AN ALTERNATIVE MODEL FOR FILIPINO PRODUCTION RELATIONS

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I. INTRODUCTION

At the present juncture the Philippines can hardly be considered sovereign in economic matters. Reeling from a foreign debt of nearly $29 billion, she has to accede to conditions imposed by her creditors. The structural adjustment and stabilization programs of the International Monetary Fund are particularly onerous. In exchange for special financing, the Philippines must swallow a package of inflationary devaluation, high interest rates (and the unemployment they bring), lower government spending—hence less social services—wage and labor repression, and heavier taxes.

Such a servile posture is largely a function of the economy's internal weakness. Sluggish production and a relatively anemic local market react together to foster external dependence.

As such, the attainment of economic sovereignty requires the pursuit of internal strength. A nation enjoying the fruits of high growth, full employment, self-reliance and social justice will not have to bend the knee to foreign capital. She will not submit to conditions dictated an ocean away. She will not lose dignity through a stance of perpetual mendicancy.

Internal strength in turn demands fundamental changes which require substantial political will. They come easily to mind and can be considered revolutionary. One is the overhaul of present debt policy to relieve the interest burden, a virtual hemorrhage on the economy. Another would be a thorough, radical, and genuine agrarian reform which does not sacrifice productivity. A third would include a drive for industrialization, of both the rural off-farm mode and that symbolized by smokestacks and steel. Then there is the need for massive education reform, to pave the way for the leap into progress.

These and others in the long agenda are all familiar and sweeping in their perspective; they scan the macro picture. Scant attention has been directed, however, at the micro level. This paper focuses

on the latter and perceives that internal economic strength can also be enhanced through reforms here. In particular, it is claimed that aggregate growth as well as equity may be advanced through changes in the firm. The micro does matter; it does alter the face of the macro.

This paper argues for direct worker ownership of firms. It serves as a means to promote productivity and equity, as the evidence reveals. However, before delving into the intricacies of the concept, it would be expedient to dwell on the macro problem of mode of production.

II. THE CHOICE OF MODE OF PRODUCTION

The advantage of the command economy or state socialism is its ability to ensure equity and justice in the population. But its ills are also well known. It is virtually impossible for government technocrats to know all the nuances of consumer demand. As such, attempts by planners to fix specific output quotas often result in shortage or gluts, as supply does not correspond to demand. Hence the empty market shelves and long queues ridiculed in American caricatures of the Soviet economy. Moreover, the lack of competition fosters lethargy in production, as gleaned by poor quality and the absence of creativity. The quota system itself has an enervating effect in the factory. Workers are hesitant to greatly exceed their quotas, knowing that the state would likely raise them in that event. In general, the government's heavy hand in the economy results in restrained production as well as limited consumer choice. Mass welfare is neglected by the controls.

The main boast of laissez faire capitalism is that the free market does a superior job of controlling itself than any centralized authority could possibly do. It can be regarded as a wonder because it efficiently arranges the activities of myriad individuals and firms though no coordinating agency could have direct knowledge of all the complicated details.

Summarized quite simply, the framework says that each person or company is free to buy and sell in the market. Every buyer will seek the lowest possible price, every seller will sell at the highest attainable price. (This holds true for human labor just as for goods at the shelves.) It will always be profitable to manufacture and sell the items that most people desire. If there is merely weak de-

mand for a particular commodity producers will have to stop offering it. They will turn instead to manufacturing goods that people want to buy. As such, the market will signal enterprises about what it wants to be produced. If a company cannot adjust to such signals it will go bankrupt. The workers and machines it has been using will thus become available for other enterprises more attuned to consumer demand.

Prices will have a tendency to fall in a competitive environment, for each company will try to manufacture and sell its goods at lower prices in order to underbid rivals. There hence exists compelling pressure to cut costs and to produce more efficiently. This discipline of the market thus helps to make sure that the economy is responsive to the consumers, while enforcing efficient production.

The free market has also helped spur people to save and pool their funds in order to invest in more modern and productive machinery and factories. By allowing people to accumulate private wealth, the system encourages them to keep expanding the productive capacity of the economy.

Economists from all shades agree that capitalism has been immensely productive. Marx and Engels write in their *Communist Manifesto* that capitalism "has accomplished wonders far surpassing Egyptian pyramids, Roman aqueducts, and Gothic cathedrals; it has conducted expeditions that put in the shade all former exoduses of nations and crusades." The problem lies in the question of equity.

From the very origins of capitalism there has been a long debate over whether or not the system of laissez faire worsens existing poverty. Baran and Sweezy sum up the argument of the critics: "as Marx pointed out in *Capital* and as the experience of the subsequent century of capitalist development has confirmed again and again, capitalism generates wealth at one pole and poverty at the other." This principle of capitalist development results in a vast number of people eking out a living below the subsistence minimum, while a minority grows more and more wealthy.

The real issue may be what is happening to people in a relative measure. Both critics and supporters of capitalism could readily concur that relatively there exist wide gaps between the poor and rich in the system. The issue is whether or not this matters. The

laissez faire capitalist will likely warn society not to divide the economic pie more equally. Such an act may shrink the pie because of the problem of incentives. Many laissez faire advocates regard social equality as both undesirable and unachievable.

