
The William Davidson Institute Research Update

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You can subscribe to the WDI Research Newsletter at <http://listserver.itd.umich.edu/cgi-bin/lyris.pl?enter=wdi-friends> Please also feel free to contact Kelly Janiga at janigak@umich.edu with comments or submissions for future updates. Instructions to unsubscribe are located at the bottom of this report.

1. Secretary Albright Hosted WDI Roundtable to Develop Plan for Post-War Iraq

On May 22, the Davidson Institute's Distinguished Scholar, former Secretary of State Madeleine Albright, hosted a policy discussion of action plans to address the urgent need for a clear economic development strategy and speedy socio-economic stability for Iraq. The session was co-hosted by U.S. Representatives Henry Hyde and Tom Lantos, and included key Members of Congress, high-level Bush Administration officials, the international community, business leaders, and researchers.

The session refined a plan charting an economic course for Iraq that goes well beyond infrastructure and oil. The plan draws on the successes and failures of reform in transition economies, emphasizing the importance of small and medium size enterprise (SME) development and economic institutions. It promises not just to stabilize Iraq, but to deliver rapid and effective economic growth.

2. Davidson Institute Policy Papers

The Davidson Institute released the first paper in its policy paper series at the Iraq Reconstruction and Development Conference in Washington DC on May 22. The paper, entitled *A Strategy for the Economic Reconstruction and Development of Iraq*, authored by WDI executive director Jan Svejnar, outlines policy recommendations to best spur

economic growth and facilitate the transition from a command to a market economy. Emphasis was placed on establishing a functioning infrastructure, legal systems and institutions, a lesson learned from the transition economies of the former Soviet Union and Central and Eastern Europe. The need for stimulating Iraq's non-oil sector was stressed as necessary for job creation and a sustainable democracy and market economy. Professor Svejnar was one of the chief architects of the Czech Republic's economic reforms after 1989 and uses much of the expertise he acquired through this experience as background for this paper. The paper can be downloaded at http://www.wdi.bus.umich.edu/events/Post-War_Iraq_policy_paper.doc. For more information regarding our policy paper series, or if you would like to receive a hard copy of the paper, please contact Kelly Janiga at janigak@umich.edu.

3. Department of State Funded Research Competition

In April, the Davidson Institute, through generous support from the U.S. Department of State Title VIII program, was able to fund nine quality research proposals ranging from a study on Equity Market Integration and Development in Central and Eastern Europe to a study on the Development of Marketing Institutions for Women-Made Fiber Handicrafts in Kazakhstan and Kyrgyzstan.

We are happy to announce that the Davidson Institute recently learned it was again awarded Department of State funding at an even higher level for the 2004 fiscal year. This funding will be to support research in Central and Eastern Europe and Eurasia for the period of 2004-2007. We will be posting a call for proposals in the fall. Further information about the research funding will be included in upcoming newsletters and on the WDI website at a later date.

4. Upcoming Conferences

Annual International Conference on Transition Economics: July 3-5, Budapest, Hungary. The Conference is organized by WDI and the Center for Economic Policy Research (CEPR), and will be hosted by The Institute of Economics of the Hungarian Academy of Science (IEHAS) and the Economics Department of the Central European University. It will provide a forum for leading economists and other social scientists working on transition and on broader issues of development and institutional change to meet, present new research, develop collaborative relationships, and complete ongoing research. The conference will also bring together key policy-makers in the region with these researchers, facilitating discussion and exchange of ideas. More information is on-line at http://www.wdi.bus.umich.edu/events/Budapest_03.htm.

Political Economy of Transition: Job Creation and Job Destruction: August 14-17, Bonn, Germany. The conference, jointly organized by the Davidson Institute (WDI) and the Center for European Integration Studies (ZEI) will bring together approximately 15 established experts and promising young researchers to further the understanding of the job destruction and job creation process and their implications for political developments and institutional change in the post-communist countries. A tentative program for the conference is available at http://www.wdi.bus.umich.edu/events/PoliticalEcon_03.htm

Research Conference on Microeconomic Analyses of Labor Reallocation: August 21-23, Kalamazoo, Michigan. The conference is sponsored jointly by WDI, the Upjohn Institute for Employment Research, and the Institute for the Study of Labor (IZA) to promote applied research that uses micro-level data from a variety of economies, including the U.S. and other industrialized countries, as well as developing and transition economies. Conference information can be found at http://www.wdi.bus.umich.edu/events/Labor_Kalamazoo_03.htm

5. Call for Papers

Financial Market Development in Emerging and Transition Economies: December 15–16, 2003, Hyderabad, India. This will be the Fifth Annual Conference, hosted by The William Davidson Institute, The Indian School of Business, CIRFRA (Amsterdam Center for International Finance Research) at the University of Amsterdam and the International Review of Finance. This annual conference is a small gathering of researchers focusing on the evolution of financial markets and corporate finance practices in emerging and transition economies. The call for papers **deadline is August 30, 2003**. The complete call for papers is at http://www.wdi.bus.umich.edu/events/CallForPapers_India_03.pdf.

6. New Additions to WDI Working Paper Series

The following 36 recent additions to the William Davidson Institute **Working Paper Series** deal with a variety of transition issues. The abstracts can be found below the titles, or click on the http address to go directly to the papers on our web site.

No. 572: Private Savings in Transition Economies: Are There Terms of Trade Shocks?

Abdur R. Chowdhury

<http://eres.bus.umich.edu/docs/workpap-dav/wp572.pdf>

No. 571 : On the long-run determinants of real exchange rates for developing countries: Evidence from Africa, Latin America, and Asia

Imed Drine and Christophe Rault

<http://eres.bus.umich.edu/docs/workpap-dav/wp571.pdf>

No. 570: A re-examination of the Purchasing Power Parity using non-stationary dynamic panel methods: a comparative approach for developing and developed countries

Imed Drine and Christophe Rault

<http://eres.bus.umich.edu/docs/workpap-dav/wp570.pdf>

No. 569: How Important is Ownership in a Market with Level Playing Field? The Indian Banking Sector Revisited

Sumon Kumar Bhaumik and Ralitzza Dimova

<http://eres.bus.umich.edu/docs/workpap-dav/wp569.pdf>

No. 568: On Types of Trade Adjustment of Labor and Welfare Gains During Asymmetric Liberalizations

Yener Kandogan

<http://eres.bus.umich.edu/docs/workpap-dav/wp568.pdf>

No. 567: Technological Progress Through Trade Liberalization in Transition Countries

Yener Kandogan

<http://eres.bus.umich.edu/docs/workpap-dav/wp567.pdf>

No. 566: Intra-industry Trade of Transition Countries: Trends and Determinants

Yener Kandogan

<http://eres.bus.umich.edu/docs/workpap-dav/wp566.pdf>

No. 565: Local Protectionism and Regional Specialization: Evidence from China's Industries

