

**Partisan Politics in the Southern Cone: Is
there anything left for the left?
Political Institutions, Privatisation, and Policy Outcome**

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Abstract

This thesis examines the capacity of left-wing governments in Latin America to implement their policy preferences in the context of the current phase of globalisation. In particular, it focuses on the policy area of privatisation. It addresses the debate concerning the extent to which increasing economic globalisation is forcing governments, regardless of their partisanship, to ‘converge’ upon a similar set of market-friendly economic policies. The thesis focuses on the ability of the left wing governments in Argentina, Brazil and Uruguay to implement their preferences in the policy area of privatisation, and the role of domestic political institutions in either facilitating or impeding these governments from doing so, using a qualitative comparative case study methodology. It hypothesises that the configuration of political institutions is a significant factor in determining the capacity of a government to pursue distinct partisan policies. The thesis finds that although the three governments had similar policies towards privatisation, the divergence in outcomes was a product of the political institutional configuration in each state. In particular, the level of executive power, and in the Uruguayan case, mechanisms of direct democracy, proved key determining factors.

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Introduction

The relevance of partisan politics in the current globalised era remains contested and misunderstood. This study argues that the focus on exogenous variables in explaining the ability of partisan, specifically left-wing governments to implement their preferences neglects an important internal variable: the configuration of political institutions. Left-wing governments continue to be important even in today's globalised world, but this depends upon the institutional power they can wield over decision-making and the institutional design and path dependent effects of specific policies. It tests this argument by examining the ability of three left-wing governments in the developing world, Argentina, Brazil and Uruguay, through qualitative comparative case studies, to implement their preferences in the policy area of privatisation.

Latin America Turns Left

Latin America is turning left. The region has, in the last ten years, witnessed the political ascendancy and electoral successes of a diverse group of politicians that all are part of a general resurgence of left-of-centre political forces across the continent. The reasons for this wider pattern are not particularly complex, given the region's unparalleled socio-economic inequalities (CEPAL, 2005). This revival of left-leaning politics in Latin America has inspired an impressive body of work concerned with the context, motivations, implications and apparent bifurcation of these leaders (see Lagos, 2008; Weyland, 2007; Seligson, 2007; Roberts, 2007; de la Torre, 2007; Castañeda & Morales, 2007; Lynch, 2007; Castañeda, 2006; Cardoso, 2006; Schamis, 2006; Cleary, 2006; Ramírez Gallegos, 2006; Panizza 2005). However, the relevance of all this scholarly interest is questionable if these left-wing governments are paralysed and constrained by exogenous forces once in power, as proponents of the 'globalisation' or 'efficiency' hypothesis would argue. According to this logic, an inexorable march towards increasing economic globalisation has ensured that governments of the left can no longer implement distinctive policies that differ substantially from governments of the right. What merits attention then, is the ability of these left-wing governments to actually implement their preferences once in power.

The Puzzle: How relevant is the contemporary left?

Partisan theory assumes that the political orientation of the party in power matters. It also assumes that governments have the ability to implement their preferences (see Hibbs, 1992; 1977). In today's globalised world, this assertion is being increasingly challenged. The literature offers two views: one is convergence driven by globalisation; the other is that under some circumstances left-leaning governments can effectively implement their policies. What circumstances has not been fully explored, in particular the role that domestic political institutions play in either impeding or facilitating left-wing governments in their attempts to implement their preferences.

The 'globalisation' or 'efficiency' hypothesis argues that increasing economic globalisation is forcing governments, regardless of their partisanship, to internalise the preferences of mobile capital if they wish to remain competitive in global markets. This has the end result of forcing governments to 'converge' upon a similar set of economic policies, ultimately leading to a withdrawal of the government from the economy, reduced social spending, a shift in the burden of taxation from capital onto labour, privatisation, flexible labour standards and even lax environmental regulation (see Przeworski & Wallerstein, 1988; Ruggie, 1994; Rodrik, 1997; Burgoon, 2001). If governments deviate from this policy mix, the now, highly-mobile capital will simply move to a more favourable location. As this mix is considered to reflect policies of the right, increasing economic globalisation is presumed to constrain, if not eliminate, distinctive left-wing alternatives. As such, left-wing governments now have little ability to implement their preferences in capitalist democracies.

Those that reject this argument also reject the treatment of economic globalisation as the sole explanatory variable. Early studies contesting the concept of policy convergence contended that left-wing politics were far from meaningless in today's world. In fact, they treated left-wing politics as an independent variable and found that, where governments were of the left, the effects of convergence, in areas such as social welfare spending and taxation reform, were lessened or even reversed (see Cameron, 1978; Hicks & Swank, 1992). The means by which left-wing politics resisted this convergence remained unclear, but it was thought that the answer lay in the relationship of these parties with labour. Later, more sophisticated studies

attempted to untangle this relationship and so began the incorporation of labour-market institutions as an independent variable into this debate. It was now convincingly argued that where left-wing governments were allied with broad and encompassing labour movements, the effects of convergence, again in the areas of social welfare spending or taxation reform, would again be either significantly slowed or even reversed (see Garrett, 1998a). So, left-wing governments can implement their preferences. They matter.

However, the domestic-level mechanisms by which left-wing governments resist the pressures of convergence still remain under-developed. The focus still remains on exogenous variables to the detriment of a more complete understanding of the effects of domestic-level variables. While the role of labour in mediating convergence has been the focus of a number of studies, the role of political institutions still warrants attention. Generally, where studies have incorporated institutional variables, they have either been very generalised, such as democracy (see Avelino, Brown & Hunter, 2005), or very narrow institutional variables, such as party fragmentation (see Wibbels & Arce, 2003), or else they have been solely concerned with the effect of labour market and partisanship institutions (see Garrett, 1998a). The links between globalisation, left-wing governments and policy outcomes still remains contested and unclear.

The Argument: A neglected internal variable – political institutions

This project aims to contribute to this literature, by attempting to further untangle the mechanisms that allow left-wing governments to implement their preferences in the face of economic globalisation. Specifically, it argues that this literature, by focusing on exogenous forces to explain policy outcome, has neglected crucial internal explanatory variables. The configuration of the political institutions in each state will mediate the effect of economic globalisation on policy outcomes. So, variation in policy outcome, among left-wing governments in different states with similar preferences, cannot simply be attributed to varying levels of exogenous forces. Variation in policy outcome will also be a product of the political institutions in each state.

While strong and encompassing unions allied with the left-wing party in power will be important for demanding and providing support for specific policy outcomes, the ability of a left-wing government to achieve this policy outcome will

be primarily predicated upon the institutional control a government has over a particular policy. By institutional control, we are referring to the decision-making power of the government, embodied by a combination of executive power, control over the legislature etc; the ability of important players to veto initiatives, e.g. the judiciary; and the institutional design of policies and their path dependent effects. Taken together, the cumulative effect of these institutional variables will be either to help to enable a left-wing government to implement their preferences, by maximising their institutional control over a policy, or to hamper a left-wing government in implementing their preferences, by minimising the control this government can exert over this policy.

Figure 1 below outlines a typology of this argument. Holding all exogenous variables constant, where the level of institutional control over policy is high and the union movement is cohesive and well-organised, a left-wing government with close links to labour will have a greater ability to implement their preferences, than one with low-levels of institutional control and weak links to a fragmented and disorganised labour movement. Even when institutional control over policy is high, a lack of co-ordination on the left due to a fragmented and disorganised labour movement with weak links to the party may result in muted preferences. Where labour is cohesive with strong links to the party, policy may be focused and preferences clear, but a lack of institutional control over policy will constrain a left-wing government.

Figure 1: A typology of domestic-level variables

	Strong cohesive labour movement with strong links to party	Weak and fragmented labour movement with weak links to party
High levels of institutional control over policy	Implementation of preferences (strong support)	Muted preferences (weak support)
Low levels of institutional control over policy	Constrained preferences (strong support)	Blocked preferences (weak support)

Privatisation in the Southern Cone

In October 2002, after three failed attempts, Luiz Inácio Lula da Silva of the left-wing *Partido dos Trabalhadores*, won the Presidential election in Brazil. In May 2003, the little-known Néstor Kirchner, leader of the left-wing *Frente Para la Victoria* faction of the *Partido Justicialista* was elected to power in Argentina, while for the first time in Uruguayan history, a left-wing candidate, Tabaré Vázquez of the *Frente Amplio*, won the Presidential election in November 2004. All three ran on platforms that criticised the market-model of their predecessors and all three expressed similar preferences as regards privatisation during their election campaigns.¹ So, these three countries provide a good opportunity to test the argument outlined above. What is more, as shall be demonstrated in chapter two, these three states, during the period in question, had similar levels of exposure to economic globalisation and are exposed to similar levels of influence from the international financial institutions. This allows for all exogenous variables to be held constant across the three states, increasing the analytical leverage of the study over the main explanatory variables. If the argument presented above is correct, we should expect

¹ Campaign pronouncements, programmes, statements and manifestos are predictive of government preferences, even in Latin America, and governments generally attempt to act consistently with these preferences (see Stokes, 2001: 176).

variation, if any, in policy outcome across these three states to be a product of the political institutions.²

The Purpose of this Study

The ability of contemporary left-wing governments to successfully implement their preferences remains contested. While recent scholarly work has gone some way towards untangling the relationship between economic globalisation, institutions and partisanship, this relationship still remains unclear, and the focus continues to be on exogenous variables to the detriment of internal factors. In studies concerned with this issue, scholars have incorporated different institutional variables (see Avelino, Brown & Hunter, 2005; Wibbels & Arce, 2003; Garrett, 1998a). Duane Swank (1998b, 2002, 2003), in his studies of the OECD states, has emphasised the importance of institutional configurations in providing opportunities, to those opposed to the policies associated with convergence, access to decision-making. Paul Pierson (1994, 1996, 2004) has argued that the effects of economic globalisation on welfare retrenchment in industrialised democracies, where it has occurred, has been mediated and nullified by the institutional design and path dependence of existing welfare policies.

This study builds on these works. This project contends that the configuration of political institutions in a state will either enable or hamper a left-wing government to pursue distinct partisan policies. It builds upon the works of Swank and Pierson by creating a framework of institutional policy-making that captures the importance of access and control over decision-making and also the effects of policy design and path dependence. So, left-wing politics still matter, although the mechanisms through which these governments may resist convergence remain under-developed.

Most of the literature in this debate has also been focused on two policy areas only: welfare retrenchment and taxation shifting. This study proposes to widen the scope of this debate by testing the argument in, an as yet, unexamined policy area: privatisation. Privatisation is a good policy to choose as we have clear expectations concerning the relationship between economic globalisation and privatisation.

² Outcome will also be a product of labour cohesiveness and organisation, but according to the argument presented here, left-labour power will only be relevant when the left-wing party has high levels of institutional control over policy. So institutions are the primary explanatory variable.

Finally, most empirical work in this literature has been focused upon the advanced industrial democracies (for exceptions, see recent work by Rudra, 2002; Wibbels & Arce, 2003; Kaufman & Segura-Ubiergo, 2001; and Avelino, Brown & Hunter, 2005). This project will further contribute to this literature by testing the argument in three developing-world, Latin American states. Not only will this broaden the scope of this avenue of inquiry by continuing to extend it to the developing world, but it will also provide a more rigorous test of the argument, as the effects of economic globalisation are presumed to be magnified in developing world states.

The Structure of the Thesis

Chapter one outlines the dichotomy in the literature concerning the effect of economic globalisation on the ability of contemporary left-wing governments to implement their preferences. It contends that while advances in understanding the links between partisanship, economic globalisation and institutions have been made, there remains a focus on exogenous variables to the detriment of a more nuanced understanding of the role of institutional variables.

Chapter two presents the methodological approach to be employed by this study in order to test the argument presented above. It proposes the research question, justifies the selection of the case studies, explores and operationalises the institutional variables and hypothesises on expected outcomes based on the theorised impact of the variables outlined.

Chapters three and four concern the first case study, Brazil. Chapter three process traces the evolution of privatisation policy in Brazil from the return to democratic rule until the election of Lula. Chapter four is the analytic narrative of the Lula presidency. Firstly, it establishes the preferences of Lula as regards privatisation during the election; secondly, it outlines the outcome of privatisation policy during Lula's term in office; and finally, it analyses and explains this outcome in the context of the institutional and internal variables outlined in chapter two.

Chapters five and six deal with the second case study, Argentina. The structure of these two chapters exactly follows that of the Brazilian case study. Chapters seven and eight deal with the third and final case study, Uruguay, and again, these chapters exactly replicate the structure employed for Brazil and Argentina.

In the concluding chapter, the results will be discussed in light of the research question. The findings of this study will be related to the broader literature on partisan politics and economic globalisation. The findings of this research will hopefully stress the need for this literature to incorporate more complete and nuanced institutional variables, regardless of policy type and regardless of country location. Finally, a possible research agenda based on the findings of this study will be presented and outlined.

Chapter One – The Literature on Globalisation and Partisan Politics

Partisan theory assumes that the political orientation of the party in power matters. It also assumes that governments have the ability to implement their preferences (see Hibbs, 1992; 1977). Recently however, this conventional wisdom has been vigorously challenged. Increasingly, heightened levels of economic globalisation are being presented as drivers of an inexorable alteration in the traditional role of the state.³ A corollary to this argument is the issue concerning the extent to which economic globalisation has altered the role of those who operate within the state. There are two discernable schools of thought within this debate. One side of this debate (the first wave)⁴ generally contend that economic globalisation has caused an increase in the power of capital relative to labour and that governments, in order to combat the threat of capital flight, must adopt policies that internalise the preferences of capital. So, economic globalisation is leading to an inevitable policy convergence along market-friendly lines in order to satisfy capital. This has the effect of severely curtailing or eliminating the prospect for distinctive left-wing policies.⁵ As such, left-wing governments are no longer assumed to be able to implement autonomous policies. The opposing side of this debate (the second wave) however, reject this argument, and claim that the effects of economic globalisation have been overstated. Furthermore, they claim that economic globalisation may actually encourage governments to implement policies that are congruent with left-wing policies, while others again argue that the above studies fail to take into account the role of institutions in mediating the effects of economic globalisation. So, left-wing politics still matter, although the mechanisms through which these governments may resist convergence remain under-developed.

The purpose of this chapter is to review the competing arguments in this debate, and place the current thesis within a relevant body of literature. The first section outlines the arguments presented by those who contend that economic globalisation has rendered partisan politics meaningless; the second section presents

³ There are a huge range of authors who accept this point. For seminal contributions see Strange (1996) or Waltz (2000).

⁴ This chapter follows Kofman & Youngs (1996) in delineating those competing approaches in this debate as the first and second wave literature.

⁵ Empirical research has shown that the market-friendly reforms associated with this type of policy convergence are correlated with executives who represent the right rather than those on the left. See Biglaiser & Brown (2005).

the arguments of those who contend that left-wing politics still matter. The conclusion will demonstrate the value added of the current study.

1.1 The First Wave

The central tenet of the ‘globalisation thesis’⁶ literature is relatively simple, although those that support this position come from a wide variety of backgrounds and traditions. The general argument is as follows: increased economic interdependence has led to a shift in the power of capital over labour, which in turn means that states must now aggressively compete for these mobile asset holders (capital), to such an extent that it ‘constrains...the government’ (Gill & Law, 1989: 481). It is accepted that mobile asset holders prefer certain government policies over others, such as small government, little regulation, privatisation, reduced social welfare spending, flexible labour markets, low corporate tax rates and even lax environmental standards.⁷ If governments do not adopt these policies, then mobile asset holders will exercise their exit option, resulting in deleterious economic consequences for the state in question. So, all governments become forced into an inevitable policy convergence along market-friendly lines as a result of economic globalisation.⁸ It is important to note that there are two distinct groups within this literature: those that argue that economic globalisation is specifically undermining the ability of the left to introduce autonomous policies, and those that contend that economic globalisation is leading to an inevitable convergence regardless of partisan politics. This convergence is seen to centre on reducing government intervention and on liberating market forces, ‘thereby significantly circumscribing, if not eliminating, the prospects for distinctive left-wing policies’ (Garret & Lange, 1991: 540).⁹ The end result is that ‘left-wing parties will continue to seek election and occasionally win power. However, these parties will have little in common with their predecessors in terms of articulating progressive options and pursuing programmes different from the

⁶ The general term used to describe the thesis that economic globalisation is forcing an inevitable policy convergence along market-friendly lines, thus reducing the relevance of domestic politics. See Swank (2002: 22-23). Garrett has also called this the efficiency hypothesis. That is, governments adopt market-friendly policies in order to be more competitive and efficient in the global market. See Garrett (1998a). It has also been labelled the ‘race to the bottom’ thesis (see Drezner, 2001).

⁷ That is, the ‘regulatory race to the bottom’ to remain competitive in international markets.

⁸ Others suggest that this convergence is political rather than economic in nature. International organisations promote common political and cultural practices eventually leading to a similar convergence. See for example, Boli & Thomas (1999), and Keck & Sikkink (1998).

⁹ Others have suggested that convergence may be a product of domestic electoral arrangements. See Jackman (1986).

conservative or establishment view' (Kurzer, 1993: 252). Although capital flight is not a new problem for the left, the range of policy instruments available for dealing with this problem are far narrower than at any previous time (Berger, 2000: 51). Economic globalisation, the threat of capital flight and the inexorable policy convergence has ensured that 'it hardly matters whether the left or the right win elections; the constraints of the internationalized economy will oblige either party to follow the same monetary or fiscal policies or else face a loss of national competitiveness and investment' (Berger, 2000: 51).¹⁰

As Garrett (1998b: 793) has noted, the above argument is not a new one. Adam Smith (1776) suggested in *The Wealth of Nations* that capital mobility would restrain the growth and autonomy of the state, while Norman Angell (1910) argued that increasing international economic integration was eliminating the likelihood of war among states (see Garrett, 1998b: 793-795).¹¹ A special issue of *International Organisation* in 1971 stressed that realist models could no longer adequately encapsulate the role of the state as a result of increased economic interdependence (Keohane & Nye, 1971). Robert Mundell (1963, 1964, 1968) and Richard Cooper (1968, 1972), in a series of works, examined the effect of international economic integration on the role of states, suggesting that greater economic interdependence could alter the context within which states operate.¹²

It is through three different mechanisms that economic globalisation curbs policy autonomy and fosters convergence (Garrett, 1998b: 791). The first of these, increasing trade competition, stipulates that large governments are simply not 'efficient' in today's global markets. Large governments necessitate large amounts of government spending, cushioning market mechanisms and distorting prices and wages. Government largesse must be funded from somewhere, usually through increased taxes or borrowing, but government borrowing raises interest rates, while increased taxes will depress economic activity (see Garrett, 1998b: 792). So, 'as a result of these effects, output and employment suffer from public sector expansion' and ultimately, trade competition must therefore 'result in a rolling back of the public

¹⁰ This argument follows the same thread as Gourevitch's (1978) seminal work 'The Second Image Reversed' which suggested that domestic politics do not simply shape the international realm, but that the international realm may also shape domestic politics.

¹¹ For a good overview of these early works see Garrett (1998b: 793-796).

¹² Milner & Keohane (1996: 7-8) draw attention to many of these seminal studies.

economy' achieved by reduced government spending, eliminating interventionist policies and the privatisation of state assets (Garrett, 1998b: 792).

The second mechanism, the multinationalisation of production, is predicated upon the exit-threat of highly mobile asset owners. Mobile asset owners, it is assumed, prefer a particular mix of government policies (low corporate taxation, flexible and de-regulated labour markets, cheap prices for former state assets etc.) and should they not be provided with this policy mix, they will simply pack their bags and move to a more favourable location. It is this exit-threat that forces convergence along specific policy lines (Garrett, 1998b: 792). Distinctive left-wing policies are no longer feasible. However, this argument has been countered (see Garrett, 1998a; Romer 1994) by those who suggest that interventionist policies may actually be of benefit to mobile producers, but even if this is so, mobile producers may still attempt to foster tax competition, forcing the burden of taxation from capital onto labour, vitiating redistributive objectives (see Rodrik, 1997).

The final mechanism concerns the hyper-mobility of portfolio capital. The extent of financial market integration and the speed of capital movement within these markets act as a disciplinary force on governments. If the markets do not like particular government policies, capital will simply move and 'engage in regulatory arbitrage' (Drezner, 2001: 58; Garrett, 1998b: 792-793). So, governments are forced to engage in a 'race to the bottom' where distinct left-wing political alternatives are 'sacrificed on the altar of commerce' (Drezner, 2001: 53). Increasing financial integration naturally leads to increasing capital mobility and under floating exchange rates, increases in capital mobility will restrict the efficacy of monetary policy and where currencies are fixed or pegged; the restrictions are magnified (see Milner & Keohane, 1996; Berger, 2000; Philips, 2005).¹³

The positions and backgrounds of those that support the globalisation thesis, as well as the arguments they make are, as stated earlier, diverse.¹⁴ The extreme end of this spectrum is represented by what Hay (2004: 33) has termed the 'airport lounge/business school globalisation literature' (see Leadbeater, 1999; Gray, 1998; Parker, 1998; Ohmae, 1996; Thurow, 1994, Levitt, 1983). This literature assumes that capital is perfectly mobile and that there is perfect competition in a perfectly

¹³ This is according to the Mundell-Flemming theorem which states that under fixed exchange rates, increases in capital mobility renders monetary policy little more than a tool to maintain the exchange rate. See Mundell (1963).

¹⁴ See Hirst & Thompson (1996) for a good overview of these arguments.

open economy. Economic globalisation is a pre-determined end-point and this intractable situation is forcing all governments to converge along a similar set of identical market policies. As a result 'one dominant economic system is emerging' (Sachs & Warner, 1995: 1). All economies 'tend toward common ways of producing and organising economic life' and 'where they do not converge, the explanation lies in distortions introduced by history' (Berger, 1996: 1).

This extreme is best embodied by Ohmae (1996), who argues that state functions have become paralysed as a result of globalisation, even going so far as to contend that the logic of economic globalisation dictates that regional economies, or centres where economic activity is concentrated (e.g. Singapore, Hong Kong etc.), should be represented at the international level rather than nation states. For Ohmae (1996: 4), economic globalisation has rendered 'the traditional middleman function of nation-states and of their governments largely unnecessary.' Not only is the role of partisan politics meaningless, but also the role of the nation state itself.