It will startle many that some economists have concluded that in the long term, capitalism has been a societal equalizer. The ultra-conservative Milton Friedman asserts that "capitalism leads to less inequality than alternative systems of organization and ... the development of capitalism has greatly lessened the extent of inequality."

A less notorious economist, Joseph Schumpeter, has arrived at basically the same conclusion. Schumpeter observed that relative shares of national income had remained fairly constant for the previous century. But his figures concern income measured in money terms. As regards actual consumption, "relative shares have substantially changed in favor of the lower income groups." His argument is worth quoting here:

"This follows from the fact that the capitalist engine is first and last an engine of mass production which unavoidably means also production for the masses, whereas, climbing upward in the scale of individual incomes, we find that an increasing proportion is being spent on personal services and on handmade commodities, the prices of which are largely the function of wage rate. ..."

There are no doubt some things available to the modern workman that Louis XIV himself would have been delighted to have—modern dentistry for instance ... Queen Elizabeth owned silk stockings. The capitalist achievement does not typically consist in providing more silk stockings for queens but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort ... the capitalist process, not by coincidence but by virtue of its mechanism, progressively raises the standard of life of the masses.

That is an argument with substance, and every critic of capitalism should consider it. But the view has to be seen on balance. Recall that without much government involvement even this utopia of mass-production would not be achievable. This holds as production under a laissez faire framework cannot transpire without a market. Most economists agree that heavy government involvement is imperative to sustain market demand. Land reform and pump-priming activities come readily to mind.

Take note also that a purely laissez faire economy would exclude some people altogether. If purchasing power is based primarily on income derived from selling goods or labor, then the market is a desolate place for those who must buy for survival but have nothing to sell. Even in the United States, despite the presence of social welfare programs that extend far beyond the confines of laissez faire, there exist 24 million people with family incomes below the poverty line. Mass production may indeed boast of actual egalitarian effects. But that is no good for people who lack the money to buy the products. In the democracy of the marketplace where the consumer is sovereign, some have far more votes than others.

Therefore, while not dismissing the claims of Schumpeter and Friedman, one must conclude that a laissez faire economy would hardly be egalitarian.

Then there is the issue of wealth accumulating disproportionately in the coffers of an elite enclave. The distribution of wealth has indeed remained basically unchanged for the past few decades. Without radical government intervention there is little basis to expect wealth in the Philippines to become more evenly distributed. And under a laissez faire system there would be absolutely no ground to hope for this. That is precisely the problem that Marxism has attacked with its analysis of surplus value. Wealth generated by the workers is milked off by the capitalists in the form of profit.

One may summarize the lasting contributions of laissez faire as follows: 1) the awareness of the significance of economic freedom initiative and creativity; 2) the market mechanism which, with all its flaws, provides useful mechanisms for cost accounting and resource allocation, and 3) institutionalized concern for the welfare of private consumers.

All three of these are positive attributes. But when taken as a whole and constructed into an absolute system of laissez faire, they foster a callous blindness to devastation by greed and the anarchy of uncoordinated economic activity. In sum the market mechanism may be a very productive servant but it is certainly a tyrant of a master. Social market capitalism is an offshoot of that view.

Those who advocate this "mixed economy" framework are convinced that the capitalistic market is a tremendously productive tool. However, they also realize that this instrument needs to be

directed towards social objectives. In short, proponents assert that the free enterprise market should be permitted to be as productive as possible. But the fruits of such productivity should be channeled for social ends.

It is fascinating that social market capitalism is bannered by groups from a socialist origin while also expressing the altered positions of those who have always been for capitalism. The term itself is taken from the program of the West German Social Democratic Party, which began as socialist. It capsulizes the dominant themes of Britain's Labour Party and the social democratic parties of Sweden, France and Italy. In the United States, most factions of the labor movement and the Democratic Party implicitly cling to his framework.

Most of the leading Western economists are proponents of social market capitalism. Oxford authority Denys Munby explains that the mixed economy is one "in which the state in various ways controls and plans the activities of private businessmen, and itself engages directly in economic activity as an entrepreneur, but where private businessmen still play an important role." Social market capitalism in turn needs to answer some hard questions of its own. First, can it confront the incomes problem without perennial industrial strife? The traditional conflict model of Western industrial relations creates problems with peace as well as productivity. Under present conditions, it is indeed prudent to support labor unions and encourage collective action.

For what chance does one sales lady have against the entire Shoemart chain? If corporate clout, in the final analysis, is based upon immense profits, then labor must wield its own weapon to balance matters. But the issue is whether this arrangement will ultimately prove destructive, whether it is a necessary phase, or whether it can pave the way for future cooperation and more equitable shares of industrial income. There seems to be an acceptance of antagonism in social market capitalism which corrodes mutual commitment to the general good.

Secondly, can such a society tolerate great concentrations of wealth over the long run? In theory the government sets the rules and acts as the arbiter.

