

**Structural change and the nature of innovative activity:  
Legal form and firm performance**

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## **Executive summary**

This paper studies the evolution of legal forms and its effects on innovation and productivity within Colombia's manufacturing industry. The rise of a private legal structure is evidenced by the strategy of large and powerful conglomerates to increase their size and power by absorbing firms with a public setting. The paper argues that this institutional innovation is sub-optimal since adopting a private limited liability framework excludes intrapreneurial forces from access to ownership. This was the world that the classic political economy and scholars like Schumpeter were concerned with: one in which the institutional change would favour the divorce between ownership and entrepreneurship.

## **Key words**

Innovation, productivity, entrepreneurship, legal form

## **1. Introduction**

De Soto (2000), in a recent book, refers to the "apartheid" that capitalism suffers in many less developed countries. He denounces capitalism in less developed countries to be akin to a private club, opened only for a privileged minority and frustrating thousands of millions of people that look inside from outside. He argues that formal institutions have created a sort of exclusionist "glass bell" for the majority, and warns that this exclusion will continue as long as the legal and political systems hinder majorities to enter to the system of formal property. This paper proposes a similar argument but draws attention to the role of firm organisation, and, in particular, the legal form of firms. We argue that when the evolution of institutions in the legal forms of firms carries on exclusiveness in the system of property, it has a negative effect on innovative and productive processes and activities through governance structures in the workplace. The paper assesses the extent to which an institutional (legal) change in firms' forms determines or moulds the entrepreneurial performance (i.e. novel thinking, new combinations and, ultimately, new knowledge) within a firm and ultimately an industry's productivity.

The following section of the paper critically analyses the relationship between entrepreneurship and the legal form of firms within a framework of theories concerning the separation of ownership and entrepreneurship and the divorce between ownership and control. The section also discusses the limited liability institution and its value from a stakeholder and social capital perspective. Section 3 provides an empirical analysis of Colombia's manufacturing industry, examining the evolutionary relationship between the legal form of firms in Colombia's manufacturing industry and their entrepreneurial or innovative performance. Section 4 discusses the findings and Section 5 concludes.

## **2. Background**

### **2.1 *Entrepreneurship and the legal form of firms***

The emergence of the business enterprise and the managerial class during the second-half of the 19th century and beginnings of the 20th century in developed countries like UK and US has been commonly associated in previous literature with the separation of "ownership and control"; effects of which have been defined as one of the most important turning points of modern capitalism (Chandler, 1977). In the mid 19th century, top tier managers were owners, partners or major stockholders. By the 1920s, salaried middle tier and top tier managers were the dominant institution in both the US and UK, hired on behalf of the owners to coordinate resources in a multi-functional business unit and supervise the work of thousands of workers. Enterprises were

owned by tens or thousands of shareholders. In a short period of time, this institution had grown and pervaded the way of doing business.

Conventional theory (i.e. principal-agent) introduces the separation between ownership and control as one in which owners (or shareholders) hire professional managers to run their business due to the expansion and growth of the market. This view develops then a theory of incentives for the alignment of the conflict of interests between owners (principal) and managers (agent). However, if one looks back historically, the transfer of control came about the other way around: managers transferring ownership to shareholders and not, as the principal agent model portrays it, shareholders transferring control to managers. According to Lazonick (2001), it was when the owner-manager of the enterprise got an intimate understanding of the technologies and markets, that public holding stocks from outsiders was induced and consolidated in the US in the last half of 19th century.

Schumpeter's (1943) analysis was concerned with the consequences of entrepreneur-owner's loss of control in the company and handing over power to a decentralized and hierarchical structure. This however, should not be confused with the conventional view of separation between ownership and control. His analysis allows us to look beyond the problem of conflicting interests. According to Schumpeter, institutions that hold capitalism together were crumbling because the once entrepreneurship-related product was being estranged by the institutional change. Such estrangement is reflected in the change of firms' legal forms, from entrepreneurial to the classic limited liability institution, and in the entrepreneurial function's disappearance within big bureaucratic corporations. The fate of the entrepreneur was doomed as capitalism moved from the owner-managed firms into large, hierarchical, limited liability firms. One can relate Schumpeter's concern to the changing attitude of owners and worker's occurring as a result of property dispersion and rising managerial control. He refers to managers' decreasing level of affinity and attachment toward the interests of the company and shareholders' lack of caring and disattachment to property.<sup>1</sup> Although coherent and relevant at the time, this problem has to be re-stated within a broader framework that includes the consequences of loss of control from the nonowner-entrepreneurs (i.e. from an intrapreneurial perspective). If the sources of entrepreneurship are depicted in a broader way, the pillars protecting the substance and sense of property should not only motivate owner-founders or owner-managers but also other sources of entrepreneurship such as hired-managers and executives, workers in R&D laboratories, producers, suppliers, customers, etc.<sup>2</sup>

