Determinants Affecting the Privatisation of Local Government Services in Britain

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Authors

Oe-Chool Choi, Visiting Professor, Department of Social Policy, University of Newcastle, Newcastle upon Tyne, UK (Professor, Department of Regional Development, Yeungnam University, Kyungsan, South Korea) (e-mail: occhoi.@ynucc.yeungnam.ac.kr)

Young-Chool Choi, Visiting Fellow, Department of Social Policy, University of Newcastle, Newcastle upon Tyne, UK (Assistant Professor, Department of Public Administration, Chungbuk National University, Cheongju, South Korea) (e-mail: y.c.choi@ncl.ac.uk)

Abstract

This paper investigates the main determinants affecting the privatisation of local government services in Britain. The last decade in Britain has witnessed sustained 'top-down' pressure to privatise local government services. We argue that empirical policy output studies associated with the privatisation of local government services have been largely unexplored in the literature, owing to an inordinate emphasis upon an economic approach derived from public choice theory. Thus, spatial variations in the privatisation of local government services in Britain have largely been neglected and have received less attention than they should. This paper seeks to remedy this neglect via an examination of the determinants of Compulsory Competitive Tendering, which is one of the many forms or dimensions of privatisation at the local level. In order to identify these determinants, path analysis was employed.

Our research found that in the path analysis for 1991 the political variable, *party control*, was the strongest determinant influencing privatisation, whereas in the analysis for 1994 the strategic variable, *geographical location*, was the strongest. This implies a need for more in-depth case study analysis in order for us to understand more fully how privatisation has been implemented.

Determinants Affecting the Privatisation of Local Government Services in Britain

1. Introduction

This paper investigates the main determinants affecting the privatisation of local government services in Britain. The last decade in Britain has witnessed sustained 'top-down' pressure to privatise local government services. We argue that empirical policy output studies associated with the privatisation of local government services have been largely unexplored in the literature, owing to an inordinate emphasis upon an economic approach derived from public choice theory and also a theoretical battle between opposed partisan views. Thus, spatial variations in the privatisation of local government services in Britain have largely been neglected and have received less attention than they should. This paper seeks to remedy this neglect via an examination of the determinants of privatisation. In order to clarify these determinants, path analysis was employed.

In analysing the determinants of privatisation, this study will centre on 296 non-metropolitan districts in England, employing data for two time-points, 1991 and 1994, thus providing a dynamic perspective on the research question: what factors affect the output of CCT?

This study adopts DSO (Direct Service Organisation) proportion as the dependent variable. Direct Service Organisations comprise the staff employed by the local authority itself to deliver services, and form the contractor side of the authority, operating on a trading basis with client departments. More specifically, DSO output or DSO proportion indicates the distribution of tenders between the DSO and private contractors: that is, the proportion of tenders won by the DSO during the CCT process. In other words, it indicates the percentage of the total value of work that is undertaken by the DSO following the competitive tendering process.

2. Analytical framework, hypothetical causal relationships and hypotheses

2.1 Analytical framework

In this study, the analysis identifying the main factors of DSO output in the CCT policy process is primarily based on the system model. This implies that public policy is best understood by considering the operation of a political system in its environment and by examining how such a system maintains itself and changes over time (Ham and Hill, 1993: 39; Hansen, 1981: 28-32).

This perspective emphasises the impact of policy environments on policy output and the relationships between environmental variables. This study highlights the relationships between public policy output and the social, economic and political variables of local government. Fortunately, other political scientists (Boaden, 1971; Easton, 1965; Ham and Hill, 1993; Newton and Sharpe, 1977) have worked on this issue of uniting public policy with its environments. In Ham and Hill's terminology (1993: 9-10), policy output studies are studies of policy outputs which seek to explain why levels of expenditure or service provision vary between areas. They take policies as dependent variables and attempt to understand these policies in terms of social, economic, technological and other factors.

David Easton describes a model of the 'political system' that we can modify to suit our purposes. Our analytical model is based mainly on a modified version of Easton's system model, thereby providing the framework within which the variables are organised. Although some efforts have been made to refine the models of analysis, most studies so far have been based on the general theoretical approach, where a simplified version of Easton's general system model has provided the framework within which the variables have been structured (Newton, 1981: 23).

