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Building institutional capacity: from pervasive individualism to sustained coordination in small firm sectors

Abstract: The small-business sector faces a persistent dilemma: small firms often lack the human skills and financial resources to modernize and compete. How, then, can small firms overcome collective action problems to forge sector-wide modernization? This paper examines the political dynamics and the process of institutional change that underpin successful industrial upgrading through a comparative, longitudinal analysis of two policy experiments aiming at the modernization of small firm sectors in Portugal. Relying on comparative-historical analysis and process tracing, this study shows that successful industrial upgrading relies on intense and sustained political action, led by strong and stable interest leadership, in the pursuit of well-defined developmental benchmarks, and relying on the implementation of political, organizational and financial strategy according to a specific logic and sequence.

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1 Introduction

Over the past two decades, political economists have argued that cooperative industrial relations are critical for the successful modernization of small business sectors. Small firms often lack the human skills and financial resources to upgrade processes, technology, distribution, and marketing strategy. Studies on industrial development suggest that these problems can be solved by governance structures that promote mutual collaboration and that provide collective solutions for the problems of firms.¹ Well-organized and dynamic business associations can perform a fundamental role as industrial modernizers by providing collective support services that pool costs and improve the access of small businesses to resources. At a less formal level, social networks and personal links

¹ See Coleman (1988); Putnam, Leonardi, and Nanetti (1993); Boix and Posner (1998); Portes (1998); Hall (1999); Dasgupta and Serageldin (2000); Bartkus and Davis (2009).

among entrepreneurs stimulate information exchange and the dissemination of technical knowledge and updated business practices, and propitiate the development of trust and cooperative relations among entrepreneurs.²

Although there have been prolific writings on the mechanisms through which the involvement of stakeholders in structures of participatory governance and in active social networks promotes collective action, scholars tend to treat social and political institutions as pre-existing conditions of economic development. Very few studies have examined processes of development of strong social networks and effective business organization in settings where these social and political institutions did not exist previously, or where they existed but were unrepresentative and ineffective.³ My research tries to make a contribution to fill this analytical gap by examining the political dynamics involved in the development of institutions of business representation with the capacity to induce sustained and encompassing compliance with business support policy, in sectors without previous experience of dynamic interest representation and collective engagement.

It is important to examine this understudied problem, not only for theoretical reasons but also because it speaks to critical policy concerns. One of the great challenges policy-makers responsible for implementing industrial support policy face is to persuade entrepreneurs to trust and work with the supporting institutions. Policy designed to help small firms upgrade working routines and relational patterns does not automatically generate engagement, as is attested by the very limited outreach of public programs financed by the European Union for the modernization of small firms.⁴ Notwithstanding the availability of abundant

2 See Crozier and Friedberg (1977); Granovetter (1985); Scott (1988); Pyke, Becattini, and Sengenberger (1990); Pyke and Sengenberger (1992); Streeck (1992); Putnam, Leonardi, and Nanetti (1993); Emirbayer and Goodwin (1994); Locke (1995); Hollingsworth and Boyer (1997); Kristensen and Whitley (1997); Lane (1997); Boix and Posner (1998); Schmitter and Streeck (1999); Unger and van Waarden (1999); Casper (2000); Whitley (2000, 2007); Aggarwal (2001); Hall and Soskice (2001); Culpepper (2003); Djelic (2004); Love and Roper (2004); Schneider (2004); Shadlen (2004); Wellman and Berkowitz (2006); McDermott (2007); Evans (2008); Haar and Meyer-Stame (2008); Farrell (2009); Villa (2011).

3 For exceptions to this statement, see Sabel (1993); Shadlen (2004); Duvanova (2007, 2013); McDermott (2007).

4 It is estimated that SME-focused business support intervention reaches 10% of small firms in the UK and that this is a relatively high figure when compared to other countries in Europe. See Meyer-Stame and Haar (2008). For data on small firm insolvency in Europe, see Eurostat Pocketbooks (2006: pp. 14–15). Published online: http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-DH-06-001/EN/KS-DH-06-001-EN.PDF (accessed December 12, 2011). Also, see: http://ec.europa.eu/enterprise/policies/sme/business-environment/failure-newbeginning/policy_structure/support_for_policy_development/statistics_en.htm (accessed December 11, 2011).

financial support designed to promote industrial upgrading, the percentage of firms that have used the available resources and updated business practices is low and the rate of small firm insolvency remains very high in Europe.⁵ As stated by entrepreneurs and policy-makers involved in the management of the SME-targeted public support programs, the problem is that the majority of the small firms that need financial support to update processes lack the know-how and human skills to deal with the bureaucratic complexity involved in applying for support and are not represented by effective business associations that assist them with that task.

