

**RUSH!**

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## THE MIDDENDORF PLAN'S STRATEGY FOR CENTRAL AMERICAN ECONOMIC GROWTH

The threat of Soviet-sponsored communist expansion in Central America and other less developed countries (LDCs) correctly has been a major concern of the Reagan Administration. The Administration has sought to reduce this threat in two ways: first, by promoting political freedom and democracy, and second, by encouraging economic freedom and democracy through free enterprise capitalism. The Administration's support for freedom fighters and for democratic institutions constitutes one of the elements of this two-pronged strategy. Linking U.S. assistance in LDCs to free market-oriented economic reforms has been part of the second prong. Recently the Administration unveiled another critical element in its strategy for economic democracy--the Middendorf Plan for Growth and Justice--prepared by the Presidential Task Force on Project Economic Justice.

Chaired by the former U.S. Ambassador to the Organization of American States, J. William Middendorf, the task force calls attention to the successful use in Costa Rica and several other countries of various types of employee stock ownership plans (ESOPs) as a means of promoting economic and political freedom. The Middendorf Report recommends to the President that the U.S. make ESOPs a central element of its growth-oriented strategy for LDCs. Congress and the Administration should act swiftly on the Middendorf Plan's recommendations.

**Failed Government Policies.** The Third World's economic problems, for the most part, are the result of government regulation of the economy and state ownership of many major industries. These actions have suffocated enterprise and forced massive subsidies of money-losing firms. Government borrowing to cover such losses is a major cause of chronic LDC indebtedness. Yet when LDC governments seek to reverse these failed policies, they invariably encounter strong local opposition from vested interest groups. Workers in the state-owned companies particularly fear the loss of their jobs and benefits should the firms be returned to the private sector. The Middendorf Plan makes clear that ESOPs can help remedy this political and economic problem. Under ESOPs, employees purchase or are given shares in a company, or acquire ownership of the entire company itself. ESOPs now are common in the developed world, where they often have boosted productivity.

**Enthusiastic Boosters.** In the LDCs, the ESOPs provide an ideal vehicle for privatization of government-owned enterprises. The prospect of ownership by individual employees often can turn worker opposition to privatization into strong support. In Great Britain, for example, workers originally hostile to Prime Minister Margaret Thatcher's proposals to sell such state-owned enterprises as National Freight Corporation, Britain's largest trucking firm, and Hoverspeed, a cross channel ferry company, were transformed into enthusiastic boosters when the workers realized that they could own part of the new firm. Employees with ESOP incentives often can turn money-losing companies into profitable ventures. In the U.S., for example, the West Virginia-based Weirton Steel Company, once on the brink of bankruptcy, was acquired by its employees in 1982 through an ESOP. The company now is posting record profits while much of the U.S. steel industry stagnates.

ESOPs are a particularly attractive way of pursuing privatization and economic democracy in LDCs. For one thing, employee ownership generates new sources of small-scale capital, widening ownership and reducing dependency on foreign capital. For another, the cooperative ESOP form of ownership by workers preserves economies of scale and coherence of management. By contrast, the small-scale individual ownership models favored by some governments pursuing land and business reforms often undermine the economic viability of the enterprises by sacrificing economies of scale.

**Willing Freedom Fighters.** ESOPs also strengthen workers' support for free enterprise and galvanizes their opposition to communism. In the 1970s and early 1980s, for example, the privately owned Guatemalan coffee plantation of La Perla found the government unable to protect it from communist guerrilla attacks. When the owners of the plantation voluntarily sold sizable blocks of stock to their employees, the result was not only a more enthusiastic and productive workforce, but willing freedom fighters as well. The employees formed civilian patrols and purchased weapons to protect their plantation. They have now successfully driven back communist guerrillas in the region.

Democracy and economic growth in Central America--and elsewhere--require economic freedom and private property rights as well as political democracy. ESOPs give workers an ownership stake in a noncommunist, market-oriented society. The Middendorf Plan has already received wide bipartisan backing on Capitol Hill. The Administration and Congress should act quickly to explore ways of integrating ESOPs into America's foreign aid programs.

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For further information:

*High Road to Economic Justice*, Report of the Presidential Task Force on Project Economic Justice, Center for Economic and Social Justice, October 1986.

J. William Middendorf, II, "A Free Market Prescription for Third World Debt," Heritage Foundation Lecture No. 46, 1986.