Chong-En Bai, Yingjuan Du, Zhigang Tao, Sarah Y. Tong

<http://eres.bus.umich.edu/docs/workpap-dav/wp565.pdf>

No. 564: Corporate Governance and Market Valuation in China

Cong-En Bai, Qiao Liu, Joe Lu, Fank Song and Junxi Zhang

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No. 563: Revenue Sharing and Control Rights in Team Production: Theories and Evidence from China

Chong-En Bai, Zhigang Tao and Changqi Wu

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No. 562: Financial Dependence , Stock Market Liberalizations and Growth

Nandini Gupta and Kathy Yuan

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No. 561: Growth and Regional Inequality in China During the Reform Era

Derek Jones, Cheng Li, Owen

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No. 560: Choice of Ownership Structure and Firm Performance: Evidence from Estonia

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No. 559: Explaining Postcommunist Economic Performance

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No. 558: Tax Structures and FDI The Deterrent Effects of Complexity and Uncertainty

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No. 557: Provincial Protectionism

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No. 556: Nominal and Real Convergence in Estonia: The Balassa-Samuelson (dis)connection

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No. 552: So Many Rocket Scientists, So Few Marketing Clerks: Occupational Mobility in Times of Rapid Technological Change

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No. 551: Determinants of Interregional Mobility in Russia: Evidence from Panel Data

Yuri Andrienko and Sergei Guriev

<http://eres.bus.umich.edu/docs/workpap-dav/wp551.pdf>

No. 550: Gross Job Flows in Ukraine: Size, Ownership and Trade Effects

Jozef Konings, Olga Kupets and Hartmut Lehmann

<http://eres.bus.umich.edu/docs/workpap-dav/wp550.pdf>

No. 549: Technology Transfer through FDI in Top-10 Transition Countries: How Important are Direct Effects, Horizontal and Vertical Spillovers?

Jože P. Damijan, Mark Knell, Boris Majcen and Matija Rojec

<http://eres.bus.umich.edu/docs/workpap-dav/wp549.pdf>

No. 548: Does Foreign Direct Investment Increase the Productivity of Domestic Firms? In Search of Spillovers through Backward Linkages

Beata K. Smarzynska

<http://eres.bus.umich.edu/docs/workpap-dav/wp548.pdf>

No. 547: Re-employment Probabilities and Wage Offer Function for Russian Labor Market

Natalia V. Smirnova

<http://eres.bus.umich.edu/docs/workpap-dav/wp547.pdf>

No. 546: Democratization's Risk Premium: Partisan and Opportunistic Political Business Cycle Effects on Sovereign Ratings in Developing Countries

Steven Block, Burkhard N. Schrage and Paul M. Vaaler

<http://eres.bus.umich.edu/docs/workpap-dav/wp546.pdf>

No. 545: Structural Reforms and Competitiveness: Will Europe Overtake America?

Jan Svejnar

<http://eres.bus.umich.edu/docs/workpap-dav/wp545.pdf>

No. 544: Why the Rich May Favor Poor Protection of Property Rights

Konstantin Sonin

<http://eres.bus.umich.edu/docs/workpap-dav/wp544.pdf>

No. 543: Reinvested Earnings Bias, The "Five Percent" Rule and the Interpretation of the Balance of Payments – With an Application to Transition Economies

Josef C. Brada and Vladimír Tomšík

<http://eres.bus.umich.edu/docs/workpap-dav/wp543.pdf>

No. 542: The Impact of Ownership Reform in Chinese Industry, 1995-2001

Gary H. Jefferson, Su Jian, Jiang Yuan and Yu Xinhua

<http://eres.bus.umich.edu/docs/workpap-dav/wp542.pdf>

No. 541: Defensive and Strategic Restructuring of Firms during the Transition to a Market Economy

Domadenik, Janez, Prašnikar and Jan Svejnar

<http://eres.bus.umich.edu/docs/workpap-dav/wp541.pdf>

No. 540: Tenuous Financial Stability

Neven T. Valev and John A. Carlson

<http://eres.bus.umich.edu/docs/workpap-dav/wp540.pdf>

No. 539: Non-monetary Trade and Differential Access to Credit in the Russian Transition

Vlad Ivanenko

<http://eres.bus.umich.edu/docs/workpap-dav/wp539.pdf>

No. 538: International Price-Fixing Cartels and Developing Countries: A Discussion of Effects and Policy Remedies

Margaret Levenstein and Valerie Suslow with Lynda Oswald

<http://eres.bus.umich.edu/docs/workpap-dav/wp538.pdf>

No. 537: Foreign Banks in Bulgaria, 1875-2002

Kenneth Koford and Adrian E. Tschoegl

<http://eres.bus.umich.edu/docs/workpap-dav/wp537.pdf>

Abstracts of Recent Working Papers

No. 572: Private Savings in Transition Economies: Are There Terms of Trade Shocks?

Abdur R. Chowdhury

The paper examines the impact of terms of trade shocks on private savings in the transition economies after accounting for the effect of other determinants. Economic agents in the transition economies are subject to tight credit constraints which are more pronounced during bad state of nature. Thus, adverse shocks to commodity prices in the world market can force them to reduce savings by a larger amount than they would otherwise have. Empirical analysis using a dynamic panel model and data from twenty one transition economies confirm that most of the determinants of savings identified in the literature also apply to the transition economies. Favorable movements in both the permanent and transitory components of the terms of trade have a significant positive

impact on private savings with transitory movements having a larger impact than the permanent component. This reflects the lack of access to foreign borrowing that many of the transition economies have faced during the last decade. Although the impact of terms of trade shocks are found to be asymmetric, the magnitude of the impact appears to be small. The results are robust for alternative estimators, determinants, and country groupings.

No. 571 : On the long-run determinants of real exchange rates for developing countries: Evidence from Africa, Latin America, and Asia

Imed Drine and Christophe Rault

The main goal of this paper is to tackle the empirical issues of the real exchange rate literature by applying recently developed panel cointegration techniques to a structural long-run real exchange rate equation. We consider here a sample of 45 developing countries, divided into three groups according to geographical criteria: Africa, Latin America and Asia. Our investigations confirm that having a reference to assess the degree of distortion of real exchange rate is not as simple as it can be thought with the PPP concept. The real exchange rate is effectively at the centre of an economic spiral and its value depends on the economic specificities of each country. In other words, we don't have a fixed and general norm but, for each economy, the real exchange rate trajectory depends on its development level, on the way economic policy is conducted, and on its position on the international market.

No. 570: A re-examination of the Purchasing Power Parity using non-stationary dynamic panel methods: a comparative approach for developing and developed countries

Imed Drine and Christophe Rault

The aim of this paper is to apply recent advances in the econometrics of non-stationary dynamic panel methods to examine the robustness of the PPP concept for a sample of 73 developed and developing countries. Our investigations indicate that the strong PPP is verified for OECD and MENA countries. However in Africa, Asia, Latin America and the PECO, PPP does not seem relevant to characterize the long-run behavior of the real exchange rate. A widening of our analysis field shows that the nature of the exchange rate regime doesn't condition the validity of the PPP and that the PPP is more easily accepted in countries with high inflation than with low one.

