Those states that have experienced governments that tend to last the full term in office are more likely to spend more on their offices of economic development and to move more quickly up the ladder toward a dual promotional and deregulatory industrial plan. And finally, the existence of independent industrial associations tends to push states towards spending more on promoting more investment and development in their respective states. In summary, this chapter demonstrates that institutional factors play a large role in determining state industrial policymaking. The limitations of existing theory for understanding subnational Mexico are revealed and point towards the need for a more complex, and nuanced understanding of the influence of institutions and interest groups on the increasing economic policymaking responsibilities of the Mexican states.

CHAPTER 6

INDUSTRIAL PROMOTION IN AGUASCALIENTES, QUERETARO, AND SAN LUIS POTOSI – IN-DEPTH SMALL-N ANALYSIS

"What we have faced for the last 10 years or so is competition with other states in Mexico for investment and resources. I think we have been moderately successful in recognizing this here in our state, but other states have done better, while many others have done worse. There is a need for marketing, absolutely; but also the very real need for proactive programs that help to entice investors and potential investors to the state. The competition is very pronounced among states, with only the different political parties in control of each state affecting how far we push it." --Ing. Pedro Gonzalez Villalvaso, Development Sub-secretary for Promotion, Aguascalientes, 1998-2004[65]

On a warm spring afternoon in 1986, then Mexican president Miguel de la Madrid signed the official documents which placed Mexico under the auspices of the General Agreement on Tariffs and Trade (GATT). Mexico was now to embark on a path towards a national development strategy that increased its exposure to international markets and at the same time allowed for new opportunities for trade with the United States and the rest of the countries of the world already abiding by the GATT principles. For the previous 50 years plus of rule by the *Partido Revolucionario Institucional* (PRI) in Mexico, the country had pursued a strategy of a statist development model coupled with an economy that was relatively closed to the external world and its markets. While changes had been afoot since the debilitating consequences of the Latin American debt crisis that commenced in 1982, the entry into GATT signaled the start of a new era for Mexico. This new epoch would be further exemplified by Mexico's entry into the North American Free Trade Agreement (NAFTA) with Canada and the United States eight years later in 1994, and continues until today.

[65] Subsecretary, Secretary of Economic Development, Interview with author, Aguascalientes, 13 October 2003.

Along with Mexico's closer engagement of the international marketplace, there was a second concomitant political economic trend that is important for the analysis in this chapter. Beginning with the administration of Carlos Salinas de Gotari and its *decentralizacion* initiatives, on through former president Ernesto Zedillo's *neofederalismo* program, and continuing to the expansion of the role of state governments in public policy under Vicente Fox, the last 20 or so years in Mexico has seen a varied, yet steady increase in political devolution and policy decentralization. This political and policy decentralization in Mexico has been especially important in the economic development arena, as more and more states have had the primary responsibility of regulating existing corporations and approving the foundation and construction of new industry across the states. In sum, the dual trends of political decentralization, coupled with the economic liberalization provide the crucial backdrop for this chapter of the dissertation.

In this chapter I examine the impact of interest group activity and institutions on subnational industrial policy choice in Mexico. Focusing upon three states, I will argue that the diversity of policy activities at the subnational level is the result of institutional and interest group pressures framing policy choice. Because of its strong embrace of market-oriented development, the study of Mexico offers particularly interesting insights into the politics of subnational economic promotion.

Prior Research

The study of the politics of economic development has been an important topic of inquiry in comparative politics for several generations of scholarship. For much of the last several generations, this scholarship primarily consisted of theoretically and empirically-informed works that sought to examine how nation-states could best protect themselves from competition with more developed countries, and constrain those international market forces which were thought to lessen the chances for economic modernization in the developing world. For Mexico the practical consequences of this application of these protectionist ideas resulted in nearly 50% of the GDP of the country being produced in the public sector on the eve of the debt crisis in 1982 as well as a dizzying array of barriers to free trade, including high tariff barriers and thick bureaucratic regulation of the importing and exporting sectors of the economy.

In more recent decades, most scholarship and policy writing has painted a very different picture of the relationship between market forces and economic development. Instead of emphasizing the importance of the state, the dominant view is now that beyond basic economic stability, the government should withdraw from many areas of policymaking activity and let the market play a much larger role in the development process. Scholarship that inspired and stemmed from Williamson's writing on the Washington Consensus (1990) placed heavy emphasis on the relationship between the state and the international marketplace, exploring both the causes of economic openness and its consequences for growth.

Despite the major reorientation of the literature on the political economy of development, a central commonality characterizes research both past and present: namely, a central focus on policymaking at the national level. In Mexico, for example, prior research has centered on the types of policies formulated in the offices of the President of Mexico, while other scholarship has sought to explain the causal arrows that form the key relationships within the market liberalization project that has guided Mexico policy for much of the last generation. Since 1982, Mexico has gone through what can be described as an emblematic example of a "dual transition" in the economic and political spheres. The latter part of the 1980s and the 1990s can, in hindsight, be categorized as a semi-authoritarian regime in decline and undergoing a late and delayed transformation within the global third wave of democratization.

<u>Federal-level</u>

The longstanding political dominance of the office of the president of the Republic of Mexico and its occupant has been the focus of much scholarship that looks at economic policymaking. This top-down system served to guide economic decisionmaking in both the pre-debt crisis statist era, and continued on through the early years of the neoliberal period in Mexico. Camp (2002) and Chand (2001) provide very thorough coverage of this phenomena and how it played out through different PRI administrations over the course of the decades that the party dominated politics within the country. Whether it was the more statist-oriented policy reforms of the Echeverria *sexenio*, or the more market-oriented restructuring of the Salinas era, the pivotal role played by the executive branch within the Mexican state has long been a key focus of scholarship and theory-building on the Mexican case. Levy, Bruhn et al (2001) contextualize this with the aforementioned struggle for democracy that was the second track of the political game within the central government for many decades.

The role of technocratic decisionmakers within the executive branch of the central government in Mexico has also been a fruitful line of inquiry for the study of policymaking in the country in recent decades. Centeno's (1994; 1997) work on the centralization of political-economic power within the federal government's bureaucracies draws on Evans (1995) to make the argument that a network of insulated, Western-educated economists and lawyers came to hold key levers of power during the Salinas *sexenio*.

More recent scholarship by Teichman (2001) has followed up on this earlier work and examined the evolving nature of technocrats in the Salinas and Zedillo, administrations. With a beachhead established in the Finance Ministry and the Central Bank, a "cohesive and homogeneous technocratic policy elite… came to dominate and guide the process… [of economic reform for the Mexican state.] (157) Whether it was establishing relationships with global corporations, or forging new alliances with key actors within the international financial institutions like the World Bank and the International Monetary Fund, the technocrats played key roles in guiding central government policy.