Until the late 19th-mid 20th century, an entrepreneur embodied both owner and innovator. However, during the 20th century owner and innovator started to diverge. The perspective of entrepreneurship as a process starting from the base and working its way up has been discussed in an expanding number of studies in the management literature over the last two decades (see, for example, Burgelman, 1983; Ellis and Taylor, 1987; Jones and Butler, 1992; Pinchot III, 1985; Schendel, 1990; Schollhammer 1982; Spann, Adams and Wortman, 1988; Vesper 1984). The entrepreneurial process within the firm, namely intrapreneurship, distinguishes itself from the traditional concept of entrepreneurship in that innovation is done within the context of existing

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<sup>1</sup> Recent literature on 'Social Capital' works with these same notions under concepts like affinity and proximity.

<sup>2</sup> In the same way that the 'founder', the 'owner', the 'risk-bearer' and the 'manufacturer' are not the same functions but could be embodied in the same person, 'entrepreneurs' and 'innovators' do not have to be the founder or the owner or the capitalist. Just as the system of land tenure has facilitated the distinction between farmer and landowner, the corporate system has to distinguish between owners, managers and innovators (e.g. R&D units). The innovator is distinguishable from the capitalist that owns the money, even when they are the same person. Also, the innovator and entrepreneur are distinguishable because of the extended roles that innovators have other than founding a new firm and creating a bureaucracy below them.

organizations (e.g. corporations, small businesses, state companies, non-profit firms, etc). The selection environment of intrapreneurship differs from that of entrepreneurship in that it has to be selected and recognized within a hierarchy, unlike entrepreneurship that is selected in the market place. Hence, the change in governance structures of the firm and, in particular, the change in the legal form of firms has an important influence on innovative and productive processes and activities. In this paper, the type of institutional change that could be dooming entrepreneurship is studied by analysing the evolution of the legal forms of firms.

## 2.2 *The limited liability institution and stakeholder and social capital theories*

A limited liability company (also known as a joint stock company) is characterised as a “separate legal entity, distinct from the people engaged in it and with continuity, so that it does not die when the founders withdraw” (Hay, 1990). The owners or shareholders of the limited liability company provide financial capital in return for a share in the profits and their liability is limited to the capital they have subscribed, which is forfeit if the company fails. There is an important distinction between public and private companies. Shares in public companies are held and freely traded by the general public whilst shares in private companies are held by a single person or a small group and cannot be transferred without the agreement of the shareholders. The need for wider (i.e. general public) ownership in private companies is absent if the inner group has enough capital to start up a business (Clapham, 1968). However, the ex-ante action of registering a company as private brings an ex-post consequence, which is, generally, a greater restriction of access to ownership than in the public company.<sup>3</sup> The essential weakness of the private limited firm is that family law and the laws of inheritance regulate ownership relations, which constrain the efficient allocation of control. The private firm works as an “educational apparatus for the transmission of entrepreneurial competence but there is no guarantee that the hereditary transmission of ability works efficiently” (Screpanti, 1999).<sup>4</sup>

Failures of the limited company principle are not agency-related but closely pertain to the need to recognize stakeholders like trading suppliers, workforce, minority shareholders and other contributors such as intrapreneurs. The principal-agent model’s lack of flexibility sees shareholders permanently as the only risk-takers, leaving aside others like entrepreneurs and other

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<sup>3</sup> Both types of companies bear the limited liability principle, an institution that over time has facilitated the transition from familial to managerial capitalism in countries such as the UK, US and Japan, embedding a separation of ownership from management (Martinelli 1994). The main argument in favour of limited liability stems from the rights of investors to invest their capital without risking all their wealth. Joint and several liabilities are particularly deterrent for wealthy investors who are likely to be held responsible for deficiencies and judgement costs (Halper 1998). Limited liability instead encourages investment by passive investors in risky enterprises and facilitates risk diversification in specialized firms (Carney 2000). Proxy votes and voting right restrictions generally impede selling shares of the firm to the general public (Franks and Mayer 1998). Anyhow, shares may be endowed to other members of the inner group.

