

# INFORMATION AS FACTOR OF THE POLITICAL ECONOMY OF BUSINESS ENVIRONMENT

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## Introduction

Problems of information are central to understanding not only market economics but also political economy. Information economics has already had a profound effect on how we think about economic policy, and are likely to have an even greater influence in the future. The business environment is, of course, more complicated than our simple – or even our more complicated models – would suggest.

The aim of this research is to study information influence on the political economy of business environment. For the achievement of the aim there are promoted such tasks:

- to find out the point of the political economy of information,
- to carry out the analysis of the contemporary political economy of the Government of Latvia,
- to characterise business environment in Latvia and its political economy.

## 1. The political economy of information

Information affects decision making in every context – not just inside firms and households. Some aspects of what might be called the political economy of information: the role of information in political processes, in collective decision making.

For two hundred years, well before the economics of information became a subdiscipline with – in economics, Sweden had enacted legislation to increase transparency. There are asymmetries of information between those governing and those governed, and just as markets strive to overcome asymmetries of information in political processes can be limited and their consequences mitigated.<sup>(10)</sup>

Information imperfections, and asymmetries of information, are pervasive in every aspect of life and society.

Not surprisingly, then, the “information rules of the game,” both for the economy and for political processes, can become a subject of intense political debate. The United States and the IMF argued strongly that lack of transparency was at the root of the 1997 financial crisis, and said that the East Asian countries had to become more transparent. The recognition that quantitative data concerning capital flows (outstanding loans) by the IMF and the US Treasury could have been taken as a concession of the inappropriateness of the competitive paradigm (in which prices convey all the relevant information); but the more appropriate way of viewing the debate was political, a point which became clear when it was noted that partial disclosures could be of only limited value, and could possibly be counterproductive,

as capital would be induced to move through channels involving less disclosure, channels like off shore banking centers which were also less well regulated. When demands for transparency thus went beyond East Asia to Western hedge funds and offshore banking centers, suddenly the advocates of more transparency became less enthralled, and began praising the advantages of partial secrecy in enhancing incentives to gather information. The United States and US Treasury then opposed the OECD initiative to combat money laundering through greater transparency of off shore banking centers – these institutions served particular political and economic interests – until it became clear that terrorists might be using them to help finance their operations; at that point, the balance of American interests changed, and the US Treasury changed its position. (5)

Political processes inevitably entail asymmetries of information: our political leaders are supposed to know more about threats to defense, about our economic situation, etc., than ordinary citizens. There has been a delegation of responsibility for day-to-day decision making, just as there is within a firm.(7)

The problem is to provide incentives for those so entrusted to act on behalf of those who they are supposed to be serving – the standard principal agent problem. Democracy – contestability in political processes – provides a check on abuses of the powers that come from delegation just as it does in economic processes; but just as we recognize that the take-over mechanism provides an imperfect check, so too we should recognize that the electoral process provides an imperfect check. Just as we recognize that current management has an incentive to increase asymmetries of information in order to enhance its market power, increase its discretion, so to in public life. And just as we recognize that disclosure requirements – greater transparency – and specific rules of the game (e.g. related to corporate governance) can affect the effectiveness of the take-over mechanism and the overall quality of corporate governance, so too the same factors can affect political contestability and the quality of public governance.(6)

In the context of political processes, where “exit” options are limited, one needs to be particularly concerned about abuses. If a firm is mismanaged – if the managers attempt to enrich themselves at the expense of shareholders and customers and entrench themselves against competition, the damage is limited: customers at least can switch. But in political processes, those who see the quality of public services deteriorate cannot do so as easily. If all individuals were as mean spirited and selfish as economists have traditionally modeled them, matters would indeed be bleak: as I have put it elsewhere, ensuring the public good (public management) is itself a public good. But there is a wealth of evidence that the economists’ traditional model of the individual is too narrow – and that indeed intrinsic rewards, e.g. of public service, can be even more effective than extrinsic rewards, e.g. monetary compensation (which is not to say that compensation is not of some importance). This public spiritedness (even if blended with a modicum of self-interest) is manifested in a variety of civil society organizations, through which voluntarily individuals work collectively to advance their perception of the collective interests. (8)