Lately, case-study work has examined these same phenomena during the first non-PRI executive administration in Mexico City. Camp (2004) makes the argument that a similar cadre of technocratic players has dominated aspects of Mexican policymaking during the Fox *sexenio*, although the roots and allegiances of the key players are cut of a different cloth than previous PRI-dominated administrations. In this case, top bureaucratic assignments drew from a pool of U.S.-educated technocrats that spent much of the 1990s in the upper echelons of the Mexican foreign-based industries and working for PAN-led state governments in the northern and central states of the country.

Another key strand of the Mexican case literature has examined the relationship between domestic business organizations and the central government. Thacker's (2000) book that explored the theoretical puzzle that asked how it came to be that the Mexican state made the decision to pursue a greater trade relationship with the United States even though there was much early and strong opposition among the large industrial houses and among big business within Meixco. By tracing the rising and falling fortunes of what he calls the pro-trade and pro-protectionism business coalitions, we are left with a deeper understanding as to why the Mexican government under Salinas made the seemingly quick and difficult decision to forge ahead toward greater ties with the global economy, and how a pro-trade big business coalition coalesced around this policy direction. Thacker's conception of the differing national-level business coalitions informs a key segment of the subnational case analysis presented later in this chapter.

MacLeod's (2004) recent work on the neoliberal reform project in Mexico and the post debt crisis policy focus on privatization is one of the more sophisticated treatments of the declining role of the state in one broad area of the economy. He demonstrates quite convincingly that the central government's withdrawal from the aviation, telecommunications, and railroad sectors did not live up to the promise of fairer distribution and general welfare gains for the country. Williams book (2001) also makes similar claims about the reform project in the Mexican case. The special nature of the nuanced and changing relationship between big business and the state led to successful implementation of much of the privatization and deregulation agenda of the central government, while demonstrating how environmental regulatory reform stalled because of a lack of state capacity.

State-level

The last ten years have seen the publication of several works that attempt a first cut in redressing the longstanding shortage of comparative literature that examines the subnational-level in Mexico. While this previous relative dearth of scholarship is related to the very centralized nature of the Mexican political system, there existed a theoretical shadow stretched further temporally even after the facts began to change on the ground in Mexican politics. Some of the first work that analyzed the changed state of intra-governmental relations within the country came from the broad project headed by Victoria Rodriquez and Peter Ward (1999a; 1999b; 1999c) which sought to portray the underlying governance issues facing Mexico within the context of the post-decentralization policy environment. Ochoa-Reza (2004) suggests that cascading electoral reactions to decentralizing political reforms were instrumental in opening up the political system which culminated in the victory of Vicente Fox in the 2000 presidential election.

With increased political decentralization and fiscal decentralization that generally trended upward within Mexico from the late 1980s until the end of the 1990s, previously under-analyzed institutions now play a much more active role in policymaking. With the arrival of the era described variously as "new federalism" (Ward & Rodriguez 1999b), and "competitive federalism" (Bruhn 2001), came the need to understand what was happening at the subnational-level in Mexico and to provide theoretically-based explanations for variance in political conditions across the regions and states within the country. Snyder (2001) in his analysis of subnational dynamics of the post-liberalization environment in the coffee sector provides us with a thorough analysis that looks at intra-state variation in what he terms the politics of "re-regulation." As the federal government withdrew from certain aspects of its longstanding regulatory role, state governments were forced to pick up the regulatory slack, with dramatically different results across different states in southern Mexico.

Scholarship by Beer (2003; 2004) demonstrates that the increased electoral competition occurring in many of the Mexican states fostered a new calculus for understanding the role subnational actors beginning in the 1990s. Specifically, the changing role of state legislatures and governors as the political system opened up in response to increased competition, affecting policymaking, across the Mexican states. Legislators became more active and started to assume their constitutional roles within the states, while governors carved out wider policy areas with which they could attempt to build electoral coalitions.

On the economic side, recent work has demonstrated the crucial rule played by the federal system within the context of resource allocation in Mexico (Diaz-Cayeros 2004), and the diversity of poverty alleviation schemes that have cropped up in the *neofederalismo* era (Diaz-Cayeros 2003.) Tamayo (2000; 2002) has argued that comparative advantage due to labor market conditions has played a large role in determining industrial locational decisions, while the incentives provided by states have had mixed results in terms of attracting industry. Hiskey (2005) showed that there was a wide divergence of experience across the Mexican states in terms of their recovery from the 1995 economic crisis, with those states further along in terms of open, competitive electoral systems more likely to weather the crisis better, and recover faster, than those less open. Rothstein (2005) demonstrates that by utilizing a commodity chain approach, we can begin to understand the policymaking objectives of a set of state officials in Guanajuato as they attempted to lure automobile industry to the state by focusing on a sector-wide target and garnering comparative advantage relative to other states by moving down to a producer-driven model of industrial policy.

Methodology and Case Selection

This chapter examines the role played by institutions and interest group behavior on subnational industrial policy in Mexico. Drawing from the methodological arguments framed in King *et al* (1994), this chapter incorporates the study of three cases that are selected for their variability in economic policymaking, but with similar structural characteristics. The states of Aguascalientes, Queretaro, and San Luis Potosi were chosen for the case study portion of the dissertation because of their similar economic and social structural conditions. In addition, all three subnational cases are landlocked states that are positioned outside of the northern border zone with the United States, and away from the poorer and more rural belt that exists to the west and south of Mexico City. While the three cases are not identical in terms of social structure and economic development, there is a reasonable degree of control variable similarity across the three states. Figure 6-1 shows the locations of the three cases.

<u>Figure 6-1</u>: Map of Mexico with Cases Highlighted

As well, there is a good deal of variance on those institutional and interest group factors that can be expected to influence different types of politics and policy orientations.

The data presented in this chapter is from archival research, survey data, and over 50 interviews—interviews conducted in the three states as well as with persons in the federal capital of Mexico City. On the dependent side, the following pages will detail the policy promotional and deregulatory differences across the three states for the period of 1990 to 2003. The final substantive section will seek explanations for the diversity of policies in the three Mexican states by examining empirical data.

Evidence from the Three Case Studies—the Dependent Side

In order to test the hypotheses generated from the general comparative, Mexican, and U.S. political economy literatures, we need to examine what transpired in the three cases over the course of the last 15 years. The data points to a large amount of variance across the states of Aguascalientes, Queretaro, and San Luis Potosi in terms of industrial promotion activity and industry-oriented deregulation over the course of the time period under examination. In particular, this section will make the case that the three states can be differentiated in terms of activity on both the promotional and deregulatory policy fronts. Specifically, this section will examine the variance across the cases by looking at the level of subsidies, the sectors targeted, the degree of state self-promotion to the domestic and foreign-based private sector, the deregulation of the *tramite* clearance procedures, and the degree of importance placed on large-scale privately owned industrial parks in the respective state's development agenda.