<sup>4</sup> Moreover, as property endurance bestows social position, agents not only try to do their best exploiting the given initial endowment but also tend not to allow others to do the same (i.e. fully developing their capacities) by preventing them from entering the closed circle of ownership. In this way, property relations are designed to embed social positions and prevent social mobility. Before the limited liability form was created and instituted, people that did not know each other could be attracted to the same business venture but would most probably not commit, because, besides there being no social proximity, all their assets would be necessarily at stake. When the limited liability legal form appeared it was created precisely for anonymous property and to limit the risk of losing all of the contributors’ wealth. Despite this, a private legal structure, although preserving the virtues of limited liability, evolved perpetuating the exclusionist vices of familial and partnership structure. In this way institutions evolved to favour the inner group of shareholders and so the institutional change developed “out of bounds”, a matter that classics were strongly concerned about.

stakeholders.<sup>5</sup> As a consequence to this lack of recognition, a feeling of disattachment is diffused through stakeholders. Although managerial mis-alignment and agency costs are important factors in a changing institutional structure, the most significant counter-effect on innovation stems from the distancing effects between owners (shareholders) and stakeholders (managers, work-force, clients, suppliers), due to their importance as sources of intrapreneurial activities. Leading stakeholding theorists (e.g. Turnbull 1998, Schmid 2000a, 2000b) argue that if one focuses on the defence of the perpetual and static shareholders' interests (which occurs in particular in the private limited liability form), that ownership evolution, has not replaced its structure with a more optimal and dynamic type of co-ownership structure. Dynamic structures protect the payoff of agents who contribute to productive entrepreneurial activities, and have been denominated as "stakeholder tenure" by Turnbull (1998). According to Turnbull (1998), the stakeholder tenure is the appropriate institutional structure for productive activities to evolve, because they replace traditional, oligarchic structures (which defend individualistic interests) with modern structures, which protect stakeholders' interests.<sup>6</sup>

Turnbull's proposal to replace such perpetual and static property rights finds favour in recent literature which suggests a metaphor for modern type of co-ownership structures, namely, social capital (Schmid, 2000a, 2000b). The underlying assumption behind this suggestion is that, in the case of modern co-ownership settings, there is greater accumulation of social capital (i.e. higher degrees of affinity and social ties), so agents would not engage in counter-innovative activities in property they co-own or are emotionally bound to, because it is unlikely that agents would steal or cheat on themselves. Wenpin and Ghoshal (1998) provide evidence that social capital increases value creation because informal social relations and tacit social arrangements encourage productive resource exchange and combination and thereby promote product innovations. Therefore, modern structures of co-ownership seem to conceive a better institutional structure for productive entrepreneurial activities to diffuse given the greater social capital embedded. Further, Fountain (1998) argues that linkages and trust provide a forum for dialogue and discussion to search for and establish consensus as a basis for collaboration, which, in turn, would enable accelerating innovation and productivity growth.

What we can learn from stakeholder and social capital theories is that if the access rights to ownership are opened, the 'way in' for innovative forces to ownership structures would be unblocked and the entrepreneurial function within the firm would unfold as co-ownership and identity deter innovation opposition and facilitate innovation. In the next section, we analyse empirically what has happened to intrapreneurs in a developing country in terms of their access to ownership structures.

### **3. Empirical analysis**

#### ***3.1 Institutional change and governance structure in Colombia's manufacturing industry***

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<sup>5</sup> As we have seen previously, this narrow scope of ideas is given by the limited view of entrepreneurship as particularly related to businesses' renewal and new ventures creation, in detriment of innovative entrepreneurship within organizations.