Discussions of the findings have focused mainly on the range, reliability and validity of the variables - both dependent and independent - used in these studies (Fry and Winters, 1970). Far less attention has been paid to the interrelationships between

variables and their relative importance in public policy output. Since the late 1970s, serious attempts have been made to revise and refine the models of analysis. One such attempt (Lewis-Beck, 1977) has used path analytical techniques based on causal models of the relationships between environmental variables underlying government public policy.

Lewis-Beck has suggested that research efforts to date have failed to assess accurately the relative importance of environmental variables for public policy, in large part because they have relied on statistical techniques that are inadequate for the task (Lewis-Beck, 1977: 559-60). Thus, in order to make accurate assessments of the relative importance of socio-economic and political variables, and their relationships, it is, according to Lewis-Beck, necessary to specify the underlying causal structure and estimate its parameters. He suggests the use of 'effect coefficients' which combine the direct and indirect effects of causal variables.

How, then, are we to interpret the relationships between political and environmental characteristics? It seems more reasonable to treat them as interrelated factors in analysing public policy output, which public authorities may influence, than to consider the political variable only as a filter which other environmental variables should pass through to affect the policy output. In other words, the decision process is affected by a number of factors surrounding the policy process, including political and other environmental variables. In this model we interpret these relationships of variables as a causal chain, and assume that there are direct and indirect causal links between environmental variables and policy output.

2.2 Hypothetical causal relationships

There is a substantial body of work on the behavioural determinants of local government policy output, drawn from a variety of different intellectual disciplines, including economics, political science and organisational theory (e.g. Barnett *et al.*, 1990; Danziger, 1976; Ferris, 1986; Sharpe and Newton, 1984; Tiebout, 1956). Such

research has mainly (but not entirely) focused on expenditure or revenue. Also, it has rarely been concerned specifically with CCT or privatisation policy, in spite of the fact that since the early 1980s CCT or privatisation policy has played a major role in British local government service provision. Much of the literature concerning local authorities in Britain deals with overall expenditure levels, fiscal decisions or budgetary decision- making.

In the meantime, most of the literature on CCT has taken a descriptive, institutional and political approach. This has concentrated on changes in government policy, the response of local authorities and public unions to CCT and the savings arising from competition. Much less attention has been paid to the determinants of CCT policy output. All in all, the output study employing an analytical approach has a lot to commend it as a method for elucidating the policy process. This study employs such an approach in building a framework for the analysis.

It seems that there is no generally agreed method of assessing the impact of factors affecting policy output (Page *et al.*,1990: 44). This study addresses an array of environmental and contextual factors, including economic, political, demographic, strategic and organisational factors and DSO proportion (DSO output), primarily employing the system theory. In the absence of a comprehensive theory, it is necessary to create hypothetical causal relationships for analysis in accordance with the purpose of the research.

Figure 1 shows a hypothetical framework for the analysis of DSO output. The elements shown have mostly been dealt with in the field of policy analysis and organisational analysis. However, they are supplemented in line with the purpose of the research, and the interrelationships between the posited variables are to a certain extent intuitive and exploratory. In the following section, we discuss the anticipated effect of these sets of variables on DSO output, touching upon the theoretical expectations and empirical findings.
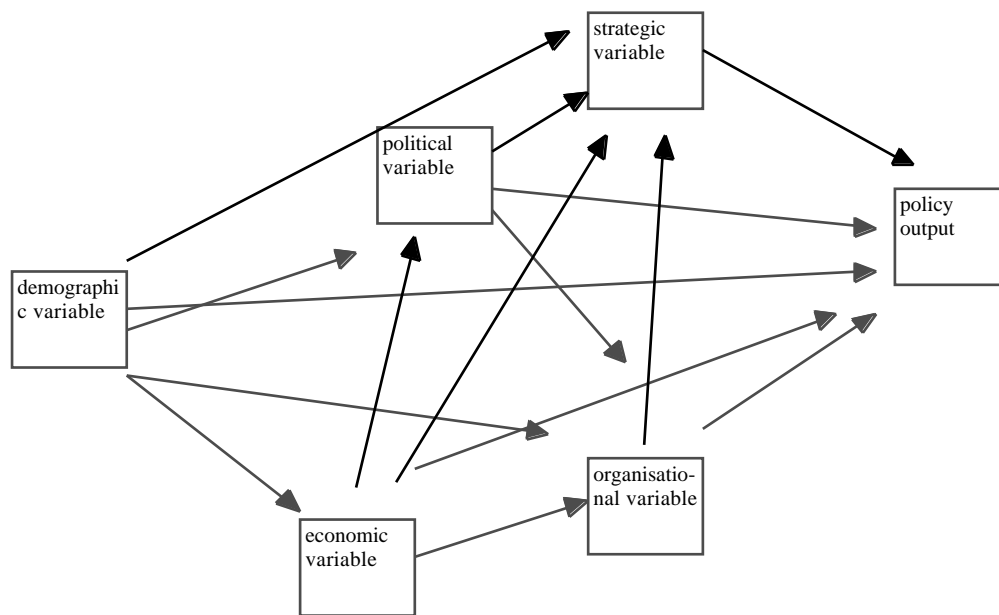
Figure 1 Hypothetical causal relationships for the analysis of DSO output