With aggregation of seven distinct areas of promotional and deregularoy policy behavior during the 1990s by the states, we can rank them according to their reformist orientation. For the purposes of this chapter, Aguascalientes is the most reforming state, San Luis Potosi the least, while Queretaro is the middle state in the measurement of the dependent variables. Table 6-1 summarizes the seven areas of promotional and deregulatory policy activity in the three states:

Table 6-1: State Activity on Dependent Variables

	Aguascalientes	**Queretaro**	**San Luis Potosi**
Promotional			
Subsidy Adoption	Early	Average	Average
Level of Subsidies	Medium	High	Low
Target Sectors	Yes	Yes	No
Marketing Level	High	Medium	Low
Deregulatory			
Permit Clearance	Very Early	Early	Late
Transparency	High; Improving	Medium; Stable	Low; Declining
Priv. Infra. Priority	High	High	Low

Promotional Activities

The three states have had varying levels of industrial subsidies and the prioritizing of industrial sectors during the recent decade and a half of economic policymaking. Aguascalientes, an early adopter of an industrial subsidy strategy, began offering a wide array of tax abatements and site location write-offs to companies in 1992. At the time, the then PRI-dominated state was the first non-PAN and non-northern state to offer a comprehensive investment package for new investors to the state. Based on an earlier successful one-time promotional package that lured Nissan to locate one of its main automobile and light truck manufacturing plants in the state, the state's Commission for Economic Development and Foreign Trade developed a comprehensive policy for attracting industry over the course of late 1991 and early 1992.

As a key player in the development of the policy white paper stated: "We had been relying heavily on our connections with the central government until this point. We had strong connections with some of the technocrats that were developing policy for Salinas and we received favorable treatment from them early in his *sexenio*. But we thought that things might change in 1994 and we wanted to be proactive..."[66] An analysis of the Industrial Promotion policies for Aguascalientes from 1987, 1993, and 1999 (Informe) reveal a state that actively pursued industry by targeting industry in specific sectors. Sectors targeted during the early part of the 1990s were those tied to the automobile industry and the electronics and software industries. An attempt was made to utilize a commodity chain approach (Gereffi 1994) by trying to lure part suppliers for Nissan and Texas Instruments in their respective sectors.

The state of Queretaro implemented a comprehensive policy of offering industrial subsidies across sectors in mid-1994. This places them roughly in the middle, temporally, of central and northern Mexican states in terms of the speed by which they began offering sales tax abatements and relocation monies. When the first PAN government came into power in the state in 1997, the state quickly increased by 40% the money to be devoted to attracting industry via subsidies. The first plan put out by the newly reorganized Secretary for Sustainable Development included promotional measures that would increase the amount of tax subsides based upon how large the proposed investment was going to be, and how quickly it would be made (Plan de Desarollo de Queretaro 1997).

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[66] Assistant to State Commissioner for Economic Development, Interview with author, Aguascalientes 7 October 2003.

As compared with the other two case studies, Queretaro had a high overall level of subsidies that increased after the 1997 victory of the PAN in the state. In addition, beginning in 1998 the state offered special fiscal arrangements to "target areas" but this program soon lapsed as business from non-targeted sectors were quite displeased at the perceived favoritism shown to a narrow range of industry. As a member of the governing board of a U.S.-based multinational stated: "Originally we were looking at four states for possible investment opportunities—Guanajuato, Queretaro, San Luis Potosi, and Jalisco. We ended up settling on Queretaro but only after they [the state government] agreed to give us the subsidy help that they were offering to hi-tech and computer firms."[67] Soon thereafter, shortly before the state's midterm elections in 2000, the state officially ended its targeted subsidy program but still allowed for additional help from site location officials that would favor potential high growth sectors.

San Luis Potosi, on the other hand, has been somewhat of a laggard state when it comes to targeted subsidies and providing tax abatements for new investors in the state. Only in 1999 did the state proffer its first official, detailed policy paper on what sectors would receive particular help from the state government. Additionally, while the state had a standard package of incentives that it offered to companies beginning in the mid-1990s, many in the private sector within the state and in neighboring states said that the office on economic development was in such disarray from 1991 to 1994 that it was difficult to get San Luis Potosi government officials to follow through on verbal commitments to help with the new investment. As the company relations official for a major radial tire manufacturer in Queretaro said: "We had wanted to build our factory in

[67] Chief Financial Officer, U.S.-based machinery company, Interview with author, Queretaro, 12 September 2003.

San Luis Potosi, but we never were able to get clarity about how they were going to help us... We ended up building in Queretaro after a year of delays."[68] In addition, newspapers from the state have run stories detailing the graft that took place within the Office on Economic Development during the government of Teofilo Torres Corzo in the mid-1990s.

The three cases were divergent in terms of the relative level of state marketing undertaken by the state during the time period. Based upon state budgetary data and records of the states' participation in foreign and domestic trade shows, and number of trade promotion offices overseas, the difference in the level of promotional activity across Aguascalientes, Queretaro, and San Luis Potosi is readily apparent. During the course of the 1990s, under PRI and PAN governments, the government of Aguascalientes consistently spent more money on the marketing of the state to potential investors.[69] In addition, there was a high level of "effective" spending by the state as well—in other words, that the money actually went towards promoting the state and not to graft and profligacy. Queretaro spent about the average amount, as compared to the other 30 state governments in Mexico, for the marketing of the state during the decade. Although there was a surge in state spending during 1996 as the incumbent PRI government increased total budgetary expenditures in the lead-up to the state's elections in 1997, Queretaro only climbed to the 10th position among subnational governments in Mexico in terms of monies devoted to promoting the state to potential investors. And, similar to our measures of other promotional policies on the part of the states, San Luis Potosi spent the

[68] Director, large tire manufacturer, Queretaro, 4 September 2003.
[69] From 1992 to 2002, Aguascalientes was the top spending state per capita on "external marketing" and third only to the must larger states of Jalisco and Mexico in terms of gross spending.

least amount on the marketing of the state. It was not until 2001 that the state began to devote significantly more resources to promoting the state.

During the era under discussion, the states also varied in the degree to which they participated in trade fairs and maintained trade promotion offices in Mexico City and in foreign countries. Although all three states staffed trade promotion offices in the capital, there is some variance in the level of financial and manpower commitment given to their respective offices. In 1993, Aguasalientes, Queretaro, and San Luis Potosi had four, four, and three representatives, respectfully, acting on behalf of each of the states in the Federal District. By the end of the 1990s the numbers were six, five and, and three for the states. In addition, the offices of Aguascalientes and Queretaro were given much more leeway for offering incentive packages and site locational help on behalf of their state governments. San Luis Potosi, on the other hand, while having fewer staff members and occupying offices in a much less prestigious area of the capital, also were not tasked with the ability to independently offer help depending on the needs of the potential investor.[70]

Deregulatory Policy Activity

Each of the three states has prioritized the deregulation of the industrial clearance procedure to differing degrees. Due to the decentralization reforms at the center, the federal government has declined in importance in terms of granting *tramites*—or permits—to new industry before construction and occupation of an industrial facility. While Mexico City maintains control over a small array of labor, environmental and "social" permits to open a new business, the bulk of the approvals needed to construct

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[70] Sub secretary for Industrial Development, Federal Government, Interview with author, Mexico City, 27 July 2002.

and occupy a new manufacturing or industrial facility must be granted by subnational governments. The states are responsible for granting, on average, 55 permits, while the municipal government with jurisdiction grants a handful as well. There is much variance across the Mexican states in the permit process that exists in each state. Likewise, Aguascalientes, Queretaro, and San Luis Potosi vary in their regulatory framework that governs the granting of *tramites* in each state.