<sup>6</sup> Turnbull (1998) stresses that although ownership rights evolved while seeking to maintain political power and wealth in property, there are no longer reasons to grant an unlimited life to proprietorship, not even in a corporate structure. These objectives rights are no longer consistent with economic justice, efficiency and sustainability: "modern techniques of investment analyses reveals that unlimited life property rights are not required and that they result in investors obtaining benefits in excess of the incentive required to bring forth their investment".

The evolution of the institutional environment concerns the legal ground rules that define the context within which economic activity of business enterprises develops.<sup>7</sup> The manufacturing industry of Colombia was chosen empirical analysis for a number of reasons. First, reliable, disaggregated time series data was available from the National Department of Statistics (DANE) in Bogota. Second, although much has been written regarding the changing legal form of firms in developed countries such as the US and UK, much less has been written on less developed countries. Nevertheless, modern literature (such the new/old institutionalism and new growth theory) has recognised institutional change as a key determinant for growth and development and international organizations like the World Bank and the United Nations have been very concerned with institutions for development.

The institutional evolution of firms' legal structures within Colombia's manufacturing industry has been similar to that of other capitalist countries. As Graph 1 shows, over the last 30 years the Limited Liability Company (LLC hereafter) has taken over from more classical types of legal structure. The industrialization process in Colombia's manufacturing industry, which began in the early 20<sup>th</sup> century, was particularly active during the 1930s and 1940s (Bejarano, 1998; Cuevas, 1986; Ocampo, 1994). The result of this change was that by the 1960s and 1970s the majority of the entrepreneurial firms that initiated this process in previous decades began to outlive their original creators. In order for these firms to have continuity, the legal framework had to be changed. One can see this change occurring during the 1960s and 1970s with the adoption of the LLC form.

As Graph 1 shows, in 1968 the majority of establishments were proprietorship companies and less than 30 per cent approximately were LLCs. The remainder, less than 15%, were cooperatives, partnerships, state companies and non-profit organizations.<sup>8</sup> The ownership and share-trading distinction between private and public LLCs and the main reason for excluding wider ownership in private companies (i.e. private individuals with sufficient capital to start-up the business) conceals the fact that the ex-ante action of registering a company as private is pre-emptive (i.e. deliberately avoiding unwelcome access to ownership by powerful rivals) but has ex-post consequences at different levels within the firm.<sup>9</sup> By the end of the 1990s, the institutional evolution of industrialization process had been reflected in the rise of private LLCs (with a restricted circle and limited number of owners). Graph 1 shows that although the public companies have shown a steady increase, private companies have increased rapidly. This pattern is repeated at the intra-sectoral level, except for sectors like Beverages, Tobacco, Paper and its by-products and Industrial chemical substances, where there is a stronger presence of public companies (Author, 2002).

## INSERT GRAPH 1

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<sup>7</sup> According to Williamson (1994, p. 102), the institutional environment are "the rules of the game that define the context within which economic activity takes place. The political, social, and legal ground rules establish the basis for production, exchange, and distribution". The institutional environment shapes the governance institutions, which are the *social structure* that exercise authority, direction and control within firms of Colombia's manufacturing industry (Zingales 1998).

<sup>8</sup> Author (2002) compares evidence from a number of manufacturing sectors (e.g. Beverages, Tobacco, Paper) and found similar results across the sectors. From the 1970s onwards, the LLC gradually overtook the individual companies as the legal choice. This period, however, only shows the end of the process that had started presumably in previous decades.

<sup>9</sup> Proxy votes and voting right restrictions generally impede selling shares of the firm to the general public (Franks and Mayer 1998). Anyhow, shares may be endowed to other members of the inner group.

The following analysis attempts to explain this empirical phenomenon based on an analysis of the ownership structure of Colombia's manufacturing industry and its relationship with the governance institutions of innovation. A priori, one can say that in response to the oligopolisation and concentration processes of previous decades in Colombia's manufacturing industry, the private legal framework has been adopted as a strategy to avoid being taken over by other – more powerful – firms, such as those belonging to Business Groups.<sup>10</sup> Nevertheless, we argue that the strategy of adopting this legal framework is strongly associated with low productivity and the innovation processes.