This paper examines how it is possible for business associations to reverse non-cooperative behavior and induce encompassing engagement of small firms with industrial upgrading policy. The central argument developed below is that successful industrial upgrading relies on intense and sustained political action, led by strong and stable interest leadership, in the pursuit of well-defined developmental benchmarks, and relying on the implementation of political, organizational and financial strategy, according to a specific logic and sequence. The study relies on comparative historical analysis and process tracing to identify key periods in that sequence, and examine the political, organizational and relational developments that characterize each period, how the developments of each period expand entrepreneurs' cooperation with policy and how the accomplishment of each developmental benchmark contributes for subsequent upgrading goals.⁶

The paper will make an account of the contrasting trajectories of two experiments with similar scope and aims of industrial reorganization in low-technology, atomized business sectors, in Portugal. The very similar industrial structure of the sectors under analysis at the beginning of industrial intervention contrasts with the subsequent trajectory of institutional development and the outcomes of the modernization effort. Thus, a comparative longitudinal study of the two cases offers excellent conditions to formulate a set of preliminary hypotheses on the political and institutional dynamics that influence industrial upgrading, and on the importance of the order in which specific kinds of political and organizational intervention are implemented in the process of change.

Portugal offers very good conditions for a comparative longitudinal analysis contrasting successful and failed industrial intervention. The country is known

5 This statement draws on many interviews I have conducted over the years with small business owners and managers of public policy targeting the modernization of SMEs. For literature supporting this claim, see Meyer-Stame and Haar (2008). Also see http://ec.europa.eu/enterprise/policies/sme/small-business-act/index_en.htm (accessed February 7, 2011).

6 As explained in the next section, this reasoning is inspired by Hall (2010).

for its long-lasting social anomie and historical legacies of weak and ineffective business associations – aggravated by four decades of authoritarian corporatism which lasted until 1974.⁷ Amidst the poor economic performance of many of the small firm sectors that make the core of the country's entrepreneurial fabric, there are exceptional cases of sectoral modernization, steered by business associations that provide the tools, skills, resources and strategy that allow firms to solve problems of scale and secure innovation and competitiveness. The analysis of unexpected cases of successful reorganization of business interests and industrial upgrading in this socially anomic national setting offers vital insights on the development of new institutional patterns – and societal dynamics – that deviate from the national model of capitalism, thus contributing for the literature on Varieties of Capitalism. The study will also engage the literature on social capital, regulatory politics and industrial development, as we will see next.

2 The importance of political sequence in processes of industrial upgrading

We know from a wealth of studies on political economy that the competitive character of economic activity and the different business goals and interests of entrepreneurs in any given sector create obstacles for collective action. Differences in size, corporate organization, end-product, geographical location lobbying capability, and in the age, academic background, core values and beliefs of entrepreneurs create obstacles for collective action.⁸ The literature reveals that these obstacles can be overcome by institutional mechanisms and social structures and explains why and how political and social institutions can facilitate cooperation among rival actors. Accordingly, structures of deliberation where stakeholders meet to discuss and vote on collective policy are very important, for several reasons. In ensuring inclusive and equitable representation of divergent interests in processes of decision-making, those structures reinforce the credibility of the actors who lead industrial intervention.⁹ Furthermore, the interaction

⁷ Economic historians generally agree on the backwardness of the Portuguese economy and on the structural weaknesses of the Portuguese productive system, i.e., the inability of most sectors to innovate and update technological methods of production and managerial practices. See Lopes (1996); Amaral (2002: p. 40); Royo (2002: p. 2); Lains (2003).

⁸ See Olson (1971); Offe and Wiesenthal (1986); Bowman (1989); Coleman (1990); Swenson (1991, 2004); Crouch (1993); Traxler (1993); Haydu (1999); Roy and Parker-Gwin (1999); Schmitter and Streeck (1999); Ostrom (2000: pp. 184 and 200).

⁹ Fung and Wright (2001).

of entrepreneurs in structures of sectoral governance and in social networks exposes them to new information that may change their antagonistic perceptions and facilitate consensus on the development of common policy tools.¹⁰ More generally, regular face-to-face meetings in the ambit of deliberation processes and in social networks stimulate mutual trust and exchange of information and this contributes to disseminate updated technologies and practices.¹¹ Interaction also facilitates the development of monitoring capacity by the leaders of interest representation – another element that scholars point out as essential for collective action: when stakeholders know that non-compliance with central policy can be detected and punished, the incentives to collaborate become very strong.¹²

Studies on corporatism suggest that state-led attempts at industrial reorganization tend to be ineffective and fail to stimulate new social and organizational behavior, precisely because of problems related to the inadequacy of interest representation.¹³ Accordingly, corporatist arrangements tend to reproduce disproportionate distribution of resources and antagonisms in a given sector and this leads to a continuity of internal conflicts that impede cooperation.¹⁴ Structures of business representation that rely on the state for financing and/or staffing are also particularly vulnerable to corruption and state capture.¹⁵ While business association leaders have direct stakes in their sector and have inside knowledge on how business works and on the problems and needs of firms, politicians and civil servants are not directly in a position of ownership and this means that the structure of incentives and the informational resources differ between state- and associational-intervention.

Although the existing studies provide a lot of information on the institutional mechanisms that overcome the problems that the actors who lead industrial reform confront when trying to enforce common policy, and on the problems of excessive state interference with business organization, the literature does not offer sufficient information on the processes that underpin the effective reorganization of interest representation providing structures of business support, in contexts dominated by long-lasting individualism and weak and unrepresentative

10 Crozier and Friedberg (1977); Fung and Wright (2001); Varanda (2005). Also, see Schmitter (1981); Streeck (1992); Hall and Soskice (2001); McDermott (2007).