Aguascalientes was one of the first governments out of the 31 Mexican states to implement a single-window (*ventanilla unica*) clearance mechanism for approving industrial permits. By the end of 1995 the state had a comprehensive document issued through the government record and by the Office on Economic Development for the state.[71] At the time, the state was the only non-PAN governed state that passed legislation implementing a single-window clearance process for new business entering the state. Queretaro did not formalize its single-window clearance process until 1998, while San Luis Potosi passed legislation in 2000 that dictated the parameters of the single-window clearance procedures in the state.[72] This was cited by numerous private sector business leaders of being broadly reflective of what they saw as the differences among the three cases in terms of their permit clearance systems.

Another way in which Aguascalientes was superior to the other two cases in movement towards streamlining the process for starting a new business was the existence, starting in 1996, of a state-municipal coordinating board. The board met once a month to coordinate between municipal and state single-window government officials

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[71] *Desregulacion de Tramites para Instalar una Empresa en el Estado de Aguascalientes*, Compendio de Publicaciones en el Periodico Oficial en Materia de Desregulacion, 1997.
[72] Information obtained from *San Luis Potosi, Avanza Unido* planning document, 2000 and *Queretaro Economic Yearbook* 2001

on the status of the permit process for each industry that had applications to invest and construct on file. However, there was some degree of variance between Aguascalientes, Queretaro, and San Luis Potosi as to how the single-window process worked. As one factory head in Queretaro commented: "There was a single-window clearance law when we invested in 1999 but it did not work out perfectly. It still took a long time and we still had to talk to over 17 offices to move things along in a timely manner." This sentiment can be seen in a more formalized way in the following paragraphs which looks at results from recent surveys on business perceptions of the quality of regulation across the Mexican states.

There are two organizations within Mexico that have carried out in-depth, country-wide, and yearly surveys on the attitudes of the Mexican private sector towards the relative degree of administrative transparency in each of the 31 states and the federal district. Their rankings of the three subnational cases conform to our positioning of these states. Table 5-2 lists the ranking of each of the states:

<u>Table 6-2</u>: Case Studies and Transparency of State-Private Sector Interactions

	Aguascalientes	**Queretaro**	**San Luis Potosi**
Transparencia Mexicana	**4**	**18**	**27**
Centro de Estudios Económicos del Sector Privado I	**1**	**27**	**30**
Centro de Estudios Económicos del Sector Privado II	**7**	**13**	**19**

Sources: *Transparencia Mexicana* (2004) and *Centro de Estudios Económicos del Sector Privado(2003)*

For the purposes of all three studies, the lower the number, the higher the rank of the state in the measurement of transparency and good governance, and each of the rankings extend out to 32 . Specifically, the *Transparencia Mexicana* study measures corruption by state-wise surveys of businesses in the country that asks how often they have had to pay bribes associated with their interactions with state officials. In this study we find that Aguascalientes is the fourth best state in the republic, while Queretaro and San Luis Potosi are ranked 18th and 27th in that order.

The first *Centro de Estudios Economicos* study ranks the states, based upon private sector surveys, on the firms overall opinion as to the quality of their regulatory reform programs. Aguascalientes again does better than the other two cases and secures the overall number one position in the country. Queretaro and San Luis Potosi are near the bottom of the rankings, coming in at positions 27 and 30 respectively. Likewise, the second *Centro de Estudios Economicos* survey, which examines private sector rankings of how long it takes to secure all the needed permits to open a new business has results with the three states in the same rank order. Aguascalientes is perceived as the seventh fastest state, while Queretaro and San Luis Potosi are 13th and 19th.

And finally, the three subnational cases also differed on the degree to which they encouraged private infrastructure via the promotion of industrial parks within their states. While all three cases encouraged the development of private sector industrial locations by the end of the 1990s, Aguascalientes and Queretaro passed legislation earlier in the decade that further deregulated the ability of private developers to set up large scale industrial zones that could generate electricity privately and be free of many of the permits required in other areas of the states. These were modeled directly on the Singapore and Chinese-style Export Processing Zones (EPZs) that had played such a crucial role in the rapid economic development within those two countries in the previous decades. Aguascalientes first liberalized the *tramite* process for the industrial parks in 1993, and Queretaro—along with other states in the heartland of the country—by the end of 1995. San Luis Potosi, also significantly reformed its policies on privatized industrial parks in early 1996. Although by early 2003, San Luis Potosi and Queretaro had many more private industrial parks than Aguascalientes, this can be, in part, attributed to Aguascalientes smaller geographic size and its government's pledge in late 1999 to turn the whole state into a "special economic zone."

In sum, it has been shown that the three cases diverged in terms of promotional and deregulatory industrial policies during the 1990-2003 period. Aguascalientes was the state that, on average, had higher levels of promotional and deregulatory policy activity during the reform period. While there is some variance depending on the specific sub-category, Queretaro and San Luis Potosi usually occupied the second and third positions respectively on our measures of the dependent variables. The rest of the chapter will assess the explanations for the divergence in policy behavior by examining the role played by institutions and interest groups in the forming and framing of promotional and deregulatory industrial policy in the three subnational cases.

Evidence from the Three Case Studies—the Independent Side

This section explores the effect of institutions and interest groups on industrial policy in Aguascalientes, Queretaro, and San Luis Potosi from 1991 to 2003. The following table summarizes the independent variables as drawn from the hypotheses discussed in the previous section:

Table 6-3: Causal Variables from 1991 to 2003

	Aguascalientes	**Queretaro**	**San Luis Potosi**
Institutional:			
Party Frag.	Low	Low	Medium
Number Parties	2.23	2.41	2.48
Gov/Leg Different	3 years	3 years	0 years
Party Compet	High post 1995	High post 1999	Low
1st non-PRI Gov.	1997	1998	2003
1st non-PRI assemb.	1994	1998	2003
Out Party	1998-2000	1999-2000	2000-2003
Number of Exec.	3	3	7
Bureaucratic Turn.	Medium	Medium	Low
Interest Group:			
Indust. Assoc. Dens.	High	Medium	Low
Labor Strike	Low	Low	Medium

This section will begin with a discussion of electoral competition within the three case studies, followed by an analysis of executive and bureaucratic stability within the states. Subsequently, the effect of organized business and labor militancy on policy outputs will be scrutinized.

