Does globalization help to overcome the "crisis of development"? Political actors and Economic Rents in Central America and the Dominican Republic

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Abstract

This paper explores the expansion of global production in Central America and the Dominican Republic to evaluate the opportunities for economic and political transformation in the current era of globalization. I identify three potential political opportunities. First, the emergence of international labor alliances together with the existence of preferential trade arrangements creates new pressures for labor-friendly legislation. Second, the diffusion of corporate social responsibility and consumer pressures in value chains force suppliers to be more respectful of labour rights. Third, some domestic suppliers within global production networks are forced to continuously upgrade their operations and find new sources of competitive advantage. These new capitalists may be more inclined to support and even demand productivity enhancing social spending than the traditional elite.

Despite these potential positive effects, however, the diffusion of GPNs has also created new structural constraints that are hard to overcome. As Kaplinsky (2005) has demonstrated, globalization had resulted in a simultaneous process of extension of manufacturing production among a larger number of countries and a concentration of buyers. Pressures to reduce costs are intense at the firm and national levels.

Central America, the Dominican Republic and many other developing countries are thus faced with difficult policy challenges to overcome the "crisis of development". They must try to use the new political opportunities created by globalization to secure more democratic, dynamic and equitable relations in the labor market. At the same time, however, they will be tempted to compete through low wages and weak labor standards (a losing strategy in the short run) for the time being.

1. Introduction

Sustaining development requires both political and economic change and depends on internal and external forces. Productivity growth, structural transformation and improvements in the distribution of income may not happen without an effective state, a dynamic capitalist class and strong social movements. Economic change may also trigger political changes—a reason why elites may be hesitant to promote them (source). Yet we still tend to pay relatively little attention to the way the political and economic arenas interact over time either reinforcing or contradicting each other.

Globalization—i.e. the growing cross-border flows of goods, people and money as a result of which "economic developments in any one country are influenced to a significant degree by policies and developments outside its boundaries (Milberg, 1998: 71)—has created both opportunities and challenges for developing countries in the political and economic realms. Globalization has been made responsible for processes as different as the diffusion of human rights and democracy, the transformation of exports or the deterioration of opportunities for income redistribution all over the world (ECLAC, 2002).

This paper is interested in the contradictory pressures that globalization exerts on the political and economic structures of developing countries. Is it contributing to the emergence of "active citizens and effective states"—the two key ingredients to promote development for Oxfam's Head of Research Duncan Green (Green, 2008: 12)? In particular, does it strengthen or weaken those actors who may demand a sustainable expansion of real wages and redistributive social policies? Can globalization help to create the type of vibrant economies that generate the resources needed to adopt those same policies?

To answer these questions I concentrate on some of the impacts of globalization in Central America and the Dominican Republic (CAC). Traditionally characterized by patrimonial states, rentist capitalist classes, weak trade unions and primary specialization, CAC countries have witnessed dramatic transformations in political and economic structures. While different processes have driven these changes (from the globalization of human rights, to the global expansion of democracy and the increase in migration and finance), I focus on the impact of their growing participation in global production networks (GPNs) in sectors like apparel and, to a lesser extent, electronics.[1]

Without aiming to be exhaustive, the paper identifies three *political opportunities* created by new dependence on GPNs during the last two decades. First, the emergence of international labor alliances together with the existence of preferential trade arrangements (like the Caribbean Basin Initiative, CBI) created new pressures for labor-friendly legislation. Second, the diffusion of corporate social responsibility and consumer pressures in value chains forced suppliers to be more respectful of labor rights at the micro-level. Third, domestic suppliers within GPNs are being forced to continuously upgrade their operations and find new sources of competitive advantage. These new capitalists may be more inclined to support and even demand productivity enhancing social spending than the traditional elite.

[1] By doing so, I also hope to contribute to bringing politics to the literature on global value chains. As McDonald (2008, 13) puts it, this literature has traditionally suffered from a "tendency to regard supply chains as part of the 'private' institutional domain – properly studied through primarily economic or sociological lenses – rather than as potential sites of *political* power, contestation and governance."

At the same time, however, the paper argues that any positive impact of the expansion of GPNs is limited by the existence of new *structural constraints* in the global economy. As Kaplinsky (2005) shows, globalization has resulted in growing competition between developing countries for investment and, at the same time, oligopolistic concentration of buyers. These trends reduce the value added received by local suppliers in developing countries, which, in turn, respond by reducing labor costs and tax contributions. In recent times, the emergence of China as a global competitor and the global recession may be erasing some of the positive political impacts of GPNs on domestic political economies.

The paper is divided in four sections. The first section discusses the role of labor markets in promoting equitable development and highlights the changes that CAC has experienced in the last century. The following two sections concentrate on the political opportunities and structural constraints that participation in GPNs has created for the creation of more positive interactions between workers, firms and the state. The paper concludes with some reflections on the policies at the national and international levels that can help to create more spaces for equitable development in Central America and beyond.

2. Equitable development and labor markets in CAC and beyond

The labor market is at the heart of the process of economic development. Creating well-paying jobs still is the best way to reduce poverty and improve the standards of living of a majority of the population (Amsden, 2010). Given the central role of payroll taxes to fund social programs, higher formal employment will also have a positive effect on redistributive programs in many parts of the developing world (Martinez Franzoni and Sanchez-Ancochea, forthcoming). The two main actors in the labor market (workers through trade unions and firms through business associations) also play a central role in the shape that social spending takes in different parts of the world (Hall and Soskice, 2002; Huber et al, 2006)

Unfortunately, most developing countries have traditionally failed to create well-paying jobs for most of its citizens. Central America has not been an exception. Inequality in the distribution of land and the asymmetric power of the landowning elite within the capitalist class reduced the incentives for wage growth and the accumulation of skills (Bulmer-Thomas, 1987; Huber, 2003). According to Bulmer-Thomas (1983:270), in Central America "agrarian interests (the traditional oligarchy) exercise[d] preponderant influence over political affairs." Starting during the liberal revolutions of the late 19th century, the Central American economic model was driven by primary exports within a system of "coerced rural labor" (Bayloria-Herp, 1983: 298). Since low wages and low taxes contributed to sustained profitability and the production process did not require skilled labor, there were little incentives to expand education and other social services. At the same time, agriculture production was based on latifundios, which "made independent peasant political organization difficult if not impossible" (Huber, 2005: 14).