Perhaps unsurprisingly, these arguments are not without their critics. They have been criticised for completely ignoring institutional variables (see Philips, 2005; Hay, 2004; Busch, 2000), for the highly deterministic nature of their argument (Hay, 2004), and for their causal empiricism, exemplified by a highly selective use of evidence (Busch, 2000).

Przeworski & Wallerstein's (1988) theory of 'structural dependence of the state on capital,' arrives at a conclusion similar to the one propagated by the literature described above, albeit one derived from a very different perspective. Drawing on Marxist theories, Przeworski & Wallerstein begin with the hypothesis that society in its entirety depends upon the allocation of resources chosen by capital owners, and as a logical extension of this contention, if 'the entire society depends on the owners of capital, so must the state' (1988: 12). Capital owners will only invest where they can maximise the returns on their investment. To achieve this, they search for states with little government intervention, little labour market regulation and low taxation ensuring that 'governments face a trade-off between distribution and growth, between equality and efficiency' (1988: 13). Traditional left-wing policies (interventionist government, large public sectors, regulated labour markets and high levels of taxation) will represent a lack of competitiveness to capital owners who can simply move to a more capital-friendly location (Wallerstein & Przeworski, 1988: 1995).

Andrews (1994) builds upon the structural dependence thesis, and posits that capital mobility should be treated as a structural feature of the international system. He presents the 'capital mobility thesis,' which suggests that when capital is highly mobile across borders, the macroeconomic policy options available to states are 'systematically circumscribed' (1994: 193).¹⁵ This occurs because internationally mobile capital will reward some state behaviour but punish others (1994: 193). Economic globalisation has 'enhanced the capacity of capital asset-holders to evade the jurisdiction of unfriendly regulators' (1994: 199). The new competitive pressures that states face in attracting capital are forcing them to adopt the same policies, rendering partisan politics at the domestic level, somewhat useless (1994: 199).

Gill & Law (1989), on a similar wavelength, highlight the primacy of capital in understanding the shifting alternatives available to national governments as a result of economic globalisation. They argue that 'governments are increasingly constrained by the economic policies of other states, as well as the investment decisions of internationally mobile capital' (1989: 485). They cite the example of France in the 1980s under socialist Mitterrand. Previously, France under de Gaulle had taken a nationalist stand-point as regards foreign investment, but by the 1980s, globalisation and the economic realities it generated, forced Mitterrand to become more flexible towards foreign investment, even to the extent of welcoming and pursuing Japanese capital (1989: 485). For Gill & Law, this example serves to highlight the fact that the structural power of capital has risen relative to labour and the state (1989: 487). As a result of the dominance of capital, they contend that 'an elected socialist party with a radical programme would therefore be constrained in its policy choices by the nature of the business climate, not least because it would need tax revenues and/or loans to finance its ambitious spending plans' (1989: 481). A variant of this argument is also shared by Mishra (1996), who posits that parties of the left are conclusively constrained from developing progressive policy, primarily as a result of the dominance or prevalence of the neoliberal rhetoric.

Cerny (1996: 83), in common with the literature above, contends that as markets expand they subsume all types of political, economic and social processes, and the rise of capital brings into question the autonomy of the liberal democratic state in the contemporary world. The increase in capital mobility, the

¹⁵ See also Cohen (1993) and Webb (1991) who both subscribe to variants of the 'capital mobility thesis.'

internationalisation of finance and the new drive for governmental austerity at the macroeconomic level are causing a transformation of domestic political actors, forcing left-wing governments to converge around market-friendly policies (1996: 85). This process involves monetary orthodoxy and fiscal retrenchment on a wide range of issue areas including industrial policy, labour market policy, taxation, and the welfare state etc., a situation which forces left-wing political parties to adjust to these new realities (1996: 85). Pro-market ideology seeps downwards towards national institutions, policy makers and other actors: 'A climate of embedded financial orthodoxy will permeate the budgetary process, with widening circles of government austerity reaching ever-increasing parts of the state' (1996: 95). For Cerny (1996: 91), it is the internationalisation of finance and the rise of capital mobility that is the main reason for this 'competition state.' This process is rendering the state little more than 'an enterprise association organised around serving the needs of financial capital' (1996: 93). Cerny's view regarding the ascendancy of capital leaves little room for partisan politics.

Ruggie (1994) argues that the new hierarchies and priorities of the global market have destroyed the social pact that came into being after the Second World War. This pact is what Ruggie (1982) termed 'embedded liberalism,' that is, trade liberalisation combined with domestic measures that cushioned and compensated those that stood to suffer most from liberalisation. Ruggie (1994: 525) believes that the new world economy has now become 'disembedded,' leading to a loss of direction for national governments (1994: 525). This in turn, has provided the opportunity for pro-market ideologues to call for a rectification of the market/state role and to propagate the dominance of pro-market ideas (1994: 523). 'Policy attitudes towards the new world economy have shifted in the direction of Neoliberalism' (1994: 525), leaving left-wing political parties with little scope for redistributive policies. This ideational shift has been compounded by financial integration, which, from a Keynesian perspective, has forced governments to adopt fixed exchange rates in order to increase market confidence (Ruggie, 1997), but in doing so, macroeconomic autonomy is sacrificed at the altar of capital. Consequently, governments, if they wish to remain 'efficient' and competitive in global markets, can no longer compensate workers in the face of increasing liberalisation.

Compensation and redistributive programmes are funded primarily through progressive taxation, but mobile asset holders are simply unwilling, in the current international climate, to fund government redistributive programmes through high levels of corporate taxation (Rodrik, 1997). So, the only way to prevent capital flight and remain competitive is to shift the burden of taxation from capital, which is mobile, onto labour, which is immobile (Scharpf, 1991; Kurzer, 1993; Steinmo, 1993). Eichengreen (1997: 378), warning of the ‘tyranny’ of the financial markets, argued that:

Economic theory supports the notion that financial globalisation has shifted the burden of financing the welfare state onto labour...The most basic principle of the theory of tax incidence is that elastically supplied inputs into production escape the burden of taxes; try to tax them and they vanish. The international mobility of capital has just this effect of offering capital an exit option. It is not surprising that capital’s share of taxes paid in OECD countries has been trending steadily downward in recent years.

Government’s fiscal policy is constrained by capital mobility, since taxes cannot be raised without reducing the competitive advantage of domestic producers. Large budgetary deficits, without the possibility of exchange rate adjustments, raise prospects of inflation and higher interest rates (Pierson, 1994; Esping-Anderson, 1990; Rodrik, 1997). So, in the context of increasing economic globalisation, increased social spending will reduce competitiveness in the global market. It is simply not efficient.

This ‘efficiency hypothesis’ is widely supported by empirical evidence.¹⁶ Brian Burgoon’s (2001: 546) study indicated that trade openness does have an effect on welfare outcomes in the OECD states, but he does caution that openness ‘is far from the most important determinant of welfare efforts’ in these states. Garrett & Mitchell (2001), while they did find evidence to suggest that integration into global markets has not lead to a shift in taxation from capital onto labour in the OECD states, did find evidence suggesting that increasing trade liberalisation has resulted in lower government social spending in these same countries. Garrett (1999), in a global sample, found that trade integration has a consistently negative effect on

¹⁶ The alternative argument to this ‘efficiency hypothesis’ has been labelled the ‘compensation hypothesis.’ See section 1.2.

aggregate social spending and that this is compounded by openness to capital markets. Scharpf and Schmidt (2000), examining change in welfare policies over three decades in 12 advanced industrial democracies, concluded that globalisation forced government after government to reduce the role of the welfare state. For Scharpf & Schmidt (2000: 335): 'regardless of the political orientation of their governments, none of them (states) could fully defend the achievements of their post-war golden age' (2000: 335). In an interesting variant on this theme, Bailey, Rom & Taylor (2001) found evidence to suggest that as international competition increases, governments view spending on education as 'redistributive' and so reduce expenditure on education.

Moses' (1994) qualitative study analysed the demise of the mix of social welfare programmes and progressive taxation in Sweden and Norway. Moses (1994: 126) came to a definitive conclusion: 'social democratic institutions were designed for an environment that no longer exists. The conditions no longer exist because of changes that occurred beyond the regulatory reach of social democratic officials.' Moses argues that the demise of the welfare state in the Nordic states was a direct consequence of increasing capital mobility. Specifically, fixing the exchange rate, in conditions of capital mobility, ensures that 'economic policy autonomy, regardless of its specific ingredients evaporates' (1994: 140). In the context of economic globalisation 'domestic policy autonomy, of any variant, is costly' while social democracy 'is perhaps the most obvious victim' (1994: 142).

Recently, this avenue of inquiry has been extended to the developing world. Nita Rudra's (2002) findings, based on a sample of 50 developing states, indicated that welfare spending in these states does indeed respond to greater trade flows and capital mobility. Rudra (2002: 435) argued that while labour could successfully defend their welfare benefits in developed states, the increasing number of low-skilled workers, coupled with surplus labour populations, exacerbated 'collective-action problems' in developing states, reducing labour's ability to protect its welfare benefits and demand compensation. Consequently, the pressure of convergence is magnified in the developing world. Kaufman & Segura-Ubiergo (2001), examining social welfare spending in Latin American states, concluded that the effects of trade openness clearly favoured the efficiency over the compensation hypothesis. They did discover however, that this is only in the context of social security transfers (specifically pensions). Increasing trade liberalisation did not appear to bring about

reductions in health and education expenditure (2001:554). Wibbels & Arce (2003: 125) examining taxation in Latin American states, although their results were mixed, did uncover evidence to support the thesis that increasing economic globalisation has a 'negative impact on the progressivity of tax policy.' Interestingly, they concluded that taxation was increasingly shifted to labour where capital controls were high, indicating a unique, developing world policy trade-off (2003: 125-127).¹⁷

Clearly, the empirical studies described above have been primarily concerned with external economic imperatives – increasing trade liberalisation, capital mobility etc. resulting in reduced social spending and corporate taxation in order to foster 'efficiency' and therefore remain competitive in the international market. They are not particularly concerned with government partisanship *per se*, although logically, potential left-wing governments will be most affected by these eventualities. Large social welfare programmes and progressive taxation are more associated with governments of the left than with governments of the right.¹⁸ So, the cumulative effect of the efficiency hypothesis is to seriously circumscribe, if not completely eliminate, distinctive left-wing political strategies and policies.

Other empirical studies have been directly concerned with government partisanship. Ross (2000) concluded that left-wing parties have had as great an impact on the demise of the welfare state as have had parties of the right. Castles (1998) and Huber & Stephens (2001) found little evidence that contemporary left-wing governments expand the welfare state once in power. Charles Boix (2000), examining fiscal and monetary policy for a sample of OECD states, found evidence that while partisanship (left-government) and institutional differences between states do matter in the conduct of macroeconomic policies, these policies are severely constrained by the international context in which they are embedded. With increasing capital mobility, an autonomous monetary policy becomes harder and harder to pursue. Milner and Keohane (1996) co-ordinated a study taking into account the effect of institutions in mediating the potential effects of 'internationalisation,'¹⁹ focusing in particular on the effects that increasing internationalisation may have on left-wing government strategy and policy. They do find that economic globalisation

¹⁷ Trade openness appeared to have little impact on taxation, whereas portfolio capital and foreign direct investment did (Wibbels & Arce, 2003: 125).

¹⁸ See Biglaiser & Brown (2005)

¹⁹ Milner & Keohane use the term internationalisation to describe the macroeconomic effects of economic globalisation.

has undermined the policy autonomy of national governments, although their conclusions could be considered rather cautious (1996: 256).²⁰ They are in agreement with Andrews and suggest that capital mobility should be considered a structural feature of the international system (1996: 257), and with respect to left-wing governments, they posit that the net effect of this increasing internationalisation is a serious limitation on the policy autonomy and therefore efficacy, of left-wing parties in the global economy. For Milner & Keohane (1996: 18), 'internationalisation will undermine the autonomy and efficacy of government macroeconomic policy. It will seriously constrain the behaviour of left-wing governments than of right-wing governments.'²¹

Saskia Sassen (1996) also arrived at a more moderate conclusion to those who assume economic globalisation is leading to an inevitable universal policy convergence. For Sassen, institutional state capacities have not been obliterated, but they have been reconstructed and partly displaced into other institutional areas outside the realm of the nation state (1996: 29), resulting in a 'privatised world of governance,' whereby commercial arbitration and supra-national economic regulations will bypass national laws (2002: 66), leaving states with a reduced role in the global economy, ultimately ensuring that partisan politics begins to lose meaning. Like Milner & Keohane, she does caution that this position is not as black and white as it may appear. States still have an important role to play in the current era of globalisation, but this role is often as a provider of an institutional home for the new policy regimes dictated by economic globalisation (2002: 69).

In addition, Alesina and Roubini (1992), taking the rational partisan model of the economy as a base,²² which suggests that left-wing governments expand the economy when they come into office, while right ring-governments contract the economy, examined this effect in small, highly trade dependent countries. Their

²⁰ Interestingly, they argue that this has resulted largely from rising capital mobility rather than trade, an argument that contradicts the prevailing wisdom in the compensation-efficiency debate. Much of the empirical work in this literature has found that while trade openness exerts an effect, the effect of capital mobility is negligible. See for example Burgoon (2001).

²¹ Importantly, Milner & Keohane (1996: 251-255) also suggest that institutions may have three main roles in mediating the effects of economic globalisation; by blocking price signals emanating from the international environment, by freezing coalitions and policies into place that would resist the convergence hypothesis, and by channelling different national responses to economic globalisation (1996: 251-255).

²² This model is derived from the literature on macroeconomic policy making, which shows that a rational partisan model of the economy is a powerful predictor of policy-makers behaviour. In this model, left-wing governments expand the economy when they come into office, while right ring-governments contract the economy.

study found no evidence of rational partisan macroeconomic cycles, suggesting that very high levels of economic globalisation, significantly constrain distinctive left-wing macroeconomic strategies (Alesina & Roubini, 1992).

From the above literature, a clearly discernible common theme can be identified as regards the efficacy of left-wing politics in the face of economic globalisation, despite the variety, nature and quality of these arguments. The central argument of this literature is that as a result of increasing economic globalisation, governments must now compete for increasingly mobile international capital. Consequently, capital has increased in power relative to labour, due to the credibility of the highly mobile capital's exit threat. Capital prefers a certain mix of government policies, concentrated along market-friendly lines, involving little government intervention or spending in the economy, a roll-back of the public economy through privatisation, flexible labour markets, reduced social welfare spending, and low levels of corporate taxation. If governments fail to provide policy along these lines, capital will simply exercise its exit option and move to a more favourable location. All governments, regardless of their political orientation, must converge along these policy lines. However, this policy mix is more congruent with the preferences of right-wing politics and as such, this inexorable policy convergence along market-friendly lines significantly reduces, if not completely removes, the prospects for distinctive left-wing policies. In the context of economic globalisation therefore, left-wing governments do not have the ability to implement their economic policy preferences.

1.2 The Second Wave

The core tenets of the globalisation thesis have been vigorously challenged in the form of the so called 'second wave' literature (see Kofman & Youngs, 1996; Hay & Marsh, 2000),²³ and just as those that support the globalisation thesis do so from a variety of positions and backgrounds, so too do those that challenge this thesis.²⁴ Roughly speaking however, those that contest the wisdom of the globalisation thesis can be divided into three main groups, none of which are mutually exclusive. Firstly, there are those authors who contest the very notion that markets today are globalised

²³ The 'second wave' literature has also been labelled 'sceptical.' See Held *et al.* (1999).

²⁴ Only in the area of monetary policy is it widely accepted that economic globalisation undermines the policy autonomy of national governments (see Garrett, 1998a, 1998b; Berger, 2000; Philips, 2005).

or are in the process of becoming globalised. They argue that the international global economy is no more integrated and capital no more mobile than it has been during other periods of history. Secondly, there are those specifically concerned with the 'efficiency hypothesis' who suggest that increasing economic globalisation may place pressure on governments to 'compensate' sectors of the population disadvantaged by increasing liberalisation. So, in order to cushion and compensate these sectors, increasing economic globalisation will actually encourage governments to increase social welfare spending and refrain from shifting the burden of taxation from capital onto labour. What is more, a strand of this literature has begun to untangle the institutional and partisan effects that may mediate the effect of economic globalisation and magnify compensation. Taking their lead from these authors, a third group contend that those who propagate the globalisation thesis neglect to take into account the specific configuration of national institutions or domestic political factors. They argue that in many instances, welfare retrenchment or alterations in the taxation regime can be laid at the door of domestic political and institutional factors rather than some external economic imperative, or alternatively, where the public economy has increased, this may be as a result of specific national issues, rather than increased uncertainty as a consequence of globalisation. Partisanship in this context still matters.

So, the departure point for the second wave literature is those who have convincingly argued that the first wave grossly exaggerated the nature and extent, as well as the 'qualitative novelty' (Hay, 2000: 141) of economic globalisation (see Zevin, 1992; Berger & Dore, 1996; Hirst & Thompson, 1996; Evans, 1997).²⁵ Specifically, this literature has argued that today's markets are no more 'globalised' than they were say, at the end of the nineteenth century (see Maddison, 1995; Krugman, 1995; Obstfeld & Taylor, 1997; Hirst & Thompson, 1996, Wade, 2000), that capital's main loci of operation remains national economies (Hay & Watson, 1998; Weiss, 1997), that the vast majority of international economic activity remains concentrated in a small number of developed world states (Wade, 1996; Frankel, 1997), and that production for the domestic market remains the norm in all bar integrated city-states such as Hong Kong and Singapore (Krugman, 1994).²⁶ By

²⁵ For an overview of the second wave see Hay & Marsh (2000).

²⁶ It is important to note that not all second wave theorists are simply dismissing the effects of increased interdependence. They do acknowledge that this process has some effect on policy making

challenging the very existence of increased economic interdependence and by extension the increasing power of capital, this literature attempted to remove one of the core theoretical tenets of the first wave. Hirst & Thompson (1996) challenged the claims concerning the hyper-mobility of capital and suggested that contemporary patterns of trade and investment have become no more internationalised than in other historical periods. Indeed Hirst (2000), questioning the veracity of the first wave, and examining in detail the extent of openness, trade and foreign domestic investment in the developed world, argued that ‘the scope of national policy in the advanced world has not been diminished to the degree the globalisers believe,’ (Hirst, 2000: 20-28) leading him to the conclusion that ‘globalisation is a myth, un-sustained by the evidence’ (2000: 28). In this respect, this cross-section of the second wave literature has argued that economic globalisation is an exaggerated and poorly understood phenomenon and consequently, it has not led to the erosion of national policy autonomy. As such, left-wing politics still has considerable meaning and autonomy in today’s world.

Those that first proposed the ‘compensation hypothesis’ were not concerned with questioning the veracity of economic globalisation. They argued, in contrast to the ‘efficiency hypothesis,’ that increasing economic globalisation, manifest in the form of trade liberalisation, would actually lead to increases in government social spending (Cameron, 1978; Blais, 1996; Hicks & Swank, 1992). The foundations of the ‘compensation hypothesis’ are to be found in Karl Polanyi’s (1944) ‘double movement’ from his *Great Transformations*. Polanyi argued that industrialised societies, in the face of increasingly autonomous markets, which in the first place they themselves created, in turn implemented policies to cushion their societies from the dislocating effects of these same markets. Following a similar logic, the ‘compensation hypothesis’ suggests that governments will increase social spending in order to offset the social costs of increasing trade liberalisation. They will cushion the effects of liberalisation for those sectors of society who do not stand to benefit from integration.²⁷ Initial studies suggested that the positive effects of trade openness on social spending were related to the scope of collective bargaining within

at the national level. Their main argument, however, is that these effects have been largely over exaggerated.

²⁷ Theorems of international trade, Heckscher-Ohlin, Stolper-Samuelson and Ricardo-Viner suggest those sectors of society who benefit or lose from international trade will be defined by their stakes in the factors of production (see Berger, 2000: 49).

states, levels of union density and by the partisanship (left-wing) of the governments in power and opposition (Cameron, 1978: 1256; Hicks & Swank, 1992: 669-670), but the political links between trade openness and welfare spending still remained unclear.

However, a number of later studies supporting the ‘compensation hypothesis’ were to ‘go further than anyone else in disentangling the ties that bind openness and welfare effort, especially in analysing how labour market and partisanship institutions mediate the relationship between openness and welfare’ (Burgoon, 2001: 515).²⁸ These studies rejected the globalisation thesis and argued that domestic institutions (namely labour institutions), depending on their specific configuration, would mediate the effects of economic globalisation in different manners for different states. Garret and Lange (1991: 541), building on an earlier work (Garrett & Lange, 1989), examined social welfare spending and taxation policies in the advanced industrial democracies and argued that while the effects of economic globalisation have been substantial, ‘they have not eliminated partisan economic separation between the left and the right.’ Furthermore, Garret and Lange (1991) highlighted the importance of institutions in mediating the assumed and blanket policy convergence suggested by the first wave literature. Specifically, left-wing governments allied with broad labour movements have the potential to implement autonomous policy, which is consistent with policies of the left. They concluded that ‘governments of the left – in alliance with powerful labour movements – have been able to maintain their traditional goals of redistribution, welfarism, and full employment’ (Garrett & Lange, 1991: 564).²⁹

In a later study, Garrett (1996: 81-88) found ninety different effects of economic globalisation on public policy, yet he rejected the argument that left-wing politics is no longer relevant in the face of market forces. Garrett (1998b: 823), examining the effects of economic globalisation on the OECD states, concluded that governments that have persisted with interventionist policies have not been hamstrung by damaging capital flight. He did discover that the integration of

²⁸ In this discussion on the ‘compensation hypothesis’ I include studies on the burden of taxation. Generally this term refers to studies on social spending, but as others have pointed out, taxation is part of the ‘compensation hypothesis.’ Social spending is financed through taxation, and therefore the compensation hypothesis should be considered to encompass the social welfare-progressive taxation mix. See Wibbels & Arce (2003).