### ***3.2 Evolution of the legal institutional environment and innovation and productive processes***

Rigidities in selling or transferring ownership on the part of the entrepreneurial firms' heirs, family, in-laws, etc, is deeply entrenched in the business culture of Colombia's manufacturing industry (Revista Semana, 2001a). Some studies show that the typical firm in the manufacturing industry is characterized by being a SME with familial start-up capital (Revista Dinero, 1999) and others note that the business structure of Colombia is concentrated in hands of one class to the exclusion of others (Ogliastri and Dávila, 1992). Historically, this matter of unwillingness to let go of ownership and control is not exclusive to Colombia's manufacturing industry.<sup>11</sup>

The implications of a delayed transition of familial firms or individual proprietorship to a public legal institutional environment are that owners diversify their portfolio, reduce risk and transfer control to (more) capable agents. Therefore, the unwillingness to yield control to other capable employees either inside or external to the firm may lead to conscious strategic decisions to forswear growth or to unconscious decisions that stunt the growth and development of the organization (Daily and Dollinger, 1992). The private firms maintain personal control rather than impersonal, formalized and hierarchical procedures to monitor the production process. Mechanisms like social methods of control uphold the organizational cohesion that professionally managed firms generally forsake. Fourie (1989 cited in Hay 1990) argues that the firm should be regarded as “an institution to which employees ‘belong’ and to which they contribute their work and skill”. Schmid (2000b) stresses the importance of affinity and regard among people as an important economic asset for development. However, Coleman (1994), explicitly following Weber (1983), shows that social capital (i.e. affinity) can become too stringent and its economic value can depreciate.

Some family firms, despite not increasing in size, undertake more profitable business (Daily and Dollinger, 1992). For example, many of the surviving family firms of American business have been associated with good management practices, business values, regard for quality of product, respect for employees, and a focus on long-term problems. Publicly traded companies have acknowledged the traditional strengths of many large family firms and “their use of advertising and logos to project images linking past long-standing service with present efficiency” (Church

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<sup>10</sup> Evidence shows that many consolidating Business Groups practised the strategy of absorbing many of the public companies during the early stages of the industrialization process of Colombia in order to get rid of competition and build entry barriers to the industry. The historical evidence is found in the studies of Hommes and Silva (1981) and Narváez (1985).

<sup>11</sup> Hay and Morris (1984) show that owners of large unquoted companies in the UK, although committed to the firm (which sometimes bears the family name) and the wealth it represents, fear losing independence by means of inheritance taxes arising from the death of a major shareholder. This is one of the reasons why in the UK, in contrast to what happened in US, the transition to public share offering came quite late. Hannah (1979) shows that in 1914, 80 per cent of large joint stock companies in Britain were still private rather than public. 50 years later, all but a small minority of large firms were public companies. In the US, this transition occurred more rapidly: Berle and Means (1932) claimed that in 1929 no single shareholding was greater than 5 per cent within 58 per cent of the top 200 US companies.

1993). Although one could argue that the governance institutions of private firms generate the social cohesion and key for vigilance and attention, the empirical data seem to show a rather different picture at the level of productivity efficiency. The relative contribution of private and proprietorship companies to the increase in labour productivity (=value added / no. of employees) of the industry at the total level (see graph 2) in Colombia's manufacturing industry is modest compared to productivity gains shown by public companies.

## **INSERT GRAPH 2**

Evidence shows that value added and employment in public companies have increased Colombia's average manufacturing industry's performance, whilst private and proprietorship companies have maintained or decreased, respectively, their contribution to total value added and employment.<sup>12</sup> Indeed, the same institutional differences are strongly associated not only with low productivity but also with a low performance of the innovation process (see Author, 2002). This suggests that legal institutions –and not only firm size– count in the explanation of productivity and innovation differences.

### **4. Discussion**

Conditions for an increase in the number of public LLCs' in Colombia's manufacturing industry are different to conditions in countries like UK and US, where diffusion is commonly related to the divorce between ownership and control (Chandler, 1977). Cuevas (1986) acknowledges that the publicly quoted company was an important mechanism through which Colombian manufacturing industry attracted new capital since the 1930s. The creation and regulation of the Bogota's Stock Market in 1931 gave a great stimulus to the public LLCs (Cuevas, 1986). Echavarría (2000) argues that the foremost industrial development in Colombia's manufacturing industry was based on the public LLCs in the 1930s, where stockholders were predominantly members of minorities and underprivileged groups.