Electoral competition and party systems

An expanding section of the political science literature has examined how different types of party systems affect policy output. Subnational Mexico provides a diverse set of cases to examine the proposition that changes in party system fragmentation, the effective number of parties, the level of party competition, and state-federal government party differences constrain and foster certain types of economic policy. The cases of Aguascalientes, Queretaro, and San Luis Potosi are largely similarly situated in the socioeconomic context of federal Mexico, while there is much variance in terms of their economic policymaking and the causal variables outlined above. For the time period we are examining, there was a minimum of three different governors, and five different legislative assemblies in each state.[73]

Over the course of the 1990s, many states' party systems settled into an approximation of a two-party structure. In states that have this type of system within Mexico, there are two possible party dyads: either a state has a PRI/PAN party system or a PRD/PRI party system. Much of the northern part of the country, as well as the *bajio* heartland north of Mexico City contains states that have party systems now dominated by the PAN and the PRI. In other states immediately surrounding Mexico City and to the west and south are states with what have increasingly become party systems dominated by the PRD and the PRI.[74] All three of the cases discussed in this chapter have party systems that evolved, over the course of the 1990s, into PAN/PRI party structures. On average, across the three states, these two parties were garnering over 85% of the vote in state-wide and federal balloting. In addition, the large metropolitan areas with the states

[73] Elections within each of the three states were as follows: Aguasalientes, gubernatorial elections in 1989, 1995, and 2001, and assembly elections in 1989, 1992, 1995, 1998, and 2001; Queretaro, gubernatorial elections in 1991, 1997, and 2003, and assembly elections in 1988, 1991, 1994, 1997, 2000, and 2003; and San Luis Potosi, gubernatorial elections in 1991, 1997, and 2003, and assembly elections in 1988, 1991, 1994, 1997, 2000, and 2003.
[74] With notable exceptions like Zacatecas in the north-central that has a PRD/PRI two-party system.

(the state capitals and environs) had municipal assemblies dominated by the PRI and/or the PAN.

Aguascalientes, the state that moved more quickly on the promotional and deregulatory industrial policy fronts than the other two states has a low amount of fragmentation and the state with the effective number of parties closest to two. Up until 1995 the PRI dominated the legislative assembly, while the party held the governorship of the state until 1998. Of the three states under discussion, Aguascalientes was the first to become controlled by the PAN. And, most crucially for this analysis, the state had a PAN-controlled legislative assembly, with a PRI governor from 1995 to 1998. These three years overlap with some of the key years of policy innovation within the state. The governor from 1992 to 1998 was from the PRI. Otto Granados Roldan, a former press secretary and policy aid to former Mexican Presdient Carols Salinas de Gotari, received rave review from the western press for his proactive economic stewardship of the state. Fawning coverage in the *Wall Street Journal* attests to the merits of the industrial policies that the Granados administration implemented.[75] While the state's early success at attracting industry and streamlining the regulatory process can be attributed to the state's special relationship with the center, it was the key mid-decade time period of 1995 to 1998 that resulted in many changes in the state's industrial policy on both the promotional and deregulatory fronts.

With its narrow victory in the Aguascalientes mid-term elections in 1995, the PAN took control of the state's legislative assembly. With the PRI governor Granados remaining in office for three more years, the state now faced what few states in the

[75] "One Mexican City Proves it Can Attract Investment, Serve as a National Model," Jonathan Friedland, 09 July 1998, *Wall Street Journal.*

country had experienced—divided government. While there was policy deadlock in many areas of the state's public policy—including much needed education reform and water regulation—the three years of divided government fostered much industrial policy change in the state. As one former aid to Governor Granados explained: "The administration was of two minds. One, we wanted to continue the policy development that we had started in the first three years. And second we knew that to hold off a PAN surge in 1997 we would need to have things for our party candidates to campaign on." A key element pushing the reform project forward in Aguascalientes was that the state settled into a two-party, competitive system before the other two cases. As well, the three years of overlapping party control help to push forward to the industrial policy reform agenda with the state.

Querétaro was the second state among the three cases to see the PRI fall from its dominant status in the state's electoral arena. The state elections in the summer of 1997 found the PAN candidate for governor, Ignacio Loyola, sweeping into office while besting the PRI candidate by over 5%. Likewise, the PAN took over control of the state assembly with nearly 50% of the vote and with a 7% advantage over the PRI. The next two election cycles would find the state maintaining itself as a highly competitive environment as the PAN and the PRI would poll within 5% of each other for both governor and assembly elections. The movement of Queretaro from being a state dominated by the PRI to a competitive, two-party system also helped to provide an environment conducive to industrial policy innovation.

The new PAN government in Queretaro immediately set about working on the single-window clearance reform after taking office in 1998, modeled on similar proposals in other PAN controlled states in the country. The effect of the structure of party system was such that by the assembly midterms of 2000, the PRI was campaigning on improving the deregulatory measures undertaken during the first three years of the Loyola *sexenio.* As one investor with ties to the auto parts supply sector posited: "We had a situation where the PRI took a while to rebound after their surprise loss in 1997... but when they did, they began to call for increased transparency and argued the state should be doing more to promote itself overseas like neighboring states like Guanajuato had been doing."[76]

Conversely, the first competitive election between the PRI and the PAN did not occur in San Luis Potosi until the summer of 2000. Although the PRI maintained its hold on the legislative assembly, only a handful of seats separated the parties. It was not until 2003 that the PAN, in very close elections, captured the statehouse and the executive. This made the state one of the last holdouts in the *bajio* and north to have a PRI-dominated assembly and a PRI governor. Many people in the private sector suggested that this was one reason for the glacial pace of the deregulatory reform project in the state and helps to explain why the state did not start marketing itself to investors on par with other states until the very end of 1999. As an investor from that time stated: "Perhaps I am biased, but what you had was a government that was more interested in colluding with business that was politically well connected as opposed to spending funds to attract new business." It was very short-sighted but this end up changing... just later than other states." The lack of progress on the development of the single-window framework can, in part, be traced to the lack of a competitive electoral system in the state.

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[76] Managing Director, Automobile electronics firm, Interview with Author, Queretaro 15th September 2003.

The impact of the out party measure on the policy orientation of the three states is difficult to completely differentiate from the broader breakdown of PRI dominance in each state and its replacement by PAN governments with narrow pluralities of support. From 1998 to 2000, Aguascalientes was in control of the PAN, while the federal government was still in the hands of the PRI. State officials who worked in the government said that the lack of support from the center was noticeable, but quite commonly experienced by other PAN-run states in the region. As the PANista former Coordinator for Investment in the Gonzalez administration (1998-2004) claimed: We already knew what we were going to face based upon what happened to PAN governments in Guanajuato and Baja. I would not call it outright interference, but instead a total lack of support from the PRI federal machine. We had to take care of things by ourselves, without help from the DF."[77]

A similar type of situation was faced by the new PAN Queretaro governor and administration in Queretaro from 1999 to 2000, with the central government and Ministry of Economic Development controlled by the PRI and its appointees. In fact, just as the administration in Aguascalientes state knew what they were facing because of interactions with officials from Guanajuato state, the incoming administration in Queretaro had received guidance from the administration that had been governing Aguascalientes for the last year. The PAN state governments were not autonomous laboratories of governance, but instead increasingly connected to each other at the subnational level, even as the PRI maintained control of the central government in Mexico City.