11 Useem (1984); Offe and Wiesenthal (1986); Bowman (1989); Ostrom (2000); Fung and Wright (2001); Evans (2004); Martin (2005); McDermott (2007); Hall (2010).

12 Olson (1971); Crozier and Friedberg (1977); Bowman (1989); Sabel (1994); Ostrom (2000); Hall and Soskice (2001); Varanda (2005).

13 See Beyer and Hoepner (2003); Duvanova (2007, 2013).

14 McDermott (2007).

15 See Hellman, Jones and Kaufman (2000); Beyer and Hoepner (2003); Duvanova (2007, 2013).

business associations. Research in Varieties of Capitalism has only recently begun to focus on processes of institutional change, partly as a response to critiques of the static nature of the VofC model.¹⁶ There are almost no studies on sectoral institutional evolution and on the transformational dynamics that steer the emergence of unexpected organizational and relational patterns at the sectoral level which differ from the dominant industrial relations of a national Variety of Capitalism. Thus, we have little knowledge on how processes of decision-making and the goals of the actors who lead industrial reform and their mobilization strategy vis-à-vis stakeholders and the state evolve in processes of industrial reorganization.

Recent research suggests that one would expect these elements to change and that one would also expect a logical progression in the implementation of policy leading to successful organizational renewal. As stated by Peter A. Hall, scholars should make an effort at identifying key periods in that progression, dissect the institutional and political configuration of each period, and examine how each phase matters for subsequent developments.¹⁷ In other words, there is still significant work to be done to expand our knowledge on how the relationship between actors, institutions, and processes evolves in trajectories of successful industrial reorganization, and how such evolution differs from failed trajectories of sectoral adjustment. Are the elements of inclusive and equitable representation, active and encompassing deliberation, monitoring and sanctioning present and equally important at all stages in the progression from pervasive individualism and laggard business practice to effective interest reorganization and collective upgrading? How and when do coalitional politics and coercive strategy play a role in successful trajectories of change? Is the hands of the state important for effective sectoral reorganization? If so, at what developmental stages and in what ways is it important? How do relations between central and local structures of representation and between business leaders and stakeholders evolve in the process of industrial upgrading? Do we trace a specific political order and logic in the process? What are the explanatory links that characterize it?

The next two sections will investigate these queries by means of condensed historical narrative of the contrasting outcomes of attempted industrial reorganization in the wine and pharmacy sectors, in Portugal. I will first examine the unsuccessful attempt by the Portuguese state to intervene and steer the modernization of table wine producers in central and southern Portugal during the Estado Novo through the creation, in 1933, of a corporatist organization with the

¹⁶ Hall and Thelen (2009); Thelen and Mahoney (2010).

¹⁷ Hall (2010).

mission to reorganize the sector, i.e., the Federação de Vinicultores do Centro e Sul de Portugal (FVCSP). Secondly, I will trace the masterful reorganization of the pharmacy retail sector under the leadership of a new, voluntary business association created by a group of entrepreneurs – i.e., the Associação Nacional de Farmácias (ANF), at the onset of democratization, in 1974. I will compare the political sequence of both attempts at restructuring, showing how the contrast between the political approach in each phase and in both cases contributed for the divergent outcomes.

Although each of the restructuring experiments started out at a 40-year distance, the corporate structure and the social, economic, and political challenges faced by the small firms of the two sectors at the beginning of attempted industrial renewal were so strikingly similar that they allow for a solid comparative study.¹⁸ At the onset of their respective processes of reorganization, the wine and the pharmacy retail sectors looked alike in the internal organization of the firms and the economic and cultural characteristics of business practice – based on low skills and weak technical knowledge and technological resources; the small size of the large majority of the competing firms – nearly 2000 single-owned pharmacies and a similar number of micro-landowners involved in wine production in central Portugal, and a small number of large firms in both cases; and the corporatist restrictions on entry of new firms.¹⁹ The past legacy of inoperative interest representation, the mistrust of entrepreneurs vis-à-vis any attempt by state authorities or business leaders to intervene in the sector, the intense political uncertainty related to the beginning of a new political regime, and the clash between state interests and the interests of the small firms in the two sectors reinforced the similarity at the start of the reorganizing effort.

Notwithstanding the initial commonalities, the outcomes of intervention could not contrast more. The state-led Federation of wine-makers was short-lived and ineffective, unable to conquer the allegiance of producers and to stimulate the changes in culture and business practices that would be necessary to overcome economic backwardness and promote collective modernization and market expansion. The bottom-up design of a plan of collective modernization in the

18 For a similar kind of argument on the comparability of institutional experiments that unfold in different contexts, see Fung and Wright (2001: p. 17).

19 It is important to note that the timing of reorganization of the pharmacy sector, i.e., the onset of democratization, was not more favorable to inter-firm cooperation than the onset of authoritarianism had been for wine producers. Rather, the state had antagonistic interests vis-à-vis pharmacy retailers because of its nearly monopsony of the pharmacy retail market; furthermore, the socialist ideology that dominated the transition to democracy and the threat of nationalization intensified entrepreneurs' fear, suspicion and mistrust vis-à-vis policy intervention.

pharmacy sector became an outstanding example of the societal making of a robust voluntary business association, with exceptional institutional strength, instilling sustained coordination among a large number of small firms and culminating in the sweeping modernization of a sector that had inherited weak social ties and lacked experience in collective problem-solving.²⁰

Ideally, one would choose to compare cases that intuitively seem more alike, but I had access to detailed and unique information on the political action involved in the attempted restructuring of these two sectors which was ideal for a comparative longitudinal analysis addressing the theoretical queries on political sequencing stated above. The information on these two cases is one of its kind and existing studies on industrial restructuring could not be used to expand analysis because they do not offer sufficient detail on the political sequence that has underpinned modernization. Future research will allow to extend the preliminary comparison and to generalize the findings presented here.