No. 569: How Important is Ownership in a Market with Level Playing Field? The Indian Banking Sector Revisited

Sumon Kumar Bhaumik and Ralitzza Dimova

It has long been argued that private ownership of firms leads to better firm performance. However, theory as well as empirical evidence suggest that factors like agency problems may not allow privately owned firms to operate more efficiently or perform better than state owned firms. At the same time, it has been argued that competition and hard budget constraints can induce state owned firms to operate efficiently. In India, banking sector

reforms were initiated in 1992-93, leading to entry and other forms of deregulation, and a level playing field for all banks. Data for 1995-96 through 2000-01 suggest that by 1999-00 ownership was no longer a significant determinant of performance; induced by competition, public sector banks were able to eliminate the performance/efficiency gap that existed between them and domestic private sector and foreign banks.

No. 568: On Types of Trade Adjustment of Labor and Welfare Gains During Asymmetric Liberalizations

Yener Kandogan

This paper modifies the two-industry, two-country Heckscher-Ohlin model with intermediate goods to decompose trade into its horizontal and vertical intra-industry, as well as inter-industry parts. Acknowledging that liberalization affects each type of trade differently, and that changes in each imply labor adjustment of different magnitudes, the paper analyzes the effects of widely observed asymmetries in liberalization policies. The paper concludes with the implications of the model for the liberalization between the East and the West through the Europe Agreements.

No. 567: Technological Progress Through Trade Liberalization in Transition Countries

Yener Kandogan

Trade liberalization increases competitive pressures on domestic firms, and thus creates incentives for reducing costs of production through technological progress. Through this channel, backward countries get a chance to narrow their technological gap with more advanced countries. In this paper, the case of transition countries is analyzed. A simple model of oligopolistic firms' strategic decision on R&D is developed to motivate the empirical analysis. The results suggest that some initial conditions such as size of the initial technological gap, and initial openness to international trade, as well as the stage of the market reforms, in particular, rate of liberalization and structure of domestic markets are important factors in narrowing the technology gap.

No. 566: Intra-industry Trade of Transition Countries: Trends and Determinants

Yener Kandogan

This paper analyzes trends in different components of trade of transition countries. To explain the cross-country differences, the paper points out the important distinction between the determinants of inter-industry trade and intra-industry trade (IIT), and horizontal and vertical IIT. Using varieties of gravity models, it is shown that variables from Increasing Returns Trade Theory, such as scale economies, similarity of income levels, and number of varieties produced play important roles in IIT, especially in horizontal IIT, whereas factors such as comparative advantage, dissimilarity in income levels, and having more developed trade partners of Heckscher-Ohlin Trade Theory are crucial in determining inter-industry trade and vertical IIT to a lesser degree.

No. 565: Local Protectionism and Regional Specialization: Evidence from China's Industries

Chong-En Bai, Yingjuan Du, Zhigang Tao, Sarah Y. Tong

This paper uses a dynamic panel estimation method to investigate the determinants of regional specialization in China's industries, paying particular attention to local protectionism. Less geographic concentration is found in industries where the past tax-plus-profit margins and the shares of state ownership are high, reflecting stronger local government protection of these industries. The evidence also supports the scale-economies theory of regional specialization. Finally, the overall time trend of regional specialization of China's industries is found to have reversed an early drop in the mid 1980s, and registered a significant increase in the later years.

No. 564: Corporate Governance and Market Valuation in China

Cong-En Bai, Qiao Liu, Joe Lu, Fank Song and Junxi Zhang

This paper studies the relationship between the governance mechanisms and the market valuation of publicly listed firms in China empirically. We construct measures for corporate governance mechanisms and measures of market valuation for all publicly listed firms on the two stock markets in China by using data from the firm's annual reports. We then investigate how the market-valuation variables are affected by the corporate governance variables while controlling for a number of factors commonly considered in market valuation analysis. A corporate governance index is also constructed to summarize the information contained in the corporate governance variables. The index is found to have statistically and economically significant effect on market valuation. The analysis indicates that investors pay a significant premium for well-governed firms in China, benefiting firms that improve their governance mechanisms.

No. 563: Revenue Sharing and Control Rights in Team Production: Theories and Evidence from China

Chong-En Bai, Zhigang Tao and Changqi Wu

This paper presents a model of the joint venture that is grounded in the stylized facts we found from a sample of 200 joint venture contracts. The model incorporates the revenue-sharing contract into the incomplete contract frameworks of Grossman-Hart-Moore Property Rights Theory and the Transaction Cost Theory of the firm, and emphasizes the impact of expropriation. Joint control can be optimal as well as unilateral control. Our econometric analysis of the revenue-sharing and control arrangements offers strong support to our Property-Rights-Theory motivated model with self investment but rejects that with cooperative investment. The Transaction-Cost-Theory motivated model leaves some important empirical findings unexplained. Our findings also reject some of the existing theories of joint ownership.

No. 562: Financial Dependence , Stock Market Liberalizations and Growth

Nandini Gupta and Kathy Yuan

Stock market liberalizations provide a natural experiment to test for the causal relation between financial development and economic growth. We test this relation by investigating whether liberalizations facilitate growth through the particular mechanism of reducing capital market imperfections that drive a wedge between the external and internal cost of capital to firms. Using panel data on a large sample of emerging markets, we find no evidence of a uniform shift across all sectors in average industry growth following liberalization. Instead, consistent with the hypothesis that liberalizations lower the incremental cost of external capital, it appears that industries that depend more on external finance experience significantly higher growth following liberalization. We also find that growth occurs through the creation of new establishments, which is more likely to require external funds, rather than through an expansion in the average size of existing establishments, which firms are more likely to finance with internal cash.

These results are robust to alternative hypotheses, country and industry specific controls, other economic reforms, world business cycle effects, and contemporaneous macroeconomic shocks.

No. 561: Growth and Regional Inequality in China During the Reform Era

Derek Jones, Cheng Li, Owen

Chinese city-level data indicate that differences in growth rates are far more severe than indicated in previous studies which typically use data at higher levels of aggregation. We estimate growth equations using city-level data and find that the policy of awarding a special economic zone status enhances growth substantially, increasing annual growth rates by 5.5 percentage points. Annual growth rates of open coastal cities are, on average, 3 percentage points higher. Our qualitative results on the role of policy and the effects of FDI are similar to those of earlier studies that have employed provincial-level data; but, quantitatively, our results are substantially different. We also provide evidence of an indirect role of policy in the growth process through its ability to attract growth-enhancing foreign direct investment.