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[77] Coordinator for Investment (Foreign), Secretariat for the Economic Development of Aguascalientes, Interview by author, Aguascalientes, 16 October, 2003.

The reverse of this imbalanced federal scenario took place in San Luis Potosi. Although the PRI continued to hold power in the state until 2003, with Vicente Fox's victory in the 2000 Mexican presidential election, many of the central ministries were staffed by appointees of Fox's PAN loyalists and party members. The tables had now turned. PAN state governments that had testy relationships with the center now were informed of and consulted on many aspects of economic policy that impacted Mexico's federal political structure. But for San Luis Potosi, its increasingly testy relations with the appointees of Fox and the executive branch in the Federal District, the ability to rely on support from the center was gone. Fernando Silva Nieto was the final PRI governor of the state to date, and faced a less friendly atmosphere after Fox took office in January of 2001. As one former minister in the Silva administration characterized it: "It was almost like we had the table kicked out from under us. It was a complete reversal of fortune. Other states surrounding us had been complaining at regional development conferences about perceived discrimination by the center, but now everything was good for them and bad for us."[78]

Executive and Bureaucratic Stability

For each of the three cases, the number of executives and the amount of administrative churn that each state experienced seemed to impact the policymaking coherency within the states. Aguascalientes and Queretaro experienced a large amount of bureaucratic turnover in the each state's administrative service after the PAN took over in the states in 1998 and 1999 respectively. Contrary to our hypothesized expectations that this would prove problematic for policy coherency and consistency, the new industrial

[78] Secretary, Council on the Development of SLP, interview by author, San Luis Potosi, 11 December 2003.

promotion officials that were charged with policy reform and administration began pushing the states towards more external promotional efforts almost immediately.

Of the 12 key officials in the Office on Economic Development in the state of Aguascalientes during the first three years of the PAN's control of the state's executive branch, eight of the officials were new to government, and six of these came from the private sector. Similaryly, when the PAN came to power in Queretaro in 1999, a majority of the 10 non support staffers came directly from the private sector. For both these subnational case, bureaucratic turnover after a new party came to power resulted in increased levels of industrial promotion and deregulatory activity. Conversely, there was a minimal amount of bureaucratic turnover in San Luis Potosi from 1991 to 2004. This was cited repeatedly in interviews with private sector business leaders as being a crucial reason why the state government in San Luis Potosi was slow moving on the industrial promotional front until the early 2000s. As one early 1990s investor described it: "Even though each governor would rename the office when coming to power, the people stayed the same and the policies stayed the same. Different colors on the brochures, and new names, that was it."[79]

Likewise, while Aguascalientes and Queretaro had three governors each during the 1991-2003 time period, San Luis Potosi had seven different governors. Owing to corruption scandals, PRI infighting, and actions by the central government in Mexico City, the average tenure of a governor in San Luis Potosi during the 1990s was less than one-half what it was in the other two cases. Even though the governors were all PRI party members, they often times would replace and be replaced by a governor from a

[79] U.S. Multinational company, External Relations Head, Interview with Author, San Luis Potosi, 4 December 2003.

different wing of the state or federal party. After this would happen, there would be a large amount of ministerial turnover and a general lack of clarity from the political leaders of the government as to what tact the offices on economic development should pursue. As one business official in the state lamented: "From 1990 to 1993 we had five different governors in the state. One of them for only 13 days! There was very little policy consistency in all areas of the government and also on the industrial promotion side."[80] This, in part, explains the slow movement in the early to mid 1990s by the *Potosino* state government in taking seriously the challenge of competing with their neighboring states to the south and north.

Interest Group Influence

The degree of formal business sector organization within the three cases of Aguascalientes, Queretaro, and San Luis Potosi also seemed to influence the character of state industrial policymaking during the 1990s. Beginning in the 1980s and continuing throughout the time period under review, the density of business association membership in the state was quite high. Owing to active participation on the part of firms tied to the automobile and to a lesser extent the textile industries, the state had a very high level of private-public interaction as compared to the other cases. Some of this can be attributed to the unique situation of the state as having only one major industrial area surrounding the state capital. Nevertheless, business enjoyed a close relationship with the PAN governments of the latter years, but more uniquely, also with the earlier years of PRI rule in the state. Some business leaders point to the relationships forged in the early 1980s when Nissan and other auto parts manufacturers located or relocated to Aguascalientes because of the perception that it was a state in which business had the ear of the

[80] Industrial Fabrication Plant Manager, Interview with Author, San Luis Potosi, 1 December 2003.

government. In terms of active membership in trade and industrial peak association groups, Queretaro and San Luis Potosi have lower levels of formal business association activity. While both states score about average when indexed against all 31 federal states, they have patterns of interaction that are noticeably less than other states.

The influence of labor strife and union activity on subnational industrial policy in the three states varied to a larger degree in the early part of the decade. Specifically, large investors in Aguascalientes in the 1980s like Nissan and Texas Instruments were able to bypass the need to interact with the PRI-dominated unions and effectively run their businesses as open shops. Almost unheard of at the time in the country, state policymakers had effectively given a green light to these two large investors by way of a pledge to control labor activity within the state. While unions in Puebla and Guadalajara were gaining influence during this time in the auto parts and automobile industry, in Aguascalientes labor was effectively made to bargain only without the threat of a slowdown or striking. Labor unions in Queretaro were rarely striking in the state by the mid 1990s and a tacit agreement was struck between the government and the PRI union chief to quell any disturbance in return for a pledge to revisit contracts once every two years in all of the larger plants. San Luis Potosi, with its history of labor strife, has levels of strike activity that is higher than the other two states.

Overall, the expectations drawn from the hypothesis on interest group impact on subnational industrial policy meets with mixed evidence from the cases. The higher rates of formal business interest group participation in Aguascalientes seems to have helped push that state more rapidly toward non-particularistic deregulatory policies, while its relative labor peace did not seem to detract from its rapid movement toward industrial promotional policies. Queretaro, with its roughly average density of formal business association strength and low levels of labor strife, was comparatively active on the promotional front by mid-decade, and began the reforms of its industrial-permit granting process later than Aguascalientes. And finally, the comparatively low levels of formal business sector organization in San Luis Potosi most certainly slowed down the progress on the deregulatory front in the state. The state's relatively high levels of labor strikes did not seem to provoke the state into pushing for more promotional efforts, but did seem to temper the move toward additional deregulatory measures by the government.