There are strong forces on the part of those in government to reduce transparency. More transparency reduces their scope for action – it not only exposes mistakes, but also corruption (as the expression goes, sunshine is the strongest antiseptic). Government officials may try to enhance their power, by trying to advance specious arguments for secrecy, and then saying, in effect, to justify their otherwise inexplicable or self-serving behavior, “trust me... if you only knew what I knew.” (9)

There is a further rationale for secrecy: secrecy is an artificially created scarcity of information, and like most artificially created scarcities, it gives rise to rents, rents which in some countries are appropriated through outright corruption (selling information), but in others are part of a “gift exchange” in which reporters not only provide puff pieces praising the government official who has given the reporter privileged access to information, particularly in ways which are designed to enhance the officials influence and power, but distort news coverage. Without unbiased information, the effectiveness of the check that can be provided by the citizenry is limited; without good information, the contestability of the political processes can be undermined.

One of the lessons of the economics of information is that these problems cannot be fully resolved, but there are laws and institutions which can decidedly improve matters. Right-to-know laws, demanding transparency, have been part of governance in Sweden for two hundred years; they have become an important if imperfect check on government abuses in the United States over the past quarter century. In the last five years, there has become a growing international movement, with some countries, such as Thailand, going so far as to include them in their new Constitution. Regrettably, these principles have yet to be endorsed by the international economic institutions.(10)

## **2.Contemporary political economy of the Government of Latvia**

Since the regaining of independence in 1991 all the governments of Latvia consistently implemented the transition to market economy and integration into NATO and the EU.

Latvia realizes a liberal foreign trade and foreign investment policy. The law guarantees protection of foreign investment, foreign nationals may freely repatriate their profits and capital, and equal terms are provided to domestic and foreign entrepreneurs.

The priorities declared by government are:

- sound and efficient public administration;
- full-fledged membership of Latvia in the decision-making processes of the NATO and the European Union;
- strong and independent judicial power, corruption and crime prevention;
- information society and knowledge-based economy;
- health quality of the society;

- integrated civic society, strong modern national identity;
- balanced development of Latvia's regions, high-level employment.

To create preconditions for stable economic growth, the government supports stability of exchange rate of the national currency (LVL), low inflation and budget fiscal deficit at the level not above 3% of GDP. The medium-term aim – non-deficit budget. The current account deficit will be gradually brought down by fostering exports and by ensuring economic growth.

The government has already reduced and plans further reduction of tax burden on businesses. Starting with 2002 the corporate income tax is being gradually brought down from 25% to ultimately 15% (22% in 2002, 19% in 2003 and 15% in 2004) to attract more investment. The legislation stipulates certain corporate income tax exemptions, for example, to large (supported) investment projects as well as to the enterprises producing high technologies or software or operating in special economic zones; small businesses, etc.

Starting with January 1, 2003 it is planned to decrease social insurance contributions from 35.09% till 33.09% and starting with 2004 property tax rates will be brought down from 1.5% till 1% of the cadastral value of the respective property.(11)

The government actively fights tax evasion. The priorities in this field are: fighting all kinds of smuggling, VAT fraud and eradication of the “envelope” salaries.

The law “On Establishment of the Anti-Corruption Authority and Fight Against Corruption” gained effect on May 1, 2002. The government has made the commitment to ensure efficient work of the anti-corruption authority by reinforcing its independence, granting bigger investigative authority and attracting international experts as well as wider involvement of the society in fighting corruption.

Procurement Supervision Bureau started to operate in 2002 having much wider authority to control purchases made by central and local governments. The government has promised to ensure complete transparency of state and municipal procurement orders by publishing all information about purchases, including the submitted offers, decisions of the evaluation commission, concluded contracts, their amendments and annexes.

To prevent overlapping and irrational use of resources it is planned to carry out audit of functions of public administration institutions, to transfer to “zero” state budget development principle — to verify usefulness and efficiency of utilisation of all budgetary resources and to eliminate wasteful employment of the budget resources. Creation of a single system of remuneration in the state civil service has been started. The government plans to consolidate the whole civil service and include all agencies subordinated to the Cabinet of Ministers in one system.