The expansion of import substitution industrialization (ISI) did not change this pattern of state-society relations significantly. Contrary to the experience in larger countries, ISI in Central America took place "on top of" the primary export-led model (Bulmer-Thomas, 1987). The landowning elite remained highly influential and avoided an excessive expansion of taxes on primary production, while manufacturing production was inefficient and dominated by monopolies. Skilled labor was now more important than in previous periods and primary education and social security expanded in all countries, but social programs were concentrated in the urban sector and trade unions systematically persecuted. Costa Rica's success in developing universal social policies may have been exceptional, but even there trade union rights in the private sector were never protected (Martinez Franzoni and Sanchez-Ancochea, forthcoming).

CAC's economic model has changed dramatically in the last two decades. The combination of civil wars and difficult economic conditions triggered a rapid growth of migration to the United States. Remittances have become the main source of foreign exchange in El Salvador, Guatemala, Honduras and Guatemala and also important in the Dominican Republic. Tax incentives for non-traditional exports and tourism have contributed to a dramatic transformation of the region's export structure. Between 1990 and 2005, the share of traditional primary exports such as sugar, coffee and cacao in total foreign income from goods and services (mainly tourism) decreased from 76% to 35% in Nicaragua, from 34% to 15% in Costa Rica and from 31% to just 2% in the Dominican Republic.

Assembly of apparel and, in Costa Rica and the Dominican Republic, electronics and medical equipment have expanded rapidly due to a combination of internal and external factors. All government in the regions created new export processing zones (EPZs)—i.e. isolated manufacturing parks where export producers received generous tax incentives—and tried to maintain weak exchange rates. The region also benefited from US incentives within the CBI and from the transnational corporations' need to find new outsourcing bases. Between 2000 and 2006 manufacturing exports from the EPZs and related regimes grew by 5.7% per year in CAC (Padilla-Perez and Hernandez, 2010). By 2006, there were 155 EPZs in Mexico and the Caribbean Basin which were responsible for more than 5 million (mainly female) jobs (Singa, 2007).

New manufacturing exports have created some opportunities for upgrading, which so far only Costa Rica and the Dominican Republic have partly seized (Paus, 2005; Sanchez-Ancochea, 2011 and forthcoming). The expansion of the EPZs has also created a new class of more dynamic firm owners in some countries and opportunities for North-South civil society alliances all over the region. Exploring the extent to which all these processes have shifted opportunities for development in the region is the aim of the rest of the chapter.

3. Potential positive effects of the globalization of production on labor

The increasing participation of CAC in GPNs has affected relations between the state, the business elite and trade unions and has triggered some processes that could potentially reshape the domestic political equilibrium in the long run. I concentrate on three different effects in this section, but my list is by no means exhaustive. First, transnational alliances to protect labor rights have in some cases increased the bargaining power of domestic workers at the firm level. Second, and more broadly, trade unions have used the threat of US trade sanctions to push for reforms in the labor code and other major legislation. Third, new exporters, who face intense competition to create new competitive capacities, may be more willing to support social spending in health and education than the traditional elite in countries like the Dominican Republic, El Salvador or Guatemala—although the evidence of this trend is still patchy. The state remains at the centre of all these new processes and its reaction to the initial changes usually determines the ultimately trajectory of the country.

3.1. GPNs and the power of brands: Transnational consumer pressures and corporate social responsibility

Customers in developed countries have become increasingly reluctant to purchase clothes, shoes or other consumer goods produced by companies that do not respect basic human and labor rights. This new situation opened a new role for transnational social movements. By pressuring their own universities and organizing boycotting campaigns, students in the North began influencing the labor conditions of workers thousands of miles away. Activist stockholders with just a few shares could now demand information on companies' supplying arrangements. Corporate social responsibility (CSR) became a major marketing instrument to improve the ethical and environmental value of various brands (Sklair, 2000).

New transnational alliances of trade unions and social movements thus emerged in parallel to the creation of GPNs. Trade unions and non-government organizations (NGOs) from developed countries joined forces with their counterparts in developing countries to pressures companies involved in global production. According to Anner and Evans (2004, 35), "the ties among 'workers of the world' are being replaced by 'workers and consumer activists of the world'. Growing labor-rights campaigns focuses on brand-name images." New campaigns have usually been driven by trade unions and NGOs from the North, with actors in the South playing a vital but subsidiary role.

These transnational processes affect patterns of *domestic* state-society relations in at least two ways. By enforcing union rights at the firm level and promoting partnerships between trade unions and social movements, they can gradually increase the political influence of workers. By promoting codes of conduct and CSR, they can also change the behavior and preferences of firms, reducing the incentives to maintain a 'low road' to economic development. Both of these channels have been evident in various Central American countries in the last two decades. The region became a fertile arena for transnational collaboration in labor issues due to its closeness to the US, the existence of trade preferential arrangements (particularly the CBI) and the historical weakness of unions. Campaigns have usually been organized around labor rights –including freedom of association- in specific factories and, in many occasions, have succeeded where exclusively domestic efforts failed.

The case of Mandarin International, a Taiwanese-owned apparel factory in El Salvador is a good example (Anner, 2003, Frundt, 2002). Workers decided to organize in the early 1990s to fight against poor working conditions –including lack of drinking water and unpaid and mandatory overtime. The first two attempts to create a trade union, however, were failures and led to massive firings.[2] The third attempt resulted in the creation of a trade union, but the company responded by firing the union leaders. The conflict soon escalated beyond the factory as new actors got involved. A group of national NGOs began denouncing the situation in the maquila sector using the Mandarin problem as a showcase. When the US National Labor Committee (NLC) learnt about the case and found out that Mandarin was a supplier for The Gap, it launched a broad campaign on the issue in collaboration with Salvadorian trade unions. The campaign was ultimately successful and resulted in the rehiring of the union members and the creation of a monitoring mechanism –the first of its kind in El Salvador.

[2] This was not an isolated problem but a general problem in El Salvador. According to Anner (2002), between June 1995 and June 1996 efforts to create unions in various maquilas resulted in only three hundred new union members and more than five thousand workers fired.