²⁹ Hay (2000) characterizes this position as the dual convergence thesis, that is, two Pareto optimal frontiers in the face of economic interdependence.

financial markets does curtail policy to a greater extent than either trade or the multinationalisation of production, however once again, Garrett's analysis led him to the conclusion that the policies of left-wing governments are not undergoing an evitable convergence as a result of economic globalisation (1998b: 823).

Garrett's (1998a) pioneering *Partisan Politics* highlighted the importance of domestic political institutions in mediating the effect of economic globalisation. Garrett not only argued that trade openness may lead to an increase in social spending as governments compensate those sectors of society who do not benefit from integration, but he also suggested that international markets may, in fact, favour this outcome. Garrett's argument is a relatively simple one. It is widely believed that greater economic interdependence will 'favour' a specific government model, comprised of deregulated free-market capitalism, with little social protection, government intervention or regulation in the economy. However Garrett, through an analysis of the advanced industrial democracies, contends that this is not necessarily the case. In fact, Garrett (1998a: 1) posits that in political economies where left-wing parties are allied with 'broad and centrally organised labour movements,' economic interdependence will favour this policy coherence and this will be reflected in solid macroeconomic outcomes. In this respect therefore, for Garrett (1998a:1), 'the relationship between the political power of the left and economic policies that reduce market-generated inequalities has not been weakened by globalisation; indeed it has been strengthened in important respects.' Conversely however, policy incoherence, or situations where left-wing parties are not allied with broad and encompassing labour market institutions, will not be 'favoured' by economic interdependence, resulting in poor macroeconomic outcomes (1998a: 9).

Garrett rejects the assumption that left-wing government policies will ultimately lead to capital (mobile asset holders) exercising their exit option. Rather, he outlines two specific reasons why the opposite may be the case. The first is primarily concerned with the 'new growth theory.'³⁰ This theory posits that government spending on infrastructure and human capital (through welfare payments, education etc.) is actually beneficial to the economy, in that it provides and nurtures a healthy, productive and well-educated workforce. Garrett (1998a: 8) argues that asset holders can realise the benefits of such government spending and as

³⁰ See for example Romer (1994)

such, it is 'unlikely to provoke capital flights in global markets.' The second reason is more general, and relates directly to the institutional structure of the political economy. Where labour unions are broad and encompassing, Garrett argues that they will prevent isolated groups of workers from pushing up their wages through institutional wage setting, which is regulated by the encompassing labour union (1998a: 8-9). This wage setting, coupled with cooperation between capital and labour, will reduce instability and tension in the political economy, leading to greater productivity.³¹ So, for Garrett, 'enduring cross-national differences in the balance of power between left and right remain' (1998a: 10-11) and consequently the autonomy of left-wing policies has not been undermined by economic globalisation. The central point to draw from Garrett's analysis is the importance of institutions, specifically the nature of labour market institutions in the political economy, in mediating the effect of economic globalisation.

Building on Garrett's work, other studies find evidence to support the 'compensation hypothesis.' Allan & Scruggs (2004), employing quantitative techniques and examining the role of partisan politics in welfare state retrenchment, found little evidence of economic globalisation having an effect on welfare state reform (2004: 506). Their results did suggest that corporatist institutions may play a role in reducing welfare retrenchment (2004: 507), but they cast some doubt on the idea that pre-existing institutional arrangements necessarily constitute major barriers to change (2004: 509). Their study led them to the conclusion that 'contrary to claims that partisanship no longer matters, we find that partisanship exerts a considerable effect on welfare state entitlements' (2004: 497).

Swank (1998a: 679), examining corporate tax burdens for OECD states in the 1990s in the face of rising capital mobility, finds little change since the 1970s, although he could discern no tangible effect of partisanship on taxation. In relation to the impact of international capital mobility on corporate profits taxation, he discovered that 'if anything, direct effects of globalisation of capital markets are associated with slightly higher business taxes, and to a degree the diminution of tax policy responsiveness to the conditions that underpin investment' (Swank, 1998a: 690-691). Other studies have reached similar conclusions (see Steinmo & Swank,

³¹ Again, Garret (1998b) draws similarities between these arguments and those of Polanyi's (1944) double movement, the first a move towards *laissez-faire* capitalism driven by free trade, the other a move towards social protection to cushion the effects the of free-market capitalism.

2002). Likewise, Garrett (1998a) concluded that economic globalisation does not diminish a government's capacity to tax, nor even its options for progressive taxation. Social democratic governments allied with broad and encompassing labour movements are associated with bigger government and higher corporate tax rates. Although trade openness did appear to have an effect on social spending, Garrett & Mitchell (2001) did find that integration into global markets has not resulted in reductions in capital tax rates, or shifts in the burden of taxation from capital onto labour. Prakash & Potoski (2006) examining environmental standards across 108 countries, found no evidence that increasing trade liberalisation was leading to a 'regulatory race to the bottom' in order to maintain competitiveness.

It can be clearly seen that the focus of this literature has been on the advanced industrial democracies. Few empirical studies have expanded this issue to the developing world. Moreover, the vast majority of attempts to theorise this relationship in the state-economy interdependence debate have been overly reliant on the experiences of this small selection of states (Philips, 2005: 83). For Philips (2005: 83), 'this reliance has carried a range of implications for the theoretical lens through which state debates have been approached, and has imbued these debates with a range of biases.' However, a small number of important recent studies have attempted to rectify this theoretical and empirical poverty.

The majority of these studies have shown that the effects of increasing economic globalisation appear to be magnified in the developing world. Kaufman & Segura-Ubierno (2001), examining social welfare spending in Latin American states, found evidence in support of the 'efficiency hypothesis.' Increasing trade openness resulted in reductions in social security transfers. Nita Rudra (2002) discovered similar findings. Wibbels & Arce (2003) cautiously concluded that the mobility of portfolio capital and FDI did have a negative impact on the progressivity of taxation systems in Latin America. A recent study by Avelino, Brown & Hunter (2005) however, would appear to contradict some of these findings. Their study of social welfare spending in Latin America appeared to bolster support for the 'compensation hypothesis.' Trade openness (depending on how it was operationalised) did have a strong positive association with spending on social security and education in Latin American states, while financial openness appeared to have no impact (2005: 637).

Even those that did find evidence for convergence in the face of increasing economic globalisation in the developing world, were cautious in their support for

the globalisation thesis. In fact, they all found evidence to suggest the importance of partisanship (left governments) in cushioning the effects of increasing integration. Kaufman & Segura-Ubiergo (2001: 583) concluded that ‘popularly based governments’³² in Latin America are an important force for the protection or extension of welfare transfer programmes.’ Nita Rudra’s (2002: 436) analysis showed that there ‘are political factors (such as strong labour support and democracy) that can positively affect welfare spending in this era of globalisation.’ For Wibbels and Acre (2003: 132): ‘despite arguments that mobile capital would sweep all national politics before it and that politicians of the left, right and centre would all be impelled to bow to the demands of the markets, the political power of the left continues to have important implications for public policy, even in Latin America.’

However, Garrett (1998a), the earlier works of Garrett & Lange (1989, 1991, 1996) and consequently many of the empirical studies they have inspired, are not without their critics. In fact, Hay (2000: 138) has stated that Garrett’s argument in *Partisan Politics* ‘only marginally modifies the narrow economic logic of more orthodox ‘globaloney.’’ It is specifically the issue of labour market institutions that Hay takes issue with. For Hay, the suggestion that left-wing governments coupled with broad and encompassing labour movements constitute a second *pareto optima*, does not necessarily refute the argument that partisan politics has been rendered meaningless by economic globalisation. In fact, Hay ponders whether such an argument is actually consistent with this view (2000: 139). Where previously the logic of economic interdependence summoned an inevitable path to market-friendly policies, Garrett’s argument suggests that this path is now bifurcated. Hay contends that the logic is no less inevitable and no less inexorable when it is considered that social democratic outcomes are dependent on social democratic institutions.³³ For Hay (2000: 143), Garrett’s arguments constitute an ‘interesting variant on the prevailing orthodoxy rather than a rejection of it.’ So, in a state with no encompassing labour market institutions, such as Britain, social protectionism or left-

³² The term Kaufman & Segura-Ubiergo use to describe social democratic, left-wing, centre left, or union based political parties

³³ Garrett (2000) did reply to Hay’s critiques and constructed an analysis of European states without reference to his institutional typology. Interestingly, he does find evidence that fiscal policy has been constrained where governments commit to fixed exchange rates. Here, Garrett argues that this is not as a result of economic interdependence, but rather as a result of the project of European integration.

wing policies are no longer viable, summoning precisely the logic of no alternative that Garrett set out to challenge (2000: 145).

The third section of the literature contesting the globalisation thesis partly bases its insights on arguments borrowed from the two strands discussed above. These studies also reject the assumption that globalisation is the *only* independent variable to explain changes in social welfare policy. They argue that increasing demands for compensation may be more a product of a specific domestic factor, de-industrialisation, the shift from manufacturing to non-tradable service industries, rather than increasing liberalisation (Iverson & Wren, 1998; Iverson & Cusack, 2000). Domestic-level variables may have just as much explanatory power, if not more, than exogenous variables.

On a similar note, ‘the new politics of the welfare state’ literature (Pierson, 1996), also contests the idea that changes in welfare expenditure can be solely explained by economic globalisation. In fact, this literature highlights the importance of political institutions in nullifying or mediating the potential effects of increasing economic globalisation on welfare retrenchment. Pressures for retrenchment mostly emanate from socio-economic, particularly domestic-level issues, such as the ageing of the population, the maturation of welfare programmes or reliance on faulty economic policy tools (Notermans, 1993: 167). What is more, where retrenchment does occur, the extent of this retrenchment has nothing to do with any external economic imperative, but rather is a product of national institutional configurations and the path dependence of existing welfare state structures (Pierson, 2004). Those that advocated retrenchment could only achieve their preferences where the existing institutional structures were favourable to their goals and *vice versa*. Consequently, welfare retrenchment has proved resilient and change incremental (Pierson, 1994). For example, where partisan governments have been committed to preserving core features of the welfare state (Netherlands), institutional structures have allowed a range of reforms that have ensured that the central tenets of the old redistributive model remain (Levy, 1999). So, policy outcome has been primarily a product of domestic political battles that have occurred within and been shaped by, existing national institutional structures rather than some exogenous economic force (Pierson, 1994, 1996, 2001, 2004).

Campbell (2004: 129), using institutional theory to track the evolution of taxation systems, argued that economic globalisation is not leading to the

homogenisation of policy across nation-states. Rather, he convincingly contended that ‘divergence remains the rule rather than the exception because national institutions, which vary across countries, mediate the degree to which global pressures affect decision-making by states and private actors in ways that militate against convergence’ (Campbell, 2004: 129). Policy outcome is a product of specific institutional configurations and the path dependence of existing taxation structures. For Campbell, the idea of economic globalisation has been used by conservatives to create an ideological climate that suggests government intervention is futile and could hurt national competitiveness (2004: 170).³⁴

Duane Swank (1998b, 2002, 2003), building upon the theme of institutions mediating economic globalisation, examined how political institutions ‘provide or restrict opportunities for representation for those that are adversely affected by globalisation and for those ideologically opposed to – or materially harmed by – the common neoliberal responses to globalisation’ (2002: 6). The general argument: ‘The domestic policy impacts of international capital mobility should vary substantially across specific configurations of national institutions’ (2002: 34). For Swank (2002: 39) the:

[p]roponents of globalisation theory fail to take into account the broad array of domestic political actors whose material interests, concrete policy preferences, and ideological goals are threatened by internationalisation and attendant neoliberal reform programmes; they also say little about the roles of political institutions in shaping the relative political power of these pro-welfare state interests to resist neoliberal reform.

When taking into account the role and nature of institutions it is viable and legitimate to argue that an alternative to dramatic and market-friendly social and labour policy reforms exist (Swank, 2002). Taken in this context, partisan politics still matters.

All of these arguments reflect similar themes in studies concerned with national varieties of capitalism (Albert, 1993; Soskice, 1991; Streeck, 1997; Hall & Soskice, 2001).³⁵ In this literature, the notion of an inevitable policy convergence has been challenged by detailed analyses of the divergence of government policies in the

³⁴ See also Block (1996) and Gilpin (2000) who make similar claims concerning the dominance of ideas that suggest there is no political alternative to increasing economic interdependence.

³⁵ For an overview of some of this literature see Berger (2000)

face of increasing economic globalisation, as a result of different state capacities (Boyer & Drache, 1996; Weiss, 1998), domestic institutional structures and political party adaptations (Weiss, 2003, Clift, 2003).

So, from the above literature, it is clear that there is an alternative position to the globalisation thesis. A number of common themes can be identified; the extent and nature of globalisation is exaggerated; increasing economic globalisation may actually lead to left-orientated policies due to compensation pressures; labour market and partisan institutions will magnify this effect, suggesting left-wing governments do matter; and the configuration and path dependence of political institutions will mediate the effects of economic globalisation by either providing opportunities for left-wing governments to achieve their preferences or by constraining these governments. Institutions can protect and insulate states from the ruinous 'race to the bottom' that is outlined in the globalisation thesis. As such, domestic politics still have significant policy autonomy in the context of economic globalisation. Even in the face of increasing economic globalisation, partisanship (left-wing governments) matter.

1.3 Conclusion

A review of the above literature clearly distinguishes dichotomous schools of thought on the effects of economic globalisation on partisan politics. One side contends that economic globalisation has rendered partisan politics meaningless, due to the risk of capital flight and a loss of national competitiveness and as such, has precipitated an inevitable policy convergence along market-friendly lines. The opposing side posits that the effects of economic globalisation have been overstated and exaggerated and other explanatory variables, particularly the partisanship of the government in power, will mediate the threat of convergence. Left-wing politics still matters. This literature review places the current thesis within a body of literature and provides a context for the main research question.

This study will contribute to the above debate in three ways. The study is focused upon the effects of political institutions and will add to other work in this vein in the literature. Scholars have moved beyond employing economic globalisation as the sole explanatory variable when examining the globalisation thesis. Early studies utilising left-wing politics as an independent variable found that, where governments were of the left, the effects of convergence were lessened or

even reversed. The means by which left-wing politics resisted this convergence remained unclear, but it was thought that the answer lay in the relationship of these parties with labour. Later, studies began to focus on labour market institutions to explain the efficacy of left-wing politics in mediating the impact of economic globalisation. However, the domestic-level mechanisms by which left-wing governments resist the pressures of convergence still remain under-developed.

Studies have incorporated institutional variables, such as democracy (see Avelino, Brown & Hunter, 2005), party fragmentation (see Wibbels & Arce, 2003), or else labour market institutions (see Garrett, 1998a). Duane Swank (1998b, 2002) has emphasised the importance of certain institutional configurations in providing opportunities, to those opposed to or materially harmed by the policies associated with convergence, access to decision-making. Paul Pierson (1994, 1996, 2004) has argued that the effects of economic globalisation on welfare retrenchment, where it has occurred, have been mediated and nullified by the institutional design and path dependence of existing welfare policies. This research builds on these approaches by examining one policy area within a framework of institutional policy-making that attempts to capture the importance of access and control over decision-making and also the effects of policy design and path dependence. A qualitative study of this nature can help further shed light on the multi-faceted effects of political institutions on the policy process.

Secondly, the vast majority of empirical studies in this debate have been concerned with the advanced industrial democracies, although some recent studies have expanded aspects of this debate to the developing world (see Rudra, 2002) and to Latin America in particular (see Wibbels & Arce, 2003; Kaufman & Segura-Ubiergo, 2001; Avelino, Brown & Hunter, 2005). This research continues the effort of expanding this debate to the developing world, but so far, no studies have placed any serious focus on the role of political institutional variables in mediating the effects of economic globalisation in the developing world. As such, this study will be one of the first major attempts to decipher the institutional mechanisms that enable left-wing governments to resist convergence in the developing world. A study of this sort should provide us with a greater understanding of the role of left-wing governments in general, and in the developing world in particular.

Thirdly, the empirical studies within this debate have focused on specific policy areas only: monetary policy or shifts in the burden of taxation and social

welfare spending and reform.³⁶ No studies have utilised privatisation policy as the dependent variables in empirical studies. Privatisation is a good policy to utilise because we have expectations regarding the relationship between economic globalisation and privatisation. According to the globalisation thesis, increased economic integration, particularly for developing states, should lead to increased levels of privatisation. However, this thesis remains to be empirically tested. A study examining government intervention (privatisation) in the economy would be a significant contribution, as it would empirically widen this debate to other policy areas.

³⁶ Some interesting studies have begun to extend this literature to other areas. Prakash & Potoski (2006) examined the effect of economic globalisation on environmental regulations, Bailey, Rom & Taylor (2004) on education, Rodrik (1996) on labour standards and Prakash & Kollman (2003) on genetically modified organisms.

Chapter Two – The Research Design

At the heart of this project is an interest in the conditions that may grant left-wing governments the ability to implement autonomous policies in the face of the ‘convergence thesis.’ Specifically, this project is concerned with the role of political institutions in mediating this convergence. The previous chapter demonstrated that this research is grounded in a body of theory, but it is also possible from the discussion of this literature to identify a number of explanatory variables that may have an effect in mediating the policy convergence advocated by the first wave authors. This project intends to examine the mechanisms by which left-wing governments can implement autonomous policies in an era of economic globalisation by means of comparative case studies. In order to provide structure for these case studies, the project intends to utilise the analytical narratives approach.³⁷

The purpose of this chapter therefore, is to explain the research design. The first section will focus on the research question itself and the theoretical and real-world contributions of this research. The second section will discuss the comparative approach and justify the selection of the case studies, while the third section will explain the methodology and the advantages of the analytical narratives approach. The fourth will identify the dependent and independent variables and outline the means by which the project will operationalise these variables. The final section will present the expected outcomes based upon the understanding of the explanatory variables.

2.1 The Research Question

Partisan theory assumes that governments have the ability to implement their preferences (Hibbs, 1992). However, the globalisation thesis posits that in this era of increasing economic integration, this is no longer the case. The initial scholarship in this debate, employing economic globalisation as the sole explanatory variable, argued that the increasing mobility of capital as a product of economic globalisation, was leading to a policy convergence along lines that internalise the preferences of this capital. This policy mix is congruent with the preferences of the political right, rather than the politics of the left. If left-leaning governments do not adopt this mix, they will face a potentially ruinous capital flight. So, left-wing governments would

³⁷ This is to prevent the case studies from becoming ‘just-so stories.’ See Bates *et al.* (2000: 700).

now appear to have little ability to implement their preferences (see Ohmae, 1996; Przeworski and Wallerstein, 1998; Ruggie, 1997). 'Even if today there are still strong domestic incentives for governments to pursue distinctive partisan strategies, these interdependence arguments suggest that such incentives are now overwhelmed by international constraints' (Garrett & Lange, 1991: 542).

Those that rejected this argument also rejected the focus on economic globalisation as the sole explanatory variable. Early studies contesting the concept of policy convergence contended that left-wing politics were far from meaningless in today's world. In fact, they treated left-wing politics as an independent variable and found that, where governments were of the left, the effects of convergence were lessened or even reversed (see Cameron, 1978; Hicks & Swank, 1992). The means by which left-wing politics resisted this convergence remained unclear, but it was thought that the answer lay in the relationship of these parties with labour. In later studies, the focus now shifted to labour market institutions and it was convincingly argued that in situations of increasing economic globalisation, where left-wing governments were allied with broad and encompassing labour movements (left-labour support), combined with compensatory pressures, the effects of convergence would be reversed (see Garrett & Lange, 1991; Garrett, 1998a). So, left-wing governments can implement their preferences.

Empirical studies however, still challenge the efficacy of contemporary left-wing politics even when taking into account the mechanisms described above (see Ross, 2000; Boix, 2000). Others have argued that another exogenous variable, the influence of the international financial institutions, may also place serious pressures on left-wing governments (particularly in the developing world) to adopt policies congruent with the globalisation thesis (see Wibbels & Arce, 2003; Avelino, Brown & Hunter, 2005). Swank (1998b; 2002) and Pierson (1996, 2004) have both highlighted the importance of political institutions, either by providing left-wing governments and those opposed to globalisation with access to decision-making structures, or as a result of path dependent effects that nullify or mediate the pressures for convergence.

Evidently then, the focus has shifted from simply treating economic globalisation as the sole explanatory variable in examining policy convergence to a more nuanced approach incorporating other variables. However, the mechanisms by which left-wing governments resist the pressures of convergence remain under-

developed and highly-contested. The purpose of this project is to further explore the role of other variables in helping or hindering left-wing governments achieve their policy preferences. Therefore, the main research question of this thesis is guided by the theory described above.³⁸ Specifically, it seeks to discover, *what ability do left-wing governments have to implement policies that are congruent with their preferences in the context of increasing economic globalisation? If any, under what conditions can they implement policies that are congruent with their preferences?* This question particularly seeks to unravel the effects of political institutions in mediating convergence, while simultaneously creating space for left-wing governments to implement policies that reflect their preferences. The overarching puzzle in this debate concerns the relevance of partisan politics in the contemporary environment, and an empirical study of this sort will contribute to a better understanding of the relevance of partisan politics in the political economy.

King, Keohane and Verba (1994: 15) highlight the necessity for a research question to make a ‘specific contribution to an identifiable scholarly literature,’ while at the same time being ‘important in the real world.’ This thesis aims to contribute to the existing scholarly literature in a number of specific ways. The contributions this study will make to the literature have been addressed in greater detail in the previous chapter. Firstly, the focus on exogenous variables in this literature has been to the detriment of a more complete understanding of the effects of domestic-level variables. In particular, the role of political institutions in mediating convergence warrants further attention. Some cross-country econometric studies have incorporated institutional variables (see Avelino, Brown & Hunter, 2005; Wibbels & Arce, 2003), as have some qualitative in-depth case studies (see Swank 2002, Campbell, 2004, Pierson, 2002).³⁹ This study builds upon these works and examines how different institutional configurations affect the control of partisan actors over decision-making and result in varied path-dependent effects. This purpose of this study is to further contribute to our understanding of how political institutions either provide opportunities for, or constrain, left-wing governments from achieving their preferences. Furthermore, utilising political institutions as an explanatory variable in econometric studies can often lead to issues of endogeneity in decisions of what to

³⁸ See Pennings *et al.* (2006: 20) and King, Keohane & Verba (1994: 14-19) on the importance of formulating a research question that is guided by a theoretical underpinning.