In practice, it would be difficult to neutralize the overwhelming influence of wealth on the state. This issue is made all the more

compelling by the vast reach and resources of transnational corporations. Perhaps measures can be devised for nations to collude to bring the TNCs into a semblance of accountability. Perhaps global agencies can force these corporations into becoming clear blessings. One cannot expect the tremendous reservoirs of corporate power to be shared automatically and without a fight. Perhaps democracies can actually succeed in taming the tigers they are riding. But these are all conjectures.

Finally, can such production relations point the way to greater social equality? Social market capitalism defends inequality by asserting that the economy needs incentives for adequate production. And incentives in the end involve inequalities. Some inequality will indeed seem a fair fee for entrepreneurship. More welfare would be lowered by insisting upon equality in poverty rather than allowing for some inequality in an economy which yielded a greater harvest for all. Relative poverty in a nation of abundance is preferable to absolute equality in an extremely destitute one. While that line of reasoning is quite valid, the trouble is that it has fostered complacency among the social market capitalists.

Analysis, as such, must penetrate into deeper strata. Of primer importance here is the matter of equity, which social market capitalism does not seem to address.

The problem of equality appears to be rooted on the issue of alienation. As Marx points out, the dichotomy between the worker and his means of production has resulted in perpetual class conflict. The ancient slaves who did not own themselves were locked in struggle with their masters. The serfs who did not own the land in antagonism with their feudal lords. The workers who do not own the factories are in perennial hostility with their capitalists.

In each relation of production is created a pyramidal structure whose apex consists of a rentier enclave and whose base is the class of the working masses. What transpires is not a trickle down of wealth but a trickle up: incomes derived from actual labor flow into the coffers of the leisure set. Socialism seeks to correct this alienation between the worker and his means of production. To use a popular formula, it is a system where the workers own and the owners work. Class struggle is supposed to cease once the masses take control over state power. The vanguard party is thus charged

with protecting the interests of the working classes and defending the gains of the revolution.

Two observations deserve space here. First, there is reason to doubt that present governments declaring themselves socialist have solved the alienation problem. Factories belonging formerly to capitalists in a previous era have now passed to the hands of the state. They are not directly owned by the workers. As such, these workers have to abide by government quotas and sell at government prices. Economic equality is no difficulty here, as the income range in socialist countries is rather egalitarian. Rather, the problem is one of motivation to be productive.

This leads to the second observation. Alienation is intertwined not only with social justice but also with productivity. The evidence indicates that labor productivity is positively correlated with personal ownership of the instruments of production.

Such a trend is perceptible even in agriculture, as high efficiency is associated with small family-owned farms, not with large plantations. Research done on 15 countries has concluded that per acre output on small farms can be four to five times higher than on large estates. In Kenya, for example, farms under ten acres use an average of nine times more labor per acre than do farms with 100 acres or more—resulting in six times more output per acre than bigger farms achieve. In Cuba, small privately owned farms consistently surpassed sugarcane yields of huge state farms in the same provinces—despite less access to irrigation and nitrogen fertilizer. In China, when responsibility for land was delegated to individual families from the former communes, production advanced well ahead of population growth. Agricultural output per capita grew a phenomenal 39 percent in just six years.

The leap in productivity counts itself among the goals of agrarian reform, notwithstanding arguments on support services and economies of scale. (Besides, agriculture is less susceptible to the drag of the latter, vis-a-vis industry.) Personal ownership of the land, and the security it brings, motivates farmers to invest more work in the field. This stands in contrast with the plantation laborer whose sole interest is his daily wage, and who will thus refrain from exerting extra effort.

The call of land to the tiller thus finds an echo in the industrial sphere: the factory to the worker. This paper maintains that

direct ownership by workers over their concerns will spark increases in productivity, promote industrial peace, and advance economic justice.

III. THE CASE FOR WORKER COOPERATIVES

Advocates of direct worker ownership repeatedly summarize the concept's advantages like a refrain. Cooperatives will generate more employment and need less capital investment than capitalist firms. Worker cooperatives shall also tend to maximize employment subject to some floor on economic returns. They will experience greater labor productivity vis-a-vis capital when contrasted to capitalist firms. And cost and productivity of labor are subject to less fluctuation or risk in cooperatives.

Efforts towards maximizing employment are based largely on principles of solidarity, no matter the ideological color. Workers in cooperatives seem to prefer low and even varying wages to the reduction of employment levels. In times of an economic slump, such firms would choose an across-the-board pay cut over the layoff of a number of workers. A University of Michigan research has concluded that employee-ownership firms are 10 percent less likely to go out of business than conventional firms (which practice the ultimate in variable employment).

The behavior is more common in the Third World than in socialist nations. This is because worker benefits are much more prevalent in the latter than in the former, or in capitalist nations for that matter. As such, workers in developing societies are less secure about their employment prospects, especially if the economic climate is one of labor surplus.

The higher productivity of labor in cooperatives leads such firms to hire more workers and to acquire less capital. The higher productivity in turn is due to a number of factors which shall be considered in turn.