Collaboration between Central American (and Mexican) trade unions and NGOs and their US counterparts expanded rapidly during the 1990s. The Union of Needletrades, Industrial and Textile Employeers (UNITE) became an active partner of maquila groups in Mexico, Honduras and the Dominican Republic. Other social organizations like the United States-Guatemala Labour Education Project, Witness for Peace, the support Committee for Maquiladora Workers and the NCL promoted the creation of unions and the improvement in labour conditions all over Central America (Armbruster-Sandoval, 1999). The student movement in US universities was also instrumental (Anner and Evans, 2004) and United States against Sweatshops expanded to over 180 campuses, using its force to pressures university managers to buy ethically all over the world.

Most of these alliances have concentrated in securing freedom of association in specific companies (and ultimately in the whole maquila sector). Yet consumer pressures have also forced TNCs to adopt a broader response. Through various codes of conduct and other voluntary initiatives, TNCs and international buyers have committed to secure labor rights in all stages of their value chain (Gereffi, 2005). They have also become responsible for effective monitoring of their suppliers in developing countries. As Auret Van Heerden, president of the Fair Labor Association (one of these initiatives), puts it, "one of the most powerful vehicles we have for ensuring the implementation of labor standards in global supply chains is the multinational enterprise."[3]

While both transnational social alliances and codes of conduct have been used effectively to promote labor rights at the micro-level, they are unlikely to have macro-impacts for at least three reasons. First, transnational collaborations involve complex interactions between different groups within and between countries. There are multiple opportunities for conflict because each group has a different agenda and responds to different constituencies. Disagreements between trade unions and other social movements in developing countries are common and may end up reducing the overall strength of workers. At the same time, relations between trade unions and their counter-parts are still asymmetric and sometimes "weaker Southern actors find that their Northern counterparts tend to dominate campaigns strategies and agendas" (Anner and Evans, 2004).

Second, the extent to which all these initiatives have really changed the distribution of power between workers and firms is unclear. Codes of conduct have sometimes been marketing operations with little impact on the behavior of firms. Large buyers and TNCs in the buyer-driven value chains have difficulties to monitor the behavior of their suppliers, which sometimes use sub-subcontracting to maintain exploitive labor conditions (Gereffi, 2005). In an evaluation of the Ethical Trading Initiative—a transnational alliance that promotes codes of conduct—in the Vietnamese apparel and footwear sector, Barrientos and Smith found minor positive effects on labor conditions (IDS, 2006). They also describe the difficulties to monitor the code because of the existence of an array of unaccountable subcontracting arrangements.

[3] Testimony before the Congressional Human Rights Caucus "Human Righats and Brand Accountability: How Multinationals Can Promote Labor Rights", February 8, 2006. The FLA is a tripartite organization in charge of monitoring the implementation of a code of conduct among all member firms. The FLA was created by the Apparel Industry Partnership, an initiative promoted by the Clinton administration that brought together some companies, NGOs, trade unions and the Department of Labor. At the moment, there are 31 participating companies as well as a substantial number of participating suppliers. See FLA (2006) and the FLA webpage www.fairlabor.org

Probably the largest limitation of the approach based on targeting specific TNCs and specific unionization drives has been its limited macro-effect. Even if workers succeeded in organizing trade unions in all apparel exporting firms in Central America, this would benefit a few thousand workers as most firms of all sizes are not affected. This is why efforts to influence labor regulation and enforcement may be more important.

3.2. GPNs, international trade agreements and labor standards

A weak process of industrialization and the dominance of unequal relations in the agricultural sector conspired against strong trade unions in CAC during the period 1950-1985. Even in a democratic country like Costa Rica, workers in the private sector faced constraints to join unions: in 1971 the Secretary of Labor recognized that “trade union freedoms as such do not exist” (cited in Estado de la Nación, 2001). By the mid-1970s, only 5% of private workers were members of trade unions compared to 43% in the public sector (Rottenberg, 1993).

Efforts to improve labor rights through institutional and legal reform during this period failed in all Central American countries. By the early 1980s, El Salvador had ratified only four International Labor Organization (ILO) conventions, Honduras 14 and Nicaragua –the leader in this regard-41. The average in the rest of Latin America was 49 (data from Schrank and Piore, 2007). In 1989 the Dominican Republic still used the 1951 Labor Code approved by the Trujillo dictatorship, despite a series of strikes demanding changes.

The situation changed dramatically during the 1990s. According to data from Murillo and Schrank (2005), all Central America countries but Honduras introduced union friendly reforms in their labor laws in the early 1990s.[4] The impulse for the reforms came from the participation of all countries in apparel GPNs, which depended on preferential market access to the US. The Dominican experience constitutes a good example of the combined role of GPNs and US incentives.[5] After decades of resistance, the Dominican government finally decided to introduce a more progressive labor code in 1992. The new code included a “fuero sindical” (protection of trade union leaders against discrimination by firm owners), created a tripartite commission to set minimum wages (the “Comisión Nacional de Salarios”), promoted the modernization of the Labor Courts and expanded firing compensation.[6]

This significant transformation, which strengthened the role of trade unions at least formally, was primarily the result of international factors. In 1990 the ILO introduced a special reference to Dominican Republic’s labor violations in the report of the Conference Committee on the Application of Standards. In response to the report, the American Federation of Labor-Congress of Industrial Organization (AFL-CIO) requested the withdrawal of the Dominican Republic’s preferential access to the US market and European tour operators threatened with significant reductions in the number of tourists. Given the risk

[4] According to their data, Guatemala and Nicaragua also suffered some episodes of counter-reforms in the 1990s. In Costa Rica, there were also some anti-union reforms (which strengthen the alternative labor organizations called “solidaristas” organizations) in the early 1980s.
[5] The following discussion is based on interviews that took place in Santo Domingo (Dominican Republic) in June and July 2002 with Rafael Alburquerque (Secretary of Labor from 1991 to 2000 and current vice-president of the Republic) and trade union leaders from the trade union confederations Central General de Trabajadores (CGT), and the Confederación Sindical de Trabajadores Clasistas (CSTC). See also Murillo and Schrank (2005) and Schrank (2009).
[6] The last benefit was at the end not as generous as initially expected. The original draft elaborated by Alburquerque and two other labor lawyers established compensation equivalent to 30 days of salary per year in the job but business leaders succeeded in reducing it to 21 days.

of losses in apparel and tourism—two growing sectors based on participation in GPNs—the Dominican government was forced to appoint a special commission that wrote a new labor code.