³⁹ See King, Keohane and Verba (1994) and Pennings *et al.* (2006) for the benefits to be gained from detailed, rigorous and structured qualitative work.

take for granted and what to explain. These problems can be overcome in historically grounded, country-specific, research of the type proposed here (Spiller, Stein & Tommasi, 2003: 7).

Secondly, previous studies have focused on the advanced industrial democracies (for exceptions see Rudra, 2002; Wibbels & Arce, 2003; Kaufman & Segura-Ubiergo, 2001 and Avelino, Brown & Hunter, 2005). The proponents of the convergence thesis suggest that we should witness this phenomenon in all parts of the world, yet there is still a dearth of research extending the claims of the first and second wave theorists to the developing world. What is more, no studies have placed any serious focus on the role of political institutional variables in mediating the effects of economic globalisation in the developing world. As such, this study will be the first major attempt to decipher the institutional mechanisms that enable left-wing governments to resist convergence in the developing world. This research is partly driven from the dissatisfaction with the current literature in this under-researched area.

Thirdly, the empirical studies within this debate have focused on specific policy areas only, to the detriment of an understanding concerning the wider policy implications of the convergence thesis. No studies have utilised privatisation as the dependent variable in empirical studies. A study focusing on privatisation will widen this debate and contribute to a better understanding of the role of partisan politics in the political economy.

While the 'political' contribution of any study is essentially a societal judgement (King, Keohane & Verba, 1994: 15), the role of partisan politics in the context of increasing economic globalisation has significant ramifications for the developing world. In an era of increasing discontent within parts of the developing world with market-friendly policies, we have witnessed an increase in the number of left-wing parties elected to power. However, if the convergence thesis is correct, then this essentially vitiates electoral responses to this dissatisfaction with market-friendly policies. The shift to the left in Latin America has been heralded as a rejection of the dominant economic mode of governance. The ability of left-wing governments to implement policies that reflect their preferences in South America may have wider implications for electoral politics in general, and for the developing world in particular.

2.2 The Comparative Approach and Case Study Selection

The Comparative Approach

In order to answer the research question set out above, this project will employ a comparative approach across three case study countries.⁴⁰ The comparative approach is not a method *per se*, but it is one of the most adequate ways to connect theory with what is actually going on in the world (Pennings *et al.* 2006: 5). Furthermore, ‘all social science requires comparison, which entails judgements of which phenomena are more or less alike in degree or kind’ (King, Keohane & Verba, 1994: 5). Comparison is an instrument to verify or falsify relationships between phenomena. For this we need ‘to reduce the complexity of reality and thus to control for variation – this is what the comparative approach allows for’ (Pennings *et al.* 2006: 23). Therefore, comparison is necessary in order to control the variables that make up the theoretical relationship (Sartori, 1991: 244). Comparative research must have an extensive theoretical argument underlying it, and a methodologically adequate research design to undertake it (Pennings *et al.* 2006: 20). This study follows these basic rules and therefore replicates the comparative approach. The research question is drawn from the extensive theoretical underpinning that is provided by the rich literature on the relationship between economic globalisation and partisan politics, and the methodology is the use of an analytical narrative across three comparative case studies with clearly defined and operationalised variables. The theory-guided question within any type of comparative analysis is ‘to what extent the political in terms of explanatory units of variation (variables), can indeed be accounted for and is shaped by the political actions in one social system compared to another’ (Pennings *et al.* 2006: 27). This approach and the attempts to explain it by systematic comparison distinguish the comparative approach from other approaches in the social sciences.

In the social sciences, debate continues to rage concerning if, when and how to compare (see Pennings *et al.* 2006; Lijphart, 1975). There are also a number of methodological problems to take into account when using the comparative approach (Collier & Collier, 1991).⁴¹ Two of the principal problems identified by Lijphart are

⁴⁰ This is the closed universe of discourse, that is, the selection of two or more case at a few time intervals. See Pennings *et al.* (2006).

⁴¹ See Pennings *et al.* (2006) for a discussion of the three main problems facing the comparative approach. The first of these issues is whether the research question is embedded in the correct approach in terms of a variable-orientated design or a case orientated design. Secondly, there is the

simply ‘many variables, small number of cases’ (Lijphart, 1971: 685). Both are clearly interrelated, but the former is common to all social research, while the latter is peculiar to comparative research. Another problem stems from the distinction of what Collier and Collier (1991: 13) classify as ‘splitters’ and ‘lumpers.’ Splitters are quick to see contrasts between cases and to focus on the distinctive specific attributes of each case. This research is valuable in terms of generating new hypotheses and for providing basic data. The lumpers, on the other hand, are quick to identify generalisations and commonalities that contribute to grander theory. In the case of the lumpers, the danger is to generalise from cases that may not be conducive to such generalisations, due to unique, historical, social or political contexts (Collier & Collier, 1991: 14).⁴² A variant of this problem is to generalise from the best known case or cases. Generalisations of this nature all too often present a single picture, forming a composite that ultimately corresponds neither to the original case or cases on which the generalisations are based, nor to other cases to which is it applied (Collier & Collier, 1991: 14). As Collier & Collier (1991: 14) note, ‘what is too often missing is an analytic middle ground between splitters and lumpers that encompasses simultaneously a concern with similarities and differences.’ Such a middle ground ‘employs the systematic examination of similarities *and* contrasts among cases as a means of assessing hypotheses’ (Collier & Collier, 1991: 14).

If one is to occupy such a middle ground, then it is crucial to recognise the fact that any claim that two countries are similar or different, does not in fact, definitively ‘assign to them the overall status of being similar or different cases’ (Collier & Collier, 1991: 14). For example, Uruguay and Argentina are often heralded as being very similar countries in terms of political processes and dynamics, but in reality, Uruguay’s party system has more in common with Colombia than with its Southern Cone Neighbour. This does not mean that Uruguay has more in common with Colombia than Argentina or *vice versa*. Rather, it simply means that ‘it shares with each important similarities and differences,’ ensuring that a methodological stance that adopts such a middle ground ‘recognises the contribution of both splitters and lumpers, but insists on a flexible application of a middle position that

issue of whether or not causal or conditional explanations can be achieved by means of empirical corroboration. Thirdly, there is the issue whether or not comparisons are only meaningful by applying the longitudinal dimension and confining the relevant number of cases to be analysed.

⁴² Collier & Collier (1991:14) illustrate this by discussing Kenworthy’s (1973) article ‘The Function of the Little Known Case in Theory Formation or What Peronism Wasn’t.’

acknowledges a diversity of similarities and contrasts among any combination of cases' (Collier & Collier, 1991: 15).

Consequently, Collier & Collier (1991: 15) recommend a 'most similar *and* most different systems design.' This approach is a combination of the 'most similar systems design' (Przeworski & Teune, 1970) and the 'most different systems design.' A 'most similar' design is intended to reduce variation in the context to the barest possible minimum by means of selecting cases that are by and large identical, except for the relations between variables under review that represent the research question (Pennings *et al.* 2006: 35). The logic of the 'most different' design approach is to compare countries that have no common features except for the outcome that is to be explained (Landman, 2003). These two approaches are 'ideal types' and the reality is that the matching and contrasting of cases that they posit is never perfectly achieved in any real analysis (Collier & Collier, 1991: 15). However, a combination of these approaches, through a 'most similar and most different' design is more empirically realistic, allows for an analytical middle ground between the splitters and lumpers, and ensures that 'the context of analysis are analytically equivalent, at least to a significant degree' (Collier, 1997: 40), while their differences 'place parallel processes of change in sharp relief because they are operating in settings that are different in many respects' (Collier, 1997: 40). In effect, it recognises that the three case study states, Argentina, Brazil and Uruguay, share important similarities and differences. Causal inferences can be made by exploiting these similarities and differences when we attempt to explain the outcome. For these reasons, this project will employ the 'most similar and most different' design.

The Countries Selected for Examination

All of the above is contingent upon choosing appropriate case studies to answer the research question. For that purpose, three case studies are chosen: Brazil, Argentina and Uruguay. These three cases have been selected with the criteria of a 'most similar and most different' design in mind. Latin America is a particularly apt region to chose cases from, not only because it further extends the debate on the relationship between economic globalisation and the relevance of partisan politics to the developing world and challenges the long-standing focus of empirically investigating this debate through the lens of the advanced industrial democracies, but also because, in the last few years, the region has witnessed a broader trend 'in which political

parties, that can broadly be characterised as being from the left and the centre-left are in power, have been in power or have good chances of gaining power' (Panizza, 2005: 716-717). The relevance of left-wing governments in the current era of economic globalisation and their ability to implement policies that are congruent with their preferences is a particularly salient issue, not only in Latin America, but for the rest of the developing world also.

The overall analysis of these three states may be considered a 'most similar' systems design. The three cases, located in the Southern Cone in South America, are geographically contiguous. Choosing countries from the same area can lend itself to the comparative method because of the cluster of characteristics that areas tend to have in common and that can therefore, be used as controls (Lijphart, 1971: 688), thus ensuring that being geographically contiguous acts as a natural control. Heckscher (in Lijphart, 1971: 688) has stated that 'area studies are of the very essence of comparative government' as while 'the number of variables is still very large, it is at least reduced in the happy choice of area.' Cox and Macridis (in Lijphart, 1971: 688) have also noted that the area concept will be of great value, since certain political processes will be compared against units within the area against a common background of similarities. Furthermore, they point to Latin America as an area that is particularly amenable to comparative studies. However, choosing comparable cases from the same region is not without problems. Lijphart (1971: 688) cautions that comparability is not a quality that is inherent in a case study, but is rather a quality that is imparted by the observer's perspective. This is an important point to remember, and while choosing states from Latin America forms a natural control, the actual case selection must conform to the 'most similar and most different design.'

Among the countries of Latin America, these three have the longest history of urban, commercial and industrial development overall (Collier & Collier, 1991). All three were former colonies and have subsequently developed within similar regional and cultural contexts.⁴³ All three attempted some form of autonomous industrial

⁴³ Both Argentina and Uruguay were colonies of Spain; Brazil was a colony of Portugal. However their experiences of independence were quite different. Following the Napoleonic conquest of Europe, Argentina and Uruguay came to independence through the military exploits of José de San Martín (1812-1817) in the former and José Artigas (1819-1830) in the latter. During this period, the Portuguese Royal Court fled to Brazil in 1808 to escape Napoleon, and following elite resentment of the Portuguese crown, they placed Dom Pedro, the prince regent, on the Brazilian throne in 1823 as an independent monarch. See Burns (1993) for more detail.

development through Import Substitution Industrialisation (ISI) in the 1960s and 1970s and after all three endured periods of military rule, they turned to democratic systems of governance during the third wave of democratisation (see Huntington, 1991).⁴⁴ Furthermore, in the subsequent decade following democratisation, all three adopted liberalising reforms that were congruent with Neoliberalism.⁴⁵ Also, all three have similar levels of economic development in terms of Gross National Income (GNI) per capita.⁴⁶ Finally, all three have recently elected left-wing governments to power. Néstor Kirchner of the *Partido Justicialista* (PJ – Justicialist Party) was elected to power in Argentina in May 2003. Luiz Inácio Lula da Silva of the *Partido dos Trabalhadores* (PT – Workers Party), convincingly won the election in Brazil in October 2002, while for the first time in Uruguayan history, the left-wing candidate of the *Encuentro Progresista - Frente Amplio* (EP-FA – Progressive Encounter – Broad Front Party), Tabaré Vázquez, won the Presidential election in November 2004. All three ran on platforms promising to reverse the market-friendly policies of their predecessors, with specific reference to halting all ongoing privatisations.

It is important to note that this project is not choosing a control case, that is, a case study that has a right-wing government during the same period. The reasoning behind this choice is relatively simple. The research question has been designed to examine left-wing governments only, and as Pennings *et al.* (2006: 10) state:

The issue is to control for contextual or exogenous variation given the Research Question. For instance, if we wish to analyse the role of parties in government with regard to welfare statism, we could decide – on the basis of the research question – to restrict ourselves to a certain type of party or government.

In this respect, the research question of this project is focused on the ability of left-wing governments to implement policies congruent with their preferences. As such, three left-wing governments are chosen as case studies.

⁴⁴ For good general overviews of these periods see for example, Bulmer-Thomas (2003), Williamson (1992) or Bakewell (2004).

⁴⁵ Although all three countries attempted stabilization measures and some market reforms earlier (under Alfonsín in Argentina, Sarney and Collor in Brazil, and Lacalle in Uruguay), governments did not pursue market reforms in a concerted way until Menem's government in Argentina after 1989, Cardoso's in Brazil and Sanguinetti's and Batlle's in Uruguay.

⁴⁶ The Gross National Income (GNI) per capita (2005 est. Atlas Method) for Brazil is \$3,550, Uruguay \$4,360 and Argentina \$4,470 (World Bank Statistics Database, 2007).

The cases selected represent a ‘most different’ systems design on the basis that, as we shall see, they vary across two of the key independent variables, political institutions and labour support.⁴⁷ They have similar levels of economic globalisation and are susceptible to similar levels of influence by the international financial institutions. This project is primarily concerned with the effect of political institutions in mediating the effects of the convergence thesis, so this ensures that economic globalisation and the influence of the IFIs can be held constant, providing greater leverage over the explanatory power of both political institutions and left-labour power with respect to the convergence thesis.⁴⁸

Unpacking the Left in Latin America

It is important to outline what the thesis actually means when it refers to left-wing politics. By left-wing, in the context of the three case study countries, the thesis is specifically referring to those political parties with strong historical links to their respective national labour movements and that exhibit the central characteristics of traditional left-leaning politics, such as an advocacy of redistributive social policies and economic nationalism, combined with a discourse that is frequently critical of market mechanisms. The left in Latin America, while far from homogenous, is different in many respects from its contemporaries in other parts of the world. Much of the literature on economic globalisation and the resulting constraints facing modern partisan politics focuses nearly exclusively on the left in Western Europe or in the advanced industrial democracies (see Garrett, 1998). However, the left in Latin America, due to its unique historical trajectory and development, is not easily comparable to the left in other parts of the part. What is more, the left in Latin America generally has a different perspective as regards the role of the state, state enterprises and privatisation, in comparison to its contemporaries in Europe (see Eley, 2002; Castañeda: 1993).

Although the ‘left’ is perhaps best defined with reference to the right, there are a number of common themes, preferences and objectives that are identifiable among the broad spectrum that encompasses the Latin American left. According to

⁴⁷ See King, Keohane & Verba (1994: 137-138) for selecting cases on the basis of the explanatory variables. As they state: ‘The best intentional design selects observations to ensure variation in the explanatory variable (and any control variables) without regard to the values of the dependent variables’ (King, Keohane & Verba, 1994: 140).

⁴⁸ Discussed in greater detail in section 2.5

Castañeda (1993: 18), the left in Latin America traditionally has tended to stress national identity and sovereignty over economic integration (free trade, foreign investment etc.); social justice over economic performance (employment over efficiency, national control over strategic sectors of the economy over 'free enterprise' policies); income distribution over well-functioning markets; reducing inequalities over competitiveness; and social spending over controlling inflation. Although nearly two decades of structural reform and Neoliberalism has altered the reality in which the contemporary Latin American left operate, many of these themes, preferences and objectives continue to have resonance today (Clearly, 2006; Panizza, 2005). For Roberts (2007: 10), while the left today differs from its historical antecedents, the contemporary left takes 'a critical perspective towards the organisation of society in accordance with the principles of market individualism.' While the modern left in Latin America can also be defined by the practical acceptance of some of the principles of the neoliberal model, such as a sound fiscal policy, the importance of low inflation and the superiority of market mechanisms for setting prices, the central platform of the left remains increased state activity and ownership in the economy, and redistributive social policies designed to address the stark inequalities that exist in many Latin American societies (Panizza, 2005: 727; Roberts, 2007: 10).

In order to understand the unique relationship of the left in Latin America with economic nationalism and state ownership, we must trace the historical trajectory of the left's development. The Wall Street Crash of 1929 signalled the death of Latin American liberalism and the economic model of primary commodity exporting (see Cortés Conde, 1992; Bulmer-Thomas, 2003). The mix of ideologies competing to replace the vacuum left by liberalism began to coalesce around a number of key themes, including the need for state guidance and participation in the economy and the need to reclaim the natural resources of Latin America from 'foreigners.' Indeed, as Williamson (1992: 328) notes, 'ideologues of both right left advocated the break-up of the vast landed estates as well as the nationalisation of mining and petroleum companies.' The shock of the great depression heralded the rise of economic nationalism in Latin America, and inspired the substantial growth in the state's productive sector (see Evans, 1995; Thorp, 1992; Bulmer-Thomas, 2003). It was during this period of state growth that the ancestors of the contemporary Latin American left first began to develop. The old-school Communist parties first began

to emerge in the 1920s. They were a product of urbanisation and industrialisation that had begun to occur in many Latin American states and these groups had their roots in the nascent working classes and organised labour movements of the 1920s and 1930s (Castañeda: 1993: 19). The second group, the nationalist or popular left, were linked to the 'classic populist' leaders who began to emerge in Latin America in the 1930s and 1940s (Castañeda: 1993) and these populist leaders, such as Getúlio Vargas in Brazil, Lázaro Cárdenas in Mexico, José María Velasco Ibarra in Ecuador and Juan Domingo Perón in Argentina advocated a strident economic nationalism, and often created corporatist economic structures that indelibly linked national labour movements to their political vehicles and patronage (Evans, 1995; Thorp, 1992; Bulmer-Thomas, 2003). During this period of 'natural corporatism,' the number of state-owned enterprises began to grow rapidly and the state became the central dispenser of patronage (Williamson, 1992: 347). From the very beginning, economic nationalism, represented by the growth and importance of state enterprises, was intricately linked with the growth and development of the Latin American left (Castañeda: 1993).

The importance of the state for the left in Latin America was only heightened after the end of the Second World War, when 'industrialisation was incorporated into a comprehensive nationalist theory of Latin America's relations with the external world' (Williamson, 1992: 333). The theory, first developed by Raúl Prebisch, and propagated by the Economic Commission for Latin America and the Caribbean (ECLAC), stressed the developmental chasm between the industrialised nations of the world and the industrialising nations, by highlighting the significantly higher price for industrial products, compared to primary commodities, on the world market. As such, this would lead to an increasing gap in the balance of trade between industrialised states and those that relied on the export of primary commodities. Consequently, the primary commodity exporters were structurally dependent upon those few core industrialised states. The only method to rectify this situation: de-link yourself from the core and launch a programme of planned state industrialisation that would eliminate the need to import industrial products from abroad (see Prebisch, 1950; Cardoso & Faletto, 1973; Frank, 1969).

This theory served as the basis for the model of Import-Substitution-Industrialisation (ISI), adopted by most Latin American States in some form or other until the debt crisis of the 1980s, and which triggered the further explosion in the

growth of the state's productive sector (Evans, 1995; Thorp, 1992; Bulmer-Thomas, 2003). The left jumped upon Prebisch's theories and utilised them to reformulate Lenin's theory of imperialism. International trade was intrinsically imperialistic and the only way to escape this imperialistic international structure was to support the development of large state industrial sectors (Williamson, 1992: 354), an idea that informed not only the political-military left that developed after the success of the Cuban Revolution, but also the reformist left of the 1970s and 1980s, with its base in organised labour and its crucial role in the processes of democratisation throughout the region (Castañeda: 1993; Panizza, 2005; Angell, 1996). As a consequence of this historical trajectory, by the early 1980s, the size and role of the state in Latin America far outweighed the size of the state in nearly all other regions of the world. What is more, the centrality of the state in Latin American economies, and its development alongside the left in Latin America, has ensured that the left has a unique relationship and affinity with state enterprises that is not replicated by other leftist political parties in other parts of the world.

Even today, we can witness the importance of state enterprises for the contemporary Latin American left. Hugo Chávez in Venezuela, Evo Morales in Bolivia, Manuel López Obrador in Mexico, Fernando Lugo in Paraguay and Rafael Correa in Ecuador have all stressed the importance of the state in rectifying the failings of the market, and all have either advocated, supported, or overseen the nationalisation of key economic sectors (see Chavez, 2007). While the Latin American left, as the left has in other parts of the world, developed an awareness of the inefficiencies associated with many forms of state intervention and state ownership (Panizza, 2005: 727), the relationship of the left in Latin America with the state, and the role ascribed to state enterprises, still differs significantly from that of the left in Western Europe and other parts of the globe (see Anderson & Camiller, 1994; Eley, 2002).

However, this is not to suggest that the left in Latin America is homogenous. As stated earlier, there are common themes that can be identified among the 'new left' in the region, such as an emphasis on state involvement in the economy and an advocacy of redistributive programmes (Panizza, 2005: 727; Roberts, 2007: 10), but there are also significant differences among the left across the region. A number of scholars have highlighted a bifurcation among the 'new left,' between the radical populists and more conservative social democratic reformers (Castañeda, 2006;

Cardoso, 2006). Others have rejected this typology and instead have stressed the complexity and diversity of the 'new left' (Ramírez Gallegos, 2006; Schamis, 2006; Corrales, 2006), while others still have highlighted the division between those with access to commodity revenues, which are then used to fund ambitious redistributive programmes, and those with no access to such funds (Weyland, 2007). In reality, there are those that have their roots in indigenous movements, such as Evo Morales in Bolivia and Ollanta Humala in Peru; those who display elements of classic populism (no institutionalised political party, redistribution based on resource revenues) such as Hugo Chávez in Venezuela and Rafael Correa in Ecuador; those who stress the importance of addressing the inequalities in their respective states above all else, such as Manuel López Obrador in Mexico and Fernando Lugo in Paraguay; and finally those from traditional left-leaning political parties with strong historical links to the labour movement.