3 The failure by the state to induce cooperation in the wine industry

At the onset of the authoritarian corporatist regime, in the early thirties, the wine growers of central and southern Portugal were responsible for producing the largest quantity of table wine in the country. Like cereal production, wine production was as an essential part of the country's agricultural activity, which contributed significantly for the national GDP and for national exports, engaging half of the working population.²¹ Table wine production, distribution and sales were important not only for the economic survival of thousands of micro landowners and large farmers but also for providing employment. State authorities hence perceived the sector as vital for social peace and for the consolidation of the political regime at the local level.²²

As happened in the case of the micro-firms of other traditional sectors, wine growers confronted critical challenges and were not prepared to respond

²⁰ The analysis of the pharmacy retail sector is based on my own field work, drawing from 70 semi-structured interviews with business association leaders, firm owners, leaders of complementary sectors – namely pharmaceutical producers and distributors – and with former Ministers and Secretaries of Health (Evans 2008). Analysis of the case of wine producers draws from the historical research conducted and published by Freire (2002, 2010).

²¹ See Freire (2010: pp. 20, 26).

²² *Ibid.* 18.

to up-and-coming international competition. Illegal practices and unfair competition were rampant and strived on the state's lack of accurate information on business dealings. The relation between quality and the price of wine was poor. Many producers had inherited the land from the previous generation and did not have the knowledge and financial resources to respond rapidly to technological change and to invest in upgrading vineyards with new, selected, castes and the adoption of modern production and storage techniques so as to improve the quality of wine. The micro-firms also lacked the capability to coordinate and establish effective distribution channels. Entrepreneurs were very individualistic and resisted any policy change and any external interference in their ways of doing business. The shrinking demand and the closure of international outlets under the Great Depression added to these problems in making it increasingly difficult for the producers to sell in international markets. Many were forced to reduce activity and this contributed for social disruption, by increasing unemployment and lowering salaries. The populations of the affected areas expected that the government would enact economic and social policy so as to address these problems and criticism to the new political regime started to build up.

On October 1931, wine growers from the city of Torres Vedras in the center of Portugal formed a committee with the support of shopkeepers, public servants and liberal professionals from neighborhood cities, with the goal to pressing the government for the establishment of a corporatist organization that would address the problems of the sector and defend the interests of producers. One year later, and after several meetings, the commission delivered the Minister of Commerce and Industry a draft proposal on the statutes for a new corporatist entity that would regulate economic and political activities in the sector.²³ The government agreed that it was necessary to intervene to help solve the problems of table wine growers and that the most adept way to do so was to establish a new institutional framework for market regulation and economic coordination in the sector. On November 1933, the *Federação de Vinicultores do Centro e Sul de Portugal* (FVCSP) was created by decree-law, with the mission to reorganize table wine production.

The legal act stated that the FVCSP had the task to create logistical and financial mechanisms to help producers improve the quality of wine, respond to fluctuations in national and international demand, secure access to new markets, and secure stable employment, salaries and comprehensive social benefits to workers. In order to do so, the FVCSP should intervene and impose the storage of excessive production in good years and enforce sales of stored wine during years

²³ See Freire (2002: p. 180).

of sparse output. This would curb the price instability caused by unpredictable weather conditions and by fluctuation in national and foreign consumption. The Federation was also assigned with the task to watch over and discipline illegal practices which disrupted the market.²⁴

Although the Federation emerged as a response to societal pressure, as manifested in the draft proposal by the Torres Vedras Committee, in reality the regime conceived this new corporatist structure as a tool for asserting its power at the local level. State authorities were convinced that the Torres Vedras Committee was dominated by republicans who opposed the regime. Because of this, the government did not appoint the leaders of the committee to the leading structures of the new Federation. Furthermore, the regime approached inspection activities as the engine of financial viability, a sign of organizational prestige, and the centre-piece of local control. From the outset of its existence, the Federation focussed almost exclusively on securing producers' compliance with successive bureaucratic decrees that regulated wine sales and that varied across localities. Until 1935, the activities of scrutiny were carried out by 240 inspectors who worked for the municipal *Grêmios*, i.e., local corporatist structures also created in 1933 to represent agricultural entrepreneurs at the local level, on the basis of product, in this case wine.²⁵

Like any new institution aiming to intervene in the daily activities of producers, the FVCSP met with resistance from its potential members. The conflicts became visible soon after the Federation was created. Important segments of the sector were excluded. Although the draft delivered by the Torres Vedras Commission to the Ministry of Commerce and Industry foresaw that the new, corporatist organization would represent all property owners in the sector, the legal act enacted by the National Assembly excluded 80% of producers, by establishing that only wine-growers who produced more than a specific amount of wine would be entitled to full membership and privileges. The state's intervention was thus primarily concerned with large producers and left out the thousands of micro-firms that made up the bulk of the sector.²⁶ Many members were unwilling to pay compulsory dues, upon which the new corporatist entity relied.