However, predominantly due to the weak anti-competitive regulations, this pluralistic and democratic start did not last (Narvaez, 1985). Many of the now most respectable public LLCs of Colombia's manufacturing industry like Nacional de Chocolate or Colombiana de Tabaco were created by the merger or takeover of small enterprises in the 1930s (Hommes 1996). Similarly, the anti-trust policy of the government during the 1950s and 1960s gave too much freedom of action to economic groups pursuing anti-competitive practises (ibid.).

The evidence shows that Business Groups used public legal form because it allowed them to absorb as many rival companies as they could.<sup>13</sup> They were able to incorporate all owners of rival firms as small shareholders (given that there was no upper bound for the number of owners).<sup>14</sup> For example, the predatory strategy of Grupo Suramericana saw them merge with financial organizations such as banks and insurance companies to maintain a flow of capital for the corporation's expansion, multiplying the shareholding and credit power. Indeed, ownership over financial institutions, which by law could be acquired through shares purchased in the stock

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<sup>12</sup> As a reflection of the national level, the evolution of productivity, value added and employment at the sectoral level depict a very similar picture (Author, 2002).

<sup>13</sup> This strategy was adopted by many companies such as Coltabaco, Nacional de Chocolates, Fabricato-Coltejer, among others (Álvarez, 2003).

<sup>14</sup> Groups would then transform the absorbed companies into spin-offs, legally dependent or subsidiary firms, or simply shut them down (Hommes and Silva 1981). The private legal form would not allow this behaviour, given the maximum of 25 permitted owners, hence frustrating ex ante any predatory strategies.

market (e.g. insurance companies before 1970s and financial companies in the 1970s), allowed the conglomerates to increase their power of shareholding across the sectors in which it had stakes. The evolution of the modern public LLC generated a highly concentrated model of finance and control. The patterns of concentration were substantial and incremental from the beginning of the industrialization process (Bejarano, 1998). Diversification of stronger firms was a key strategy to retain market share. So, for example, Argos, instead of growing internally, opted for creating two new companies: Cementos del Valle and Cementos del Caribe. Argos was used as holding company and, by multiplying the legal entities, increased their market power (Hommes and Silva, 1981). The alternative strategy, firm expansion and growth, would mean gathering new external sources of capital at the expense of losing some control, and this was deemed too risky for the inner group. Thus, the public legal form was adopted less by the weaker firms, given their vulnerability to powerful groups and the exclusive dependence of the public companies on the capital market. Instead, the public legal form was more used by powerful Business Groups, where fusion and merging activities between financial organizations such as banks and insurance companies constituted the strategy in order to maintain a flow of capital for the Group's expansion. Besides Argos other companies such as Coltejer and Fabricato followed a similar development strategy.<sup>15</sup>

In Colombia's manufacturing industry the creation of Business Groups and powerful interest groups was done at the expense of other (more democratic) groups, such as the cafeteros i.e. coffee producers (Saenz, 1992). Hommes and Silva (1981) explain that the public LLCs were a tool used for concentration and monopolization in Colombia's manufacturing industry. By attracting the mostly weaker competitors (by making them minor shareholders in their firm), the strongest capitalist groups were able to manipulate public savings by offsetting any potential threat to control the market. From the 1930s up to the end of 1960s, the public LLC had virtually monopolized public savings because it constituted the first mechanism at the disposal of financial capitalist to use public savings (Hommes and Silva, 1981). This financial capital would then be used to facilitate the take over of other firms and create a pervasive control capability.