Pressures from American trade unions and NGOs –in alliance with domestic actors- were also important for reforms in other Central American countries. These groups used the US Trade and Tariff Act of 1984, which required countries to comply with international labor standards to maintain benefits under the Generalized System of Preferences, GSP (Schrank and Piore, 2007). In Costa Rica, for example, the trade union confederation Rerum Novarum together with other Costa Rican trade unions asked for the elimination of the GSPs in 1993, alleging lack of respect to the freedom of association. The government was then forced to reform the labor code, reducing the number of workers required to create a trade union and securing labor rights for trade union leaders.[7] In Guatemala, petitions for the review of preferential access to the US led to improvement in minimum wage regulation.

In principle, all the reforms should have facilitated union drives and strengthened the participation of trade unions in policy discussions, design and implementation. Yet the strength of this channel has in part depended on the governments' ability and willingness to enforce the new regulation. In fact, given the structural weakness of the labor movement, the creation of complementary institutions to sustain improvements in working conditions has become fundamental.

The state has, for example, been instrumental in contributing to a gradual improvement in labor regulation in the Dominican Republic. Since the mid-1990s, the Secretary of Labor used the civil service law to improve the professionalization and stability of its labor force. According to former Minister Rafael Alburquerque, during his term in office (1991-2000) sixty per cent of all workers in the Secretary became civil servants appointed through competitive examination –including most labor inspectors.[8] The subsequent Minister of Labour, Milton Ray Guevara, maintained the same policy approach.

According to Schrank (2009), the professionalization of the labor inspectors triggered a virtuous circle of higher labor standards and increasing productivity. The new labor inspectors started pressuring firms in various sectors to respect labor regulations, while simultaneously assisting them in implementing technological upgrades to increase productivity.[9] There are some signs that the Dominican Republic could be witnessing a simultaneous strengthening of trade unions at the national level and more positive collaboration between workers, firms and the state—although this collaboration is by no means obvious in most sectors of the economy.

3.3. New domestic producers and the accumulation of human capital

[7] Meeting with a leader of the Trade Union Confederation Rerum Novarun, San Jose (Costa Rica), September 2002.
[8] Meeting with Rafael Alburquerque in Santo Domingo, Dominican Republic, June 2002.
[9] The fact that the Dominican Republic followed the French model of labor regulation also contributed to this virtuous circle (Schrank and Piore, 2007). While the Anglo-Saxon model is "bureaucratic and inflexible" (p.14) and focuses on penalties, the French is a tutelary model that tries to modify firms´ behaviour through persuasion. French inspectors work with owners to simultaneously secure better labor standards and increases in productivity.

In the long run, survival in GPNs depends on a sustained upgrading of the firm's capabilities—a point that the more dynamic firms are slowly learning. According to Kaplinsky (2005: 87), businesses competing in the global economy "need to develop a new way of working, not just with their existing labor force, but often recruiting new and different skills." As a result, some suppliers in GPNs are now demanding workers with at least some years of secondary education and, in some sectors, college training as well.

The Dominican experience gives again some indication of the competitive pressures that the new exporting elite face and the *potential* effect that this can have on state-society relations. The expansion of export processing zones (EPZs) since the beginning of the 1980s led to the emergence of some domestic suppliers, particularly in the Cibao region. Companies like D'Clase corporation, Interamericana Products, Bratex Dominicana and Grupo M were created after 1985 –in many cases by former managers from foreign firms. They grew slowly in size and soon became some of the largest apparel exporters in the Caribbean Basin.

While initially specializing in basic assembly, by the mid-1990s these leading companies were forced to move into full package.[10] According to managers from Bratex Dominicana and Grupo M, this decision was a response to new demands from international buyers who were no longer interested in participating in production. As a manager of Grupo M explained in 2002, "a few years ago our clients told us… 'My area of expertise is marketing and design and I need someone that supplies me the rest'. For us then the decision was imposed because they told us 'If you do not supply me with all of this, we will move to Asia'". Full package operations contributed to an increase in profits, but also increased the risk that Dominican companies had to bear and the working capital they required.[11] When the apparel sector faced problems to respond to competition from China after 2003, some of these same entrepreneurs began investing in other sectors. The owner of D'Clase, for example, invested in a call center and promoted alliances with Indian IT firms.[12] Peter Weinerth from Bratex Dominicana invested in the production of communication hardware within the new Technological Park of Santo Domingo.[13]

In order to sustain this gradual process of change, the new Dominican capitalists have collaborated with the government in various projects of human resource upgrading. A public-private alliance, for example, was behind the expansion of training programs delivered by the National Institute for Technical and Vocational Training (INFOTEP). These programs have trained more than 74,000 workers from the EPZs and have contributed to the expansion of skills at the management level (Schrank 2006). More recently, the Dominican Association of Export Processing Zones (ADOZONAS) has also supported the expansion of education and new training projects. In a series of meeting with the government in September 2006, for example, members of ADOZONAS made clear that investment in human capital was a necessary condition for Dominican participation in GPNs of electronics and footwear.[14]

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[10] Full package refers to the process by which frms find their own fabrics, cut them, sew them, add all the complements and sned the final product to the client.

[11] Interviews with managers from Grupo M (Santiago de los Caballeros, Dominican Republic, June 2002) and Bratex Dominicana, (Santo Domingo, Dominican Republic, July, 2002).

[12] Data provided by Andrew Schrank.

[13] Secretaria de Estado de Economía de la República Dominicana "Inventores nacionales trabajan 14 proyectos en Parque Cibernético", http://www.stp.gov.do/noticias/noticia_inv_03042006.htm (accessed on August 8, 2007).

[14] See ADOZONAS-Gobierno Dominicano "Presentación: Un Presente Forjando el Futuro", September 2006 in http://www.adozona.org/manager/dlm/applications/DocumentLibraryManager/upload/PrADOZONA.pdf (accessed August 8, 2007)

Other countries are witnessing similar processes. In Costa Rica, for example, some TNCs like Intel are leading supporters of new programs in tertiary education (World Bank, 2006).