The proliferation of regulation on competitive practice led to great confusion, even among those who were in charge of enforcing the decrees, and the latter were virtually ignored by producers, who continued to engage in rampant malpractice. The leaders of the Federation suspected that the inspectors who worked for the municipal *Grêmios* were not enforcing the legislation and favored

²⁴ *Ibid.* 176, 183 and Freire (2010: p. 19).

²⁵ Freire (2002, pp. 183–187, p. 191).

²⁶ *Ibid.* 183–186.

their local friends. In 1935, the government withdrew the powers of inspection away from the *Grêmios* and hired a small number of inspectors who worked directly for the Federation. These new inspectors, who became known as the “motor brigades” because they traveled by motorcycle when patrolling business activity, were backed by police and by the National Guard. They focused on intercepting vehicles so as to charge fees and fines and were viewed by producers as “hunters” in constant search of the co-payments to which they were entitled as a reward for surveillance, and therefore seekers of personal benefit. The leaders of the municipal *Grêmios* considered it intolerable to have staff of the Federation ruling over them and frequently resigned because of that. This undermined institutional stability. There was no face-to-face interaction between interest representatives and the entrepreneurs. This added to the state control of the Federation and to the intense patrolling activities to play up the perception among producers that they were largely excluded from decision-making and that the Federation acted as an external agent chastening their behavior rather than offering a helping hand.²⁷

The Federation certainly did not secure the expected business improvements and this meant it had not fulfilled the economic goals that had steered its creation. By focusing intervention on the enforcement of administrative rules and fines, it did not help producers revise practices and routines. Wine growers responded by trying to escape fees, compulsory contributions, and the rules on distribution and sales. The costs of production remained high, prices continued to oscillate, entrepreneurs continued to be afflicted with the difficulty in placing wine in the market, and local employment and industrial relations were affected by all these problems. The consequent economic and social malaise led to waves of protest at the local level.²⁸

Without building adequate links between central authority, local representatives and producers, the FVCSP failed to establish strong grassroots, disseminate allegiance and help firms modernize and conquer new markets. The inability to meet the expectations of a sector that was vital for the national economy and the continuing noncompliance with regulation were interpreted by the regime as a sign of the failure of corporatist intervention at the local level and a sign of the institutional frailty of the Federation. On February 1937, the National Assembly dedicated two sessions to debating the action of the FVSCP and the state extinguished it in the same way it had created it, i.e., by Decree-law.

²⁷ *Ibid.* 187–192.

²⁸ *Ibid.* 178–9, 187, 192 and Freire (2010: p. 22).

4 The successful creation of social capacity in the pharmacy retail sector

At the onset of the democratic regime in Portugal, in 1974, there were nearly 2000 small pharmacies, spread all over the country. The prices of the core products they sold, i.e., medical drugs, were set by the state. The latter was the largest customer of pharmacies because social insurance funds provided partial coverage for medication prescribed to members. Although pharmacies were neither significant in terms of votes, nor as employment-makers, the sector was important for policy-makers because retail pharmacists played a vital role in the implementation of primary health care. Payments from social insurance funds to pharmacy owners were nevertheless invariably delayed and this caused serious financial shortages.

Most firms relied on low skilled and low paid employees to deal with the manipulation and sales of drugs. Employees' skills were acquired through apprenticeship rather than formal training. Administrative tasks weighed particularly heavily on daily routines, because the increasing number and diversity of medical drugs exacerbated the complexities associated with co-payments. There were frequent out-of-stocks, and, as happened in the wine sector, there was widespread non-compliance with regulation. Pharmacies located near large public institutions and large firms negotiated quantity discounts on bulk sales, so as to secure clients. This was illegal competitive practice. Often workers worked without the supervision of a licensed pharmacist, and this was illegal too.

Pharmacies needed to update vocational training, stock management and supply systems, so as to tackle those challenges and improve quality of service. In order to have the financial capability to invest in these spheres, pharmacists needed to receive timely payments from social insurance funds. But this would not happen without effective political pressure. The corporatist *Grémio das Farmácias*, created in 1933 to organize the sector, played a very limited role in interest representation. In essence, it conveyed information to business owners on administrative duties, labor agreements and the regime of co-payments by social insurance funds. State scrutiny over its activities was tight and the Grémio lacked decision-making autonomy. Although authorities heard its leaders in the process of administrative authorization for the establishment of new pharmacies and in the ambit of legislative projects and National Plans of Development (*Planos de Fomento*), inclusion did not mean more than polite and inconsequent consultation.

After the authoritarian regime was toppled in April 1974, the provisional government decreed the dismantling of the state-controlled organization of sectoral

representation via the corporatist *Grêmios*. The latter were to cease activities and entrepreneurs were to devise new structures of representation in accordance to democratic principles, i.e., business associations relying on voluntary, rather than compulsory, membership, and with autonomy from state financial and political control. Retail pharmacists held a national assembly to discuss the reorganization of interest representation in the sector. A group of recently graduated pharmacists invited colleagues from all regions, political tendencies, age and gender, as well as leaders and opponents of the old *Grémio* to join them in a constitutive committee that would design the new structure of business representation. The committee was generally perceived as representative of a compromise between all factions and interests in the sector, and, on October 1974, pharmacists approved the statutes of the new business association it proposed, i.e., the *Associação Nacional das Farmácias* (ANF).