It is this last grouping that concerns this thesis. The *Frente Amplio* in Uruguay, the *Partido Trabalhadores* in Brazil and the *Frente para la Victoria* in Argentina can all be considered as traditional labour-based left-wing political parties. Although inevitably, there are differences among these three political parties, in the context of the wider 'new left' throughout the region, they do have a number of core similarities. All three are considered the main left-leaning party in their respective states and all three have strong historical links to labour. The PT emerged from a series of major strikes in the 1970s that undermined the military government and was widely seen as the only true ideological party in Brazil, with extensive links to 'new unionism,' and since its inception in 1983, the *Central Unica dos Trabalhadores* (CUT) (see Branford & Kucinski, 2005; Flynn, 2005; Ellner, 2004). The *Frente Amplio* emerged at the beginning of the 1970s as a coalition of communists, socialists and Christian democrats with strong links to the union movement, opposed to the authoritarian and conservative government of the time (see Lanzaro, 2004; Garcé & Yaffé, 2004; Yaffé, 2002). Although the FpV emanates from the Peronist party and while the PJ is considered heterogeneous in the ideological realm, spanning *Montonero* guerrillas to ultra-nationalists, to neoliberals under Menem (see Stokes, 2003), this project follows Levitsky's (2003) seminal study and treats the PJ as a labour based-party. The PJ has traditionally had very close and intricate links with the organised labour movement in Argentina; although this relationship was strained as a result of many of Menem's labour reforms in the

1990s (see Murillo, 2001). It is also argued that Kirchner adopted a distinctive left-wing strategy in comparison to other members of his party: *Duhaldistas* or *Menemistas*. He established movements within the PJ to promote his brand of leftism, firstly the *Corriente Peronista*, and subsequently his own parliamentary party, the *Frente Para la Victoria*.

The Time Period

The time period of the narrative under consideration incorporates the period after the election of the left-wing governments. Each case study will be preceded by a chapter charting privatisation policy after the return to democracy in each of the three states. Taking institutions as the main explanatory variable may lead to questions of endogeneity. However, as Spiller, Stein & Tommasi (2003: 7) argue, these problems can be overcome in historically grounded, country-specific research. So, the historical background chapter before each case study enables the narrative to process trace (see George & Bennett, 2005) the evolution of the political institutions in each state after the return to democracy. For the period after the election of the left-wing governments, the project is concerned with the first three years in power of these governments. Three years is a sufficiently long time for governments to implement their policy preferences.⁴⁹ Part of the value-added of this study is to assess the ability of left-wing governments to implement policy over short time frames. As Garrett and Lange (1991: 563) have commented, what is lacking in this debate are studies that ‘shed light on the effect that changes in government within individual countries over much shorter periods of time have had on economic strategies.’ There is also a public perception that a left-wing government would alter policies quicker, so accordingly, three years is a reasonable time frame.

2.3 The Methodology: An Analytic Narrative

In order to answer the research question and assess the impact of the independent variables, through three comparative qualitative case studies, this study will employ the analytic narrative approach. The motivation for employing an analytic narrative is rooted in the desire to combine elegant and parsimonious models of behaviour with rich empirical detail in order to generate transparent explanations of the process

⁴⁹ The time period chosen is also due to restrictions on the amount of data available. As these three leaders are relatively recently elected, it may prove difficult to access data post-three years in power.

under investigation. An analytic narrative is simply the combination of analytic tools with the narrative form. It is narrative in that it examines stories, contexts and accounts, while it is analytic in that it extracts ‘explicit and formal lines of reasoning, which facilitate both exposition and explanation (Bates *et al.* 1998: 10). The rationale behind the analytic narrative approach is to construct logically persuasive and empirically valid accounts that attempt to explain how and why events occurred. The application to history and narrative provides a rich empirical account that allows for process tracing and evaluation of the model (Bates *et al.* 1998: 13).

Obviously, analytic narratives are not the only means to provide structure to the case studies. A number of other excellent comparative methods exist that could also provide the project with structure and rigor, foremost among these, Charles Ragin’s (1987, 2000) Qualitative Comparative Analysis (QCA), and the more recent Fuzzy-Set Qualitative Comparative Analysis (fsQCA).⁵⁰ Both QCA and fsQCA were developed for the analysis of small and intermediate -N data sets (Rihoux & Ragin, 2004: 2). Originally intended as a middle ground between case-orientated research and variable-orientated research (Ragin, 1987: 168-169), QCA is an extension of John Stewart Mill’s methods of inductive inquiry: the methods of agreement and the method of difference (Ragin, 1987: 15; Mahoney, 2000: 394). The method, ultimately concerned with identifying the necessary and sufficient conditions that are linked to a particular outcome, is grounded in Boolean algebra, the algebra of sets (as opposed to linear algebra, the basis of regression analysis) and seeks to unravel causal complexity by applying set-theoretic methods to cross-case evidence (Ragin, 2005: 37; Rihoux & Ragin, 2004: 2). Set-theoretic relations concern explicit connections, as opposed to correlations, which address tendential connections (Ragin, 2000). The initial version of QCA required dichotomised variables, while the latter variant, fsQCA, allows for ‘fuzzy values’ between 1 and 0 that ‘describe the membership of a given case in the category formed by the variable’ (Schneider & Wagemann, 2006: 752), values that are assigned on the basis of theoretical knowledge and empirical evidence (Ragin, 2000: 150-170). The key tool for QCA is the truth table, which ‘lists the logically possible combinations of causal conditions (e.g. presence of presidential versus parliamentary form of government, presence/absence of party fractionalisation) and the outcome associated with each

⁵⁰ Other variants include Multi-Value Qualitative Comparative Analysis (MVQCA) (see Cronqvist, 2004).

combination (e.g. whether democracies with each combination of conditions consolidate)’ (Rihoux & Ragin, 2004: 5; Ragin, 1987: 85-102).⁵¹ Truth tables examine specific combinations of causal conditions across cases in order to determine if they share the same outcome, the ultimate goal of which is ‘to identify explicit connections between combinations of causal conditions and an outcome’ (Rihoux & Ragin, 2004: 6).⁵²

Both approaches have a number of advantages, and both are not without their critics. Carpenter (2000) critiques analytic narratives on the basis that there appears to be some confusion as to what narratives actually are, at least when they are not graced with formal models. For Carpenter (2000: 654), this confusion renders analytic narratives, at their most sophisticated, as ‘sequences of facts chronologically arranged.’ Jon Elster (2000) is even harsher in his critiques. He argues that analytic narratives fail to execute the programme that was proposed, that is, the application of formal theories to elucidate complex cases. Rather, they become guilty of the sin they are trying to avoid, becoming ‘just so stories.’ Bates *et al.* (2000: 700) recognise that this is a problem, but counter with the fact that all an analytic narrative can do is lay out the basis for the analytic decisions, and apply the criterion of falsifiability to the hypotheses. Elster (2000) also believes that the method suffers due to the lack of incorporation of independent evidence for intentions and beliefs. That is, how individuals construct understanding of their world. Again, Bates *et al.* (2000: 697) freely recognise this as a problem, but in their defence they argue that as yet, no model exists that can adequately capture the evidence for intentions and beliefs. Finally, Elster (2000) criticises the analytic narratives approach because of the attempt to generalise from small-N studies. This has always been a problem of social sciences (see King, Keohane & Verba, 1994), but for Bates *et al.* (2000: 702) the analytic narrative approach, if nothing else, at least attempts ‘to bring some analytical tools to the task of studying case studies, a question long of interest to political scientists.’

On the other hand, for Seawright (2005) and Achen (2005), QCA represents nothing that is necessarily methodologically new. Rather, for them, QCA is a repackaging of statistical methods that ultimately reduces to regression analysis. For

⁵¹ The number of causal combinations is a geometric function of the number of causal conditions (see Rihoux & Ragin, 2004: 6).

⁵² The truth table is reduced and simplified through a bottom-up process of paired comparison that parallels the minimisation of switching circuits (Ragin, 1987, 2000).

Achen (2005: 31), Ragin, by constructing a quantitative methodology that mimics case study logic, has asked ‘Why can’t a man be more like a woman?’ Seawright (2005: 10) further criticises QCA on the basis that all variables (conditions) of interest have only two values, and argues that even fuzzy set QCA fails to eliminate the necessity to dichotomise variables. Furthermore, in dichotomising variables, QCA requires assumptions that are no less problematic than assumptions required to make causal inferences in regression analysis (Seawright, 2005: 26). The necessity of assigning scores to variables in QCA also assumes that the analyst is able to measure all variables correctly. A change in the score of a variable could lead to a significant change in the understanding of that variables causal relevance. As such, QCA does not allow any notion of measurement error (Mahoney, 2000: 397). QCA has also been criticised for its inability to make any allowance for missing variables (Mahoney, 2000: 395; Seawright, 2005: 29), while other problems associated with QCA include the issue of complexity, and limited diversity associated with the low number of cases (Schneider & Wagemann, 2006: 756-757). If too many variables are introduced into QCA, the result may become overly complex, to such an extent that they become ‘impossible to interpret in a theoretically meaningful way’ (Schneider & Wagemann, 2006: 757).

Despite these problems, both approaches are very useful analytic tools for comparative studies and indeed both share a number of similarities, for example, their emphasis on repeated iteration between theory and data (see Ragin, 1987; Bates *et al.* 2000). However, this study can only utilize one of these methods. Notwithstanding the excellent strengths of QCA, in particular its ability to analyse complex causation (Ragin, 1987: 2000; Rihoux & Ragin, 2004) and its provision of an ‘explicit and systematic’ process for considering counterfactual cases (Rihoux & Ragin, 2004), a major weakness of analytic narratives (Carpenter, 2000: 658), this study will employ the analytic narrative approach.

The analytic narrative approach lends itself to this project for a number of reasons. Analytic narratives generally refer to rational choice theory and game-theoretic models in particular, but they can also be applied to other forms of theory, with a range of models serving ‘as the basis of analytic narratives,’ for example, ‘those derived from the new institutionalism’ (Bates *et al.* 1998: 3). Rational choice theory, and game theoretic models as Margaret Levi (2004: 202) notes, ‘is only one of the flavours of analytic narratives.’ For example, Ira Katznelson (1997) uses the

label to describe her approach to large-scale macro-historical questions, while for Skocpol and Somers (1980), their preferred method is labelled ‘macro-analytic comparative history.’ This is most similar to what Levi (2004: 203) describes as ‘causal narrative,’ a process by which the sequences and variables in an historical narrative are disaggregated in a way that allows cross-case comparisons. As an approach ‘analytic narrative is most attractive to scholars who seek to evaluate the strength of parsimonious causal mechanisms’ (Levi, 2004: 212), and it compels scholars to make causal statements and to identify a small number of variables. The model in this project and the variables within this model, are primarily drawn from new institutionalism (see Spiller, Stein & Tommasi, 2003; Mainwaring & Shugart, 1997),⁵³ and as such, analytic narratives provide a ready framework for such a model focused on political institutions. This makes the analytic narrative approach particularly suited to the structure of the current project.

As a corollary to the point regarding the compatibility of analytic narratives and new institutional models and therefore the suitability of this approach for the project, is the issue of causation. New institutionalism and analytic narratives are well-suited because they both share the same logic of causation. The main independent variables in this thesis are derived from new institutionalism, a variable-orientated approach that adopts a strategy of causal inference based on insights from quantitative work (Mahoney, 2000), a strategy some scholars have long encouraged for qualitative work (see King, Keohane & Verba, 1994). Analytic narratives also share this logic of causation, and they explicitly attempt to follow the statistical rules of causal inference (Levi, 2003: 8; Bates *et al.* 2000: 696; King, Keohane & Verba, 1994). However, the variable-orientated ordinal strategy of causal inference shared by new institutionalism and analytic narratives, differs from the logic of causation small-n researchers adopt when using nominal comparison (Mahoney, 2000: 406-407). QCA is a case-orientated method of nominal comparison that does not base its strategy of causal inference on statistical rules, but rather ‘seeks out patterns of causality in which the association between cause and effect is in certain respects fully predictable’ (Mahoney, 2000: 407). Indeed, Ragin himself (1987, 2005) cautions against employing quantitative causal inference as a basis for informing small-n research. In effect, Ragin employs case-orientated causal inference as the basis to

⁵³ See also Spiller, Stein & Tommasi (2003: 11) who suggest that the transactions framework, upon which the institutional variables here are partly based, ‘speaks’ to the AN project.

inform quantitative work (Achen, 2005: 31). This thesis is variable-orientated research inspired by new institutionalism. The analytic narrative approach is also variable-orientated and process driven (Bates *et al.* 1998), and is informed by the same logic of causation as new institutionalism. QCA however, is a case-orientated approach that is driven by a different logic of causation. As such, the compatibility of new institutional models, analytic narratives and the purpose of this study is one of the reasons why the analytical narrative approach was chosen ahead of QCA or fsQCA.

Furthermore, the institutional model that is developed in this thesis is concerned with capturing the impact of path dependence on policy outcome, specifically the institutional design of privatisation programmes in the case study countries in the early 1980s and 1990s. A major strategic advantage of analytic narratives is that they allow the researcher to deal with dynamic processes that have a temporal dimension, and allow for the consideration of time-sensitive concepts such as path dependence (Levi, 2003: 21; Parikh, 2000: 679). Narrative accounts are much more likely to capture these elements. In the literature on the relationship between economic globalisation and left-wing governments, cross-sectional approaches have been repeatedly employed (see Kaufman & Segura-Ubiergo, 2001; Wibbels & Arce, 2003; Scruggs & Lyle, 2004). These studies have attempted to assess the effect of different institutions by means of this approach, but, for Parikh (2000: 679), ‘cross-sectional approaches...are unable to deal with the sequence of decisions and events that must be analysed in order to explain the outcomes under investigation.’ Specifically, these approaches may fail to grasp dynamic processes, or time-sensitive concepts such as path dependence. Even many small-n comparative approaches cannot account for path dependence. For example, QCA is unable to incorporate a temporal or path dependent dimension into its models (Schneider & Wagemann, 2006: 753).⁵⁴ It is the ability of analytic narratives to incorporate such a temporal dimension that further lends this method to the current project.

Finally, analytic narratives are well-suited for (very) small-N studies (Bates *et al.* 1998, 2000) and as this project adopts only three case studies, this further supports the suitability of analytic narratives as a method for this project. Although QCA is often cited as a small-N method, it is perhaps best suited for intermediate-N

⁵⁴ Although recently, some scholars have attempted to add a temporal dimension to QCA. See Caren & Panofsky (2005).

research designs. Initially, QCA was designed as a means to ‘address large number of cases without forsaking complexity, (Ragin, 1987: 171) and of its more than 250 applications, only one QCA study employs an N as small as five cases, and in fact only 6 per cent of all contemporary QCA applications employ 10 cases or less. The vast majority of applications employ between 10 and 80 cases (see Rihoux & Ragin, 2004: 7). Indeed, for Schneider & Wagemann (2006: 775) QCA techniques are ‘one appropriate methodological tool for assessing complex causal theories – especially in mid-size N designs.’

Despite the weaknesses and problems associated with analytic narratives, this method was chosen for this thesis. It is quite reasonable to assert that other methods could structure this project just as efficiently, but this thesis can only choose one method to guide the comparative approach adopted here and, for the reasons outlined above, the analytic narrative approach was selected.

In order to provide substance for the narrative, the research drew from a number of primary and secondary sources, including books, regional, local and international newspapers, government reports, government decrees, resolutions and laws, union and employer organisation reports and data archives, industry reports, central bank reports, letters of intent signed with international financial institutions, economic and political datasets and political party websites, manifestos, speeches and pamphlets. Much of the core research for the narrative was collected during field research in Montevideo, Buenos Aires and São Paulo between June and September, 2006. In Argentina, all data concerning laws, decrees and resolutions was drawn from information provided by the *Dirección Información Parlamentaria* (DIP) of the Argentine Chamber of Deputies in Buenos Aires. The offices of the *Frente para la Victoria* (FpV) in Buenos Aires also provided copies of manifestos and election materials, while archival research was conducted at the offices of *La Nación* and The Buenos Aires Herald. In São Paulo, the office of the *Partido dos Trabalhadores* provided access to party manifestos and materials from the 2002 election. In Uruguay, information concerning all government laws, decrees and resolutions was provided by the *Información Parlamentaria* of the Uruguayan Chamber of Deputies in Montevideo, supplemented by the electronic *Sistema Información Parlamentaria* database. Statistics and a number of reports were utilised from the Central Bank in Montevideo while archival research, both at their offices and at the Universidad de la República, was conducted for *El Observador*, *Busqueda*, and *Crónicas*. The offices

of the *Frente Amplio* in Montevideo provided all relevant election manifestos and campaign materials. In addition, in order to supplement patchy or scarce data and for useful background information, interviews were conducted with political scientists from the region, in particular from the Universidad de la República in Montevideo and the Universidad del CEMA in Buenos Aires. Where such information is utilised in the narrative, details of the scholar in question is provided.

2.4 The Dependent Variable: Privatisation Policy

Where capital is completely mobile and where states remove their trade and capital restrictions, monetary policy is severely curtailed. Governments are left with a choice between the money supply or the interest rate, and where currencies are fixed or pegged; the restrictions are magnified (see Garrett, 1998b; Berger, 2000; Philips, 2005).⁵⁵ However, the effects of increasing economic globalisation are thought to be far more pervasive than just monetary policy. The loss of monetary policy autonomy places pressures on fiscal policy also and this in turn, will have a restraining effect on other policy areas, precipitating ‘a race to the bottom’ in industrial policy, welfare spending, taxation, labour market reform, privatisation, environmental regulations etc. So far however, the literature has primarily focused on two specific policy areas: taxation and social welfare spending, and even within these policy areas there still remains disagreement as to the effect of economic globalisation and the role of other explanatory variables (see chapter one).⁵⁶

In an effort to move beyond the policy areas of social welfare and taxation reform, one of the motivations of this study is to extend the analysis of economic globalisation and the efficacy of left-wing governments to other policy areas. This study differs from previous empirical works in this literature by choosing privatisation policy as the dependent variable. According to the logic of the convergence thesis, the constraining effects of economic globalisation should extend to a variety of policy areas (Cerny, 1996), and privatisation policy should be no exception. We have a clear set of expectations regarding the relationship between privatisation and globalised markets. Increasing trade competition and the multinationalisation of production place downward pressures on the size of the

⁵⁵ The Mundell-Flemming theorem, see Mundell (1963).

⁵⁶ Although there have been some interesting variants. Prakash & Potoski (2006) examined the effect of economic globalisation on environmental regulations, Bailey, Rom & Taylor (2004) on education, Rodrik (1996) on labour standards and Prakash & Kollman (2003) on genetically modified organisms.

public economy and this leads to the privatisation of state assets (Garrett, 1998b: 791-792). Big government stifles private investment and prevents wages and prices from reaching market generated equilibriums. Government spending must be funded by increased taxes, which not only discourages private investment, but also, due to the multinationalisation of production, provides mobile asset holders with an incentive to exit the national economy and move to a more tax-favourable location. Likewise, government borrowing to fund this increased spending increases interest rates, depressing entrepreneurial activity and eventually causing output and employment to suffer (Garrett, 1998b). If governments wish to be competitive in terms of trade, and continue to attract mobile asset holders, they must roll-back the public economy, and privatisation is a key element in this process.⁵⁷

Privatisation can also be a particularly effective means for developing world countries, with little else to offer investors, to attract mobile asset holders and remain competitive in the international market. Mobile asset holders will be attracted by the sometimes below market-value sale of potentially lucrative state companies, often in near monopolistic market conditions. Developing world governments can use the proceeds to invest in infrastructure, further enhancing their attractiveness to mobile assets, or to pay off existing debts, signalling economic stability and orthodoxy. The proceeds of large-scale privatisations reduce the need for government borrowing, removing upward pressures on interest rates. Conversely, and following the same logic, nationalisations will simply prove impossible. Capital and mobile asset holders will not invest in states where they fear expropriation.⁵⁸ If nationalisation is a credible threat, capital will simply go elsewhere. So, there will be pressure on all governments, regardless of their political orientation, to privatise in order to remain competitive in terms of trade and the attraction of mobile asset holders. Nationalisation should prove out of the question. This however, has never been empirically tested, hence the motivation for using privatisation policy as the dependent variable in this study.

⁵⁷ Furthermore, the policy paradigm that the first wave advocates all governments are converging upon, could be described as Neoliberalism, although even this term is subject to heated debate (see Boas and Gans-Morse, 2006 for a good review of this issue). The blueprint for neoliberal reforms has been embodied in a ten point structural reform package commonly referred to as the Washington Consensus (Williamson, 1993). Of those ten points, one bluntly states: 'State enterprises should be privatised' (Williamson, 1993: 1333).

⁵⁸ Exceptions to this will probably be in high-earning commodity extraction industries, e.g. oil.

Specifically then, this project is concerned with the degree of change in privatisation policy after the election of left-wing governments in the case study countries selected. Partisan theory assumes that governments have the ability to implement their promises (Hibbs, 1992), but the globalisation thesis argues that this is no longer the case. If privatisation policy has changed according to the preferences of the left-wing government elected, then this would suggest that partisan politics still matter. If however, we find that the left-wing governments were unable to implement policy in this area congruent with their preferences it would suggest that partisan politics is no longer as relevant as traditionally believed. According to the prescriptions of the partisan thesis, left-wing governments should be expected to stop all on-going privatisations and refrain from initiating any further privatisations in all areas, or key strategic sectors (see Levy, 2001). In certain cases, though not always, they may even renationalise previously divested state enterprises. This dependent variable and the observations selected to operationalise this variable, follow the rules of King, Keohane and Verba (1994: 108).⁵⁹

In order to operationalise this variable and correctly identify the degree of change in the dependent variable, if any, there are two distinct areas to examine. The first is the levels of privatisation within the economy. This can be observed simply through the number of state-owned enterprises that have been privatised, or alternatively re-nationalised, if that is the case, and through the overall proceeds from privatisation, as a gross figure and as a percentage of Gross Domestic Product (GDP).⁶⁰ It is important to disaggregate between the two measures, as the simple count of privatisations may hide the fact that large-scale state enterprises have been sold, whereas the revenue figures will capture the scale of state divestiture.