It is assumed that firms avoid risk. One claim is that cooperatives face more predictable costs and productivity in labor than do capitalist companies. The risks to capital are more or less equal since capital exhibits predictable productivity.

To understand why risk differs between these two types of firms, one need merely to observe the status of labor in each

Cooperatives are governed by workers or their representatives. Hence, policies must be formulated pursuing the interests of the worker members. In contrast, capitalist firms are organized to promote the interests of those who hold capital. Since members of cooperatives receive not only wages but also part of the surplus generated, they have a compelling incentive not to disrupt production. Moreover, since workers have the power to change the wage structure, they will prefer to lower wages during slack season rather than depress employment. Hence, cooperatives are not likely to reel from worker challenges that disrupt production.

In contrast, capitalist firms hire workers under wage contracts. This arrangement provides little incentive to employees to maintain high productivity. If the workers are able to organize they can confront capital with costly disruptions. There is also the threat of clandestine challenges such as sabotage or intended neglect Thus a capitalist firm assumes the risk that the expected value of labor productivity and its costs are subject to high variability.

Another claim is that cooperatives tend to display not only less variability in output but also higher day-to-day productivity. For any particular combination and level of factor use, cooperatives will exhibit greater total factor productivity (TFP) and a higher marginal productivity of labor than conventional firms.

This is due to the very direct link between the success of the whole cooperative and the individual gain of the workers. Like capitalist firms, cooperatives reward members according to differences in training, skills, and responsibilities. But the distribution of these rewards tend to be far more egalitarian in cooperatives.

Further there are two main influences that tend to promote work effort and productivity in a cooperative. First, if a cooperative prospers, all of the workers will be better off. Second, workers tend to reinforce productivity and work effort through collegiality and peer pressure.

Since work is delegated democratically, all the workers participate in governing the firm. There is strong social reinforcement and an ethic for working together. Similarly, there are strong social sanctions for members who do not exert their maximum effort.

While capitalist companies have promotion procedures that reward individual productivity, the system must be handled by per-

sons outside the work process. The information requirements for identifying individual differences in productivity create additional costs for a capitalist firm. Such costs are absent in worker cooperatives. The laborers themselves are in the best position to know.

Note that social reinforcement among worker peers is antithetical to the capitalist organization. Workers are locked in direct competition with their colleagues for promotion and pay. Further, the majority of the work is cut up into minute tasks. As such the failure of one worker to perform is not perceived as affecting the pay of all the others. In this environment, the attempt of one worker to excel over the others is seen as a threat by them.

The result is that workers tend to be more productive in cooperatives compared to capitalist firms. Studies indicate that absenteeism and turnover are lower and there is a greater work effort. Such minimal absenteeism can be traced to greater loyalty to their work organizations and the fear of social sanctions. The subnormal turnover rates in turn are due to greater employment security, the incentives of payoffs in the future for present work, greater involvement in the work process, the relative non-liquidity of worker shares, and community collegiality.

Similarly, cooperative workers are spurred to be more flexible, learning several jobs to assist other workers during bottlenecks in production. And such workers have more incentive to take care of the machinery and other forms of capital which they work with. This further increases productivity. In contrast workers in capitalist firms may even allow the equipment to break down to give them a break from their chores. Witness the behavior of drivers in bus consortiums.

There are other sources of savings. The fact that cooperative workers have an incentive to produce quality goods means that the firms will need few supervisors and quality-control inspectors. The cooperative is thus able to save on a large cadre of middle managers. Such firms have few unskilled workers. Given the relatively equal pay scales there, unskilled workers will be immediately put on training programs.

Cooperatives rotate work roles among members and train them in a variety of jobs as mentioned earlier. This flexibility stands in contrast to the drudgery of capitalist firms which stress routine

and repetitive tasks. It enhances the attachment of the workers to the work process and the company.

IV. CASE EXAMPLES OF COOPERATIVES

The classic success story is Mondragon. Located in the Basque region of northern Spain, it is the largest cooperative movement in the world. The cooperatives there are remarkable for their size and their diversity, the variety of the product mix, their rapid growth rate, their ability to generate capital and to obtain technical acumen, their success in penetrating the national and international markets, and their realization of economic democracy in the workplace.

The Mondragon cooperatives were started in 1956 with a single firm, expanding by 1981 to some 91 industrial companies and four agricultural enterprises.

All these cooperatives share in common the same social statutes, a system of social security, clinics, a major financial institution, a research and development center, and a renowned technical school. By the end of 1981 nearly 19,000 members were churning out products such as machine tools, winches, lathes, industrial refrigerators, household appliances, and electronic components. The sale of these products amounted to about one billion dollars in 1981. One of these cooperative firms, Fagor, is the largest manufacturer of refrigerators in Spain.

To provide sources of finance and technical advice, the movement created a banking system. By 1981 Mondragon's bank had three-quarters of a billion dollars in assets and 271,000 depositors. It has more than seventy branches. It has developed an entrepreneurial division to assist member firms in all aspects of their operations.