No. 560: Choice of Ownership Structure and Firm Performance: Evidence from Estonia

Derek Jones, Panu Kalmi, Niels Mygind

In this paper we use rich panel data for a representative sample of Estonian enterprises to analyse diverse issues related to the determinants of ownership structures and ownership changes after privatisation. A key focus is to determine whether ownership *changes* are related to economic efficiency. While employee owned firms are found to be much more prone than other firms to switch ownership categories, often “employee owned” firms remain “insider-owned” as ownership passes from current employees to managers and former employees. Logit analyses of the determinants of ownership structures and ownership changes provide mixed support for several hypotheses. As predicted: (i) wealth and resource constraints play a crucial role in the determination of ownership, with foreigners buying firms with the highest equity levels and insiders buying firms with

the lowest equity valuations; (ii) risk aversion explains subsequent ownership changes, especially away from employee ownership; (iii) allocation of ownership depends on the pre-privatisation origin and location of the firm, and these factors also influence subsequent ownership changes. Finally we compare our findings with those achieved by using

more conventional approaches to analyze efficiency that use very similar data. Reassuringly the evidence presented in this paper is consistent with the view that efficiency considerations drive ownership changes (while earlier analysis for Estonia and for many other transition economies has identified the impact of ownership on economic performance.) However, the findings in this paper also establish that there are important influences besides economic efficiency that affect enterprise ownership and ownership changes.

No. 559: Explaining Postcommunist Economic Performance

Lawrence P. King

Does Neoliberalism Work? Comparing Economic and Sociological Explanations of Postcommunist Performance

No. 558: Tax Structures and FDI The Deterrent Effects of Complexity and Uncertainty

Kelly Edmiston, Shannon Mudd, and Neven Valev

In this study we examine the connection between the varied experiences of the transition countries in attracting FDI and their diverse experiences in transforming their tax structures to be consistent with a market economy. In particular, we study whether complexity and uncertainty in their tax laws have deterred foreign direct investment by increasing transaction costs, the compliance burden and the unpredictability of tax liabilities. Our results indicate that complexity and uncertainty, in the sense of multiple tax rates, indeterminate language in the tax law, and inconsistent changes in the tax laws have a significant negative effect on inward foreign direct investment.

No. 557: Provincial Protectionism

Konstantin Sonin

In a federal state, the political leaders of constituent units might protect their enterprises from the federal center (e.g., allowing them not to pay federal taxes). The effectiveness of such protection depends crucially on the ability of local authorities to extract rents from enterprises. They can easily do so, if there is a small number of enterprises with large employment, and local monopolies can be effectively sustained. They cannot do it so easily if regional industry is competitive, political opposition is strong, and the federal center has enough means to enforce payment of taxes. We build a simple model to argue that it is the industrial structure of constituent units that determines political relations between them and the federal center. The theory is supported by the recent experience of Russia, China, and Argentina.

No. 556: Nominal and Real Convergence in Estonia: The Balassa-Samuelson (dis)connection

Balázs Égert

The objective of the paper is to analyse the nominal and real convergence process in Estonia drawing on the Balassa-Samuelson (B-S) framework. A 15-sectoral breakdown for GDP and a 5-digit level CPI data disaggregation with over 260 items is used for the period 1993:Q1 to 2002:Q1 to show that the productivity differential is related to the GDP-deflator relative price of non-tradable goods in the long-run. Furthermore, the role of regulated prices in the CPI basket is also investigated: we show that excluding regulated prices makes it possible to detect a robust relationship between productivity and the relative price of market services in CPI. The B-S effect could have possibly contributed to CPI by a yearly average of 2% to 3% over the sample period, with 1% to 4% at the beginning of the period and 0,5% to 1% in 2000 and 2001. The potential long-run impact of the B-S effect in Estonia is estimated to amount to 1%-2% . The analysis of the influence of the B-S effect on the inflation differential and the real appreciation of the exchange rate against Finland, Sweden, Germany and the UK shows that whereas the inflation differential attributable to the B-S effect seems to be higher in the early 1990s, it explains better the real appreciation, which has occurred in recent years.

No. 555: Banks-Firms Nexus under the Currency Board: Empirical Evidence from Bulgaria

Nikolay Nenovsky, Evgeni Peev and Todor Yalamov

This study analyses bank lending in the larger context of bank-firm relations within the Bulgarian specificity of currency board. It focuses on the ‘intersection’ of credit supply and demand on the side of banks and firms simultaneously. We suggest both traditional and new hypotheses corresponding to the specific conditions of the Bulgarian ownership change, transitional corruption and other institutional and political factors. The model is based on a survey on Bulgarian banks and a unique database on firms. The study found that the dynamics and structure of credit is affected mainly by the features of the institutional environment, whereas the ‘resource’ and traditional factors became secondary. During the period 1998 – 2001, there is separation of the banking sector activity from the activity of the real sector in Bulgaria. In the new conditions of currency board, the dual sector of enterprises and the specific institutional environment continue their existence. Despite its disciplining effect the currency board by itself is not sufficiently effective to overcome the remaining ‘institutional obstacles, associated mainly with the inefficiency of the judicial system, corruption, state capture, uncertain property rights, etc.

No. 554: To Steal or Not to Steal: Firm Attributes, Legal Environment, and Valuation

Art Durnev and E. Han Kim

Newly released data on corporate governance and disclosure practices reveal wide within-country variation, with the variation increasing as legal environment gets less

investor friendly. This paper examines why firms practice high-quality governance when law does not require it; firm attributes that are related to the quality of governance; how the attributes interact with legal environment; and the relation between firm valuation and corporate governance. A simple model, in which a controlling shareholder trades off private benefits of diversion against costs that vary across countries and time, identifies three relevant firm attributes: investment opportunities, external financing, and ownership structure. Using firm-level governance and transparency data on 859 firms in 27 countries, we find that firms with greater growth opportunities, greater needs for external financing, and more concentrated cash flow rights practice higher-quality governance and disclose more. Moreover, firms that score higher in governance and transparency rankings are valued higher in the stock market. Equally important, all these relations are stronger in countries that are less investor friendly, demonstrating that firms do adapt to poor legal environments to establish efficient governance practices.

No. 553: Corporate Stability and Economic Growth

Kathy S. He, Randall Morck and Bernard Yeung

Greater instability in a country's list of top corporations is associated with faster economic growth. This faster growth is primarily due to faster growth in total factor productivity in industrialized countries, and faster capital accumulation in developing countries. These findings are consistent with the view that economic growth is more closely tied to the rise of new large firms than to the prosperity of established large firms.

Although a stable list of leading corporations is highly correlated with government size, it is unrelated to other possible policy goals, such as (successful) income equalization and avoiding economic crises, it is related to other political factors. However, the list of top firms is more stable in countries with fewer rights for creditors in bankruptcy and with bank-based rather than stock market-based financial systems.

These findings appear to oppugn arguments of the form “What’s good for General Motors is good for America”. We propose that political rent-seeking by large established firms underlies increased corporate stability.

No. 552: So Many Rocket Scientists, So Few Marketing Clerks: Occupational Mobility in Times of Rapid Technological Change

Nauro F. Campos and Aurelijus Dabušinskas

The transition from centrally planned to market economy involves a process of massive occupational change that has been largely neglected in the literature. This paper investigates this process using data from the 1995 Estonian Labour Force Survey. We find that between 35 and 50 percent of wage earners changed occupations from 1989 to 1995 and that job tenure is a consistently important determinant of occupational mobility. Our results also show the speed with which the market mechanism takes root: the returns to current and alternative occupations play, over these few years, increasingly important roles in explaining occupational change.