How was the legal institutional environment supposed to adapt in this stringent and concentrated industry? The evidence from Colombia's manufacturing industry seems to support the theory that stringent environments require radically restrictive measures. Inside an industry with big and powerful capitalist groups, starting up one's own business can be a daunting task, even when one belongs to a Business Group. When the creation of a new business is financially viable, the new venture should counter with a pre-emptive strategy: not giving access of entry to those Business Groups that have used the public LLC as a tool for centralization of control and concentration of capital. The new business creator and her/his associates do not want powerful rival firms to take over the majority of the equity of the firm through public holdings: public LLC structures would be the last option. When a pre-emptive strategy is established, a self-sustained mechanism ensues. This, in the context of Sugden (1989) and Young (1993), would have the characteristics of an evolutionarily stable institution (see Author and Daniels, 2003). This salient pre-emptive characteristic is embedded in Colombia's manufacturing industry giving it the enhanced ability to survive and reproduce. The private legal setting established itself as a socially habituated way of action among firms when the big and powerful conglomerates absorbed those that opted to adopt a public setting. This precisely happened to those firms that were absorbed in order to create the Nacional de Chocolate or Colombiana de Tabaco (Hommes, 1996).

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<sup>15</sup> It is interesting to contrast the case of Colombia with that of Taiwan (see Campbell, 1997 or Author, 2002 for a discussion).

## 5. Conclusions

The private legal setting of firms has the characteristics of an evolutionarily pre-emptive and stable institution, which was entrenched historically in Colombia's manufacturing industry. The predatory strategies that caused this entrenchment, however, had significant collateral effects. With the pre-emptive strategy, firms were able to avoid hostile takeovers from predatory rivals, but, as a collateral effect, an exclusive property structure, which excludes not only stakeholders but also intrapreneurs, emerged. The evolution leading to entrenchment and its consequences for the economic performance of firms are still unresolved issues and require further work. In this paper, we provide historical evidence to suggest that such evolutionarily pre-emptive and stable institutions have led to an institutional 'lock-in' in Colombia's manufacturing industry. The statistical evidence suggests that businessmen, by adopting the private firm's structure, were undertaking technical but not symbolic institutional change. Businessmen did not anticipate that it would deeply affect the economic performance of their firms. It seems that Colombia's manufacturing industry's institutional evolution has perpetuated a major weakness of the classical capitalist system due to the concentrated and stringent system it is embedded in. The pre-emptive exclusive ownership strategy has had ex-post consequences and has left the Colombian companies exposed to the vices inherited from the classical capitalist system.<sup>16</sup> These conditions established an exclusive, restrictive, and static group of owners. Moreover, transferability is restricted not only to outsiders but also to insiders such as intrapreneurs and other stakeholders. This constitutes a situation resembling de Soto's apartheid-like capitalism in which intrapreneurial activities are frustrated whilst they look inside the ownership structure from outside. This exclusionist "glass bell" also matches Schumpeter's concern with the separation between ownership and entrepreneurship, which subsequently would doom the entrepreneurial activities.

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<sup>16</sup> Small and medium enterprises in the Colombian capitalist system distinguish themselves from other Andean countries for being generally private companies and with start-up capital mainly coming from familiar sources (Barriga 1998). Nearly 80% of the big private enterprises, including the majority of Business Groups, were (some of them still are) family businesses although having a setting as modern managerial firms (Revista Dinero 1999).