It should be pointed out here that any comprehensive analysis of DSO is incomplete by definition if policy situation is not included with the other contextual variables. Therefore, this analytical framework also deals with the strategic variables associated with the policy situation, which other studies in the literature on policy output have not considered.

2.3 Hypotheses

Urban researchers (Haworth *et al.*, 1978; Hirsch, 1982) analysing urbanisation and urban growth have identified population size and degree of urbanisation as being positively and significantly related to the fiscal independence or fiscal power of a local government. It is generally accepted that there is a very strong relationship between population size, degree of urbanisation and fiscal independence.

In addition, every commentator on urban inequality has argued for a very strong association between geographical location (north/south, east/west, white region/non-white region, etc.) and the fiscal independence of local government (Chakravorty, 1996; Cheshire and Carbonaro, 1996). Hence:

> *H1*: Fiscal independence (*fin*) is directly and positively affected by population size (H1a) and degree of urbanisation (H1b). Fiscal independence is also affected by geographical location (H1c).

It is acceptable to hypothesise that political party composition is affected by population size and degree of urbanisation. The pattern of the effect of demographic variables on the political variable varies from one country to another. In Britain, it is assumed that the less urban the local authority is and the smaller the population of a local authority is, the more Conservative the local authority will be (Byrne, 1994: 150-4; Hampton, 1987: 120; 1991: 128; Stoker, 1991: 40-9).

Political scientists studying voting behaviour point out that social and economic factors such as social class, income level, degree of education, etc. can be important determinants of political ideology. It is generally accepted by political theory that the higher the income level of residents in a local authority area, the more likely it is that they will support the Conservatives. Sharpe and Newton (1984: 177) support this argument, stating that Labour authorities are generally poor and that their purchasing power seems to be relatively low.

In view of these arguments, it is hypothesised that in Britain, local authorities with high fiscal independence are more likely to have a high proportion of Conservative local councillors. Finally, it is generally accepted by political scientists that the political party composition of local authorities varies according to geographical location (Painter, 1995). Hence:

H2: The proportion of Conservative councillors (*con*) in the total number of councillors in local government is directly and negatively affected by population size (H2a) and degree of urbanisation (H2b), as well as being directly and positively affected by fiscal independence (H2c). The proportion of Conservative councillors is also affected by geographical location (H2d).

The characteristics of Labour Party councillors are understood to be opposite to those of Conservative Party councillors mentioned above. Often coming from working-class backgrounds and with a history of active involvement in the trade union movement, these councillors have pioneered innovations and developments in welfare services (Goss, 1989).

It is expected that, in Britain, the more urban the local authority is and the bigger the population size of the local authority, the higher will be the proportion of Labour councillors (Byrne, 1994: 150-4; Hampton, 1991: 128; Stoker, 1991: 40-9). In addition, in view of the general ideological characteristics of Labour, it is theoretically assumed that a local authority with a high level of financial independence is likely to have a low proportion of Labour councillors. In accordance with the hypothesis made above, it is hypothesised that the proportion of Labour councillors varies according to geographical location. Hence:

H3: The proportion of Labour councillors (*lab*) in the total number of councillors in local government is directly and positively affected by population size (H3a) and degree of urbanisation (H3b), as well as being directly, and negatively affected by fiscal independence (H3c). The proportion of Labour councillors is also affected by geographical location (H3d).

It is assumed that in a situation where the population size, degree of urbanisation and fiscal independence of a local authority are high, the local authority can effectively resist a policy imposed from above without fear of sanctions. Power-dependence theory (Wilson and Game, 1994: 110-12) implies that the local authority which has sufficient resources is likely to be more powerful in negotiating or bargaining with central government. Accordingly, it is assumed that a local authority with a high population size, a high degree of fiscal independence and a high degree of urbanisation will be the target of more sanctions from central government during the CCT process.