Throughout this thesis, the operationalised dependent variable is often referred to as the policy outcome. By policy outcome, the thesis simply means the observable final policy that was implemented by government x in time t . Obviously, the design and ultimate implementation of a policy may differ significantly from the initial preferences of a particular administration, mainly as the result of a number of variables (in this instance, political institutions), that will constrain and channel these

⁵⁹ These three rules are as follows: The dependent variable should be dependent, thus removing the danger of endogeneity, the selected observations based on the dependent variable should ensure that it does not remain constant, and finally the dependent variable should represent the variation we wish to explain (see King, Keohane & Verba, 1994: 108-109).

⁶⁰ This data is readily available from the World Bank Privatisations Database, the IMF and from individual national accounts at the respective finance ministries.

preferences. Therefore, we can observe the initial *desired* policy outcome of a government (preferences), and *actual* final policy outcome (dependent variable). So, in terms of government spending, government *x* may wish to spend a specific amount on education in a specific year, but because of budgetary constraints etc., will actually only spend 75 per cent of that amount in that year. This is the policy outcome. In this case, the level of privatisations or nationalisations implemented during the first three years of each administration is the policy outcome we wish to observe. Clearly then, we should also expect different policy outcomes depending upon the partisanship of the government in power. As discussed above, the left in Latin America are concerned with redistributive social spending, progressive taxation and interventionist economic management. Specific policy outcomes such as these could generally be described as partisan supply-side policies. But as the literature has emphasised, there are numerous other factors that impede partisan governments from achieving their desired outcome. Therefore, it is necessary to establish what the policy outcome actually was.

Likewise, when it comes to privatisation, there are specific partisan-supply side policies that we would expect from left and right governments, but we need to establish exactly what these are. Privatisations may occur in various forms that do not necessarily imply a reduction in the size or responsibilities of the state, 'since privatisation may only change the form of government intervention concerning service provision, regulation and financing' (Zohlnhöffer *et al.* 2008: 97; Levi-Faur, 2005). Privatisations have many different facets: formal privatisation, re-privatisation, public-private partnership, public-private enterprise etc. Formal privatisations refer to the complete or partial sale of a state enterprise. Re-privatisation refers to the re-sale of a company that the state had already sold, but was forced to take over due to financial difficulties, while a public-private partnership, also called a functional privatisation, refers to a public service or business that is operated jointly by a state enterprise and one or more private enterprises. Alternatively, a new company, a public-private enterprise, where the state and private investors have joint ownership, may be established to operate a public service. A public-private enterprise may also be established by the partial sale, e.g. 40 per cent, of a state enterprise (see World Bank, 1993; Zohlnhöffer *et al.* 2008: 97).

At the simplest level, right-wing parties can be expected to privatise all state enterprises while left-leaning parties can be expected to oppose all formal privatisations. These parties will face a major electoral incentive to do so because workers in state enterprises and public sector unions, who stand to lose most from privatisation, are a crucial constituency for the left (Zohlnhöffer *et al.* 2008: 102). At the opposite end of the spectrum lies nationalisation. Nationalisation was central to the left's economic strategy in Latin America after the failure of liberalism in 1929 (see Evans, 1995; Thorp, 1992; Bulmer-Thomas, 2003), and due to the unique relationship that the left in Latin America has developed with the state (see above), parties of the left in the region might be expected to attempt to regain control of strategic sectors. However, given the realities of the modern international political economy, and the necessity of all states to attract capital and foreign investment, nationalisation may be considered an extreme policy outcome in the context of the contemporary left. So, we have a continuum of a sort, with formal privatisations representing the most undesired outcome, and nationalisations at the other end of the spectrum representing the most desired, if not the most realistic, outcome. Within this continuum lie public-private partnerships, public-private enterprises and re-privatisations.

As stated above, the realities of the international political economy require states to attract much-needed foreign investment. Facing such pressures, the left, rather than endorsing formal privatisations but without the necessary funds, may be expected to resort to public-private partnerships or the establishment of public-private enterprises for the provision of certain public services or the building of infrastructure (see Levy, 2001: 273).⁶¹ As regards re-privatisation, it may be expected that no government will oppose this, simply because re-privatisation merely divests the state of a financially burdensome company that the state was forced to administer. Also, the focus of government policy on this issue is important. It is necessary to identify the sectors that receive attention in any privatisation programmes such as infrastructure, public utilities or pension fund reform.⁶² Left-wing governments may be expected to be more concerned with ensuring that key

⁶¹ See Levy (2001) for a discussion on the 'left-wing twist' that may be given to privatisation policy, differentiating policy from the market-friendly convergence type and constituting a genuinely different partisan policy.

⁶² This data is readily available through government pronouncements, policy documents, presidential decrees and bills introduced to the legislature.

sectors of the economy remain in state hands, including public utilities such as electricity, water or sanitation, vital resources such as oil and gas, and public transport, health services and social security and pension transfers. Certain infrastructure, banking and some industrial sectors may be of less concern to left-wing governments (see Levy, 2001: 273-274).

The measures chosen therefore, to operationalise the dependent variable are clearly observable, thus ensuring empirical verification or falsification. This ensures that the dependent variable maximises concreteness (King, Keohane & Verba, 1994: 109).⁶³

2.5 The Independent Variables

From the literature on economic globalisation and partisan politics, it is possible to identify four main explanatory variables that have been employed to examine the mechanisms by which left-wing governments may successfully implement their preferences. These four variables are: economic globalisation, political institutions, left-labour power, and the influence of the international financial institutions.

Economic Globalisation

In the era of Keynesian-policies post World War II, with capital controls and trade barriers, governments were able to use interest rates, the supply of money and exchange rates as a means to impose control upon their economies (Berger, 2000: 53). As the international environment has changed, and as barriers to trade and capital have diminished, the ability of governments to introduce autonomous policies has been curtailed. Under fixed exchange rates, increases in capital mobility essentially vitiate an independent monetary policy (Garrett, 1998b). Likewise, floating exchange rates under complete capital mobility may reduce the efficacy of fiscal policy (Milner & Keohane, 1996: 17). So, the central tenet of the globalisation thesis contends that the increasing mobility of capital and openness of international trade severely curtails, if not eliminates, the ability of left-wing governments to implement their preferences. Increasing trade competition forces the removal of the state from the economy, while the increasing mobility of capital acts as a disciplinary force on government policy, leading to a policy convergence along lines that

⁶³ Concreteness refers to choosing observable concepts that can be readily identified and thus subjected to empirical verification or falsification (King, Keohane & Verba, 1994: 109-111).

internalise the preferences of this capital. This policy mix is congruent with the preferences of the political right, rather than the politics of the left. If left-leaning governments do not adopt this mix, they will face a potentially ruinous capital flight. So, left-wing governments would now appear to have little ability to implement their preferences (see for example Ohmae, 1996; Przeworski and Wallerstein, 1998; Ruggie, 1997). Although the impacts of economic globalisation are contested it is reasonable to hypothesise therefore that *economic globalisation will undermine the ability of left-wing governments to implement autonomous privatisation policies. A left-wing government in a state that is highly exposed to economic globalisation will have less ability to implement autonomous privatisation policies, than a left-wing government in a state that is not so highly exposed to economic globalisation.*

In order to provide conceptual clarity for the operationalisation of this variable, it is worth following Milner & Keohane's (1996: 4) definition of economic globalisation as 'the processes generated by underlying shifts in transaction costs that produce observable flows of goods, services and capital.' However, while studies in the welfare compensation-efficiency debate have repeatedly found evidence that trade openness affects welfare spending, a number of these studies have also indicated that capital mobility has a smaller, if not negligible, effect on spending (see Avelino, Hunter & Brown, 2005; Rudra, 2002). Despite this, Kaufman & Segura-Ubiergo (2001) appeared to find evidence that capital account liberalisation did compound the effects of trade openness on welfare spending; while Wibbels & Arce (2003) found that trade openness, in contrast to portfolio capital, FDI flows and capital controls, appeared to have no discernable effect on the capital tax ratio.

Logically, we would expect privatisation to respond to a multifaceted conception of economic globalisation: trade openness, capital flows, and FDI flows. Increasing trade competition and the multinationalisation of production will place downward pressures on the size of the public economy, while the increasing mobility of capital will encourage developing world states to privatise state assets in an effort to attract this capital. So, in order to operationalise this variable, three composite indices of globalisation are utilised. These three indices all incorporate measures of trade openness, capital controls, FDI flows and capital flows, among others. Three different measures from the KOF Index of Globalisation are employed.⁶⁴ The first,

⁶⁴ Available at <http://globalization.kof.ethz.ch/>

‘Economic Globalisation,’ is a composite measure of actual flows and restrictions on trade and capital.⁶⁵ The second, ‘Actual Flows,’ is comprised of a composite measure combining trade openness, FDI as stocks, FDI flows and portfolio capital. The third and final KOF measure, ‘Globalisation Index,’ is simply the overall value capturing the level of exposure of the three states to globalisation.⁶⁶ In order to provide accessible, comparable figures for the three states during the period under analysis, the yearly values (2002-2005) for each of the three measures above are averaged (see Table 2.1).

Two measures from the AT Kearney/Foreign Policy Index of Globalisation are employed.⁶⁷ The first, ‘Economic Globalisation,’ again is a normalised composite measure capturing each state’s trade openness (imports plus exports as a percentage of GDP) combined with FDI flows (inward plus outward FDI as a percentage of GDP).⁶⁸ The second measure, ‘trade integration,’ captures trade openness only. Again, the yearly values (2003-2007) for both measures are averaged in order to provide a reasonable composite measure capturing each state’s exposure to economic globalisation during the period in question. The last measure is taken from the Heritage Foundation’s Index of Economic Freedom.⁶⁹ This is simply the overall ranking of each of the three case study states, based on their composite score of economic freedom, from a global sample of 157 countries.⁷⁰ Again, the yearly rankings (2002-2007) for the three states are averaged.

Table 2.1 below, outlines all the measures utilised to assess the level of economic globalisation across the case study states. These different indices provide a composite measure for economic globalisation for the three states. They also clearly indicate that there is little substantial meaningful difference between the case study countries as regards their exposure to economic globalisation, during the period

⁶⁵ This measure includes: trade (as a percentage of GDP), FDI flows (as a percentage of GDP), FDI stocks (as a percentage of GDP), portfolio investment (as a percentage of GDP), income payments to foreign nationals (as a percentage of GDP), hidden import barriers, mean tariff rate, taxes on international trade and capital account restrictions.

⁶⁶ Again this is a composite measure, combining the composite scores for ‘Economic Globalisation,’ ‘Social Globalisation’ and ‘Political Globalisation.’

⁶⁷ Available at <http://www.atkearney.com/main.taf?p=5,4,1,116>

⁶⁸ For a critique of the methodology utilised to construct this index, see Lockwood (2004).

⁶⁹ Available at <http://www.heritage.org/research/features/index/index.cfm>

⁷⁰ This composite ranking of economic freedom is arrived at by combining scores on business freedom, trade freedom, fiscal freedom, government size, monetary freedom, investment freedom, financial freedom, property rights, freedom from corruption and labour freedom. For more information on the methodology employed, see http://www.heritage.org/research/features/index/chapters/pdf/Index2008_Chap4.pdf.

before and after the election of these left-wing governments.⁷¹ The measures listed below represent the most popular and common measures of globalisation that are utilised in the literature. Therefore, the project will treat this independent variable as constant across the case studies. This has the advantage of providing added analytical leverage for the project to disentangle the effect of political institutions in mediating the convergence thesis.

However, there is a caveat. In everyday reality, the pressures of exogenous forces (globalisation, the IMF, bond rating agencies etc.) are not necessarily constant at all times, across Argentina, Brazil and Uruguay. In fact, it is inevitable that there would be some variation in globalisation between Brazil, one of the largest economies in the world, and a small, open, trade-dependent economy such as Uruguay. So, although from a methodological perspective, this project will treat economic globalisation as a constant across the cases, in order to better reflect reality, throughout the three case studies, the narrative will keep globalisation in view at critical moments in order to assess how various exogenous forces in each state impact on policy.

Table 2.1: Exposure to Economic Globalisation

	KOF Index of Globalisation			Foreign Policy/Kearney Index of Globalisation		Economic Freedom Index – Overall Ranking (Avg. 2002-07)
	Economic Index Overall (Avg. 2002-05)	Actual Flows Index (Avg. 2002-05)	Globalisation Index Overall (Avg. 2002-05)	Economic Globalisation Measurement (Avg. 2003-07)	Trade Integration Measurement (Avg. 2003-07)	
Argentina	57.0	69.3	63.2	50.2	55.8	56.4
Brazil	61.0	63.8	58.2	51.6	61.8	60.9
Uruguay	64.7	66.4	60.2	---	---	67.9

Source: KOF Index of Globalisation, AT Kearney/Foreign Policy Index of Globalisation/Index of Economic Freedom

Political Institutions

Ever more frequently, the focus has turned towards political institutions in efforts to explain the mechanisms by which left-wing politics may resist the effects of

⁷¹ To put these figures into context, Chile, for example, has an overall economic freedom index ranking (avg. 2002-07) of 78.0 and Venezuela (avg. 2002-07) 49.9. Chile's FP/Kearney Economic globalisation measurement (avg. 2003-07) is 19.2, Costa Rica, 32 and Panama, 4.6. Chile's Trade integration measurement (avg. 2003-07) is 35, while Costa Rica's is 20 and Panama's 8.2. The KOF Economic Index (avg. 2002-05) for Chile is 83.14, 76.52 for Panama and 48.98 for Guatemala. The KOF Actual Flows Index (avg. 2002-05) is 84.18 for Chile, 90.29 for Panama and 39.9 for Guatemala.

convergence. It was Garret & Lange (1991) and later Garrett (1998a), who first proposed the importance of labour market institutions in enabling left-wing governments to successfully implement their preferences. Cross-country econometric studies have found evidence that institutional variables impact upon the effects of convergence, although the variables utilised have tended to be very general, such as democracy (see Avelino, Brown & Hunter, 2005), or very narrow, such as party system fractionalisation (see Wibbels & Arce, 2003). Swank (1998b, 2002) has emphasised the importance of institutions in providing opportunities, to those opposed to or materially harmed by the policies associated with convergence, access to decision-making structures, while Pierson (1996, 2004) and Campbell (2004) have both argued that the effect of economic globalisation has been mediated and nullified by the policy design and path dependence of existing institutions. Even some of those who have found evidence of policy convergence (see Milner and Keohane, 1996; Scharpf and Schmidt, 2000) caution that their results may not be as conclusive as they seem, and stress the importance of taking into account institutions, and the varied impact these institutions may have on national reactions to economic globalisation. So, it is therefore plausible to expect *that political institutions will mediate the effects of economic globalisation and policy responses accordingly. The configuration of these institutions will either constrain left-wing governments in the pursuit of their preferences or will provide them with an opportunity to pursue their preferences.*

In operationalising the institutional variable, the project borrows from the ‘inter-temporal transactions framework,’ which analyses the manner in which political institutions affect policy outcomes, developed by Spiller, Stein & Tommasi (2003) and Spiller & Tommasi (2003). This framework argues that ‘institutions do not affect outcomes directly, but rather through their impact on the process by which policies are designed, approved and implemented’ (Spiller, Stein & Tommasi, 2003: 3). The study is designed to search for the *effects* of political institutions (explanatory variable) on a particular outcome (forward looking hypothesis), in this case privatisation policy (dependent variable). In doing so, hypotheses can be formulated to control the length of the chain of causation, ensuring that ‘interaction effects from other variables are less of a problem’ (Spiller, Stein & Tommasi, 2003: 11). In arguing that the institutions in place in each country determine the policy-making process, questions of endogeneity may arise. However, as Spiller, Stein & Tommasi

(2003: 7) argue, the questions of what to explain and what to take for a given, although providing a problem for ‘econometric work, are easier to answer in historically grounded, country-specific, research.’ As such, each analytical narrative will be preceded by a historical chapter that process traces the development of privatisation policy in each case study country (see George & Bennett, 2005). Four particular institutional variables, within which the policy-making process of privatisation occurs within each case study state, must be examined:

- Executive Power
- Legislative Support
- Judicial Independence
- Policy Delegation

As each case study country boasts a presidential political system and as the project is concerned with the ability of left-wing governments to implement their preferences, the logical starting point for operationalising the institutional variable is executive power. Executive power simply refers to a strong or a weak president, that is, the President’s ability to ‘put their own stamp on policy’ and implement their preferences (Shugart & Mainwaring, 1997: 40). This particular variable refers to the ‘constitutional powers’ available to the President, the extent of which ‘allows presidents to shape the policy output of the system regardless of whether they head a party or bloc of parties that controls a legislative majority’ (Shugart & Mainwaring, 1997: 13). Shugart & Mainwaring (1997: 41) divide the President’s constitutional power into *proactive* and *reactive* powers. Proactive powers allow the president to establish a new status quo and are best embodied by decree power. Reactive powers on the other hand, allow the president to defend the status quo or prevent the legislature from establishing a new status quo. Reactive powers are embodied by the full and partial veto and the power of exclusive legislative introduction (Shugart & Mainwaring, 1997: 41-48). The particular combination of proactive and reactive powers available to the president will determine the extent of his/her constitutional power and consequently the degree to which the president can implement his/her preferences.

However, regardless of the extent of a president’s constitutional powers, the ability of the president to implement his/her preferences is also predicated upon the extent and unity of the president’s support in the legislature (Cox & Morgenstern,

2002: 453; Foweraker, 1998: 658-659), what Shugart & Mainwaring (1997: 13) term the president's 'partisan powers.' Latin American legislatures are largely reactive bodies, but they are still important in the policy-making process (Cox & Morgenstern, 2002: 446).⁷² A president may have extensive constitutional powers, 'yet be stymied in effecting real change by a legislature in which his or her own party either holds a small minority of seats or, although holding a majority or large plurality, is deeply factionalised and undisciplined' (Mainwaring & Shugart, 1997: 395). So, the greater the unity (discipline) and cohesiveness (single party majority, multi-party coalition, minority etc.) of the president's support in the legislature, the greater the ability of the president to implement his/her preferences (Foweraker, 1998: 657-659).⁷³ This legislative support is dependent upon two variables: party system fragmentation and the level of party discipline, which in turn, are determined by specific institutional configurations (Mainwaring & Shugart, 1997). In a highly-fragmented multi-party system, no party will hold a majority and so typically the president will be forced to forge unreliable governing coalitions. Conversely, a low number of parties will enable the president's party to hold a majority or sizable legislative contingent increasing the cohesiveness of the president's legislative support. In turn, the degree of party system fragmentation is primarily a result of the electoral rules within a state (Mainwaring & Shugart, 1997). The degree of party discipline affects the extent to which presidents can rely on their party's support for their initiatives or alternatively the extent to which the president must secure support from other parties or individual legislators (Mainwaring & Shugart, 1997: 418). So, the higher the level of party discipline, the greater the unity of the president's legislative support. In turn, party discipline is primarily determined by three features of the electoral system: the control over candidate nomination for election; control over the order of this nomination; and the possibility of accumulating votes among a party's candidates (see Shugart & Carey, 1992: 174-178). The cumulative levels of party fragmentation and party discipline will determine the level of presidential

⁷² See Cox & Morgenstern (2002) who argue that Presidents adopt a particular strategy depending upon their support in the legislature.

⁷³ For a comprehensive discussion outlining the importance of unified legislative support for the executive in presidential systems and how multi-partism and party discipline impact on this support, see Foweraker (1998: 657-659).

legislative support, the level of which will in turn determine the president's ability to implement his or her preferences.⁷⁴

The judiciary, particularly with respect to privatisation, can play an important role in the policy-making process, either as an 'impartial referee' enforcing political transactions by binding politicians to past agreements, or as a 'policy player' through its reactive measures (veto) or proactive rulings (Scartascini, 2007: 30-31). However, the extent to which the judiciary is an important veto player in the context of executive preferences is dependent upon the degree of judicial independence (Spiller, Stein & Tommasi, 2003: 24; Scartascini, 2007: 30; Feld & Voigt, 2003: 498).⁷⁵ An independent judiciary forces the executive to take into account their preferences when making policy, rendering it very difficult for the executive to radically change existing policies, e.g., nationalising previously privatised state-owned firms. Alternatively, 'if the judiciary responds to one of the other branches of government (executive in this case), then its actions would merely mimic the actions of that branch of government' (Scartascini, 2007: 30), enhancing the ability of the executive to implement their preferences (particularly with regard to privatisation).

The last institutional variable concerns policy delegation. Delegating policy to an independent bureaucracy, or implementing policy within an institutional and legal framework can create path dependent effects and 'prevent future opportunistic behaviour' (Spiller, Stein & Tommasi, 2003: 20). In the case of privatisation, delegating responsibility for this policy to an independent body can fortify a government's commitment to the policy and prevent subsequent administrations from halting or significantly altering the policy (Scartascini, 2007: 39). Likewise, if privatisation occurs within an institutional and legal framework, this again increases the costs of halting this policy for subsequent administrations and renders nationalisation (particularly if the judiciary is independent) very difficult. So, when privatisation has been delegated to an independent autonomous body and when this has happened within the context of an institutional and legal framework, we would expect left-wing governments to have less ability to implement their preferences as regards this policy once in power and *vice versa*.

⁷⁴ The unity and cohesiveness of this legislative support can also be affected by federalism (particularly the federal governors). See Morgenstern (2002) and Scartascini (2007).

⁷⁵ The characteristics of judicial independence include: budgetary autonomy, transparency of nomination process for the bench; stability and tenure of judges; and extent of judicial power (see Scartascini, 2007: 30).

The degree of executive power, party system fragmentation, judicial independence and policy delegation will ensure that left-wing governments in the chosen case study countries will either have high capacity to implement their preferences or low capacity to implement their preferences.

There is significant variation in terms of these institutional variables across the three chosen case study states. As we are interested in searching for the *effects* of these explanatory variables (forward-looking hypothesis), it is this variation that allows us to hypothesise on expected outcomes. For example, Table 2.2 below indicates the varying levels of presidential legislative power across the case studies. As can be clearly seen from this table, the proactive and reactive powers of the President of Argentina are extremely high, while the proactive powers of the President of Brazil are high, but the reactive powers are, in general, rather low. As Shugart and Mainwaring (1997: 48-50) argue however, proactive powers are, in conventional terms, more important than reactive power, and so the overall legislative power of the Brazilian President remains high. The high level of reactive power and low level of proactive power of the Uruguayan President renders the executive with a medium level of overall legislative power in Uruguay.