Conclusions

This chapter presented data on industrial promotion policies in three states in Mexico for the 1991 to 2003 time period. Specifically, this chapter evaluates the impact of institutional conditions and interest group dynamics on industrial policy outputs in Aguascalientes, Queretaro, and San Luis Potosi. By testing hypotheses generated from the comparative, Mexican, and U.S. literatures, the chapter has argued that the three subnational cases behaved differently in the policymaking realm during the 1990s, and that some of this variability is the result of different institutional and interest group conditions within the states over the course of the time period examined. With the dual movement toward political decentralization and economic reform during the reformist period in Mexico, the 31 states were forced to engage in increasing levels of competition with each other for investment. Oftentimes, this competition for Mexican and international (mainly U.S. and Japanese) investment took place in terms of industrial promotion programs and movements toward the deregulation of the economic sphere within each state.

Aguascalientes, by the measures utilized here, was the state that was the most proactive on both the promotional and deregulatory fronts. It has been demonstrated that some of the hypothesized influences on the state's industrial policy carry empirical weight for explaining why state officials did what they did over the course of the 1990s. Among the three subnational cases, the state was the most active on the promotional and deregulatory fronts. The relatively early transformation of the political party structure in the state to a competitive one impacted the dependent variables in the expected direction, while the high degree of bureaucratic turnover in the state had the opposite effect of what was hypothesized. Queretaro, on the other hand, was the state that was in the middle on our measures of promotional and deregulatory policy activity. While its electoral environment became quite competitive soon after the same increase occurred in Aguascalientes, the state was slower in responding to the competitive nature of the inter-jurisdictional fight for new investment among the Mexican states. As well, Queretaro's roughly average degree of formalization of the business sector was found to have played some role in the state's adoption of a single-window clearance framework and in pushing the state towards opening additional trade missions and promoting the state for investment.

For the case of San Luis Potosi, the slower transformation of the political party system in the state led to a negative impact on both the promotional and deregulatory fronts. The large amount of instability in the office of the governor and low degree of bureaucratic turnover played a part in the state's slow movment toward the dual strategy of promotion and deregulation. And finally, while the low level of organized business influence on state policy fits with our expectations, the relatively large amount of labor strife did not push the state towards more promotional types of activities.

CHAPTER 7

CONCLUSION

This dissertation argues that local-level institutions and interest group strength determine the content of subnational industrial policy. For both the cases of India and Mexico, subnational governments can be seen to be increasingly responsible for the content and context of economic policy. With the dual transition in both countries—toward greater political decentralization and economic liberalization, states have become "laboratories of policymaking" across many different areas of the policy spectrum. In both countries, former one-party states have opened up as the electoral arena has become much more competitive. As well, subnational governments within India and Mexico are increasingly responsible for policymaking that was once the preserve of the federal government in each country. Although current comparative political economy theory does a respectable job of explaining the general trends in national-level policymaking that the developing world has seen in the last two generations, but it has severe limitations when it comes to explaining subnational government policymaking.

This dissertation has contributed to five broad areas of comparative politics scholarship, and also informed debates within the policy literature. This chapter argues that the findings contained in this dissertation help to bring new light to the deregulatory state and development state literature. As well, a case has been made that there is a false divide between some of the comparative U.S. state and general comparative literatures. In addition, these findings suggest that a more nuanced view of the institutional design literature must include information from the subnational level. And finally, owing to the dissertations novel research design, we have an important contribution to the progress towards new ways to carry out comparative political economy research in the increasingly globalized world.

Key Findings

As a review, a brief summary of the main findings from the four empirical chapters is in order. Generally, the dissertation posits that there are two broad categories of independent variables which partially determine the industrial policymaking differences that exist within subnational India and subnational Mexico. Specifically, in the quantitative chapters, the dissertation has tested hypotheses generated from the broader comparative and U.S. literatures, as well as from scholarship from the India and Mexico case literatures. The assortment of hypotheses tested in chapters three and five are categorized as either institutional or an interest group-based explanations for subnational policy choice. In addition, to supplement the hypothesis testing, and to more fully uncover the underlying linkages between politics and policy at the subnational level, chapters four and six trace the process of policymaking in three case studies from each country.

The findings from the Indian chapters suggest that both party systems and interest groups affect the level and content of subnational economic policy choice within the country. Party systems seem to play a great role in influencing the amount of activity, as those states with more competitive and bipartite systems tending to spend more. Similarly, Indian states that have out and/or regional parties appear to influence the types of policies pursued in the state over time, making them much more likely to pursue promotional and later the combined promotional and deregulatory types of policies.

Executive stability and bureaucratic stability were also found, in the qualitative Indian chapter, to greatly influence the policymaking environment in the states, with more stable executives and bureaucracies more likely to make more coherent industrial policy. While union strength as measured by the visibility of strikes seems to have little effect other than to dampen the movement towards deregulation, greater levels of formal industrial association density leads to both more spending and a movement towards more deregulation.

The findings form the Mexican chapters largely parallel the Indian subnational findings, but with some key differences among the institutional and interest group hypotheses. Competitive, two-party subnational electoral systems swayed policies in the Mexican states, with those states spending more and moving towards a dual strategy more quickly. Another key factor influencing subnational industrial policy in Mexico is that the earlier a state had a non-PRI government, the more likely it was to be a faster moving state in terms of marketing itself, spending more for industrial promotion, and legislating a single-window clearance mechanism for industrial permits. As well, states with greater executive instability also were slower moving on both the amount of monies spent on industrial promotion, and on the movement towards a dual strategy. And finally, industrial group density also seems to have an impact on subnational economic policy, with those states with higher numbers of independent industrial associations more likely to spend greater amounts on their offices of economic development.

The dissertation utilized a unique pairing of research design and methodology to ascertain what subnational governmental units have been doing in response to political decentralization and economic liberalization within the developing world. The pairing of

India and Mexico as most-different cases allows for greater leverage in evaluating the causal mechanisms influencing subnational economic policy. While the two countries are both large, federal states, their dissimilar socio-political histories and very different modes of insertion into the global economy result in a compelling pairing for the purposes of this study. Likewise, by nesting three paired, most similar case studies *within* each country into the broader project, we are better able to determine the relative merits for competing theoretical explanations for what is driving economic policymaking at the subnational level with the two countries.

The most reform oriented states within the two countries that are included in the qualitative chapters for each of the countries are Andhra Pradesh in India and Aguascalientes in Mexico. The newly competitive subnational policy environments in each country were met with faster than average levels of policy innovation and quicker movements towards a dual promotional and deregulatory strategy. For both states, supportive party systems and party institutions played a key role in influencing policy choice by state governmental actors over the course of the 1990s. Likewise, close business-state coordination on economic policy resulted in policies that were perceived as more responsive to the private sector and the smoother implementation of policies. Although these two reform-oriented states are half a world away from each other, the similarities are striking when examining the impact of institutions and interest groups on subnational economic policy.