As regards the relationship between sanctions and political party composition, it is understood that the Labour Party tends to resist the Conservative-initiated policy of CCT, whereas the Conservative Party tends to comply with it, leading us to expect that Labour councils are more likely to incur sanctions issued by central government than Conservative councils.

As Sharpe and Newton (1984) note, a policy has different effects in different regions, which means that local authorities may take different attitudes towards the same policy. It is hypothesised that the number of the sanctions issued against a local authority by central government can vary acccording to geographical location. Hence:

> *H4*: The number of sanctions issued against a local authority (*san*) is directly and positively affected by population size (H4a), degree of urbanisation (H4b), fiscal independence (H4c) and proportion of Labour councillors (H4d), as well as being directly and negatively affected by proportion of Conservative councillors (H4e). The number of sanctions issued against local government is also affected by geographical location (H4f).

Considering the local authority's scale of economy and its ability to make arrangements for a large contract, it is hypothesised that in a situation where the population size, degree of urbanisation and fiscal independence of the local authority

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are high, the contract size will be relatively large. Furthermore, the size of the contract will have a significant impact on the cost of the monitoring procedures. Hence it is expected that contract size will be associated with the ability of the local authority to implement the contract effectively.

From the perspective of small business, contract size strongly affects the ability to compete, and thus the success of the small firm depends on the size of the contract that the local authority is putting out (Abbott *et al.*, 1996). In view of this, Abbott *et al.* hypothesise that authorities controlled by the Conservatives will be more favourable to small businesses, allowing them to win more CCT work. In addition, considering that the Labour Party has been politically hostile towards CCT, it is hypothesised that Labour-controlled councils prefer lager contracts, whereas Conservative councils prefer small ones.

As regards the relationship between contract size and sanctions, it is assumed that a local authority which has experienced the sanctions issued by central government is more likely to make the contract smaller, because the setting-up of too big a contract is regarded as a strategy employed by a local authority to prevent private contractors from tendering for it. In addition, it is hypothesised that contract size is associated with geographical location, because it can also be affected by regional factors. Hence:

> *H5*: The size of the contract (*size*) is directly and positively affected by population size (H5a), degree of urbanisation (H5b), fiscal independence (H5c) and proportion of Labour councillors (H5d), as well as being directly and negatively affected by the proportion of Conservative councillors (H5e) and the number of sanctions issued against the local authority (H5f). The size of the contract is also affected by geographical location (H5g).

As Sharp (1990: 115) has noted, whether the location of a local authority is urban or rural affects its ability to prepare and implement the contract. As the population of a

local authority increases and the local authority becomes urban, it is assumed that there will be a corresponding increase in the contract period.

As regards the relationship between political party composition and the contract period, the period for which the contract is let can influence the level of competition. A shorter contract period may, owing to high start-up costs, discourage competition for the in-house tender (Prowle and Hines, 1989: 98). Therefore, it is hypothesised that Labour councils prefer a shorter contract, whereas Conservative councils prefer a longer contract.

Regarding the relationship between the contract period and the sanctions issued by central government, it is expected that a local authority which has experienced sanctions issued by central government is more likely to make the contract period longer, because private contractors prefer a longer contract to a shorter one. This is because a longer contract can lower the transaction costs incurred by the private contractors.

As with contract size, it is hypothesised that the contract period differs according to geographical location. Hence:

> *H6*: The period of the contract (*peri*) is directly and positively affected by population size (H6a), degree of urbanisation (H6b), fiscal independence (H6c), proportion of Conservative councillors (H6d) and the number of sanctions issued against the local authority (H6e), as well as being directly and negatively affected by the proportion of Labour councillors (H6f). The period of the contract is also affected by geographical location (H6g).

The main hypotheses relating to DSO output, the final dependent variable, are directly connected with political, economic, demographic and strategic circumstances in Britain. Drawing on the theoretical arguments about these facts advanced to date

(Atkins, 1996; Boyne, 1996; Bulpitt, 1967; Carnaghan and Bracewell-Milnes, 1993; Ferris, 1986; Wilson and Game, 1994), one can suggest the following hypotheses.