Table 2.2: Legislative Powers of Presidents

	Proactive Powers	Reactive Powers			Level of Presidential Legislative Power
	<i>Decree Power</i>	<i>Package Veto Power</i>	<i>Partial Veto Power</i>	<i>Exclusive Initiative</i>	
Argentina	High	V. High	V. High	No	V. High (1)
Brazil	High	Low	Low	Yes	High (2)
Uruguay	V. Low	High	High	Yes	Medium (3)

Source: Shugart & Mainwaring (1997) and IADB (2006)

As can be seen from Table 2.3, Brazil's open-list, proportional representation system combined with the '*candidato nato*' obligation, has resulted in high levels of party fragmentation and low levels of party discipline (see Mainwaring and Shugart, 1997; Morgenstern, 2000; Ames, 2002).⁷⁶ On the other hand, Uruguay's double simultaneous vote and closed-list proportional representation system has prevented the emergence of a multi-party system and engenders high levels of party discipline

⁷⁶ However, there are a number of scholars who argue that the informal structures and rules in Brazil, foremost of which is the President's ability to control access to political and financial resources, actually serves to engender high levels of discipline on the floor among legislators. Consequently, this enables the executive to construct disciplined coalitions, so in reality, the level of Presidential support in Brazil may actually be higher than is commonly believed (Table 2.3) (see Figueiredo & Limongi, 1995, 1999, 2000; Amorim-Neto & Santos, 2001).

(see Piñeiro, 2004; Andrés Moraes, 2004; Morgenstern, 2001; Buquet & Chasquetti, 2005),⁷⁷ while Argentina's closed-list PR system, has resulted in a low number of effective parties (relative to Brazil) and high levels of party discipline (see Jones, 1997; 2002; 2005; Morgenstern, 2002).⁷⁸ Consequently, the level of presidential legislative support in Argentina and Uruguay is high in comparison to the low level of support in Brazil.

Table 2.3: Level of Presidential Legislative Support

	Effective Number of Legislative Parties	President's Party % share of seats in lower house (or national assembly) ⁷⁹	Level of Party Discipline	Level of Presidential Legislative Support
Argentina	3.18	48	High	High (1)
Brazil	7.81	19	Low	Low(3)
Uruguay	2.73 ⁸⁰	43	High	High (2)

Source: Inter-American Development Bank (2006), Jones (2002), Mainwaring & Shugart (1997) and Morgenstern (2001)

In both Uruguay (see Aloisio & Arboleda, 2006; Bergara *et al.* 2005) and Brazil (see Amorim-Neto & Coelho, 2007; Alston *et al.*, 2006; Mueller, 2001) the judiciary is considered to be independent of the executive and legislative branches. In Argentina (see Manzetti, 1999; Chávez, 2007) however, the judiciary is considered to be subject to executive manipulation. In Table 2.4 below, the varying degrees of judicial independence across the three case study states are illustrated according to two different indices.

⁷⁷ However, these same rules are also responsible for the factionalised party system in Uruguay. See for example Piñeiro (2004) or Andrés Moraes (2004).

⁷⁸ After the Pact of Olivos in 1994, the image of the second major party, the UCR was severely tarnished and this led to the emergence of a third party, FREPASO (see Jones, 1997: 295). The UCR made something of a comeback at the end of the millennium and FREPASO was replaced as the third party by the ARI (see Jones, 2005).

⁷⁹ This is the average from the two most recent elections as of 2005. See IADB (2005).

⁸⁰ But the party system is highly factionalised.

Table 2.4: Judicial Impendence in Case Study Countries

Country	World Economic Forum Judicial Independence Scale ⁸¹	<i>De Facto</i> Judicial Independence ⁸²	Ranking of Independence
Argentina	2.17	0.333	Low (3)
Brazil	3.14	0.494	High (2)
Uruguay	4.83	n/a	High (1)

Source: Feld & Voight (2003) & World Economic Forum

As can be seen from Table 2.5, privatisation in Brazil occurred within a legal and institutional framework and was delegated to an autonomous body. This coupled with the creation of independent industry regulators in the privatised sectors and the high level to which civil servants are effectively protected from arbitrariness, politicisation, and rent-seeking, ensures that the degree of policy delegation in Brazil is high, compared with Argentina, where privatisation was carried out nearly solely at the whim of the Executive, and Uruguay where privatisation as a policy was never fully implemented.

Table 2.5: Policy Delegation in Case Study Countries

	Institutional and Legal Framework for Privatisation with Autonomous Body in Control	Autonomy of the Bureaucracy	Creation of Independent Regulatory Bodies	Overall Level of Policy Delegation
Argentina	No	Medium	Medium	Low (3)
Brazil	Yes	V. High	High	High (1)
Uruguay	No	Medium to high	Medium	Low (2)

Source: Inter-American Development Bank (2006)

Table 2.6 below, illustrates the combined effect of these institutional configurations, in terms of the capacity of the left-wing governments in the case study states chosen, to implement their policy preferences. In order to provide comparability across all four institutional variables, the presence (or absence) of each variable is simply ranked across the three case study states. In reality, not all variables are necessarily equally weighted, for example, the level of presidential power may be more important for an outcome than say the degree of policy delegation, but as an outcome will be determined by the cumulative configuration of

⁸¹ World Economic Forum, available at

<http://www.insead.edu/v1/gitr/wef/main/analysis/choosedatavariabale.cfm>. Response of surveyed executives to the question: "The judiciary in your country is independent from political influences of members of government, citizens of firms" (1=no, heavily influenced; 7=yes, entirely independent).

⁸² Feld & Voight's (2003: 503-504) variable is based upon a combination of eight objective variables such as effective average term of members of highest court, number of times supreme court judges have changed since 1960 etc.

these institutional variables, and in order to formulate working hypotheses, all variables are weighted equally.

Table 2.6: Government Capacity to Implement Policy Preferences

Case Studies	Degree of Policy Delegation	Degree of Judicial Independence	Presidential Legislative Support	Degree of Executive Power	Capacity to Implement Preferences ⁸³
Argentina	Low (3)	Low (3)	High (1)	V. High (1)	<i>High</i>
Brazil	High (1)	High (2)	Low (3)	High (2)	<i>Low</i>
Uruguay	Low (2)	High (1)	High (2)	Medium (3)	<i>Medium</i>

Labour Support

The organisation of national labour movements has a marked impact on the macroeconomic effectiveness of partisan supply-side policies and in turn, on the ability of governments to pursue them consistently (Garrett & Lange, 1991: 541). The impact of this variable stems from the assumption that the volatility and uncertainty of increased economic globalisation will fuel demands for welfare compensation, progressive taxation and increased government intervention. Left-wing governments will be more susceptible to these demands due to their historical alliances with labour. Left-labour power is therefore considered to be the political strength of the left combined with the centralised organisational strength and mobilisational power of labour. In this respect, ‘interventionist strategies are more likely where leftist governments are allied with densely and centrally organised (encompassing) unions’ (Garrett & Lange, 1991: 541).

What is more, Garrett (1998a: 8-9) has posited that increased social welfare spending may actually be attractive to mobile-asset holders as this will provide a healthy, well-educated, skilled workforce. Secondly, a high degree of left-labour power provides policy coherence, reducing the scope for isolated workers to press for wage increases, and this in turn reduces the potential for conflict in the economy between labour and capital. Capital will recognise this policy coherence and will not threaten to exercise its exit option, ensuring that left-wing governments allied with broad and dense labour movements may have the ability to implement their policy preferences.

A number of studies have examined the effect of left-labour support in the advanced industrial democracies, but some recent studies, which are more pertinent to this project, have examined the effect of this variable in the developing world.

⁸³ This capacity is relative to the three case study countries.

Kaufman and Segura-Ubiergo (2001) in their rather cautious conclusion, did find that ‘popularly’ based governments protected social welfare spending in Latin America. Likewise, Wibbels and Arce (2003: 132) concluded that ‘the left in Latin America [allied with dense labour movements] continues to have policy preferences that are consistent with historical notions of equity,’ while Rudra’s (2002: 436) analysis indicated that strong labour and democracy can positively affect welfare spending in the developing world, even in this era of increasing economic globalisation.

In relation to privatisation, it is expected that organised labour movements, especially public sector unions, would be opposed to privatisation and as economic globalisation increases, would demand that privatisation stop at least. So, labour will be an important constituency for supporting left-wing preferences as regards privatisation.⁸⁴ It is expected therefore, that *governments who command a high degree of labour support will have a greater ability to implement policies congruent with their preferences, with respect to left-wing governments who do not boast a high degree of labour support.*

There are a number of different ways in which to operationalise this variable. Garrett (1998a) developed a composite figure for left-labour power based on the number of seats in the cabinet and legislature held by parties of the left, and trade union membership combined with the number of unions that organise workers (as an indicator of concentration). That is, the higher the union density and the smaller the number of unions that organise workers, the greater the propensity for collective action in labour market institutions (Garrett, 1998a: 13). Wibbels and Arce (2003: 127) however, caution that data on the organisational concentration of Latin American union movements is extremely unreliable. In order to circumvent this issue, they used a measure of unionisation density combined with a measure of the militancy of labour-mobilising parties. Labour organisation, strength and power will be captured here by a measure of union density, the dominant level of unionisation, the number of peak organisations and the extent of leadership competition.

There is also considerable variation across the three case study countries in terms of labour support. In general, labour union power and membership has decreased significantly in Latin America following the market orientated structural

⁸⁴ There may be problems of endogeneity with this variable. Privatisation, especially in Latin America, has reduced the power of labour. Conversely, nationalisation may increase the power of labour.

reforms that occurred there in the 1990s (see for example Murillo, 2001; Stokes, 2001; Eaton, 2002). The left-wing governments in the three case study states are all allied to some degree with the labour movements in their country. The *Confederación General de Trabajadores* (CGT) has traditionally allied itself with the PJ in Argentina, while in Brazil, the *Central Unica dos Trabalhadores* (CUT) allied itself with the PT throughout the 1990s. In Uruguay, the *Plenario Intersindical de Trabajadores-Convención Nacional de Trabajadores* (PIT-CNT) has allied itself almost exclusively with the *Frente Amplio*.

As Table 2.7 shows, labour support in Argentina, across the operationalised measures, is quite high, relative to Brazil and Uruguay. Therefore, we would expect a left-wing government in Argentina to have a greater ability, due to its labour support, to be able to implement its preferences, relative to Uruguay, who in turn, we would expect to have a greater ability than a left-wing government in Brazil to implement its policy preferences.

Table 2.7: Labour support across Case Study States

	Left-Labour Power Index ⁸⁵	Union As % of Economically Active Population	Dominant Level of Unionisation	Number of Peak Confederations	Leadership Competition	Labour support
Argentina	0.438	36.1	Industry	Single	No ⁸⁶	Medium to High (1)
Brazil	0.194	29.0	Local	Multiple	Yes	Low (3)
Uruguay	0.341	20.9	Industry	Single	No	Medium to High (2)

Source: Inter-American Development Bank (2006) and Inter-parliamentary Union, International Labour Organisation, *Facultad de Ciencias Sociales, Universidad de la Republica, Uruguay*

The International Financial Institutions

The role of the international financial institutions (IFIs) in encouraging convergence has generally been omitted as an independent variable from empirical studies concerned with the advanced industrial democracies. The reasoning behind this omission is simple: the IFIs hold little sway over the economic policies of the developed states, as they are not heavily indebted to these organisations and therefore susceptible to political pressure. However, developing world states *are* often heavily

⁸⁵ This is a composite measure, consisting of the percentage seats held by the left-wing party in parliament, combined with the overall union density. The figures for union density are the most recent that could be accessed.

⁸⁶ Although the CGT remained the peak union confederation in Argentina, its leadership spilt in the 1990s and again at the end of the millennium. See Murillo (2001) and Grugel & Pia Riggirozzi (2007).

indebted to these organisations and therefore, highly amenable to pressures for reform emanating from the IFIs (Avelino, Brown & Hunter, 2005; Wibbels and Arce, 2003). Haggard and Maxfield (1996) outline the role of the IFIs in fostering convergence. When developing world states suffer balance of payments problems, they must fund their current account deficits through external borrowing. As the International Monetary Fund (IMF) and the World Bank are the main lenders to the developing world, they turn to the IFIs in order to finance this gap (Haggard & Maxfield, 1996: 214). In return for these loans they must agree to follow the policy prescriptions and structural adjustment programmes of the IFIs, which necessitate the adoption of market-friendly policies congruent with convergence. For example, Wibbels & Arce's (2003: 119) study of taxation in Latin America concluded that 'the widespread prescriptions of international financial institutions, along with the fact...their governments must signal more clearly to markets than their advanced industrial counterparts, help explain why domestic political coalitions on the left would be far less able to resist burden shifting in Latin American nations than in advanced industrial democracies.'

What is more, privatisation of state-owned assets is an essential part of structural adjustment programmes (Williamson, 1993; Hojman, 1994) and the IFIs, have actively and aggressively encouraged developing countries to embark on large-scale privatisation programmes (Welch, 1993; Hojman, 1994).⁸⁷ So, it is reasonable to expect therefore that *left-wing governments with higher levels of multilateral debt, are thus more susceptible to external political pressure from the IFIs and therefore, they will have less ability to follow their policy preferences in the area of privatisation, in relation to left-wing governments with lower levels of multilateral debt.*

Table 2.8 shows that the left-wing governments in the three case study countries paid off all remaining debt to the IMF during their terms. The majority of borrowing was done with the IMF and as it was the fund that held most sway over the decision to implement privatisation in the 1990s, the level of influence held by the IFIs as regards privatisation in these three states is now very low.⁸⁸ This low level

⁸⁷ For example, the 2003 IMF economic standby agreement with Paraguay included the stipulation that the widely contested Privatisation Law 1.615 be reactivated in that state.

⁸⁸ Multilateral debt for all three states still exists, but it remains very low as a percentage of GDP: 2.7 per cent for Brazil, 7.8 per cent for Argentina, and 15.4 per cent for Uruguay (as of Quarter 1, 2007, IMF Statistics Database and Joint BIS-IMF-OECD-World Bank statistics on external debt).

of IFI influence would encourage the study to hold this variable constant, again providing added leverage in order to disentangle the effect of political institutions and left-labour power. However, the analytical narrative will be searching for evidence of IFI influence (particularly before the debt was repaid), although we do not expect to find anything significant.

As with the economic globalisation variable, there is again a caveat. Again in reality, it is unlikely that the influence of the IMF is constant, at all times, across all the cases. Furthermore, there are other actors in the international system who will also wield influence on government policy. For example, the major international bond rating agencies, such as Standard & Poor's Rating Service (S&P) and Moody's Investor Services (Moody's), are increasingly emerging as key intermediaries between investors and recipients of foreign capital (Block & Valer, 2004; Sinclair, 2005). A change in the sovereign bond rating of a state has important impacts on the market-determined credit spreads for developing countries, thus substantially raising the cost of acquiring capital by sovereign issuers (Biglaiser & DeRouen, 2007: 122). Bond ratings respond positively to trade liberalisation, but also to other market-friendly reforms, such as privatisation (Biglaiser & DeRouen, 2007). As such, a country badly in need of foreign capital may adopt market-orientated reforms in order to receive a 'good' investment-level bond rating. Consequently, the major credit rating agencies can exert significant influence on government policy, particularly in the developing world (see Biglaiser & DeRouen, 2007; Kaminsky & Schmukler, 2002). So, although this project will treat the influence of the IMF as a constant from a methodological perspective, in order to better reflect reality, at critical moments throughout all three narratives it will examine, not only the influence of the IMF, but the role and influence of these other actors also.

Table 2.8: The Influence of the International Financial Institutions

	Argentina	Brazil	Uruguay
Action Taken	December 2005 – Argentina paid off its entire US\$9.8 billion debt with the IMF	December 2005 – Brazil clears its entire US\$15.5 billion debt with the IMF	December 2006 – Uruguay pays off the remaining US\$2.6 billion it owes to the IMF
Amount owed to IMF and Influence of IFI Variable	0 (constant)	0 (constant)	0 (constant)

2.6 Expected Outcomes

We can hypothesise expected outcomes on the basis of the variation across the key explanatory variables. Table 2.9 below, combines the variables across the three chosen case study states, and highlights the expected capacity of each left-wing government to implement their policy preferences. As can be seen clearly from this table, holding the effect of all exogenous variables, economic globalisation and the influence of the IFIs, constant, it is expected that a left-wing government in Argentina, due to its political institutional arrangements and level of labour support, will have a greater ability to implement their policy preferences, than the governments in Uruguay or Brazil. Likewise, it is expected that a left-wing government in Uruguay will have less ability than Argentina, but more ability than Brazil to implement their policy preferences. Finally, it is also expected that a left-wing government in Brazil, again due its institutional make-up and level of labour support, will have less ability than either of the governments in Argentina or Uruguay to implement their policy preferences.

Table 2.9: Aggregated Effect of Independent Variables

Case Studies Countries	Economic Globalisation	Capacity to Implement Preferences (Institutions)	Left-Labour support	International Financial Institutions	Conditions Present to Mediate Convergence Thesis
Argentina	Constant	High	High	Constant	High
Uruguay	Constant	Medium	Medium	Constant	Medium
Brazil	Constant	Low	Low	Constant	Low

Chapter Three – The Evolution of Privatisation in Brazil

The previous chapters placed this study within a theoretical framework and outlined the main research question. The first of the three chosen case studies is Brazil. In October 2002, Luiz Inácio Lula da Silva of the *Partido dos Trabalhadores* (PT – Workers Party), convincingly won the Presidential election. Lula came to power on the back of an aggressive campaign that highlighted the social ills that plagued the Brazilian state. Lula attributed these social ills and the 1999 devaluation of the *Real* to the free-market policies implemented by his predecessors. For Lula, privatisation was a cornerstone of these policies. However, when Lula became President, privatisation had already become a widely accepted and even institutionalised policy.

The purpose of this chapter is to provide historical context for the analytical narrative of Lula's Presidency. This chapter will process trace the evolution and institutionalisation of privatisation policy in Brazil until the election of Lula in 2002. The first section will briefly outline the development and role of public enterprises in Brazil. The second section will discuss the implementation of privatisation policy in Brazil during the transition to democracy, while the third will highlight the acceleration of this process under the Presidency of Fernando Collor. The fourth section will examine the Presidency of Fernando Cardoso, under whom key institutional changes were enacted in relation to privatisation, while the final section will outline the extent and institutional legacy of the Brazilian privatisation experience by the time Lula came to power.

3.1 The Origins and Role of Public Enterprise in Brazil

The state has consistently played an extremely important role in Brazil's development trajectory (Evans, 1979; Bresser Pereira & Carlos, 1983; Schneider, 1991; Shapiro, 1994), to such an extent that 'Brazilian capitalism can be defined as state capitalism' (Goldstein, 1999: 675).⁸⁹ Traditionally, the economic role of the state in Brazil could be classified according to two broad categories: the state as a regulator of economic activity, and the state as a participant in economic activity, primarily through the medium of public sector enterprises (Treat, 1983: 10). This role was a product of the 'developmentalist model' of policy-making, instituted in

⁸⁹ For analyses about public enterprises in Brazil that attempt to understand their role as regards the nature of the Brazilian state, see for example, Evans (1979), Bresser Pereira & Carlos (1983) or Treat (1983).

Brazil in the 1930s under Getúlio Vargas, and lasting more or less intact through the democratic populism of Juscelino Kubitschek in the 1950s, through military rule in the 1960s and 1970s, until the first decade after the transition to democracy (Faro de Castro & Valladão de Carvalho, 2003: 467-468). This model was characterised by the active role of the state in the promotion of economic growth through rapid industrialisation, a protectionist trade policy, the creation of regulatory and financial state structures, and ‘the direct participation of the state in production through the creation of public sector enterprises’ (Faro de Castro & Valladão de Carvalho, 2003: 468).

State enterprises grew in Brazil as a consequence of several different processes; in areas where the private sector lacked the interest or finances to invest, the state assumed the role of entrepreneur, e.g. the steel sector and *Companhia Siderúrgica Nacional* (CSN);⁹⁰ a number of enterprises were created or came into state hands due to a concern for ‘national security,’ e.g. state aircraft manufacturer *Embraer*; the verticalisation and diversification of the activities of the larger enterprises, e.g. *Petrobrás* and *Companhia Vale do Rio Doce* (CRVD) significantly expanded their activities through the creation of a large number of subsidiaries; the state has traditionally owned exclusive rights for the exploitation of natural resources, such as petroleum and iron ore and limited the participation of foreign investors in these areas, e.g. *Petrobrás*, the state-oil mega-conglomerate; and finally, the state gained control of a number of companies due to bankruptcy (Treat, 1983: 41-48; Pinheiro, 2000: 5-6; Goldstein, 1999: 675). All of these enterprises existed in two main forms: as *empresa pública*, in which the government owned 100 per cent of the company; or as *empresa de economia mista*, in which some private equity was permitted, but the government still maintained the controlling share (Treat, 1983: 36).

The end result of this uninterrupted growth of state enterprises for nearly four decades was the domination of the Brazilian economy by public companies. As Table 3.1 shows, the Brazilian state held a monopoly, or near monopoly, in a number of important areas. The scale and size of state firms grew steadily under the military dictatorship, especially during the boom years (1968-74), and by the end of the 1970s, the vast majority of large enterprises operating in Brazil were owned by the

⁹⁰ In these cases, the state did not attempt to compete with the private sector, but rather attempted to nurture a triple alliance (*tri-pé*) with multinational corporations and local investors (see Evans, 1979).

state (see Table 3.2). Public enterprises accounted for only seven per cent of the nearly 7,000 firms operating in Brazil and only 18 per cent of total employment in 1979. However, these same public enterprises accounted for 50 per cent of all capital invested in these 7,000 firms in the same year (Treat, 1983: 56).