### **3. Business environment in Latvia and its political economy**

Targeted work at the improvement of business environment is carried out introducing requirements of *acquis communautaire* and implementing the Action Plan to Improve Business Environment.

The Action Plan has assisted to reach a considerable improvement of entrepreneurial environment by lessening administrative obstacles, streamlining tax administration, customs and border crossing procedures, providing wider access to information and better protection of investors. They refer to such areas as fighting corruption, state and municipal purchases, judicial powers and corporate law.

The Commercial Law gained effect on January 1, 2002 marking a fundamental reform of the business environment. It will systematise in one place all the issues regulating business that until now were scattered in various legislative acts and will revoke series of outdated legislative provisions and will establish a safe system of protection of creditors and minority shareholders.

Protocol on European Conformity Assessment and Recognition of Industrial Goods (PECA) signed in Brussels in May 2002 plays a significant role in regulation of business environment. The protocol will provide Latvian producers the opportunity to export on easier terms their products to markets of the EU member states without additional conformity assessment procedures (certification, testing, etc.).

The Development Programme of Small and Medium-Sized Enterprises of Latvia 2003-2006 is being worked out. One of the most important tasks for the present moment is streamlining of the complicated and until now poorly co-ordinated system of state support funds so that businesses have clear understanding as to where and in what cases they can receive state support to enhance competitiveness of their business.

The Mortgage and Land Bank of Latvia will have an important place in the system of state support. The Government wants to convert this bank into a Development bank. A lot of important state supported target programmes already now are implemented through this bank. In 2000-2002 the Mortgage and Land Bank of Latvia received state guarantees to support SME projects for the amount of 10 million LVL. In October 2002 the Cabinet of Ministers passed the decision on further development of the SME crediting programme for the next three years and provided state guarantees to the bank in the amount of 20 million LVL.(11)

Also the Latvian Guarantee Agency might become an efficient mechanism of SME support. In 2003 the agency is going to receive 250 thousand LVL of state budget funds to support its work.

One of the key objectives of the government in the area of structural reforms is to improve regulation of services and reinforce competition in the energy and telecommunication sectors. On September 1, 2001 the Public Utilities Commission (a

united regulator) started its work. The authority is responsible for all public services, telecommunications, postal services, railway transportation and power industry (except local heat supply where electricity is not generated in the production process). The law says that the Regulator is independent to perform functions prescribed by the law and that the decisions or administrative acts made by the Regulator may be challenged only by the court.

After January 1, 2003, in conditions of liberalisation of the public telecommunication network, new undertakings will be able to enter this market and use the existing infrastructure for offering additional telecommunication services.

State-owned property privatisation is in the phase of completion. Only some large-scale public monopolies are not yet privatised. Privatisation of these enterprises is politically and economically significant and complicated. Certain advancement of privatisation of large-scale enterprises was reached during the last year.

The government carries out different measures to improve the situation in the area of employment. These measures are included in the annual National Employment Plan (NEP). NEP for the year 2002 contains a list of 119 employment promotion activities attracting resources in the amount of 16.6 million LVL. Measures contained in NEP are mainly focussed on perfection of working skills and support to business activity.

In line with requirements of the Accession Partnership document, the government of Latvia jointly with the DG on Employment and Social Affairs of the European Commission has prepared the Joint Declaration on Priorities of Latvia in the Area of Employment. The declaration reflects the totality of employment and labour market targets to implement the Employment Strategy for adaptation of the state labour market for functioning in the European Union.

From January 1, 2003 the minimum wage in Latvia is raised from 60 LVL till 70 LVL. The previous increase was in July 2001.(11)

Latvia has started several important reforms to address social issues. State funded or the 2<sup>nd</sup> level pension scheme was launched on July 1, 2001 and is one of the most progressive in the countries of transition. This marked the end of introduction of a 3-tier pension system. Pension reform in the area of legislation is completed. The pension age will be gradually increased. In comparison with the previous system where the pension age for women was 55 years and for men – 60 years, the new system will equalise the pension age (62 years) between men and women by the middle of 2008.