H7: DSO output (*dso*) is directly and positively affected by fiscal independence (H5a) and proportion of Labour councillors (H5b), as well as being directly and negatively affected by the number of sanctions issued against the local authority (H5c), population size (H5d), degree of urbanisation (H5e), proportion of Conservative councillors (H5f), the size of the contract (H5g) and the period of the contract (H7h). DSO output is also affected by geographical location (H7i).

Some researchers argue that political party effect on the policy output is crucial, while others underestimate this effect. Stoker (1991: 37), in particular, characterises the development of local government in the post-war period in Britain as involving a shift from an apolitical climate to one of intensive 'politicisation'. In this paper the hypothesis is advanced, based on Stoker's study, that the variable most crucial in affecting DSO output is political party compostion. Hence:

H8: DSO output is more strongly affected by the political variable (the proportions of Labour or Conservative councillors) than by any other variable.

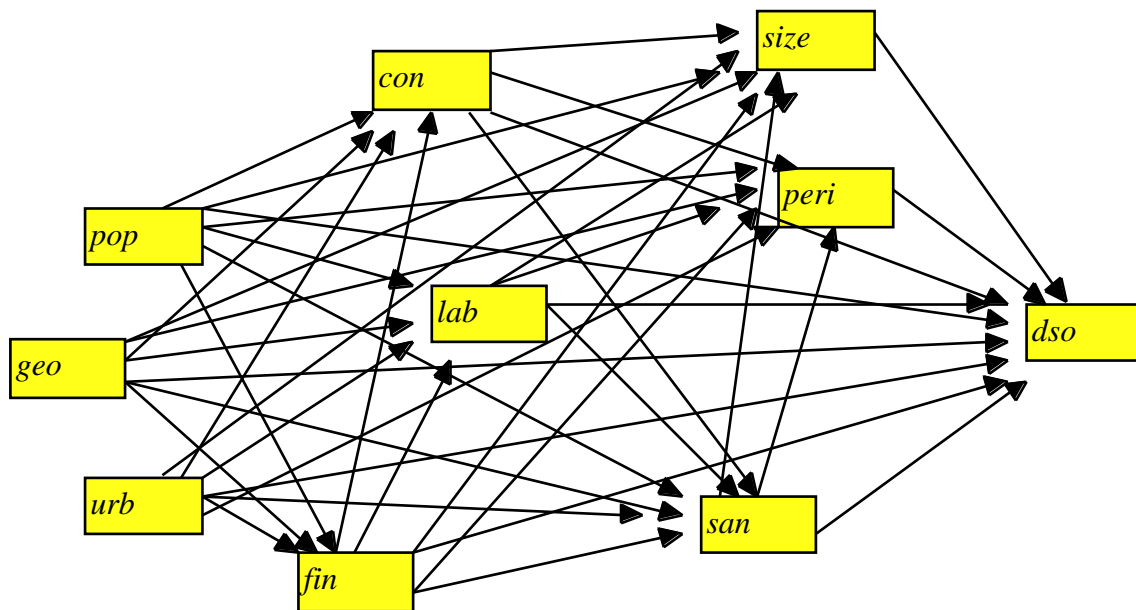Figure 2 shows the hypothesised causal model for analysis.

Figure 2 Hypothesised causal model

Key to abbreviations:

pop = population size

urb = degree of urbanisation

geo = geographical location

fin = fiscal independence

con = proportion of Conservative Party councillors

lab = proportion of Labour Party councillors

san = number of sanctions issued against local government

size = size of the contract

peri = period of the contract

dso = DSO proportion of total value of work

A number of specific terms are used in this study. These terms were defined as shown in Table 1.

Table 1 Overview of variables and indicators used in the analysis

Variables	Indicators	Name of indicators in text and tables	Operationalisation	Years covered	Data sources
Dependent variable	DSO output	dso	The percentage of the total value of work that is undertaken by the DSO	1991, 1994	The Contracts Handbook
Political variable	Political party composition	con lab	con: Conservative councillors/total number of local councillors lab: Labour councillors/total number of local councillors	1991, 1994	Local Election in Britain
Economic variable	Fiscal independence	fin	Council Tax/SSA[1] (1994), Community Charge/SSA (1991)	1991, 1994	Finance and General Statistics & Municipal Yearbook
Strategic variables	Contract size Contract period Geographical location	size peri geo[2]	The size of the contract The period of the contract Eight regions	1991, 1994	The Contracts Handbook Regional Trends
Organisational variable	Sanctions issued against local authority	san[3]	The number of sanctions issued by central government	1991, 1994	The contract Handbook
Demographic variables	Population size Degree of urbanisation	pop urb	Population size Population/acre	1991, 1994	The Municipal Year Book