The young reformers who led the transitional process were elected for the national leadership structures of the ANF and started to work immediately on building tight relations and intense dialogue with rank-and-file all over the country. The new statutes endowed the national executive with ample decision-making powers, which the new leaders believed to be critical for dealing effectively with state authorities and for securing autonomy from factions in the sector. They also considered it essential to create routines of engagement of entrepreneurs in discussions and voting on common strategy aiming at strengthening the political and organizational strength of the sector. In their view, building regular consensus via deliberation was a necessary tool for legitimizing central authority, overcoming the pervasive tendency among entrepreneurs to resist external interference on business activity and securing thorough and updated information on the problems, needs and performance of firms. Once these aspects were in place, leaders would be able to mobilize collective action. The association hence started institutional life by establishing deliberative structures at regional and local levels.

The statutes of the association established that district delegates would be responsible for organizing district assemblies which were to operate with regularity as venues for deliberation. In 1975, district delegates, who were pharmacists themselves, started to organize local and regional meetings across the country, in which pharmacists discussed and exchanged information on business needs and problems. National leaders traveled on a weekly basis so as to participate in these events and discussed with entrepreneurs across the country the most urgent financial, operational and labor problems, and the most adept strategy for tackling them. The visibility of national leaders among rank-and-file contrasted with their determination to stay away from national party politics, except in one exceptional endeavor where they used the local structures to mobilize firms against

state policy that was straining their financial situation. State authorities imposed a 7% reduction on co-payments for medical drugs via the social insurance funds. The reversal of this policy provided an ideal, unifying, common cause to rehearse the political muscle and identity of the sector. It would bring immediate financial returns to members and contribute to change the antagonism against business associations that had remained pervasive since the times of the old Grémio.

In 1975, district delegates started to organize local and district meetings where they sponsored vivid debate on the impact of the imposed discounts on the financial situation of pharmacies. In August 1977, the sector deliberated on, and the majority of pharmacies carried out, a 1 day refusal to sell drugs unless with full and immediate payment. The government fell later that year, before finalizing negotiations with the association, and the ANF re-started negotiations with the new Minister of Social Affairs, threatening that members would carry out another national stoppage, if needed. The leaders backed their threat with technical reports and data on the activities of pharmacies and their financial problems, and on their role in the implementation of primary health care, most particularly in remote areas. The reformers claimed that, although the elimination of discounts would increase state costs in the short run, it would, on the other hand, improve the financial situation of firms and hence make it possible for retail pharmacists to expand their role and range of intervention in primary health care and to assist the state in the implementation of the new national health system. In 1979, the fourth constitutional government agreed to terminate the imposed price reduction on the co-payments from social insurance funds.

The financial implications of this political victory animated confidence among entrepreneurs and induced powerful incentives for subsequent compliance with strategy centrally devised by the ANF. The association was prepared to expand the scope of intervention, on the road to industrial reform. In 1980, and riding on the tide of political and financial gains, the national executive submitted new statutes to national voting, so as to create a disciplinary council with the power to punish non-compliance with policy approved in the ANF's deliberative structures. Sanctions ranged from heavy fines to suspension and even expulsion. The district delegates, with whom the national executive was in constant contact, were already monitoring the behavior of members closely. Underlying their stated mission to organize local structures of deliberation and mobilize and engage rank-and-file in discussion and deliberation, the delegates used their frequent interaction with colleagues to convey information upwards and to disseminate central decisions and persuade colleagues to support policy. They operated as local caciques, the privileged vehicles for central command-and-control – the new “brigades” of voluntary corporatism at the vanguard of sectoral revolution.

Having consolidated organizational strength, sectoral leaders were preoccupied with the economic challenges ahead. The expansion of pharmaceutical assistance following the creation of the National Health System in 1979 and the growing number and variety of medical drugs resulting of technological advances in the pharmaceutical industry were rapidly transforming the character of demand: patients were becoming more sophisticated, expected better service, and were less willing to accept inefficiencies, namely out-of-stocks. Increased consumption of medical drugs was also causing public health problems. The state expected that pharmacists played a role in assisting it with tackling these challenges and this implicated expanded business tasks and professional responsibilities. The small firms had to deal with a growing number of regulations, procedures, and duties and needed to adjust management skills accordingly. Small firms lacked the dimension and organizational and financial capability to acquire the tools that would allow them to deal effectively with these new demands and expanded workload.

The leaders of the ANF also expected that the upcoming entry of Portugal into the EC would aggravate the challenges small firms faced. The opening of markets would bring in multinational retailers. Pharmacists had to prepare for international competition by maximizing efficiency and by expanding their role to professional areas that would turn them into indispensable and unmatched agents in the implementation of public health care. This strategy would create a market niche and strong comparative advantage over potential competitors but it would not work unless a majority of firms engaged in it. Pharmacists could not be left alone in their passive individualism. The ANF created structures that shifted complex tasks from the unit to the associative level, making it possible for the small entrepreneurs to pool costs and enjoy economies of scale and rationalize internal and external corporate strategy, without changing corporate ownership and governance.