The experience in the Dominican Republic and Costa Rica (and a few new entrepreneurs in neighboring countries) illustrates the *potential* positive effect that participation in GPNs can have on the behavior of capitalists. Yet like the rest of the channels discussed in this section, this process is still incipient and has been in many ways problematic. The number of successful new capitalists is still low and their influence in the overall pattern of development limited. More importantly, relations between the state and the new capitalists are hindered by major coordination failures. Producers from the EPZs may demand higher social spending, but have been still reluctant to "pay the bill". They still demand new subsidies and tax exemptions that are limited the ability of the government to expand social services and improve their quality. Even when it has supported tax reforms, the Central America globalized business class has concentrated on value added taxes and other relatively regressive income sources (Schneider, forthcoming).

The influence of these new capitalists on development policy is also contradictory. While they may support some development-friendly measures, they have also promoted more problematic ones. In particular, suppliers of GPNs have enthusiastically lobbied for the approval of the Dominican Republic-Central America free trade agreement with the US (DR-CAFTA), which could have negative effects on long term technological upgrading (Shadlen, 2005). Meanwhile, other actors with less political power and more to lose from new regulatory changes (such as stronger protection of intellectual property rights and new investment rules) have been left unprotected.

4. Why gains do not materialize? Structural constraints to labor improvements

In Central America, participation in GPNs may have contributed to a significant political transformations, opening some space for a more dynamic and equitable relations between state and society. Transnational political alliances of different kinds can positively affect public policy and condition the behavior of TNCs and their suppliers. At the same time, competitive pressures on suppliers may increase their support for the accumulation of human capital through public social programs.

Yet the consolidation of more progressive interactions between labor, the private sector and the state also faces structural obstacles created by the particular nature of global manufacturing value chains. Trade unions may create transnational alliances, but have to cope with the expansion of informal employment. Domestic suppliers may want to upgrade in the long run, but they first need to respond to increasing competition from China. Governments face increasing demands, but also constraints in their ability to raise taxes. This section shows that the potential positive effects of GPNs on state-society relations are hindered by difficulties in the economic global environment.

To evaluate these difficulties, the concept of rent—and how rents are distributed among actors in the global economy—constitute a good entry point. According to Kaplinsky (2005, 62), "rent describes a situation where the parties who control a particular set of resources are able to gain from scarcity by insulating themselves from competition. This is achieved by taking advantage of or by creation barriers to entry of competitors." Rents thus can be seen as an income above competitive market profits and wages. They can be created by firms (through product and process innovation), by the state (through policies like protection of the domestic market) or by the general macro-environment (e.g. quality of infrastructure, efficiency of the financial sector).

Berg (2005) offers a useful framework to analyze how the distribution of rents takes place along the value chain. She explores the division of rents in global value chains at three levels—the first two particularly relevant for our analysis:

- Division of rents between firms in developed and developing countries, which determine the share of value added in GPNs that stays in the latter.
- Division of rents between firm owners and workers in developing countries, which explains the capacity for win-win situations.
- Division of rents between skilled and unskilled workers, which is determined by education policies and by the structure of the economy.

While she uses this approach to explain raising wage inequality in the Chilean economy, the same framework can be applied to the analysis of power constellations and state-society relations. My basic argument is that the specific nature of global value chains (particularly, but not exclusively, buyer-driven ones) results in a reduction of the rents that accrue to supplier firms in developing countries. This generates immense pressures on both capital and labor, making the creation of more effective state-society relations particularly complicated. In the remaining of this section, I illustrate this point by discussing the first two levels in the division of rents within GPNs.

4.1. Division of rents between North and South: structural constraints on domestic suppliers.

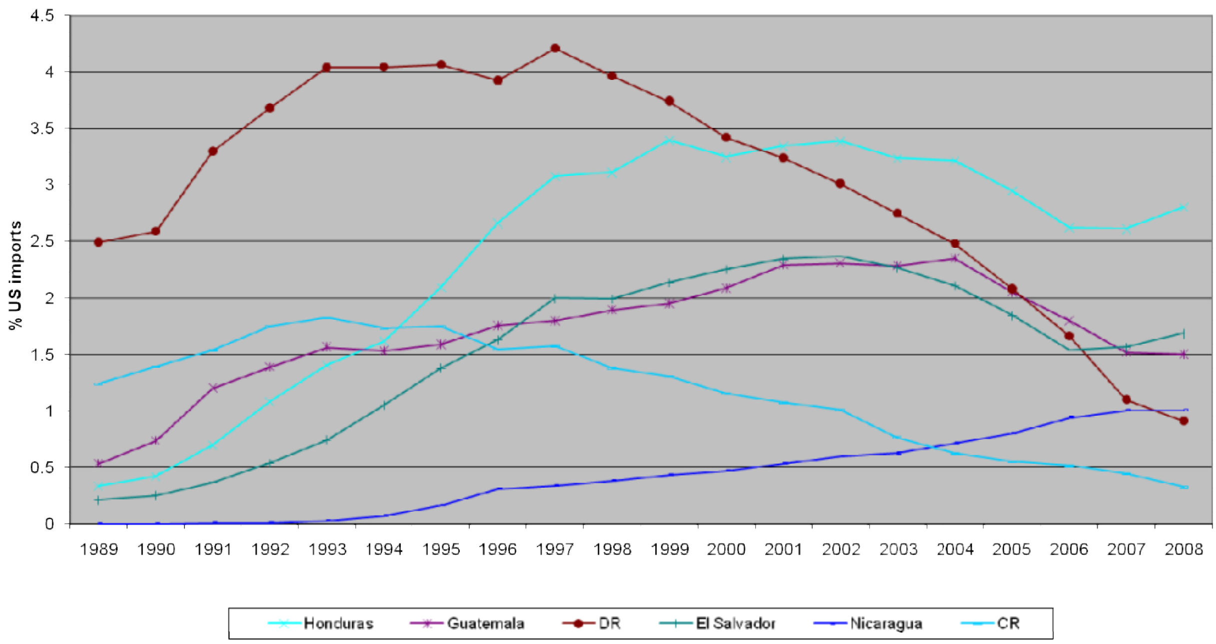
In buyer-driven GPNs like apparel, there are significant asymmetries between lead firms and suppliers. While lead firms in developed countries are witnessing a process of consolidation, the number of suppliers from regions like Central America is growing and competition is intense. As a result, distribution of rents and thus value added among firms has been highly unequal.