Notes: (1) SSA (Standard Spending Assessment); (2) dummy variable applied;
(3) dummy variable applied

3 Analysis

3.1 The path model for 1991

Table 2 shows how the total effects of the independent variables are made up. The estimation of path coefficients also makes it possible to decompose the observed empirical correlation or covariance between any two variables into two components: direct and indirect effects. A direct effect is posited as existing if a single arrow connects two variables. When two variables of interest are connected only via other intervening variables - when, in other words, the relationship is represented by

compound paths with no direct path between the two variables of interest - the effect is deemed to be indirect (Kerlinger and Pedhazur, 1973: 314-5).

Table 2 Decomposition of path coefficients (1991)

Dependent variable	Independent variable	Direct effect	Indirect effect	Total effect
fin	dum 2	-0.09	0.00	-0.09
	urb	-0.27	0.00	-0.27
con	fin	0.10	0.00	0.10
	pop	0.14	0.014	0.154
	urb	-0.23	-0.023	-0.253
	dum 5	0.16	0.016	0.176
	dum 6	0.17	0.017	0.187
	dum 8	0.49	0.049	0539
lab	dum 2	-0.10	0.00	-0.10
	dum 6	-0.13	0.00	-0.13
	dum 7	-0.35	0.00	-0.35
	dum 8	-0.46	0.00	-0.46
	pop	0.15	0.00	0.15
	urban	0.45	0.00	0.45
san	pop	0.25	0.00	0.25
peri	dum 3	0.27	0.00	0.27
dso	size	0.13	0.00	0.13
	lab	0.37	0.00	0.37
	con	-0.25	0.00	-0.25
	pop	-0.22	0.10	-0.12
	urb	0.00	0.10	0.10
	fin	0.00	0.02	0.02
	dum 2	0.00	-0.04	-0.04
	dum5	0.00	0.05	0.05
	dum 6	0.00	-0.05	-0.05
	dum 7	0.00	-0.13	-0.13
	dum 8	0.00	-0.17	-0.17

As Table 2 shows, the direct and indirect relationships between the dependent and independent variables are complicated. As regards DSO output for 1991, the political variable (*con* and *lab*), one strategic variable (*size*) and one demographic variable (*pop*) are directly related to it, while another strategic variable (*geo*), the economic variable (*fin*) and another demographic variable (*urb*) are indirectly related. These relationships can be expressed in simple diagrammatic form.

As Table 2 shows, DSO output (*dso*), the final dependent variable, is directly affected by *pop*, *con*, *lab* and *size*, and indirectly by *pop, geo* and *urb* through the mediation of *con* and *lab*. In other words, DSO proportion is a function of population size, proportion of Conservative and Labour councillors, contract size, geographical location and degree of urbanisation. Of these, the political variable, the proportion of Labour councillors (*lab*), has the greatest total effect on *dso* (0.37). It is

accepted that where there is a high proportion of Labour councillors, a low proportion of Conservative councillors, a large contract size or a low level of population size, there will be a higher level of DSO output.

3.2 The path model for 1994

As Table 3 shows, the direct and indirect relationship of the variables in the data set for 1994 is simpler than that for 1991. DSO output was directly affected by proportion of Labour councillors (*lab*,0.18), proportion of Conservative councillors (*con*, -0.11) and geographical location (*dum3*, North West, 0.26), and indirectly by degree of urbanisation, population size, geographical location (*dum2, 6, 7, 8*) via mediating proportion of Labour councillors and proportion of Conservative councillors. It is true that, as in the 1991 path model, political party composition, *lab* and *con*, was one of the important factors affecting DSO output. DSO output is a function of *lab, con, dum3, urb, pop, dum2, dum6, dum7* and *dum8*.

What is noticeable in the path model for 1994 is that the variable of geographical location emerged as one of the most important and direct factors in determining DSO output. This suggests that private companies interested in CCT chose particular regions as their main targets for competition in preference to other regions, believing that these latter might disadvantage them or that they would not make profits in those regions.

