

## BOOK REVIEW

EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE  
IN FIRMS, ORGANIZATIONS, AND STATES. BY ALBERT  
O. HIRSCHMAN. Cambridge: Harvard University Press, 1970.  
Pp. x, 162. \$1.95 paperbound.

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In a short, brilliant essay, an economist challenges the classic view that competition can or should always be relied upon to discipline firms by excluding them from the market in favor of their lower-price, better-quality rivals. The metaphor "exit" seems to cover desertion of a firm by some of its customers as well as disappearance of a firm from the market because of customer attrition. But Hirschman emphasizes the fact that big firms do not disappear, except from the model universes of some economists, and that summary exit of firms would not be desirable. Rather, the firm should receive its trouble warnings—whether from the initial exit of the most sensitive customers or from "voice"—in time to effect "recuperative" measures. The exit model of a competitive economy grows more and more remote from reality as the size and diversity of operations of the corporate giants increase. Manifestly, great corporations neither die nor fade away. They are "reorganized," sometimes with no substantial change of management, under favorable bankruptcy law provisions. Or they are rescued from fatal consequences appropriate to their entrepreneurial mistakes by loans and other support from tax sources. Or they are metamorphosed as divisions of vast acquiring corporations to whom they have special value for their tax losses; *i.e.*, survival has once more been financed at the expense of the taxpayer.

"Voice" is organized consumer complaint, of which Ralph Nader is the avatar. Its effectiveness may rest in part on the threat of exit, but it functions even where exit is difficult or impossible, as in the case of monopolies and oligopolies.<sup>1</sup> Given the reserves of unexercised

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<sup>1</sup> See HIRSCHMAN, EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES 124 (1970):

[O]rganizations and firms that are ostensibly competing and are normally sensitive to exit can learn to play a cooperative, collusive game in the course of which they take in each other's disgruntled customers or members. To the extent that the game is played successfully by competing organizations or firms, exit, compensated as it is by entry, ceases to be a serious threat to the deteriorating organizations.

Letters collected by Ralph Nader and made available to Hirschman illustrate the foregoing point:

(a) to the Ford Motor Company: ". . . You can be assured that I absolutely will not purchase another Ford of any kind no matter what your usual form letter to me will say . . ." ". . . Needless to say my Falcon

power ("slack") in all firms, and notably in lethargic monopolies (Hirschman ridicules the classic model of the "taut" economy, according to which one false move, a moment's relaxation in the obsessive effort to maximize profits, spells disaster for the firm), and given also management's desire to escape the discomfort of clamorous criticism, a determined minority of dissatisfied customers can influence policy.

But this potentiality will not be realized if exit is a readily available alternative to solve the problems of those most likely to be sensitive to decline in the quality of service and most ingenious and persistent in using voice. Hirschman takes as an example the Nigerian national railroad system. He observed that it was miserably inefficient, notwithstanding the lively competition of road transport which should theoretically have goaded it into decent performance. He explains this paradox by pointing out that the threat of exit is no great stimulus to an enterprise that can cover its losses out of the public treasury, and that voice is dampened in such a situation by the ease with which the most vigorous of the railroad's clientele can shift to the motor highways. Hirschman might well have cited, in this connection, the transport system of the United States, where potent sources of "voice" have been muffled by the easy escape of farmers and big corporations from the constraints of regulated transport through the private carriage and agricultural exemptions of the Motor Carriers Act.<sup>2</sup>

A similar analysis leads Hirschman to reject proposals for a "market" solution to the problems of public education, *e.g.*, by arrangements encouraging private schools (*i.e.*, exit from the public school system). The end of concern for the public school system by those most likely to be able to bring about its recuperation would, on this view, condemn the system to utter degradation. Hirschman also argues that, where "public goods" are at issue, *e.g.*, police, fire protection, schooling, exit is illusory; each person has a stake in others enjoying the public good; in a sense, therefore, one remains a consumer even after he exits. Accordingly, the encouragement of voice may call for the design of economic and political institutions in which exit is inhibited. It is in this connection that Hirschman identifies and examines the function of "loyalty" as a beneficent restraint on premature exit.

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is the last of any Ford product I would consider to purchase. I am a young girl of 25, reasonably attractive, who has depleted her bank account buying Falcon transmissions, when there are other things in this world where the money could be put to much better use . . ."; and (b) to the General Motors Corporation: ". . . At home we have a Chevrolet bus and a Chevrolet van. You may be sure that after all of this trouble and inconvenience and wasted time I shall never own a General Motors product again . . ." ". . . I have had a G.M. auto and wagon for many years now but maybe FORD has a better idea. I'll try to put up with this LEMON till the '70 models come out, but you can be sure there will be no G.M. product of any kind on my driveway . . ."

*Id.* 27-28 n.7.

<sup>2</sup> 49 U.S.C.A. §303(b)(6) (Supp. 1972); 49 U.S.C. §303(c) (1970). See SCHWARTZ, *FREE ENTERPRISE AND ECONOMIC ORGANIZATION* 359-62 (4th ed. 1972).