The association sponsored the creation of a cooperative that sold a single IT system for pharmacies, with the goal to standardize and automate accounting, billing, inventory, and replenishment practices. A central system was organized to provide technical-scientific information responding to any daily questions and doubts from retailers. The ANF also established protocols with academic institutions and vocational training centers, with the goal to centralize and standardize vocational training. In addition, the association signed protocols with the biggest Portuguese banks, in order to secure favorable conditions for capital investment in renovation, purchase of new equipment and materials, and in any areas that rationalized professional practice. In sponsoring the establishment of purchasing and distribution cooperatives, the association contributed for the development of cost-effective and well-timed links with wholesalers and for encompassing logistical renewal.

The ANF relied on intense politics to implement its organizational strategy. Pharmacists had to be convinced that the most cost-effective way to tackle their business problems and needs was by using the services provided by the association. National leaders used different channels of communication, so as to get the message across the sector. The journal of the association operated as the basic channel for disseminating regular and quick information on political strategy devised by the national executive, on the deliberations by district assemblies, and on benchmarks and tools for professional updating. It provided systematic, detailed coverage on technical-scientific issues identified as vital for improving quality. The association also created a forum where a group of dynamic entrepreneurs organized a series of national and regional debates involving policy-makers, academics, and foreign business leaders in the discussion of the most adequate means to respond to the challenges that loomed with economic integration. The goal was to actively engage retailers in the project of modernization and to constantly work on the consolidation of collective bonds and deep-rooted spirit of cooperation.

The collective structures organized by the association allowed small firms to overcome the problems related to small dimension, improving human and technology resources and management skills, pooling operational costs, rationalizing stock management and accounting practices, securing just-in-time supply and access to credit, as well as effective links with complementary sectors and constant access to updated technical-scientific information. By the early 1990s, when large retailers started to organize and press for entry in pharmacy retail sales, the majority of pharmacies had become modern and competitive firms, operating with efficiency, relying on qualified personnel, using sophisticated marketing techniques, displaying modern logistics, offering high quality service to consumers and providing quasi-public functions for the state in the domain of primary health care. Out-of-stocks had decreased dramatically, as had costs of inventory and replenishment, notwithstanding the accelerating number of products in the market and the growing administrative duties and responsibilities in the ambit of pharmaceutical assistance. Technical-scientific knowledge had improved, and so did customer satisfaction, as attested by public surveys. In short, the sector had adjusted to technological and social change and was prepared to face the forces of market integration without changing its traditional structure.

5 Discussion

The course of developments in the two sectors that were subject to examination speaks to the theoretical queries established in the beginning of this study. What

can we infer from the comparison? The success of the modernization programme of the pharmacy sector and its contrast to the failure of corporatist intervention in the wine sector allows us to make a set of claims on the political and institutional developments that underpin the success of industrial intervention, aiming at collective upgrading and on the order and logic involved in this process. The contrast between both cases suggests that successful organizational foundation, meaning the initial operation of a new institution formally endowed with the mission to reorganize business interests in a given sector relies on key political strategy of coalition-building. In the pharmacy sector, the preparations for institutional design – i.e., choosing the elements of the committee that would design the statutes of the new business association – included entrepreneurs that represented economic, geographic, social, political and market size variance in the sector. Inclusiveness was essential to make it crystal clear to entrepreneurs that the new association would represent and voice all interests and that smaller firms would be taken into account as were the larger enterprises that traditionally had more weight and access to policy-makers.²⁹

The analysis of the pharmacists' successful interest reorganization, in light of the contrasting fate of the wine producers also suggests that intense and continuous face-to-face interaction since the beginning of intervention between the actors who lead industrial reform and entrepreneurs is critical for allowing the former to display deep and unselfish personal commitment to solving the problems of firms. Decentralized structures of deliberation where entrepreneurs discuss common problems and vote on collective policy reinforce the credibility of intervention and endow business leaders with trust and authority. It is also clear from the pharmacists' case that participatory governance does not necessarily mean joint planning, strategizing and problem solving.³⁰ In fact, the national leaders of the new business association played a strong hand in the formulation of policy priorities and benchmarks and deliberation served mostly to legitimize the goals they had already established. Thus deliberative structures were part of a chain of persuasion that started at the central level and was reproduced downwards to district and local delegates and, ultimately, to members. These structures also served to provide information upwards, helping national leaders in identifying new benchmarks in the process of upgrading and in devising collective services that would allow firms to meet those goals.

The frequent, inclusive and personal debate between different levels of authority and at central and local levels was critical to convince entrepreneurs

²⁹ For the importance of these elements, see Fung and Wright (2001).

³⁰ Fung and Wright (2001: p. 20) have observed this.

they had an active voice in the project of collective restructuring. This pacified the negative perceptions about the ineffective and unrepresentative role of business association leaders that had lasted since the times of the old, statist *Grémio* and contributed for the development of collective identity bonds between associational leaders and rank-and-file. In turn, the economic payoffs that resulted from the early mobilization of entrepreneurs against the state-imposed discounts on quantity were vital for bringing identity activation into the subsequent benchmark of development, namely the expansion of central intervention to cover imperative business improvements. The increased revenues showed pharmacists that unity and coordination around central leadership provided important benefits that could not be attained individually. This allowed central leaders with the authority to organize the subsequent structures they deemed necessary for collective upgrading.