No. 551: Determinants of Interregional Mobility in Russia: Evidence from Panel Data

Yuri Andrienko and Sergei Guriev

The paper studies determinants of internal migration in Russia. Using panel data on gross region-to-region migration flows in 1992-99, we estimate the effect of economic, political and social factors. Although overall migration is rather low, it turns out that its intensity does depend on economic factors even controlling for fixed effects for each origin-destination pair. People move from poorer and job scarce regions with worse public good provision to ones that are richer and more prospering both in terms of employment prospects and public goods. Migration is however constrained by the lack of liquidity; for the poorest regions, an increase in income raises rather than decreases outmigration. Our estimates imply that up to a third of Russian regions are locked in poverty traps.

No. 550: Gross Job Flows in Ukraine: Size, Ownership and Trade Effects

Jozef Konings, Olga Kupets and Hartmut Lehmann

This paper documents and analyses gross job flows and their determinants in Ukraine using a data set of more than 2200 Ukrainian firms operating in manufacturing and non-manufacturing for the years 1998-2000. Job destruction dominates job creation in both 1999 and 2000. Another clear-cut result of our analysis is the strong positive effect of new private firms on net employment growth. We also find an inverse relationship between job reallocation and size for both manufacturing and non-manufacturing, while only in the latter sector is employment growth inversely related with size. The main focus of the paper is the effect of trade flows on employment adjustment in manufacturing. Our results show that both employment growth and job reallocation at the firm and two-digit sector level are affected by strong exposure to import competition and product market competition in export markets. These effects are more pronounced when we consider trade flows to the world at large and to the EU than when the analysis is based on trade flows to the CIS.

No. 549: Technology Transfer through FDI in Top-10 Transition Countries: How Important are Direct Effects, Horizontal and Vertical Spillovers?

Jože P. Damijan, Mark Knell, Boris Majcen and Matija Rojec

The paper exploits a large set of more than 8,000 firms for ten advanced transition countries in order to uncover the importance of different channels of technology transfer through FDI and its impact on productivity growth of local firms. In addition to direct effects, we also distinguish between intra-industry (horizontal) and inter-industry (vertical) spillovers from foreign owned firms to local firms. After correcting for foreign investment selection bias and controlling for endogeneity of input demand (using a dynamic system GMM approach), direct FDI effects were found to provide by far the most important productivity effect for local firms in transition countries. Direct effects of FDI are found to provide on average an impact on firm's productivity that is larger by

factor 50 than the impact of backward linkages and by factor 500 larger than the impact of horizontal spillovers.

No. 548: Does Foreign Direct Investment Increase the Productivity of Domestic Firms? In Search of Spillovers through Backward Linkages

Beata K. Smarzynska

Many countries aim to attract foreign direct investment (FDI) by offering ever more generous incentive packages and justifying their actions with the expected knowledge externalities to be generated by foreign affiliates. Despite being hugely important to public policy, there is little conclusive evidence to support this claim. This study examines firm-level data from Lithuania in an effort to further our understanding of this issue. The empirical results are consistent with positive productivity spillovers from FDI taking place through contacts between foreign affiliates and their local suppliers in upstream sectors, but there is no indication of spillovers occurring within the same industry. The data indicate that local firms benefit from the operation of foreign affiliates both in their own region and in other parts of the country, albeit the evidence of the latter outcome is weaker. A larger effect is associated with domestic-market- rather than export-oriented foreign companies. There is no difference, however, between the impact of fully-owned foreign firms and those with joint domestic and foreign ownership.

No. 547: Re-employment Probabilities and Wage Offer Function for Russian Labor Market

Natalia V. Smirnova

This research addresses labor market transformation in Russia. It elaborates on the theory of job search and focuses on the following issues: (1) evaluation of the re-employment probabilities (hazard rates) for different socio-economic groups; and (2) estimation of wage offer distribution for the transforming labor market. We use data from Phase II of the Russia Longitudinal Monitoring Survey (RLMS) to estimate the employment and wage offer functions for Russian workers who found a job after having been unemployed. We take into account the effectiveness of search strategies used and correct for truncation in wage offers.

The binomial logit-OLS estimation method with sample selection bias correction on pooled data from Rounds 5-9 of RLMS is used. The factors considered are sex, education, experience, sector of employment and search methods' success rate, which are hypothesized to capture the main determinants of job search behavior. The results show that individual characteristics, as well as the search method used, play a decisive role in the re-employment prospects of the unemployed. The private sector employment level is estimated to have the most powerful positive effect on the wage offer function. Russian women are less likely than men to find a job after being unemployed, and wage offers for women are estimated to be lower than for men.

No. 546: Democratization's Risk Premium: Partisan and Opportunistic Political Business Cycle Effects on Sovereign Ratings in Developing Countries

Steven Block, Burkhard N. Schrage and Paul M. Vaaler

We use partisan and opportunistic political business cycle (“PBC”) considerations to develop a framework for explaining election-period decisions by credit rating agencies (“agencies”) publishing developing country sovereign risk-ratings (“ratings”). We test six hypotheses derived from the framework with 482 agency ratings for 19 countries holding 39 presidential elections from 1987-2000. We find that ratings are linked to the partisan orientation of incumbents facing election and to expectations of incumbent victory. Consistent with the framework, rating effects are sometimes greater for right-wing compared to left-wing incumbents, perhaps, because partisan PBC considerations with right-wing (left-wing) incumbents reinforce (counteract) opportunistic PBC considerations.

No. 545: Structural Reforms and Competitiveness: Will Europe Overtake America?

Jan Svejnar

Not yet available.

No. 544: Why the Rich May Favor Poor Protection of Property Rights

Konstantin Sonin

In unequal societies, the rich might benefit from shaping economic institutions into their favor. This paper analyzes the dynamics of institutional subversion focusing on one particular institution, public protection of property rights. If this institution is imperfect, agents have incentives to invest in private protection of property rights. With economies of scale in private protection, rich agents have a significant advantage: they could expropriate other agents using their private protection capacities. Ability to maintain private protection system makes the rich natural opponents of full protection of property rights provided by the state. Such an environment does not allow grass-roots demand to drive development of new market-friendly institutions (such as public protection of property rights). The economy as a whole is stuck in a ‘bad’ long-run equilibrium with low growth rate, high inequality, and wide-spread rent-seeking. The Russian ‘oligarchs’ of 1990s, a handful of politically powerful agents that controlled large stakes of newly privatized property, were the major motivation for this paper.

No. 543: Reinvested Earnings Bias, The “Five Percent” Rule and the Interpretation of the Balance of Payments – With an Application to Transition Economies

Josef C. Brada and Vladimír Tomšík

We show that the imputation of reinvested profits of the subsidiaries of foreign firms as a debit item on a host country's balance of payments account tends to overstate the current account deficit. We also show that, because of the workings of the FDI financial life cycle, this phenomenon is most evident for countries that have recently received large inflows of capital. The transition economies of East Europe certainly fall among such countries, and we show that, for the Czech Republic and Hungary, this imputation has a large effect on their reported current account balance. We verify the working of the FDI

financial life cycle using two different panels of developed, developing and transition economies.