Global marketers like Nike or Gap have succeeded in creating high barriers to entry by building desirable brands and sophisticated marketing campaigns. While the actual production of a pair of shoes may be simple, developing and selling new brands is complex and extremely expensive. Distributing and retailing mass consumption goods has also become difficult and capital intensive. As a result, the number of firms in direct contact with the consumer has decreased significantly. According to data from Nolan et al (2002), Coca-Cola controls 51 percent of the global market for soft drinks and Gillette 71 percent of the market for razors (cited in Milberg, 2004). Sport footwear is increasingly dominated by only two firms (Nike and Adidas), which has made major purchases in the last decade (Nike bought Converse while Adidas merged with Reebok). Although oligopolistic competition between these firms is intense, they are still able to maintain high mark-up over costs (Milberg, 2006).

Production of mass consumption products, on the other hand, has relatively low barriers of entry as assembly of apparel or some basic electronics goods requires relatively low investment in capital goods and is not intensive in skilled workers. The resulting increase in suppliers from developing countries

At the same time, transport and communication costs have decreased rapidly, making access to developed countries from all over the world easier than ever before. The result has been a rapid increase in the number of suppliers from developing countries—each of which face increasing difficulties to protect their own market share—something that is particularly evident in the case of Central America. Figure 1 measures the market share of CAFTA countries in total US clothing imports. Costa Rica and the Dominican Republic were the first to integrate to the apparel GPNs and initially expanded their market share rapidly. The emergence of suppliers in Honduras and El Salvador, however, created significant pressures and the market share of the first comers went down. During the period 2004-2008, Nicaragua—the latest comer with lower wage costs—was the only country with a steady increase in its market share.[15]

Figure 1. CAFTA. Market share in US clothing imports in US dollars, % of total, 1989-2008



The negative implications of the asymmetric structure in buyer-driven GPNs for state-society relations are apparent in at least two ways. Given the pressures that domestic suppliers face to reduce costs and their inability to create new technology rents, they are forced to pass on all productivity increases into price reductions.[16] In this way, firms in Central America and other small developing countries are not in a position to lessen class conflicts through an adequate distribution of productivity gains –as countries in Northern Europe and, to a lesser extent, even East Asia did in the past.

Most suppliers in GPNs are also forced to adopt a short termism approach in their relations to the state. While new domestic capitalists engaged in GPNs know that their ultimate survival

[15] The entry into force of CAFTA contributed to a small expansion of the market share in Honduras and El Salvador. Nevertheless, there are some indications that this effect was short-lived and that the market share will go down in 2009.

[16] This has been a historical problem for Latin America, which has been emphasized by structuralist economists. See, for example, Prebisch (1950).

may require an expansion of public spending in infrastructure and education, they are also unwilling to pay the required tax increases. Most suppliers in manufacturing GPNs in Central America have benefited for a long time from tax subsidies within the EPZs and have fought to maintain these incentives for as long as possible. Their pressure explains why Central American governments have been very active in asking the World Trade Organization (WTO) for permission to maintain their export subsidies. Central American countries are still part of a small number of WTO members that can give tax incentives to exporters and in 2008 they succeeded in expending this exception until 2015. The president of the Dominican export processing zones association (ADOZONAS) showed his satisfaction with the agreement, claiming that "the decision… reaffirmed the external recognition that Free Trade Zones are the engine of economic development" and would contribute to the external competitiveness of the country.[17]

The situation in producer-driven commodity chains like IT is somewhat different because the process of production is still highly profitable. Therefore, attracting foreign investment from companies like Intel or Microsoft –like Costa Rica has done in recent years—could potentially overcome some of the problems just described. Companies in these sectors have succeeded in sustaining high rents through product and process innovation. At the same time, competition among developing countries in high tech is lower than in apparel because the costs of entry are higher.

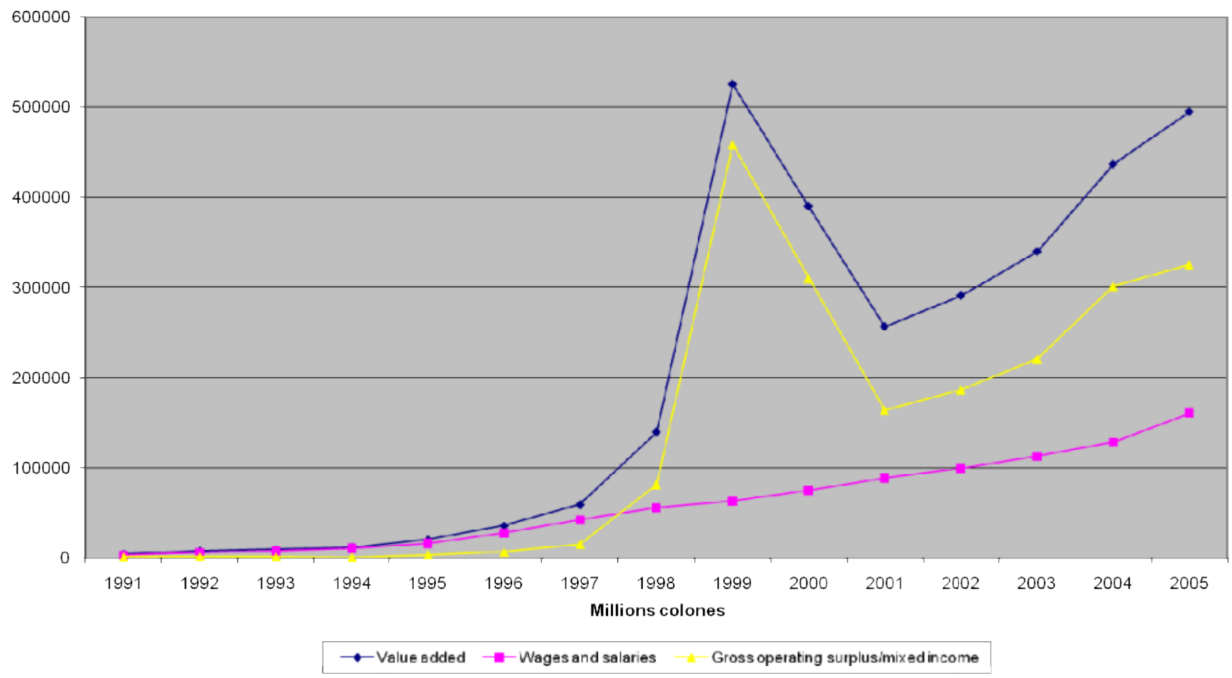
The problem, however, is that global production in these sectors is controlled by TNCs and parent companies in developed countries determine the way profits are distributed among all subsidiaries. Companies in high tech sectors make reinvestment decisions based on global not local conditions and thus have a substantial bargaining power vis-à-vis small developing countries. The experience of Intel in Costa Rica clearly illustrate the limited contribution that high tech firms make to value added and the large political clout they have. The arrival of Intel resulted in a rapid expansion of exports from the EPZs, which increased from US$892m in 1996 to $2,956m in 2000 and $4,886m in 2005. Value added—defined as exports minus imports—also grew rapidly from US$155m to 1,358 in 2008