The effectiveness of extended intervention relied on widespread compliance with the new structures. Thus, the association created new monitoring and sanctioning mechanisms, in order to shepherd deviant firms into cooperation. Again, local agents – themselves entrepreneurs – played a critical role in this ambit, by maintaining intense, informal contact with other entrepreneurs and conveying information upwards to central leaders. The sanctioning powers of the association became evident, with the expulsion of pharmacists who refused to comply with important policy deliberated in general assemblies and the consequent loss of critical benefits, ranging from the loss of timely co-payments centralized in the ANF's factoring system to the loss of all services provided by the association for business improvement. By the 1990s, every policy decision by business leaders was immediately validated and engaged the members of the association who, until 2010, represented 95% of firms in the sector.

In the case of the wine makers, reform started top-down, by the strong hand of a new authoritarian government that was striving to assert its power at the local level. Rather than making an effort at including all stakeholders in the process of institutional design, the government marginalized the community leaders, local officials and entrepreneurs who had played an active role in pushing for industrial restructuring. This raised antagonism from local elites against the new corporatist structure of interest representation. Furthermore, by defining membership according to size and production, the state excluded most small producers from the new organization. Such lack of political effort to build consensus and to display fair and equal representation exacerbated rivalry and individualistic behavior. The alienation of producers was aggravated by premature and excessive discipline: the state focussed the initial period of intervention by enacting sanctions on illegal competitive practice and used the new corporatist structures to implement them, rather than according to their stated mission, i.e., to build

coordination among producers and facilitate collective upgrading structures. The untimely discipline undermined trust in the new structures and forestalled the creation of vertical flows of information. The wine Federation was perceived as an agent of the state that had no concern for the problems and needs of producers. The sector missed the phase of identity activation.

In short, the inattention to political strategy that would display inclusiveness and participatory governance, the lack of personal interaction between the leaders of the new corporatist structure and the wine producers, the absence of any visible benefits from membership added to chastisement and undermined the legitimacy and credibility of the Federation, obliterating any prospects for the emergence of trust. The insufficient political character of the early stages of reform prevented the development of institutional conditions that would allow for the organization of collective upgrading resources that were badly needed to improve the economic situation of firms, let alone a sense of collective responsibility for, and commitment to, industrial upgrading. The weaknesses of the new corporatist organization soon became apparent and restructuring did not go beyond a false start.

6 Conclusion

Previous work in political economy provides critical contributions on the incentives that facilitate cooperation among competing actors, but the literature is less fertile in characterizing the politics underpinning the successful restructuring of laggard sectors of small firms, in contexts of long-lasting individualism and resistance to policy intervention. This paper seeks to fill this gap. I have examined corporatist attempts at industrial renewal, in two sectors characterized by little, if any previous engagement in common projects, and by an evolutionary background of anemic interest representation and failed intervention. The cases were chosen so as to account for comparable stages of development, similar historical legacies, and identical socio-economic and political challenges. Their opposite trajectories reveal a lot on the political strategy that steers the movement from backwardness to successful industrial upgrading and tell us about the institutional developments that expand collective action in adverse social settings.

Both cases have comparative importance, as they illustrate the challenges faced by micro-enterprises in many other sectors of low-to-medium technological intensity. The successful reorganization of pharmacy retail in post-authoritarian Portugal illustrates the conditions that make it possible for new societal institutions to switch evolutionary paths and overcome long-lasting structural impairment, inducing high levels of inter-firm coordination in national

Varieties of Capitalism characterized by strong statist intervention, intense individualism, social anomy and poor economic performance. On the other hand, the failed attempt by the authoritarian regime to lead the reorganization of table wine producers reveals the setbacks of intervention through state corporatism. The ways in which the new Federation of wine producers lost ground illustrate the dynamics of assertion of the national government over the opposition of local elites as the authoritarian regime was striving to gain a foothold, suggesting that poor relations between central and local structures of governance undermine the consolidation of institutional grassroots and the success of corporatist intervntion.

What lessons can be drawn from the Portuguese case and the sectors under scrutiny? The Portuguese case makes a contribution to our knowledge on the political action involved in a process of dramatic social transformation, i.e., the development of coordination in settings marked by strong legacies of rivalry and individualism. By establishing a relation between the institutions identified in the political economy literature as conducive to cooperative endeavor and the political sequence that shapes processes of industrial renewal, I have tried to lay the groundwork for a more refined account of the conditions that influence collective action. The paper shows that the actors in charge of industrial reform can reverse adverse preconditions and induce sustained and encompassing coordination, by deploying skilful political and organizational strategy according to a logical order. The comparison developed above allows us to trace specific benchmarks in this process, each relying on specific institutional tools, and every one leading to expanded levels of cooperation and upgrading. Although the limited number of cases does not allow us to formulate a strict claim that this is the only one and necessary political sequence, they suggest that the identified phases and conditions are sufficient to secure similar outcomes in comparable settings. These insights will hopefully contribute to expanding our knowledge on the relations between political institutions and economic development.

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