No. 542: The Impact of Ownership Reform in Chinese Industry, 1995-2001

Gary H. Jefferson, Su Jian, Jiang Yuan and Yu Xinhua

During the 1980s, the restructuring of Chinese industry was driven principally by the entry of new enterprises into the enterprise system and by the restructuring of managerial incentives. In 1993, China's leadership formally inaugurated the shareholding experiment. This paper examines the impact on eight performance measures of the conversion of both state- and collective-owned enterprises to shareholding enterprises. The analysis distinguishes between the direct effect of conversion and the induced effect, involving the attraction of non-state investment, which reduces the proportion of state assets and state control rights. We find evidence for SOEs that both conversion and a decline in the share of state-owned assets motivate rising productivity and R&D intensity. While rising proportions of non-state assets motivate lower employment and rising wages, the initial conversion effect is associated with higher employment and lower wages. These latter impacts may result from agreements with workers as part of the conversion process. The SOE conversion process exhibits selection bias in which SOEs with high rates of capital productivity and profitability, high tax burdens, and comparatively low wages and smaller labor forces are more likely to be selected for conversion. No similar selection bias is evident in the collective sector.

No. 541: Defensive and Strategic Restructuring of Firms during the Transition to a Market Economy

Domadenik, Janez, Prašnikar and Jan Svejnar

We develop a theoretical framework and provide empirical estimates of the extent of several forms of restructuring in 130 privatized firms in a model transition economy (Slovenia) during the 1996-1998 period. In view of the institutional developments in the transition economies, we divide restructuring into defensive (related to short-term cutting costs) and strategic (focused on increasing revenues through investment). Using predictions from the theoretical framework, we estimate a firm-level labor demand equation to test defensive restructuring and an augmented investment equation to assess strategic restructuring. The labor demand estimates point to relatively slow defensive restructuring, while the investment model estimates indicate the presence of credit rationing and bargaining in most types of soft investment. We do not find support for the hypothesis that firms treat expenditures on employee training as investment, but there is evidence that they behave similarly as those from developed countries in that they display features of profit maximizing behavior.

No. 540: Tenuous Financial Stability

Neven T. Valev and John A. Carlson

Many countries fix their exchange rate in order to bring financial stability. Usually, inflation declines and output expands but contractual agreements retain their short time

frame, investment is sluggish, and economic growth slows down a few years later. This outcome is often attributed to persistent doubts on the part of agents in the commitment and ability of the government to maintain the peg. Yet direct evidence for credibility is difficult to obtain. Unique survey data from Bulgaria reveal that expectations of devaluation were indeed very much present three, four, and five years after that country achieved financial stability under a currency board regime.

No. 539: Non-monetary Trade and Differential Access to Credit in the Russian Transition

Vlad Ivanenko

The unusual rise and fall of non-monetary trade (NMT) in the Russian transition has been a subject of heated debates. Yet, this phenomenon is often viewed as a peculiarity that one cannot explain by economic considerations alone.

In this paper we show that the resort to NMT was a rational, albeit spontaneous, reaction of industrial enterprises to the outflow of liquidity, which in turn was precipitated by the combination of persistent budgetary deficit and strict monetary policy. The IMF pledge to stand by if the government became insolvent made this policy credible.

Several mechanisms contributed to the development of credit rationing of enterprises. First, the abandonment of implicit guarantees on loans extended to enterprises by the Central Bank of Russia prompted commercial banks to shift credit to other groups of borrowers. Second, when the Federal Government moved to finance its budgetary deficit through open-market operations, it crowded out commercial credit. Third, public money was transferred predominantly to households who partially lent it back to the government. Fourth, the policy of low exchange rate kept the balance of payment close to zero, which prevented the monetary base from growing.

The default of August 1998 constituted a clear structural break. It prompted modifications in monetary and fiscal policies. The collapse of the market for state securities led to widespread bank failures. The CBR abandoned its policy of non-intervention in fiscal affairs and cleared debts that the governments and enterprises accumulated. In addition, money supply expanded because increased inflows of foreign currency were incompletely sterilized. The combination of a lesser government presence at credit markets, clearance of debts, and increase in money supply injected liquidity in domestic producers and they abandoned NMT.

Statistical evidence supports the claim that NMT was caused by credit rationing experienced by enterprises. A GLS model with four explanatory variables (and dummies accounting for a structural break of August 1998) explains more than 90% of monthly changes in NMT for the period of February 1992 – December 2001. The collapse of the market for government loans appears to be the most significant event accountable for the structural break.

No. 538: International Price-Fixing Cartels and Developing Countries: A Discussion of Effects and Policy Remedies

Margaret Levenstein and Valerie Suslow with Lynda Oswald

The U.S. Department of Justice, the European Commission, and the Organization for Economic Cooperation and Development have all recently voiced concern about international price-fixing cartels. The U.S. and European Union have increased prosecution of international cartels in the past decade, but very few developing countries have made similar enforcement efforts. If these cartels have significant effects on developing country consumers and producers, the lack of antitrust prosecutions by developing countries against these cartels is an important problem. Geographically limited prosecutions may not provide sufficient disincentives to deter collusion that has worldwide benefits for colluding firms. Ongoing prosecutions of international cartels by industrialized countries may open up markets for entry by developing country producers, but these efforts may be undermined if cartels create durable barriers to entry. Western governments are also susceptible to manipulation by domestic producers using tariff barriers and anti-dumping duties to protect the home market, both during and after the price-fixing conspiracy. Thus, developing countries may need to develop their own antitrust laws and enforcement capabilities to help deter international cartel activity. A recent ruling of the Second Circuit Court of Appeals also opens up the possibility that developing country consumers may be able to exact remedies in U.S. courts.

In this paper we examine the possible effects of private international cartels on developing countries by looking in detail at three recent cartel cases, as well as at a broader cross-section of forty-two recently prosecuted international cartels. We discuss the indirect effects on developing country producers, either as competitors or co-conspirators, as well the direct effects of cartels on developing country consumers. By combining trade data with a sample of US and European prosecutions of international cartels in the 1990s, we are able to make a first attempt at quantifying the order of magnitude of the consequences of these cartels on developing countries as consumers. In 1997, the latest year for which we have trade data, developing countries imported \$54.7 billion of goods from a sub-sample of 19 industries that had seen a price-fixing conspiracy during the 1990s. These imports represented 5.2% of total imports and 1.2% of GDP in developing countries.

No. 537: Foreign Banks in Bulgaria, 1875-2002

Kenneth Koford and Adrian E. Tschoegl

We use the analogy of ecological succession as our conceptual framework. We apply this analogy to the history of foreign banks in Bulgaria and argue that the current predominance of foreign banks is unlikely to be permanent, even without government action. Foreign banks have entered Bulgaria several times—before World War I, again after that war, and after the fall of Communism in the early 1990s. The same source countries and even some of the same banks that were present before World War II or even World War I, reappear in the 1990s. Government concern with retaining control over credit limited the foreigners' role in the banking system. However, since 1997 the

government has privatized almost all the major banks with the result that foreign banks now control over 80 per cent of the banking system's assets.