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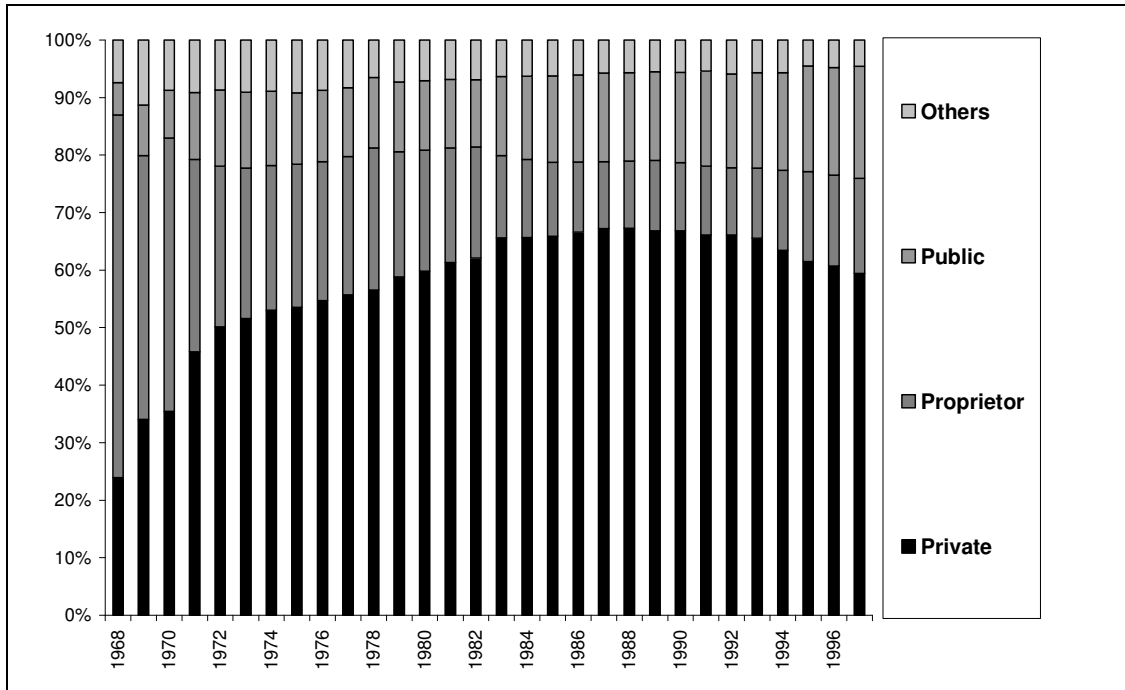
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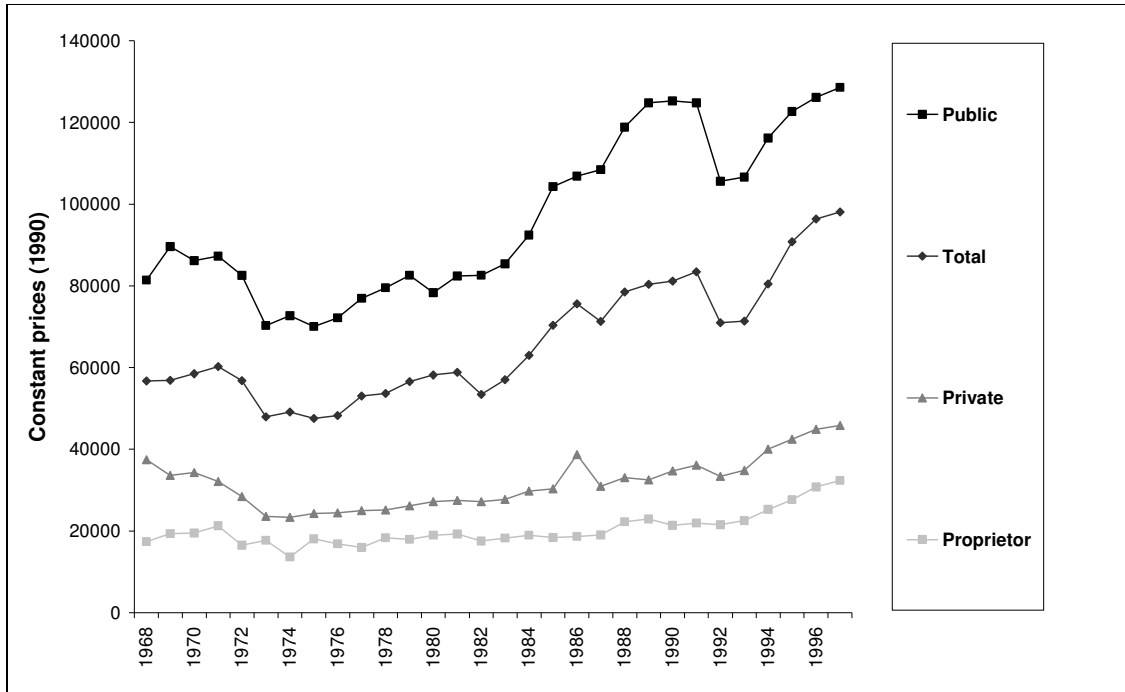
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**Graph One: Evolution of public, proprietorship, private and other corporations as percentage of the total of industries establishments in Colombia's Manufacturing Industry 1968-1997**



Source: Annual Manufacturing Survey. Colombia's National Statistics Department. Bogotá

**Graph Two: Evolution of labour productivity in total, proprietorship, private and public companies of CMI (1968-1997)**



Source: Annual Manufacturing Survey. Colombia's National Statistics Department. Bogotá