Majority of the labor force is trained in Mondragon at the Polytechnical School which is revered throughout Spain and the rest of Europe. Students take technical courses to obtain certificates while working in the cooperative firms.

The statutes govern the entire community. For example, each worker must invest to become a member. The value of his investment however, depends upon the profitability of the particular cooperative. All members vote in a general assembly which is responsible for the ultimate control of the cooperatives. The assembly

elects the leadership which in turn appoints the managers of each cooperative.

The pay scale is about three to one: the top executive receives no more than three times the pay of the "lowest" worker.

Income is collected in two forms: earnings for labor and returns on each employee's investment. Internal capital accounts are accumulated for each member based upon the annual share of the surplus credited to him. An interest rate of 6 percent per year plus the annual rate of inflation is assured for the investment. However, it must be kept within the cooperative until the member leaves.

An analysis of the capital investment, employment, and productivity of the Mondragon cooperatives is illuminative. Data culled from the *Caja Laboral Popular* indicates that the 500 largest Spanish firms utilize about four times as much capital for each job created as do the Mondragon cooperatives. The efficiency with which capital is being used in production is reflected by the amount of value-added relative to the amount of fixed capital. According to this criterion, the cooperatives showed three times as large a contribution to value-added than the 500 largest capitalist firms. Recall that a higher capital intensity gets reflected in higher labor productivity or value-added per worker. While the top 500 firms show a capital investment per worker 300 percent greater than that of the cooperatives, their value added is only about 20 percent greater. The data indicate a higher total factor productivity for the cooperatives.

This is compelling evidence that under a cooperative owned by the workers, basic industrial goods can be produced in a much more labor-intensive fashion—while showing surprisingly higher productivity. As such, cooperatives may increase employment substantially by reducing the amount of capital investment required to create each job.

In Yugoslavia, workers' self-management is the official framework of the state's economic order. After its introduction in 1958, the government slowly let go and decentralized control over Yugoslav society.

Self-managed firms function independently from the government: each enterprise wields its own managerial organization. Workers are their own managers. They run the organizations they

own, and each laborer is consulted in all matters of decision-making. The primary unit of such self-management is the workers collective. For larger enterprises with 30 or more members, the collective functions through workers' councils.

Yugoslav firms may (and do) employ professional managers to implement plans and decisions. A director is chosen by the workers' council. He may be re-elected after four years. It is important to remember that workers retain actual authority through the council. The director may participate in the council but he is not allowed to vote. In the United States there are now more than 200 worker-owned cooperatives, most with fewer than fifty employee-owners. At Linton Plywood Association in Oregon, a $20 million a year worker-owned plywood manufacturer, workers earn more than $50,000 per year—much more than people at large mills. But they must invest a substantial amount to buy a share and join the collective: around $75,000. Publix Super Markets, Florida's largest retail chain, is completely owned by its employees. Publix profit per dollar of shares is twice that of Safeway, which has the country's biggest sales.

When Weirton Steel of West Virginia became America's largest employee-owned company in early 1984, few observers predicted the success it now enjoys. But Weirton turned profitable almost immediately, earning $9.7 million the first quarter and $60 million in 1984. It was the first profit since 1981. The company brought back some 1,000 employees since the workers took over. Nearly 8,000 work there now.

The next section deals with the Employee Stock Option Plan (ESOP), an innovation which allows rank and file labor to own company stock. This lies between the conventional capitalist firm and the workers' cooperative. It can thus be viewed as a transition stage between the status quo and the mode of direct worker ownership.

V. EMPLOYEE STOCK OPTION PLANS: CONCEPTS AND CASES

There are now around 7,000 ESOP's in the United States, covering about 7-8 percent of the work force or 10 million workers. The typical plan owns 15-40 percent of the company's stock, although that ratio is rising as ESOPs mature (most are relatively

new). Employees own a majority of the stock in 10-15 percent of the companies. Most plans allocate an amount of stock equivalent to 5-15 percent of pay per year. Contrary to the popular American perception, only about 2 percent of the plans are set up in distress situations. The majority are created in profitable going concerns.

The employee stock ownership plan is relatively easy to activate. A trust is created for the employees which then borrows money from the bank, then passes it as a loan to the company. In return, the ESOP gets company stock which is held in trust for employees. Once all matters are settled, the company starts making annual payments to the ESOP, based on the firm's revenues.

Deducting the full amount from its taxable income, the ESOP then uses this money to pay off the original loan. The bank pays taxes on only 50 percent of the interest income, as provided by American law. As the loan is paid off, stock is allocated to each employee's ESOP account. When employees leave the firm, they withdraw their stock or sell it, often back to the ESOP. New employees then join the plan and begin accumulating stock.

The advantages to workers are their shares or stakes in the ownership of the firm in which they work, as well as the second income they derive from dividends. For management, ESOPs provide a source of capital expansion at far lower costs than conventional sources of funds. The tax advantages result from the fact that the firm can deduct the full amount of payment made to an ESOP. (For payments to an equivalent loan, the firm can deduct only the interest costs and not the portion used to repay the principal.) Since the payments to an ESOP are a means of repaying the loan while being treated as a contribution to employee benefits, a major tax advantage is enjoyed by the firm.