The following are 14 recent additions to the William Davidson Institute **Working Paper Series** dealing with a variety of transition issues. The abstracts can be found below the titles, or click on the http address to go directly to the papers on our web site.

No. 536: Healthy Organizations and the Link to Peaceful Societies: Strategies for Implementing Organizational Change

Jeannette Jackson and Maria Coolican

<http://eres.bus.umich.edu/docs/workpap-dav/wp536.pdf>

No. 535: Workplace Violence and Security: Are there Lessons for Peacemaking?

Frances E. Zollers and Elletta Sangrey Callahan

<http://eres.bus.umich.edu/docs/workpap-dav/wp535.pdf>

No. 534: 700 Families to Feed: The Challenge of Corporate Citizenship

Tara J. Radin

<http://eres.bus.umich.edu/docs/workpap-dav/wp534.pdf>

No. 533: Governing for Genuine Profit

Michael J. O'Hara

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No. 532: Adapting Corporate Governance for Sustainable Peace

Timothy L. Fort and Cindy A. Schipani

<http://eres.bus.umich.edu/docs/workpap-dav/wp532.pdf>

No. 531: Groundings of Voice in Employee Rights

Dana Muir

<http://eres.bus.umich.edu/docs/workpap-dav/wp531.pdf>

No. 530: Gender Voice and Correlations with Peace

Terry Morehead Dworkin and Cindy A. Schipani

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No. 529: The Organizational Model for Workplace Security

Dr. Thomas K. Capozzoli

<http://eres.bus.umich.edu/docs/workpap-dav/wp529.pdf>

No. 528: Nationbuilding 101: Reductionism in Property, Liberty, and Corporate Governance

O. Lee Reed

<http://eres.bus.umich.edu/docs/workpap-dav/wp528.pdf>

No. 527: On Virtue and Peace: Creating a Workplace Where People Can Flourish

Caryn L. Beck-Dudley and Steven H. Hanks
<http://eres.bus.umich.edu/docs/workpap-dav/wp527.pdf>

No. 526: Novartis and the United Nations Global Compact Initiative

Lee A. Tavis
<http://eres.bus.umich.edu/docs/workpap-dav/wp526.pdf>

No. 525: Why Transition Paths Differ: Russian and Chinese Enterprise Performance Compared

Sumon Bhaumik and Saul Estrin
<http://eres.bus.umich.edu/docs/workpap-dav/wp525.pdf>

No. 524: Official Regulations and the Shadow Economy: A Labour Market Approach

Maxim Bouev
<http://eres.bus.umich.edu/docs/workpap-dav/wp524.pdf>

No. 523: Children at Risk: Infant and Child Health in Central Asia

Cynthia Buckley
<http://eres.bus.umich.edu/docs/workpap-dav/wp523.pdf>

Abstracts of Recent Working Papers

No. 536: Healthy Organizations and the Link to Peaceful Societies: Strategies for Implementing Organizational Change

Jeannette Jackson and Maria Coolican

Peace conference paper. *No abstract available.*

No. 535: Workplace Violence and Security: Are there Lessons for Peacemaking?

Frances E. Zollers and Elletta Sangrey Callahan

Workplace violence has captured the attention of commentators, employers, and the public at large. Although statistically the incidents of workplace homicide and assault are decreasing, public awareness of the problem has heightened, largely through media reports of violent incidents. Employers are exhorted to address the problem of workplace violence and are offered a variety of programs and processes to prevent its occurrence. However, many techniques intrude on workers' privacy in the name of making the workplace safer. We review the scope of workplace violence and a number of organizational responses to it. In so doing, we examine each for its potential to compromise privacy interests and attempt to strike a balance between security and privacy. We also examine the processes to determine their prospects for peacemaking. We find that processes that promote trust, participation, and dignity hold the most

promise for peacemaking. We submit that such structures and processes can be transportable beyond the workplace to promote peace locally, nationally, and globally.

No. 534: 700 Families to Feed: The Challenge of Corporate Citizenship

Tara J. Radin

When Howard Lutnick, CEO of Cantor Fitzgerald, was first interviewed after September 11, 2001, a tragedy that devastated his firm and stole the life of his brother, Lutnick stated that he now had “700 families to feed.” The view that he expressed was that his firm was responsible to the families of the wage earners lost in the tragedy, even though the firm was not responsible for the events that had occurred. Such assumed corporate responsibility, consistent with a stakeholder-based approach to management, is often considered to conflict with the law. The purpose of this Article is to demonstrate that stakeholder management does not inherently conflict with the law. In fact, principles of stakeholder thinking coincide with our moral intuitions, reflect many demonstrated best business practices, and promote profit-generation as envisioned and advocated by the law. This Article explores the nature of stakeholder relationships and their impact on business enterprises. The interconnected experiences of individuals and organizations in the wake of the events of September 11, while exemplary and perhaps more pronounced, are not isolated. The purpose of this Article is to draw upon such experiences in order to move beyond the traditional hub-and-spoke model of the firm, and to integrate past and present examples in a more dynamic, stakeholder-based model of corporate citizenship that bridges the gap between stakeholder thinking and the law and is both descriptive and normative.

No. 533: Governing for Genuine Profit

Michael J. O'Hara

Business corporations seek profit. That is, after subtracting cost, they maximize net revenue. Spillovers (both costs and benefits) involve trade-offs governing boards should make. Spillovers, especially when coupled with clumsy applications of discounted present value, distort a business' perception of profit. Today, businesses are buffeted by the old risks of recession and the new risks of terrorism. If modern society is to survive, then the seeds of terrorism and their fruit of tremendous loss must be contained. Accordingly, governing boards must propel businesses towards a paradigm of genuine profit. Governing boards must insist that their businesses prospect for positive feedback loops and implement a sustainable profit stream. In short, governing boards must insist that business be entrepreneurial.

No. 532: Adapting Corporate Governance for Sustainable Peace

Timothy L. Fort and Cindy A. Schipani

In previous work, we argued that there is a link between corporate governance and the reduction of violence. In this manuscript, we further explore that link with a focus on how corporations can work toward the goal of reduction of violence in the societies in which they operate. Here, we pose the question of how well suited various corporate governance regimes are to face these complexities, and how they can do so in ways that are consistent with their fundamental principles. We focus on the corporate governance regimes of the United States, Germany and Japan. A common denominator of the political entities addressed is a commitment to a political regime of democracy.

Section I outlines our thesis that corporations are in a position to make contributions to peace in society because of shifting political balances of power. It elaborates with the idea that our contemporary world has shifted from traditional balance of power conceptions in terms of the near universal embrace of parliamentary democracy requiring some reformulated description of the optimal relations among democracy, peace, and globalization. This section establishes the general parameters of the argument that democracy and peace are linked and that there are serious charges that globalization works against democracy and thereby threatens the sustainability of peace. Section II analyzes comparative models of corporate governance and considers the extent to which contemporary corporate governance models look to peace and workplace security as aims they should achieve. Concluding remarks follow in Section III.