Yet this growth of export was not without structural limitations. First, value added as percentage of total exports in the EPZs was low: it averaged 26 per cent between 1997 and 2008, but was just 12 per cent in the case of machinery and electronics (where Intel is located).[18]

Second, much of the value added generated by Intel and other companies went to finance the capital stock and a high level of profits.[19] Figure 2 uses statistics from the Costa Rican national accounts to show the evolution of the gross operating surplus (GOS) in the EPZs – where Intel is located- since the mid 1990s. Between 1991 and 2008 the share of GOS in total value added increased from only 18 per cent in 1991 to 63 per cent in 2007—and with a peak of 87 per cent in 1999. As the figure clearly demonstrates, the arrival of Intel in 1997 is a key factor to explain the divergent evolution of profits and wages.

[17] ADOZONAS Press Release, 7 July 2007 at http://www.adozona.org/esp/noticiasdet.asp?codid=455 (accessed on 9 August 2007).
[18] Own calculations with data from the Costa Rica Export Promotion Agency (PROCOMER).
[19] In order to measure the rents, we would need to calculate the profit rate and its evolution over time and compare it with the wage rate. Unfortunately we do not have data on the evolution of capital stock. Nevertheless, figure 2 may still be useful to illustrate the growing direct control that TNCs exert on the value added generated in the Costa Rican EPZs.

Figure 2. CR. Value added and primary distribution in the free trade zones, 1991-2005



Source: own elaboration with data from the Central Bank of Costa Rica.

Decisions on what to do with profits do not depend on Intel's Costa Rican subsidiary. They are made by a committee (a "virtual factory") with managers from factories all over the world. According to a manager from Intel-Costa Rica, investment plans "is taken at the macro level, there is little autonomy in this regard." Employment and wage levels, transfer prices and most other strategic decisions are also centralized.[20] Other large TNCs in high tech GNPs located in Costa Rica also follow a similar strategy (Paus, 2005).

The importance of companies like Intel for a small economy like Costa Rica is immense and decisions on the reinvestment of its profits have a large macroeconomic effect.[21] This gives TNCs significant political influence and direct and indirect access to the government. Intel's influence is sometimes positive (e.g. demand for better technical education and infrastructure), but has more questionable development impacts in other occasions. Intel was, for example, partly responsible for an increase in tax subsidies for high tech firms and for a new push to liberalize the telecommunication system. According to Larrain et al (2001: 190), "the political balance among stakeholders in this realm [the liberalization of telecommunications] seems to have changed after Intel's arrival, and the reform are more likely to take place". The Costa Rican Investment Board (CINDE) –while a semi-public institution- has also become a powerful lobbyist in favour of some neoliberal policies preferred by foreign firms but opposed by social movements—something evident in the debate on DR-CAFTA in the period 2004-2008.

4.2.Division of rents between firms and workers: difficulties to consolidate trade unions

[20] Interview with a manager of Intel-Costa Rica, Rivera de Belen, September 2002.
[21] Costa Rica maintains two different sets of macroeconomics statistics, one with high tech firms and one without them. In 2000, for example, GDP grew at only 1.4% due to an "Intel effect". Without Intel, the company grew at 3%.

If domestic suppliers in Central America suffer from the asymmetric nature of GPNs, workers suffer even more as they confront simultaneous structural pressures at home and abroad. Neoliberal reforms have failed to reduce unemployment and sub-employment and, as a result, several countries have witnessed an increase in the *domestic* reserve army of labor. At the same time, the entry of Eastern Europe, India, and China in GPNs has resulted in a rapid growth of global labor supply, thus expanding the *international* reserve army of labor.

This second effect has been particularly dramatic. During the 1990s, the world's labor force doubled as a result of the end of the Cold War and the spread of GPNs in more countries. Employment in the EPZs increased by 91% in only five years, from 22.5m in 1997 to 43m in 2002 (Gereffi, 2005). Most new manufacturing workers came from China and other poor countries, where wages were very low. In 2002 hourly labor costs in the apparel sector (including benefits) were only US$0.7-0.9 in China, compared to US$2.7 in Costa Rica, US$1.7 in Dominican Republic, US$1.6 in El Salvador, US$1.5 in Guatemala and Honduras and US$1.0 in Nicaragua (USITC, 2004).

The expansion of the international reserved army of labor was not simply a one-time shock but will continue in the future. In China, for example, there is still between 100 and 150 million people working in low productivity, backward sectors who will likely move to export activities in the future (Kaplinsky, 2005). This immense labor force –equivalent to more than 25 per cent of the labor force in al high income countries—will exert new pressures on labor markets all over the world, as they slowly enter into GPNs in the manufacturing and service sectors.

At the same time, Central American countries have generally failed to expand employment opportunities outside the EPZs. Unemployment and sub-employment have remained high and low productivity jobs are still dominant in the economy. At the beginning of the twenty first century, between 40% and 60% of Central American employees in the urban sector worked in low productivity sectors –and in 2009 the number is likely to be significantly higher (table 1). Domestic suppliers in the EPZs thus find themselves with a large pool of workers, and thus face limited upward pressures on real wages.