From the vantage of existing stock holders, the benefit is not only the low cost of capital that ESOPs generate but also the improved performance of the company due to higher worker productivity.

Society at large stands to benefit from ESOPs as well. Current stockholders have little incentive to encourage their companies to invest for long-term growth. After all, most stockholders behave more like sophisticated gamblers than investors. They lend companies their money in the hope that the stock price will rise across the short term, not really to see the company prosper twenty years

from now. This pressure for short-term performance is accentuated by fears that higher-risk, long-term strategies that reduce current earnings per share will depress stock prices and encourage hostile takeovers. But employee-owners have relatively less interest in short-term profits and stock prices than in the long-term future of their jobs. It is thus in their interest to push for policy that will ensure long-term growth. ESOPs likewise serve as a means to provide business continuity. Many owners of closely-held businesses have no specific plans for retirement. As they near that point, they find their options severely limited. The firms may not even be attractive to outsiders.

So the ESOP can be used as a solution. The owner can have the company make tax-deductible contributions to the ESOP and then have the ESOP buy the owner's shares. If the ESOP ends up with 30 percent or more of the company's stock after the transaction, and if the owner reinvests the proceeds in the stock of other companies within twelve months, no tax is due on the sale until the new stocks are sold. At that point only the capital gains taxes are due. This makes the ESOP route the most tax-favored way to sell a business.

The ESOP can also be used as an additional employee benefit. Many companies want to provide more benefits to their workers but lack the cash. With an ESOP, the firm can simply print more shares and contribute them to the employees. These shares may dilute the ownership interests of other stockholders, but the company can argue that the resulting tax and motivational benefits more than justify the spreading of ownership. But companies do need to recall that when employees leave they will sell back their shares, so the firms will have to generate the cash to buy them. ESOPs are thus not suited for firms in financial straits.

The best known use of ESOP is to save failing companies either through an employee buy-out of a plant about to be closed, or through wage concessions in return for stocks. In the United States, 60-70 buy-outs have occurred since 1971. Fully 90 percent of the firms concerned are still in business.

Moreover, employee ownership has provided employees in more than 400 firms the ability to elect a majority in the board of directors.

Researches seem to confirm that ESOPs have been largely beneficial to the firms possessing them. A 1978 University of Michigan study has found that employee ownership companies were 150 percent as profitable as comparative firms. A 1980 survey of ESOP firms has concluded that they had twice the annual productivity growth rate of similar non-ESOP companies. Personnel managers in 59% of these companies believed the plans exerted a "good" influence on employee morale and 79% thought they stimulated "employee interest in company progress." Similar findings have emerged from the studies of Goldstein (1978) and Christiansen (1980).

The generally beneficial effects on industrial relations and morale also explain why studies on the relationship between employee stock ownership and profitability usually report positive findings (Metzger and Colletti, 1971; Conte and Tannenbaum, 1978; Frieden, 1980; Marsh and McAllister, 1981; Rosen and Klein, 1983).

A 1983 study by the National Center for Employee Ownership (NCEO) found that majority of the employee-owned firms generate three times more net new jobs per year than do other firms in their industries. And a 1984 study by the NCEO concluded that thirteen publicly held companies with 10 percent or more employee ownership outperformed 62-75 percent of their competitors, depending on the financial performance measure used.

In its research the NCEO has also realized that what makes employee ownership work or fail is how much stock workers receive every year. The more they get the more motivated they are. Participation and control are less important but not unimportant. Such employees are more willing to accept new technologies, work routines or investment decisions, and are less likely to leave the company.

Not all companies realize motivational gains, either because they transfer too little stock or fail to provide participation and opportunities that can translate motivation into ideas and results.

Employee-owned firms abound in the United States. Action Instruments, a California electronics firm, has distributed 20 percent of company stock to rank and file employees. Founder Jim Pinto states, "the future of this company is to eliminate the differences between workers, managers, and owners by making them all capitalists." Robert Metcalfe, chairman of 3Com, another California company involved with data networks, provides 11 percent

of stock for those below officer rank. He even promises entry-level stock clerks that if they contribute to the company's growth, they will be able to match their $10,000 salaries in stock gains.

"It's been good for us," claims Jerry Knapp, vice-president of CableData, a corporation in which employees control about 35% of company stock. "It puts ownership in the hands of our workers, and we feel owners are better employees than those who do not share in the growth of a company."

About two-thirds of Dana Corporation's 18,000 employees own company stock. For each seventy cents labor earns on stock, Dana adds thirty cents. At Lowe's Companies in North Carolina, there are startling stories about people retiring on the firm's ESOP: the $125 a week warehouseman who retired in 1973 with a $660,000 nest egg, the truck driver with $413,000.

People's Express is a company revolving around the ideal of self-management. It requires that all employees be stockholders. About a third of the company stock—a rather high percentage—is held by People Express managers (they are not called employees) who can purchase stock at a discount. Under their special bonus plan, People Express matches managers' purchases share for share.