No. 531: Groundings of Voice in Employee Rights

Dana Muir

No abstract available.

No. 530: Gender Voice and Correlations with Peace

Terry Morehead Dworkin and Cindy A. Schipani

The statistics regarding violence in today's society are staggering. A newly released study published by the World Health Organization, making headlines in the Wall Street Journal (Oct. 3, 2002) reports that "Violence Took 1.6 Million Lives in 2000." Notably, this report considers only the data obtained from the seventy countries that report such statistics to the World Health Organization. It does not include reports from many countries whose violence is also high, such as Burundi, Rwanda, Iraq, Liberia and Afghanistan.

This manuscript seeks to address some of these issues of violence by considering issues of gender. We pose the question whether there may be some correlation between violence and the lack meaningful involvement of women in the economy. If the countries that appear more violent are also countries where women are systematically excluded from business opportunities, perhaps one way to curb some of the societal violence would be to improve the opportunities for women in the economy. Multi-national corporations can play an important role in increasing these opportunities.

As has been argued elsewhere, a reduction in poverty promotes stability and leads to a more peaceful society. Studies show that in developing countries, involving women in the economy as wage earners can reduce poverty. As the locus of production shifts away from the home, an initial decline in employment opportunities may occur. However, this eventually disappears and both women and men benefit.

No. 529: The Organizational Model for Workplace Security

Dr. Thomas K. Capozzoli

The definition of workplace violence is a “any act of harassment (including sexual harassment), intimidation, threat, rape or homicide that takes place at a victim’s place of employment.” When the statistics for workplace violence are looked at, it is easily understood why workplace security is rapidly becoming a problem for many organizations. The situation that provokes workplace violence does not necessarily have to start in the workplace or and the act of violence does not necessarily have to happen in the workplace for organizations to be concerned.

Many organizations are just learning that violence can occur anywhere at anytime and they must be prepared to cope with the situation. This means they must take a look at their preparedness and decide what they need to do to not only increase preparedness but also to understand what procedures they do day to day that might affect a potentially violent situation. Organizations need to ask tough questions as to their hiring procedures, termination procedures, and security procedures. In today’s society, this increases from the aspect of global terrorism and how well are they prepared for the potential of a terrorist attack.

Security in the workplace will continue to be a concern but by following specific procedures and processes the risk of a situation happening can be significantly reduced.

No. 528: Nationbuilding 101: Reductionism in Property, Liberty, and Corporate Governance

O. Lee Reed

Nationbuilders in less developed countries need to understand how Western legal systems with "property" at their center have materially accounted for Western prosperity and liberty, but legal definitions of property are so abstruse that explication of this vital concept is made difficult. This paper finds an historical definitional essence to property in the right to exclude and maintains that liberty and property both share this essential meaning. The problems of corporate governance are then placed in the context of the exclusionary concept of property/liberty.

No. 527: On Virtue and Peace: Creating a Workplace Where People Can Flourish

Caryn L. Beck-Dudley and Steven H. Hanks

This article explores what virtues are necessary for human flourishing to occur in a business organization. In particular it argues that the virtue of peaceableness is missing from the current discussion of business ethics. It further argues that without peaceableness, human flourishing cannot exist. After an exploration of the connection between human flourishing and virtue ethics, the paper will look at the proposed virtue of peaceableness. In so doing, we will examine one dimension of peaceableness, i.e., freedom from conflict. In the discussion of freedom from conflict we will examine the case of Champion Paper Products, Sartel Minnesota Paper Mill, where management and labor, after a protracted labor conflict, jointly chose a proactive path toward peaceableness, resulting in significant improvements in human flourishing and organizational performance.

No. 526: Novartis and the United Nations Global Compact Initiative

Lee A. Tavis

The spirit of the Global Compact found fertile ground and has become an integral part of Novartis corporate strategy since the enterprise was formed by the merger of the two large Swiss pharmaceutical companies, Sandoz and Ciba, in 1996. Following a four-year concentration on economic consolidation and performance, Daniel Vasella (Chairman and CEO) signed the Global Compact. Together, productivity-based economic performance and a proactive approach to the expectations of society are envisioned as the key to long-term corporate success in the rapidly integrating global economic, political, and social environment of today's large multinational corporation.

This paper outlines the Novartis strategy and its implementation including the coalescing role of the Global Compact in the drive for sustainable corporate development. Following a review of extending corporate strategy to incorporate social concerns into the economic business model, the process of implementing the strategy will be assessed. In part three, specific examples of this strategic positioning will be outlined.

No. 525: Why Transition Paths Differ: Russian and Chinese Enterprise Performance Compared

Sumon Bhaumik and Saul Estrin

We use enterprise data to analyse and compare the determinants of enterprise performance in China and Russia. We find that in China, enterprise growth and efficiency is associated with rapid increases in factor inputs including management, as well as TFP, but not greatly associated with ownership or institutional factors. In contrast, sales growth in Russia is not associated with improvements in factor quantity (except for labor) or quality; TFP is not influenced by competition and privatization to outsiders does not

enhance company performance relative to insider ownership. The main determinants of TFP are instead demand and institutional factors at a regional level.

No. 524: Official Regulations and the Shadow Economy: A Labour Market Approach

Maxim Bouev

This work revisits the role of regulations in emergence of the shadow economy. In particular, it supplements the previous theoretical research that mainly ignored the fact that the decision to “go underground” is essentially a result of both employers and employees interacting in the labour market. We adapt a job search approach (see, e.g. Acemoglu 2001) to model a transitional economy with an informal sector. We apply and develop the idea first documented inter alia by Loayaza (1996) that there are two types of regulations that influence the size of the informal labour market through two different channels. Red tape and bureaucratic extortion (bribing) make starting a new business officially a not very attractive option and can lead new firms to the informal sector. On the other hand, taxes and redundancy pay make official firms offer lower wages which drives potential employees away into underground jobs. Depending on various combinations of policy parameters equilibria with different share of the informal economy are possible. The paper draws conclusions regarding the role of unemployment benefits in reducing the size of the informal economy. Policy implications are offered.

No. 523: Children at Risk: Infant and Child Health in Central Asia

Cynthia Buckley

Using Demographic and Health Surveys, government statistics, and field observations I examine trends in infant and child health in Uzbekistan, Kazakstan and the Kyrgyz Republic. Health indicators (anemia and marked bw weight for age) for the population under the age of 3 are examined nationally, regionally and by ethnic groups. Findings indicate the risk of compromised child health varies by ethnicity, but the effect is dramatically lessened by the introduction of household and maternal controls such as parental education, residence, and mother’s health status. Findings highlight the social costs of transition, illustrate the importance of maternal health across the region, and assist in the identification of groups at highest risk for poor child health within individual countries.

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