Table 3 Decomposition of path coefficients (1994)

Dependent variable	Independent variable	Direct effect	Indirect effect	Total effect
fin	*urb*	-0.20	0.00	-0.20
	dum 5	0.13	0.00	0.13
con	*urb*	-0.29	0.00	-0.29
	pop	0.17	0.00	0.17
	dum 5	0.15	0.00	0.15
	dum 6	0.18	0.00	0.18
	dum 8	0.42	0.00	0.42
lab	*urb*	0.43	0.00	0.43
	pop	0.11	0.00	0.11
	dum 2	-0.12	0.00	-0.12
	dum 6	-0.14	0.00	-0.14
	dum 7	-0.36	0.00	-0.36
	dum 8	-0.48	0.00	-0.48
peri	*lab*	0.16	0.00	0.16
	dum 5	0.21	0.00	0.21
	urb	0.00	0.007	0.007
	pop	0.00	0.002	0.002
	dum 2	0.00	-0.02	-0.02
	dum 6	0.00	-0.02	-0.02
	dum 7	0.00	-0.07	-0.06
	dum 8	0.00	-0.08	-0.08
size	*urb*	0.17	0.00	0.17
	pop	0.50	0.00	0.50
	dum 8	-0.27	0.00	-0.27
dso	*con*	0.11	0.00	0.11
	lab	0.18	0.00	0.18
	dum 3	0.26	0.00	0.26
	urb	0.00	0.05	0.05
	pop	0.00	0.04	0.04
	dum 2	0.00	-0.02	-0.02
	dum5	0.00	0.02	0.02
	dum 6	0.00	-0.01	-0.01
	dum 7	0.00	-0.06	-0.06
	dum 8	0.00	-0.04	-0.04

One of the main differences between the 1991 and 1994 analyses is that, while in the early stages of CCT the political factor was the strongest affecting DSO output, over time private contractors chose specific regions as a strategic base according to previous experience and expanded this base into other regions. Goodwin (1994) explains that this reflects the growth strategy that was employed by the multinationals during the 1980s, when their policy of mergers and acquisitions enabled them to gain bases nationally. It appears that some private companies employed the strategy of 'base and spread', with the result that geographical location has been the strongest factor affecting DSO output.

These findings can be interpreted to mean that, where the proportion of Labour councillors is high, the proportion of Conservative councillors is low, and especially in the region of North West, there will be high levels of DSO output. In addition, population size, degree of urbanisation and geographical location (Yorkshire and

Humberside, East Anglia, South West and South East) affected DSO output indirectly (positively or negatively). It can be seen from these results that the data set for 1994 confirms that the political variables *lab* and *con* and one of the strategic variables, *geo*, were the most powerful determinants of DSO output.

4. Conclusions

We developed and tested a framework that describes DSO output and its relationships to several environmental variables surrounding local government CCT. Via analysis of path coefficients and elimination of the weak paths, we subsequently refined the originally hypothesised model to create a trimmed model that should be a useful departure point for future researchers interested in understanding how DSO output may be achieved. Four main points about these findings are worth stressing briefly:

1. The results are generally not bad in statistical terms, in the sense that there are some significant beta weights even though many hypotheses are rejected. However, it should be noted that over the time-period 1991-1994, the political variable, political party composition, and geographical location prove themselves to be among the most powerful explanatory variables so far as DSO output is concerned. In other words, in data sets for the two years, organisational and economic variables have been found less useful than the political and geographical variable in explaining the variance in DSO outputs.

2. Perhaps the most significant finding was that in the earlier stages of CCT implementation it was the political variable that had the strongest effect on the DSO proportion, whereas in the later stages, it was the geographical location that had the strongest effect. This implies that over time local councillors' involvement in the CCT process declined and instead the private sector played a very important role in the CCT process.

In academic and practical literature on privatisation policy, the variable geographical location has not received much attention up until now. Although this variable was not significant in the analysis for 1991, in that for 1994 it was the most powerful factor affecting DSO output, thus leading us to assume that the practices and pattern of contracting in 1994 were different from in 1991.

3. Despite a measure of inconsistency, the findings provide us with a strong indication that the political, demographic, strategic and organisational variables for the two research periods are significant in explaining the variances in DSO output.

4. Despite the methodological efforts, causal modelling does not seem to provide any solution to the basic problem of how environmental factors can affect policy output - DSO output, or tell us what role these factors play in this process. Our results imply that another approach should be employed to answer this question.

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