The ESOP of Colorado's Fred Schmid Appliance and TV Company has been operating since 1981. Officers credit it for the sales increase from $27 million to $62 million in five years. In 1984, the chain of 15 stores transferred 100 percent of stock to employees rather than sell the company to outsiders.

In such enterprises, people get paid not for their position on the organization, but for their productivity. Pay for performance is replacing pay for just showing up in the morning. People on the "pay for attendance" model spend only about 50 percent of their time actually working, according to a study published by the American Management Association. Fellow workers who are also stockholders, resent such inactivity. Peer pressure replaces management pressure.

The Chinese are catching on to the idea. Following the economic overhaul unleashed by premier Deng Xiaoping in 1984, the state is now encouraging the purchase and sale of stock by workers.

A striking case is the Tianquiao Joint Stock Department Store (TJSDS) in Peking, a giant wholesaler of consumer goods. While

just over half of the firm's stocks are held by the state, a quarter are owned by banks, and another fifth by other enterprises; the rest belong to its own workers.

Unlike most other companies in China, the TJSDS is run not by government bureaucrats but by a board of directors. TJSDS officials report that ever since the workers purchased heavily on stocks, performance has improved tremendously. Two years ago the company put on offer RMB 3 million ($810,000) worth of its bonds. In just six days they were completely grabbed by local enterprises and by hundreds of individual workers.

The benefits of the changes in China seem obvious. Economist Li Luoli of Nankai University is emphatic about this: "When enterprises are at least partially owned by managers and workers, the latter have a vested interest in making the concerns work. They will make hard-nosed decisions when it comes to reinvesting profits or distributing them as bonuses."

Because of China's lack of experience in stocks, there is considerable debate about share ownership. There are reportedly three main schools of thought. More conservative planners favor the state retaining the majority of the assets of enterprise. Others think that businesses, perhaps in coordination with the banks, should play the major role. More audacious economists see individual shareholders—the workers and the peasants—assuming controlling interests in the future.

Recent Chinese studies confirm the notion that if employees own a stake in their concerns, their performance will take a great leap forward. A research published in 1986 surveys firms in Inner Mongolia concerning their views on stockholders.

According to the report, the cure for sluggish economic performance lies in inviting employees to buy up much of their enterprises. About 53% of the thousands of workers interviewed throughout Inner Mongolia thought that "buying stocks will buttress their concern for (the performance of) their factories." In fact, when asked why they would purchase the stocks, 51.9% said "for the sake of the development of the enterprise." Only 3.8% claimed to be after the higher interest that company bonds carry.

The survey also covered workers who were already stockholders. Some 73% said that their stocks had bound them closer to their

workplace. The more bonds that an employee owned, the more he tended to think of himself as "the master of his factory." Fully 85% of all workers quizzed in the study said they wanted to become shareholders.

Labor in Latin America appears to react positively to the notion of employee ownership. The La Perla coffee plantation in Guatemala was once beset by insurgents and appeared bound for failure. The owners thus set up an ESOP under the guidance of a *solidarista* association. In 1984, after the first provision of shares (40 percent ownership) output increased nearly two hundred percent. In fact some of the guerillas defected to the plantation. And a number of plantation workers took up arms to defend their enterprise.

In Honduras, a ladies garment manufacturer known to be antilabor suddenly shut down and abandoned a factory employing 289 women. The latter thus applied their equity in the company to obtain the factory's machines. They were able to establish, in conjunction with the Honduran Port Authority, a worker-managed enterprise.

These success stories do not suggest that direct worker ownership and ESOPs in particular are bereft of difficulties. The following section examines such obstacles.

VI. PROBLEMATIC ISSUES AND DISTORTIONS

David Ellerman of the Industrial Cooperatives Association questions the use of ESOPs as a bridge towards worker cooperatives. He stresses that ESOPs were never meant to answer the needs of democratic and worker-controlled firms. Some disparities between the interests of such firms and the ESOP structure are obvious. Since the stock will be placed in a trust (where the trustees are chosen jointly by the lender and the firm) the trustees will have the power to choose the governing board, and make major decisions for the firm. Thus, the employee-owners of a worker cooperative must obtain an agreement with the trustees that the stock will be voted only on behalf of decisions reached by the employee owners.

Further, even when stock is allocated into individual worker accounts, there is some difficulty in reconciling such ownership with the very concept of cooperative. Stockholders are entitled to traditional property rights: the more stocks one owns, the more votes one

gets. But cooperatives are based upon "people's rights" in which each member has an equal vote.

In cooperatives an arrangement is often stipulated that departing employee-owners sell back their shares to the firm to avoid outside ownership. However, during an economic slump or when extremely large numbers of members leave within a short period, this requirement may place the firm in great financial difficulty.

The fact that employees buy the firm through the ESOP mechanism does not automatically mean that they control it. That is, worker ownership in these instances has not been translated into worker control. For example, the president of the South Bend Lathe (Indiana) was also the chairman of the board, chairman of the ESOP committee, a director of the bank that functioned as a trustee for the ESOP, and the individual who chose the board of directors and the ESOP committee.