Hirschman is as interested in applying the analysis to nonprofit organizations, particularly political parties, as he is in exploring alternatives to exit in the economic field. On the political side, he sees insufficient reliance on exit corresponding to insufficient reliance on voice in economics. He uses as a prime illustration the failure of leading figures in the Johnson administration to resign over their disagreement with the Vietnam policy. Voice was here cleverly suppressed by offering potentially powerful critics the illusion of influence through "working from within." It is, of course, a nice question when to accept the harsh fact that voice, as an insider, has become ineffectual, and to go over the barrier of loyalty to exit. Hirschman sees political and business managers as regularly engaged in protecting their power positions by diverting discontent from exit to ineffectual voice, as in the Post Office's infamous statutory bar against the escape of its much-abused customers to more efficient private carriers,<sup>3</sup> or from voice to ineffectual exit, as in the cross-exit of aggrieved customers of GM to Ford, and aggrieved customers of Ford to GM.<sup>4</sup>

What are the implications of Hirschman's insights for lawyers and legislators concerned with the economy? He never relates his thesis directly to the antitrust laws, and I have difficulty envisioning any relaxation of the law on this front that he would think called for by his proposal that we not rely *exclusively* on competition. The role of voice is not to replace exit, but to supplement it, as regulation supplements the antitrust laws in contexts where competition cannot be the sole reliance to protect the public welfare.<sup>5</sup> Indeed, since regulation too is a weak reed,<sup>6</sup> voice will be at least as significant in the regulated sectors of the economy as in the putatively competitive sectors.

Should we then seriously consider blocking the exits from regulated service, by repealing or narrowing the exemptions for private carriage, contract carriage, agricultural carriage, or cooperative self-service, so as to generate voice, as implied in Hirschman's anecdote about the Nigerian national railway? I think not. The optimal mix of exit, regulation, and voice depends on the particular politico-economic setting. Even assuming that Hirschman wanted the exits blocked in Nigeria, the United States is not Nigeria. The American regulatory mechanism, for all its defects, is presumably stronger than that of Nigeria, and comes under the scrutiny of congressional committees and prestigious academic critics. Moreover, exit, under American condi-

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<sup>3</sup> 18 U.S.C. §§ 1694, 1696 (1970).

<sup>4</sup> Monopolists have need of illusory competition for this purpose. See note 1 *supra*.

<sup>5</sup> Cf. *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963); *California v. FPC*, 369 U.S. 482 (1962).

<sup>6</sup> See generally KAHN, *THE ECONOMICS OF REGULATION* (1970-1971), reviewed in 120 U. PA. L. REV. 584 (1972).

tions, powerfully reinforces voice: the legislative exemption secured by influential political groups (agricultural interests; giant corporations that can operate their own fleets of trucks) gives the lie to the myth that regulation is essential to maintain good service and low, cost-related prices. Our tolerance of exit also exposes the hypocrisy of the contention that "national defense" or highway safety requires the maintenance of a restrictionist system of transport regulation: why should "farmers" and oligopolists escape or wish to escape making their fair contribution to "national defense" and enjoying the vaunted benefits of highway safety under monopoly regulation?

One can imagine situations where exit might usefully be barred. It might, for example, be worthwhile restraining the switch from public buses to private cars by excluding the latter from central city areas. Here more is at stake than the putative gain from enhancing voice. There is also the need to recognize that classic market mechanisms do not charge the private motorist with all the social costs of his traffic-choking presence.

It is also obviously the part of wisdom to refrain from *encouraging* exit from the rails to the highways, *e.g.*, by subsidizing highway or barge transport or by holding rail rates high to pay returns on securities whose claims to cash flow should long ago have been eliminated through bankruptcy. A cold disregard for sunk capital costs, in an industry in which new investment is unlikely, might put rail rates at a level that would stop the switch of freight to trucks. Perhaps we should reexamine the trade-off between rail efforts to hold or gain customers through "discriminatory" pricing and the anti-competitive impact of such discrimination on other modes of transport or upon disfavored shippers. Loyalty must be encouraged, not a mythical virtuous loyalty that ignores self-interest, and not a loyalty unstably built upon advertising that deceptively manipulates consumer preferences, but a loyalty resting on realistic hope of improvement through customer organization and pressure. One wonders in this connection what the experience has been with associations of shippers dealing with rail and steamship carriers.

The general implication of Hirschman's essay for lawyers and legislators is that we must continually broaden our categories of remedial measures against the lethargy and abuses of concentrated power. We must learn to discriminate situations where exit is and will continue to be the best signal to industrial managers and party big-wigs from other situations where voice is the best hope and the immediate objective must be to strengthen it. Among the ways that voice might be strengthened in our economy are the following: build up the leverage of public interest groups in administrative proceedings,<sup>7</sup> establish the power of the Federal Trade Commission to order affirma-

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<sup>7</sup> See Comment, *Public Participation in Federal Administrative Proceedings*, 120 U. PA. L. REV. 702 (1972). *But cf.* *Sierra Club v. Morton*, 405 U.S. 727 (1972).

tive disclosures by advertisers, require advertising media to provide space and time for "anti-advertising" by consumer groups, devise more effective class actions in favor of consumers, subsidize independent consumer research and education, and conduct "yardstick" operations under government sponsorship in fields other than electrical power.<sup>8</sup>

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<sup>8</sup> This oblique reference to the Tennessee Valley Authority is to be understood as relating to one of the concepts that animated it at the time of its creation in the 1930's; not to the mature conservatism of the present industry-oriented bureaucracy.

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