In contrast, the two average states in terms of reform orientation in the small-n analyses of Indian and Mexican state-level industrial promotion are Madhya Pradesh in India and Queretaro in Mexico. Each state was about average for the time period under review in this dissertation in terms of the prioritizing of industrial promotion within the state and moving, by the end of the decade, to a dualistic strategy of industrial subsidies and implementation of a single-window industrial clearance process. The later part of the 1990s found each of the two states acquiring much more competitive party systems with a corresponding increase in the state's respective dedication of monetary and human capital resources to industrial development. Likewise, the nature of the interest groups systems in each state were such that the later part of the decade saw closer associations forged between the private sector and government policymakers, and more regularized business-government interaction within the state.

And finally, the two laggard states for each case as detailed in the qualitative chapters are Uttar Pradesh in India and San Luis Potosi in Mexico. On both the institutional independent measures of party system and interest group strength, the two cases conform to our broader theoretical expectations about how these factors can influence subnational developmental policy. For Uttar Pradesh and San Luis Potosi, with party systems that failed to move closer to the competitive, two-party norm by the end of the decade, industrial promotion was rarely a topic in the electoral campaigns of the two states. While Uttar Pradesh had an extremely competitive party system, it was also highly fractured with great electoral instability and executive turnover as well. San Luis Potosi, on the other hand, continued to be controlled as a one-party state by the PRI, yet still with high levels of executive instability. As the fourth and sixth chapters present in some detail, these institutional and interest group factors greatly influenced the lower levels of industrial promotion in the two states and the slower movement toward the dual promotional and deregulatory strategy.

Implications

A first area of the political science literature this dissertation impacts is that of the ongoing theoretical divide between the deregulatory state and the developmental state policy literatures. While there has been a noteworthy bias in the comparative political economy literature towards examining the national-level, this dissertation demonstrates that the division between pursuing deregulatory and promotional industrial strategies at the subnational level is a false choice. With the context of political decentralization and economic liberalization, provincial and state governments are experimenting with different types of policy sets that do not conform to the either/or classification that has dominated the literature for the last generation.

At the subnational level in India and Mexico, and in other parts of the developing world, states are cognizant of the need to be competitive within the global economy. They pursue different types of policies to spur economic growth in their respective political locality regardless of whether the policy would be traditionally associated with the "developmental state" or the "Washington Consensus." States can seek to deregulate their permit process at the same time they are trying to lure states with tax abatements and locational incentives. States can move towards the liberalization of their labor markets at the same time they are setting up "technology consultation" boards which seek to coordinate sectoral investment and growth within their state. What we find at the subnational level is a larger degree of policy variation than will comfortably fit within our existing comparative political economy theory, and this dissertation seeks to redress some of this shortcoming.

As well, the dissertation attempts to bridge the gap that exists between the comparative and U.S. political economy literatures. By generating hypotheses and testing theoretical precepts that derive from both areas of the political science literature, it shows that this too has been an artificial divide within social scientific scholarship. With the increasingly globalized world conditioning the space for policymaking for both subnational governments in the developing world and developed world, there is a need for there to be more crossover between the U.S. and comparative literatures. Also, there should be a general recognition that political devolution coupled with market liberalization creates the need to examine state and local policymaking around the world within the context of the expectation of largely similar constraints on policy due to the global economy.

Similarly, the dissertation presents empirical information from two distinct regions of the world. By examining cases from both Latin America and South Asia, this research is better able to suggest that there has been a general trend on the party of subnational governments toward pursuing a mixed development strategy. We can see at the subnational level in both India and Mexico examples of states that are pursuing largely similar industrial strategies, like the pursuit of permit clearance reform and naming it the single-window clearance mechanism, even though they are within countries with very different histories, social structures, and physical positions within the global marketplace. This has been an under explored area of the globalization phenomena: how subnational governments have been retooling and reformulating policies to compete with each other in the global economy.

Institutional design is another important topic that this dissertation addresses which informs the broader theoretical debates within the development and political economy literatures. As states compete with each other for investment, resources, and development, new institutions have been created and old institutions modified within the context of the increased pressure for local development. The dissertation shows us that subnational governments are very much aware of the new constraints they are facing and that institutions and institutional control are key ways that states can foster innovation and craft the setting that allows for new forms of private/public coordination of economic policy and, in turn, hopefully generate conditions ripe for economic growth and industrial development within the state.

And finally, the fifth area in which this dissertation makes a contribution to the larger literature in political science is methodological. This research has employed an innovative research design that is cross regional and also incorporates both qualitative and quantitative models of understanding subnational development policy. The cross regional selection of cases protects against the possibility that one might not be explaining global phenomena, but instead might be only dealing with a regional or case-specific circumstance. As well, by utilizing both qualitative and quantitative methods, the dissertation has been able to avoid the possibility of falling prey to the shortcomings of each type of methodology. Specifically, the quantitative chapters test theoretically-informed hypotheses drawn from the comparative and U.S. political science literatures, while the two qualitative chapters uncover the local logic affecting industrial policymaking in six states across India and Mexico.

The dissertation also points towards further research that should be done in light of the empirical data presented in Chapter Three to Chapter Six. On the comparative political economy side, this research suggests that more attention needs to be paid to subnational/national government interactions. We need to have a better understanding of the politics of re-regulation (Synder 2001) by subnational governments and more sophisticated theory that can help us to understand why municipal, provincial, and state governments have been doing what they have been doing in recent years in all sorts of policy areas. Whether we are referencing education reform, environmental regulation, or other aspects of the ongoing development project, more research needs to be done that incorporates the subnational role in policymaking in light of increased amounts of political decentralization around the world. And, especially with the ever increasing import of the global economy, a more nuanced view is need as to the proper role of the state in economic development.

Likewise, the dissertation points towards further research that is needed within both of the Indian and Mexican case literatures, and suggests that both of the current case literatures fail to incorporate findings from the broader comparative literature. While there has been a fair quantity of recent work that looks at state policies on the economic and regulatory fronts in India, there remains much to be understood. India, a country that has been growing at the second fastest percentage clip in the world for the last 20 years, is poised to become one of the largest and most open economies in the world in the decades ahead. While the national-level government in New Delhi is, of course, greatly responsible for this development pace and as a regulator of what is to come, state governments in the country have an equally important role to play as the country moves on to third stage reforms of the labor market and other regulatory issues. Subnational governments need to become the focus of much of the work that will be done as India transitions into a global economic superpower as subnational government policy is turning out to be ever more vital for understanding the uneven growth across the country and distinct problems that face different regions within India.

Similarly, this dissertation points to the need to recalibrate the level of analysis within the Mexican case literature. While some interesting work has been done within the last 10 years at the subnational level, much remains to be done as the country gradually stratifies into three different economies. The richer states of the north, the rapidly growing states of the center and the slow-growing states of the south all face diverse incentives for policymaking and much different constraints and opportunities for future economic growth. As the country continues to democratize and as its ties to the global economy increase in magnitude by the year, more research needs to be done that examines institution-building, policymaking, and regulation at the subnational level within Mexico.

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