Table 1. Urban population working in low productivity sectors, 1990-2007

	1990	1994	1997	1999	2003	2004	2005	2006	2007
Costa Rica	36.9	38	39.6	41.6	…	38.9	39.9	39.8	37.7
Dominican Republic	…	…	47.0	…	46.9	48.1	49.3	49.3	49.3
El Salvador	55.6	…	52.5	52.2	…	54.7	…	…	…
Guatemala[1]	54.6	…	64.4	…	57.6	…	…	58.1	…
Honduras	53.3	49.9	54.3	55.2	59.4	…	…	43.3	43.9
Nicaragua[2]	…	49.2	60.6	59.9	…	…	…	58.4	…

NOTES: (1) Guatemal refers to the years 1989, 1998 and 2002. (2) Nicaragua refers to the years 1993, 1998 and 2001.

Source: CEPAL (various years)

Suppliers within GPNs can use the closure of factories to curtail workers' ability to negotiate better real wages and working conditions. In some cases, success in unionization drives has ultimately resulted in the shutting of factories. The experience of workers in the Guatemalan factory *Camisas Modernas* between 1992 and 1998 constitutes one of the most dramatic cases[22]. Workers from the factory created a legally recognized union in 1992, but did not succeed in forcing the owner (the US shirt producer Phillips-Van Heuse, PVH) to negotiate a collective agreement. Their failure to secure the support from the Guatemalan courts moved the new trade union to embrace a transnational strategy. Together with the US Guatemalan Labor Education Project and with UNITE, the Guatemalan workers launched a media campaign in the US, which pressured both the company and its main buyer, J.C. Penny. After a long struggle, which even involved mediation from Human Rights Watch, PVH was forced to recognize the trade union and negotiate with it. The resulting collective agreement signed in 1997 resulted in a generous wage increase and some additional benefits (e.g. better medical services and subsidized transportation). As Armbruster-Sandoval (1999, 119) argues "the PVH workers and their allies defied the conventional wisdom about globalization and cross-border labor organizing and produced a stunning victory." The positive result was a great example of the development-friendly channel that I identified in the previous section. Yet the success was short-lived: in December 1998 PHV decided to close the plan and left all workers unemployed.

While capital mobility may be easier for foreign firms like PVH than for local ones, domestic suppliers are increasingly moving to cheaper neighboring countries as well. Nicaragua and Haiti are now favored destinations, given their low labor costs and geographical proximity. In the case of Haiti, for example, successful Dominican companies like Grupo M already moved the most labor intensive activities to export zones across the border several years ago.

The ability of firms to find new investment opportunities—even if they are themselves squeezed by TNCs and global buyers—and the existence of an expanding reserved army of labor has placed workers in a difficult position. Many of the gains that they can obtain through transnational alliances and labor codes are then lost by deteriorating structural conditions. The Dominican experience is again particularly illustrative. In the Dominican Republic, the long term impact of the Labor Code introduced in 1992 has been limited and trade unions remain weak. The National Wage Committee—a tripartite institution in charge of setting minimum wages—has seldom increased minimum wages above the accumulated increase in the consumer price index. Unionization rates have continued to drop (they were between 13 percent and 5 percent of the labor force in 2003 depending on the source) and trade unions do not have sufficient credibility within the working class. Moreover, the lack of political influence of trade unions has remained even during left-leaning administration. As the leader of one of the four trade union confederations puts it "the government does not take into account the demands of the labor movement. They listen much more to the business sector".[23]

[22] The following discussion of the case is based on Armbruster-Sandoval (1999) and Anner (2003).
[23] Interview with an official from the General Confederation of Workers (Central General de Trabajadores, CGT), Santo Domingo, June 2002.

5. Conclusion

This paper has mapped some of the political and economic consequences of Central America's participation in regional and global production networks. I have identified some processes that can result in positive change in labor markets but have also highlighted the difficulties at the economic level. Growing links between suppliers in Central America and US corporations have affected the way labor standards and industrial relations have been organized in Central America. Positive effects were maximized when the state used the external shocks to improve its regulatory capacity in the areas of industrial relations and social spending. Yet it seems evident that structural constraints constitute powerful obstacles for the consolidation of development-friendly long term paths. It is difficult to create better class compromises and secure more resources for the state when countries face difficulties to expand the value added they control. The growing difficulties of Central American countries to compete in the apparel sector and the negative impact of the global crisis on export growth are particularly illustrative of these economic obstacles—which also have an impact on political trajectories.

The identification of all these contradictory forces leads us to the identification of key policy challenges at the national, regional and international levels in Central America and beyond. At the national level, countries need to slowly upgrade their social and firm-level capabilities to sustain productivity growth (Paus, forthcoming). To do so, however, they may need to go beyond the East Asian model, which focused on dynamic state-capital relations and paid less attention to labor standards (Evans, 1995). Since most developing countries are unlikely to transform their economies as fast as East Asia did, they should find ways to strengthen labor rights and use wage growth to push technological learning and innovation in new sectors. The task will not be easy, given the temptation to compete only through labor costs and the pressures that governments face from traditional rentist elites.

At the regional level, social movements in the United States should find new, more creative ways to engage with developing countries and promote structural change. Shaming specific transnational corporations and its suppliers can promote some improvements at the micro-level, but may only have limited effects at the national level. Demanding greater labor standards in regional agreements without simultaneously creating incentives for economic upgrading will not contribute to better living standards either. Social movements in the North should instead simultaneously mobilize against poor behavior in global production networks and, at the same time, find ways to strengthen ties with social movements at the national level.

We should also gradually move the international agenda of development towards a more complex understanding of the links between political and economic transformation. Post-Washington Consensus reforms still focus on building an array of institutions to support free markets and formal democracy. The future agenda, however, must focus primarily on the creation of better jobs and more democratic labor relations. To do so, international institutions should focus on eliminating the most binding constraints that impede economic transformation in each country and should identify and strengthen those actors that can build more dynamic interactions between state and society. The task is not easy and change will be painfully slow but the ultimate results may be more democratic, equitable and sustainable than the ones we currently have.

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