The absence of worker consultation on important matters and the failure of management even to provide information of concern to the workers provoked them to go on strike in 1980—against a firm where they owned two-thirds of the vested shares (Moberg, 1980).

This example illustrates a basic dichotomy between using the ESOP for transferring ownership to workers, and as a method for transferring control of the workplace to the workers. The two are not exactly the same. ESOPs were designed neither to create worker control nor to establish worker cooperatives, it is claimed.

Clearly one major issue is the ambiguous role of the unions when workers acquire ownership of a firm. Historically, unions were established to represent the concerns of workers in negotiating with the owners and managers of the firm. Since that role would be practically dissolved by worker ownership, the question is whether the union could fit in a new role: in that of serving as an organizational form of governing the firm.

To the degree that unions view ESOPs requiring worker governance as a challenge to their traditional function, their support and participation may be scanty. Note that in the past, unions have not seen the control of capital as being pivotal to a strategy for defending worker interests.

Still, it is important to stress that a number of ESOPs have been established with unions playing a central role in representing the workers in ESOP negotiations.

An even more basic issue with respect to the formation of worker cooperatives under an ESOP is the problem of uncertainty faced by potential lenders. The attractiveness of lending to an ESOP for purchase of the firm will depend critically upon assessments of the company's future prospects. Both the ability to service the debt and the value of the stock used for collateral will depend upon the economic performance of the firm.

There are two aspects of economic evaluation of prime interest to the lender. The first is whether the firm is essentially sound and has strong prospects of remaining profitable. The second is whether a shift to worker ownership will provide the type of management and leadership that will ensure effective operation.

The ability of the workers to enact a smooth transition to a worker-managed firm is by no means certain. Workers will be expected to select managers without either the experience or precedent for worker participation.

The dilemma created by the situation is evident when one considers the difficulty of obtaining a loan for the ESOP without providing assurances of stability during the transition to a worker-owned firm. In general, lenders will prefer a safe passage to worker ownership in which traditional forms of management will be utilized with little worker participation.

The most appropriate approach is to formulate a detailed plan that will transfer both ownership and control through an orderly process of incremental steps. Such a plan would need to incorporate two major features.

First, there must be an appropriate structure for democratic management in which the workers can participate while ensuring an efficient decision mechanism for the firm. Second, all workers will need to acquire experience in participation. Such experience will likely be critical to the success of worker-governed firms.

In short, Ellerman suggests that each of these challenges requires elaborate arrangements to transform an ESOP into a worker cooperative. For the ESOP was never conceived to be used this way. On both ideological and pragmatic grounds he argues in favor of

direct establishment of cooperative firms with conventional financing. But of course, the problem in the first place is the absence of financial capital available for worker cooperatives. Where funding is not available, it appears the ESOPs can provide a feasible enough though less ideal solution.

Another flaw is that ESOPs are owner-initiated rather than worker-initiated. Those that are worker-initiated are often the fruit of sheer worker desperation. Workers usually sacrifice their pension rights, their workplace rules, and their union scale wages to establish an ESOP as a last-ditch attempt to save their jobs. Were ESOPs structured to give workers majority rights and to preserve their former privileges, perhaps they could evolve into progressive institutions. But such is not the case with contemporary ESOPs in the United States. As such, change in industrial relations may be largely superficial.

And there is a fundamental difficulty even when ownership is of the progressive mold of complete worker cooperatives. For cooperatives have shown a tendency to fail or stagnate in business. Some observers conclude that worker-owners in the end make poor entrepreneurs—for they are hampered by the lack of capital and business experience. And they are unwilling to innovate or take risks.

A more telling charge is that worker cooperatives tend to degenerate over time. In the cases when they succeeded as businesses they failed as democracies. They have become in effect associations of capitalists making a profit by employing workers outside their ownership sphere. Paul Blumberg has noted that the degeneration usually assumes the following forms:

"Transforming the cooperative into a simple profit-making, profit-seeking business, indistinguishable from private enterprise; exploiting a monopoly situation, often to public disadvantage... closing off of cooperative membership; raising the cost of membership to prohibitively high levels, and resorting to the anti-cooperative device of taking hired labor."

The impulse to hire non-member labor is hidden but inherent in the structure of most worker-owned firms. As a company prospers and hires additional laborers, these new recruits can become equal partners only by purchasing shares from the existing group of worker-owners. But unless they really need the money, most

worker-owners would rather not sell to these new employees. For, to add to the number of co-owners would dilute their sense of ownership. On the other hand, the presence of non-owners enhances it. Moreover, as the worker-owners retire, they often realize that they can obtain a higher price for their shares by selling them to outside capitalists rather than to other workers in the firm.

These issues, plus the nuances of Filipino work culture and the potential of worker entrepreneurship should be considered in designing an alternative mode of production. It is of course erroneous to force foreign models to fit exactly into the Filipino temperament; selective adaptation is more in order. But then again, it would be a greater mistake to completely discard the innovation due to its foreign origin. The Filipino firm may be left behind by companies abroad which have chosen to ride the wave of the future.