Better mechanisms of providing and channelling social assistance are being introduced within the scope of the reform of the welfare system to ensure efficient integration of people in social and economic life and to provide better social protection.

In June 2002 the Cabinet of Ministers accepted the concept on education for 2002-2005. The concept is the foundation for the third phase of development of education aimed to increase quality of education on all phases of learning, to ensure access to education in the context of life long learning and to increase cost efficiency of education. Declaration on the Intended Activities of the Cabinet of Ministers foresees promoting growth of the role of education in the society and training of new specialists in line with the needs of the Latvian business environment.

Long Term Economic Strategy of Latvia defines basic positions of the economic policy. The aim of the strategy is to reach the average level of per capita GDP of the EU member states in the next 20-30 years. It is planned to change the currently dominating model of the Latvian economy as it is mostly based on the use of cheap labour and production with low value added. The offered way: intensive use of knowledge and high technologies, transition from labour-intensive economy to knowledge-intensive economy. This may be reached by simultaneous revival of traditional sectors of national economy on a modern technological base and the development of new, post-industrial knowledge-intensive sectors. Latvia will create the new economy and the importance of knowledge as a resource and wealth will grow in all sectors, also in traditional sectors, products or professions.

One of the basic priorities of the government is establishment of the information society. There are plans to establish the Information Society Bureau under subordination of the Cabinet of Ministers. The Bureau will develop, co-ordinate and supervise implementation of a uniform information and communication technology policy in the state.

Quite clearly, the further development of Latvia is linked with the process of European integration and only the accession to the European Union may ensure further and irrevocable strengthening and growth of the state. On December 13, 2002 at the summit of the EU Council in Copenhagen Latvia officially closed accession negotiations and was invited to join the European Union. Provided that all EU member states ratify this decision and the outcome of the referendum is positive, Latvia may become a EU member state already from May 1, 2004.

### **Conclusion**

In this work are explained the main aspects of the political economy of information, accentuate the role of asymmetries in the forming processes of the political economy and proved the affect of information to political economy of business.

According to the theory of the political economy of information the content of the contemporary political economy of the Government of Latvia has been researched and it cleared up that one of the Governments priorities is formation of information society and knowledge-based economy and improvement in availability of the information of the business environment in Latvia.

The author draws the conclusions that availability with information increases the political economy of the business environment and furthers making successful decisions in the micro business environment as well as in the macro business environment.

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## **Zusammenfassung**

### INFORMATION ALS FAKTOR DER POLITÖKONOMIE DES MILIEUS DER UNTERNEHMERTÄTIGKEIT

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Das Ziel der Arbeit ist, den Einfluss der Information auf die Politökonomie des Milieus der Unternehmertätigkeit zu erforschen.

Zum Erreichen dieses Zieles sind folgende Aufgaben gestellt:

- 1) Das Wesen der Politökonomie der Information festzustellen.
- 2) Die Analyse der modernen Politökonomie der Regierung der Republik Lettlands durchzuführen.
- 3) Das Milieu der Unternehmertätigkeit Lettlands und seine Politökonomie zu charakterisieren.

In der Arbeit sind die Hauptaspekte der Politökonomie der Information erklärt, die Rolle der Informations- Asymmetrie im Prozess der Bildung der Politökonomie betont und der große Einfluss der Information auf die Politökonomie der Unternehmertätigkeit bewiesen worden.

Auf Grund der Theorie der Politökonomie der Information wurde der Inhalt der modernen Politökonomie der Regierung der Republik Lettland erforscht und festgestellt, dass eine der Prioritäten der Regierung ist, eine informierte Gesellschaft und eine auf Wissen basierte Wirtschaft zu bilden, ebenso auch die Verbesserung des Informationsumlaufs im Milieu der Unternehmertätigkeit Lettlands zu verbessern.

Infolge des Obenerwähnten schlussfolgert die Autorin, dass die Versorgung mit der Information die Politökonomie des Milieus der Unternehmertätigkeit verbessert und die Fassung erfolgreicher Beschlüsse in der Unternehmertätigkeit wie im Mikro-, so auch im Makroumfeld der Unternehmertätigkeit fordert.