Table 3.1: The Dominance of State Enterprises in the Economy

Sector	Dominance of Sector
Air Transport	○
Commercial Banking	□
Electricity	●
Petroleum	●
Railways	●
Steel	●
Telecoms	●
Tobacco	○
TV Broadcasting	○
Urban Transport	○
Water Supply	●

● fully or predominantly public sector; □ mixed sector; ○ fully or predominantly private sector

Source: Goldstein (1999: 676)

Table 3.2: Ownership of the thirty largest non-financial firms

Ownership	1962	1967	1971	1974	1979
Public	12	13	17	23	28
Private	18	17	13	7	2

Source: Treat (1983: 59)

By 1980, the state's productive sector was a 'black box,' to the extent that the executive was unable to figure out the assets and liabilities of these companies (Tavares de Almeida, 1999: 435). These enterprises, through their domination of the Brazilian economy, had become important political actors in their own right. They had a direct effect on macroeconomic stability and fiscal balances (Tavares de Almeida, 1999: 435). In total, by 1980, it was estimated that nearly 700 publicly-owned enterprises existed at the federal, state and municipal level. Although estimates differ, approximately 250 of these were owned by the federal government (see Table 3.3), 350 by state governments, and 100 by municipalities (Treat, 1983: 35).

Table 3.3: Economic Distribution of Federal Firms (date of creation)

Sector	Before 1939	1940-9	1950-9	1960-9	1970-5	1976-80	Total
Mining and manufacturing	2	5	4	14	24	16	65
Transport and Communication	4	1	3	8	19	5	40
Electricity	11	1	5	3	6	0	26
Finance	3	2	3	5	11	7	31
Other	46	1	---	9	28	5	89
Total	66	10	15	39	88	33	251

Source: Trebat (1983; 37)

3.2 The Beginning of Privatisation and the Transition to Democracy

The beginning of state retrenchment in Brazil can be partly attributed to the adverse economic conditions that faced the Geisel administration in 1974, particularly the unfavourable prospect of a deceleration of economic growth and harsh policies for adjusting to the increase in oil prices and the international recession (Pinheiro & Giambiagi, 2000: 7). Against this background, former Finance Minister Eugênio Gudin⁹¹ publicly observed: ‘We live, in principle, in a capitalist system. But Brazilian capitalism is more controlled by the state than in any other country, except for those under communist regimes’ (in Pinheiro, 2000: 8). This was followed a year later by a series of articles questioning the role of state enterprises in Brazil, under the title ‘*Os Caminhos da Estatização*’ (The Path to Nationalisation), published in *O Estado de São Paulo*, and by the ‘Campaign against Nationalisation’ mounted by private sector businessmen (Pinheiro & Giambiagi, 2000: 8; Pinheiro, 2000: 8-9).⁹²

The government reacted to these rumblings by adopting measures to strengthen the competitive position of privately owned Brazilian companies with regards to state enterprises and multinational firms (Pinheiro & Giambiagi, 2000: 8). However, the worsening macroeconomic situation made control of inflation and external balance top priorities. The continued expansion of the state business sector was ‘inconsistent with the idea of stabilisation and even the idea of privatisation began to permeate government discourse’ (Pinheiro, 2000: 9). In March 1979, President Figueiredo recommended measures for ‘privatisation of the SOEs and services that are not strictly essential to correction of market imperfections or for

⁹¹ These comments were made in an interview with the then, highly influential *Visão* magazine, which had elected Gudin as ‘Man of the Year’ in 1974.

⁹² Part of the business sector dissatisfaction arose from their exclusion on the *Conselho de Desenvolvimento Econômico* (Economic Development Council) from 1974 onward (Pinheiro, 2000: 8).

meeting the needs of national security' (Pinheiro, 2000: 9). This was followed by the National De-Bureaucratisation Programme and the creation of the Secretary for the Control of Public Enterprises (SEST) in order to establish stringent control over the expenditure of state-owned firms, but it was also to prevent further expansion in the state sector and to obtain a consolidated federal budget for the public sector (Tavares de Almeida, 1999: 436).

The previous expansion of state-owned firms came to an abrupt end, and shortly after the creation of the SEST, the *Comissão Especial de Desestatização* (Special Commission for De-Statistation) was established (Tavares de Almeida, 1999: 437).⁹³ This commission identified 140 companies that could be privatised in the short term, with 50 of these companies listed for sale. However, only 20 state enterprises were actually sold in 1981-1984, with eight absorbed by other public institutions, generating revenue of US\$190 million (Pinheiro & Giambiagi, 2000: 9).

Following the transition to democracy and the indirect election of the first civilian President in over twenty years, the *Nova República* under José Sarney continued to suffer from economic maladies. In 1981-89 per capita GDP rose 0.3 per cent per annum, the public deficit averaged 5.1 per cent of GDP, and inflation increased from 95 per cent to 1,783 per cent (Weyland, 1998: 67; Pinheiro & Giambiagi, 2000: 8). Sarney, in an attempt to deal with the deteriorating public finances and rampaging inflation, launched his *Cruzado Plan* in 1986, which attempted to deal with inflation by freezing prices. Sarney also adopted a hard line towards state enterprises and official rhetoric towards privatisation changed considerably (Pinheiro & Giambiagi, 2000: 8-10).⁹⁴ Sarney established the Privatisation Programme and replaced the Special Commission for De-Statistation with the Inter-ministerial Council for Privatisation (Tavares de Almeida, 1999: 438). The actual results of Sarney's privatisation drive were rather dismal.

There was a lack of political will for privatisation, exemplified by the 1988 constitution, which created a major institutional barrier for Sarney's attempts at state divestiture. The Congressional Constituent Assembly (ANC), elected in the 1986 general elections, convened in order to draft a new constitution to replace the 1967

⁹³ In Portuguese there is, like English, the verb to privatise. But, in order to avoid the actual word privatisation, the military governments chose *Desestatização*, a word which does not exist in the English language, but literally means, de-statisation.

⁹⁴ Part of the reason for this hard line was the fact that during the early eighties, state companies were ordered to borrow heavily on foreign markets in order to help finance the current account deficit. As a consequence they had been severely affected by the 1983 devaluation, further hampering the state.

Constitution still in force (Faro de Castro & Valladão de Carvalho, 2003: 472). The new constitution, reflecting the lack of support for privatisation, made strict distinctions favouring Brazilian firms to the detriment of foreign business, and it established public monopolies in oil, gas, telecommunications and coastal shipping, while creating barriers to foreign ownership in mining and electricity (Fleischer, 1998: 121). As such, the '1988 Constitution was clearly a nationalising one' (Pinheiro, 2000: 13).

Despite this, Sarney continued his legislative activity, creating the *Programa Federal de Desestatização* (Federal Programme of De-statisation) by decree.⁹⁵ The aim was to broaden the scope of the privatisation programme to include all state-owned enterprises, except for the public monopolies upheld in the Constitution (Tavares de Almeida, 1999: 438). It was no surprise when congress rejected Provisional Measure 26, which would have enabled Sarney's decree, in 1989. So, by the end of Sarney's Presidency only 17 privatisation processes had been completed, all in the manufacturing sector, generating revenue of US\$549 million and transfer of debt of the order of US\$620 million to the private sector (Velasco, 1999: 2).⁹⁶ The World Bank described this first effort at privatisation in Brazil as a 'classical example of failure' (Treisman, 2003: 100).

There are a number of important points to note about this initial attempt at privatisation in Brazil. Firstly, the emergence of privatisation in Brazil as a potential policy was not the result of external pressure. By the late 1980s, the major requirement mandated by the multilateral lending agencies was structural adjustment and privatisation. These multilateral agencies were one of the few sources of capital available to Brazil at this time, but the Brazilian government demonstrated no interest in being bound to politically unpopular programmes of reform. In 1982, Brazil was forced to sign a letter of intent with the IMF, and since then, they have proved reluctant to agree to externally imposed reforms (Molano, 1997: 37-39; Valesco, 1999: 3). In 1988, privatisation was introduced in the agreements between Brazil and the IMF, but it did not become an iron-clad conditionality (Tavares de

⁹⁵ Decree 95,886, March 29, 1988.

⁹⁶ Not all of the privatisations that occurred under Sarney were insignificant. Included in the 17 sold entities were *Eletrosiderúrgica Brasileira* (Sibra), the largest producer of ferro-alloys; *Aracruz Celulose*, one of the largest pulp and paper companies; and *Caraíba Metais*, the only copper smelter under state ownership (Velasco, 1999: 2).

Almeida, 1999: 451). Consequently, 'multilateral lending agencies had little impact on actual Brazilian policies' (Molano, 1997: 39).

Secondly, the decision to introduce privatisation onto the policy agenda was not ideologically motivated. It was necessitated by the economic conditions of that time (Pinheiro, 2000; Velasco, 1997: 1999; Pinheiro & Giambiagi, 2000). The priority of Brazilian Presidents, from the late 1970s onwards, was control of inflation and overcoming the foreign exchange crisis. Since state-owned enterprises comprised a considerable portion of domestic investment and consumption, some form of control over their expenditures and elimination of their deficits was crucial in order to stabilise the economy.⁹⁷ The gradual move towards privatisation 'was not an ideological about-turn on the developmental role of the state, but rather a change in the emphasis of economic policy, imposed by changes which were up to a certain point outside government control' (Pinheiro, 2000: 10).

Thirdly, one of the most significant developments in this period was the importance of the *Banco Nacional de Desenvolvimento Econômico e Social* (Brazilian Development Bank - BNDES) in the privatisation process. Indeed, the move towards privatisation was not only a product of the economic conditions at that time, but also a product of internal BNDES decisions (Valesco, 1997: 1999). Of the 17 privatisations that did occur during the Sarney administration, 11 were of companies controlled by BNDESpar, a wholly owned subsidiary of BNDES, and two (those related to *Siderbrás*) were managed by BNDES as the privatisation agent (Valesco, 1999: 3). The decision to sell these companies was made because BNDESpar reported annual losses between 1982 and 1987, the vast majority of which could be attributed to these underperforming and bloated state enterprises (Valesco, 1999: 4). The bank, of its own volition, then decided to sell these companies and rid itself of this burden (Pinheiro & Giambiagi, 2000: 10). The head of BNDES during Sarney's reign, Marcio Fortes, together with Ignácio Rangel, one of the chief economists, recognised the benefits of privatisation in order to streamline and reduce the losses of the bank (Montero, 1999: 34; Werneck, 1991: 62). BNDES' influence was to prove extremely important, as the procedures developed by BNDES became the model that was to be adopted under the future privatisation law (Pinheiro

⁹⁷ See Pinheiro (2000), who argues that privatisation, has been an essential element of all the Brazilian stabilisation plans. As such, privatisation and stabilisation enjoyed a symbiotic relationship in terms of Brazilian economic policy.

& Giambiagi, 2000: 10) and BNDES emerged as a potential autonomous institution that had the ability and expertise to manage privatisations.

3.3 Privatisation under Fernando Collor and Itamar Franco

It was with the surprise election of Fernando Collor de Mello in 1990 that privatisation finally became a standard policy instrument in Brazil. Collor, with no links to the main political parties, ran in the 1989 election on behalf of the newly created *Partido da Renovação Nacional* (National Reconstruction Party – PRN), which lacked any sort of party structure (Valença, 2002: 116). Collor deliberately portrayed himself as a newcomer who would embark on sweeping reforms to save the ailing Brazilian economy and moralise politics (Weyland, 1998: 75). Collor's campaign was centred on an anti-corruption platform and he promised to hunt out the '*maharajahs*,' the extremely rich and powerful managers of the huge state companies. His economic proposals focused on two main issues: trade liberalisation and privatisation of public sector enterprises (Valença, 2002: 118).

Once in power, Collor adopted an imperial Presidential style and promised 'to kill the tiger of inflation with a single bullet' (Faro de Castro & Valladão de Carvalho, 2003: 477). In order to this, he needed to address the issue of the huge public sector in Brazil, which continued to have an inflationary impact on the economy.⁹⁸ On the day after he took office, Collor launched an ambitious stabilisation plan. In the congress, nearly 2,000 draft amendments to the plan were proposed, but Collor, unwilling to accept any dilution of his reforms, hinted that he would revert to mass mobilisation if the legislature continued to thwart his initiatives. Eventually, by mid-April, his package was approved with little change, with the support of all the main parties (Valença, 2002: 115). The Collor Plan was the most drastic stabilisation plan in Brazilian history, confiscating financial assets above a low limit (approximately US\$1,300) for eighteen months (Weyland, 1998: 75).⁹⁹ A crucial element of this new economic package was Law 8,031, which established the *Programa Nacional de Desestatização* (The National Programme of Destatisation – PND) (Tavares de Almeida, 1999: 449). Part of the rationale for this programme was the hope that once the frozen savings were returned in eighteen months time, the public would use them to buy shares in the state enterprises that were being privatised (Pinheiro & Giambiagi, 2000: 12). These reforms would ultimately

⁹⁸ Inflation was running at 84 per cent a month in the early 1990s (Pinheiro & Giambiagi, 1999).

⁹⁹ An estimated US\$40 billion in new *Cruzados* were frozen.

prepare the ground for the emergence of ‘economic pragmatism’ under Cardoso (Faro de Castro & Valladão de Carvalho, 477).

The PND established a clear and transparent legal and regulatory framework for state retrenchment.¹⁰⁰ A special Privatisation Directive Committee (DC) was established in order to supervise the programme and provide some autonomy for the process, with the President of BNDES, Eduardo Modiano, at its head. The DC would also decide on key issues such as the methods and conditions of sale and the minimum auction price (Montero, 1999: 28).¹⁰¹ The BNDES was assigned the task of actually managing the PND. The BNDES is functionally independent, and the decision to place them in control of the PND was taken because in Brazil, ‘the predictable opposition to privatisation made it preferable to insulate technical decisions from political pressures’ (Goldstein, 1999: 682-683). Two consulting firms would propose an initial evaluation, the DC would decide upon a minimum price and every privatisation would then be audited from start to finish. It would also be closely monitored by a subcommittee of the House of Representatives, the judiciary, and the Federal Audit Court. Shares in the newly privatised firms could be purchased, not only in cash, but also with many different types of debt securities (Pinheiro & Giambiagi, 2000: 8).¹⁰²

Initially, the government was extremely optimistic about the success of the PND, promising forecasted revenues of US\$9 billion by the end of the year. The reality, was however, rather different. Privatisation under the PND actually turned out to be a lot more difficult than initially anticipated. The many safeguards in the PND for ensuring that the process was transparent and fair meant that each transaction took months to complete. Furthermore, the poor financial state of the companies proposed for privatisation also created a delay, as their accounts had to be placed into some form of meaningful order (Pinheiro & Giambiagi, 2000: 17). *Usiminas*, one of the largest of the state steel companies, was chosen as the first company to be privatised under the PND. This was significant as the company was both profitable and technologically up to date, thus supplying credibility to the programme, but also

¹⁰⁰ Article 1 of Law 8,031 states the main purpose of the PND – 1. To change the federal strategic approach to economic policy through the transfer of activities unduly performed by the public sector to private initiative (Pinheiro & Giambiagi, 1999: 15).

¹⁰¹ The committee consisted of 12 to 15 members, nominated by the President, with only five of these members belonging to the government. They were subject to approval by Congress.

¹⁰² These securities, which were mostly unpaid government debts, became commonly known as ‘*moedas podres*’ (rotten or junk money) (Montero, 1999: 44).

indicating that privatisation had shifted from the state merely divesting itself of unprofitable and dying enterprises, to a concerted and focused effort to privatise (Velasco, 1999: 10). However, the government had to settle 37 different lawsuits concerning the sale of *Usiminas* before it could be sold and this pattern replicated itself with other privatisation attempts right up to 1997, further delaying progress (Pinheiro & Giambiagi, 2000: 16). By October 1992, the PND had sold only 17 firms, generating US\$3.9 billion, a figure well-short of the initial government projection (Montero, 1999: 39).

However, by the end of 1992, it appeared as if Collor's reform attempts would be cut short. Mounting opposition to his imperial Presidential style, the lack of any party structure to support his initiatives, and the emergence of a corruption scandal, ultimately led to Collor's impeachment in late 1992 and his forced resignation from the Presidency (Weyland, 1998: 79).¹⁰³ Collor's dramatic exit spelled problems for the PND, as Collor's successor, Itamar Franco, the Vice-President, had none of Collor's enthusiasm for the programme. Franco had been a long-time defender of public steel and mining companies in his home state of Minas Gerais and he had actually opposed the privatisation of *Usiminas* (Montero, 1999: 50). Franco replaced Modiano with Antônio Barros de Castro as President of BNDES, and Castro's deputy, Marcos Vianna, took over the PND. Both had been key economists during the state-led development strategy of the 1970s (Montero, 1999: 50). Initially, Franco attempted to freeze the PND for three months, during which all procedures of the PND were fully examined. But, mounting fiscal and inflationary pressure, together with the continued activity of BNDES staff supportive of privatisation, prompted Franco to continue the PND (Goldstein, 1999: 684; Montero, 1999). In December 1992, Franco signed a decree re-activating the PND, but with an emphasis on cash payment rather than debt securities (Montero, 1999: 51).

In 1993, the new Minister of Finance, Fernando Henrique Cardoso, launched his stabilisation programme, the Real Plan, which managed to bring inflation down from an annualised rate of 7,736 per cent in the first half of 1994, to 91.7 per cent by the second half of the year (Pinheiro & Giambiagi, 2000: 14). Cardoso, together with

¹⁰³ The corruption scandal was focused on two main issues. Firstly, it emerged that Collor and members of his administration had moved large sums out of Brazil, days before they launched the Collor Plan, freezing all savings, and secondly, it emerged that key members of his administration were taking bribes from various groups. See Weyland (1998).

Pérsio Arida (the new head of BNDES who replaced Castro in 1993), spearheaded the preparation of Decree 362, which stipulated that all live money generated by privatisation be used to reduce public debt. The decree also allowed foreign investors to buy up to 100 per cent of the shares of public companies that were up for sale (Montero, 1999: 52).¹⁰⁴ Decree 1,068 also changed the privatisation law to include all minority shares held by the state in a number of companies (Goldstein, 1999: 682). Ironically, although Franco was initially hostile to privatisation, new privatisations under his administration generated US\$2 billion, with 72 per cent of these sales now taking the form of cash (Montero, 1999: 53).

By the end of the Collor/Franco reign, 33 companies had been privatised, with revenues of nearly US\$8 billion, and transfer to the private sector of US\$3.3 billion in debt. The vast majority of the companies sold were in the manufacturing sector, with the revenues concentrated in the steel, petrochemical and fertilizer industries (Pinheiro, 2000: 16).

Again, there are a number of important points to note about this period of privatisation. There was considerable opposition to the PND during this period, led by the PT and Lula, and allied with the *Central Unica dos Trabalhadores* (Central Worker's Confederation – CUT), and the *Central Geral dos Trabalhadores* (General Worker's Union – CGT) (Montero, 1999: 47). Lula was committed to strengthening the state and for him, the solution to the ailing Brazilian economy, was to rescue the state, rather than liquidate it. He promoted an end to privatisation and in specific cases, the nationalisation of banks, transport, education and health (Valença, 2002: 127). In response, in early 1992, Modiano, the then-head of the BNDES, proposed the use of US\$1.5 billion owed by the federal treasury for a forced savings scheme for severance pay called the *Fundo de Garantia por Tempo de Serviço* (Guaranteed Fund for Service Time – FGTS). This would enable the FGTS to be converted, at the discretion of workers, into *moedas sociais* (social money) and then into Certificates of Privatisation (CPs) at the banks with a 70 per cent discount.¹⁰⁵ This would, according to BNDES, democratise the privatisation process (Montero, 1999: 47-48). By June 1995, more than 105,000 workers in the public sector had purchased shares, averaging 10 per cent of the total shares for each public firm up for sale. Labour

¹⁰⁴ Foreign investors were allowed to participate in privatisations under the PND, but the law stipulated that they could acquire no more than 40 per cent of any company, unless they received special prior approval from Congress (Pinheiro & Giambiagi, 1999: 14).

¹⁰⁵ One of the debt securities utilised in the early phases of the privatisation process.

purchased US\$290 million in shares, which, by 1995, were worth more than US\$1 billion (Montero, 1999: 48). This BNDES scheme had the desired effect of splitting the PT/CUT/CGT alliance against privatisation. For example, union leaders opposed the sale of *Embraer* in 1994, but rank and file members, wishing to gain from the FGTS, threatened to leave the union. Likewise, during the privatisation of *Acesita*, local leaders of the metallurgical union sided with the investors against the wishes of the national union, which opposed all steel privatisations (Montero, 1999: 49).

The PND provided an institutional and legal framework for the policy of privatisation that continues to exist. Furthermore, BNDES, which is functionally independent of the government and now, head of the PND, continued to play an important role in the policy. Indeed, although Franco was initially resistant to privatisation, one of the reasons the policy continued was because of the ‘continued activities of proponents of privatisation in the BNDES’ (Montero, 1999: 52). This combination of the institutional framework of the PND and the autonomy of BNDES ensured that ‘despite significant political challenges to this policy constituency, the embedded autonomy of Brazilian privatisation guaranteed the continuation of the process’ (Montero, 1999: 54). This embedded policy structure proved sufficient to resist opposition from below (labour, Lula and the PT), and from above (Franco) (Montero, 1999: 54).

Secondly, the influence of international capital can also be witnessed during this period. As the failure of Collor’s first stabilisation plan became increasingly evident, the government began to rely on the PND as proof of its commitment to structural reform (Pinheiro, 2000: 16), ‘a sort of ‘seal-of-quality’ for economic policy, a sign of commitment to market orientated reforms... for attracting capital inflows’ (Pinheiro & Giambiagi: 2000: 14).

The appointment of Cardoso as Minister of Finance, and the subsequent success of the Real plan, was to have a significant impact in boosting his popularity during the electoral campaign of 1994. Cardoso, who had been convinced of the benefits of privatisations during his tenure as Minister, and instrumental in altering the PND to become more overarching, was to become responsible for instigating the largest and most aggressive phase in the Brazilian privatisation process during his two terms as President.

3.4 The Election of Fernando Enrique Cardoso

The success of the Real Plan, and Cardoso's resulting popularity propelled him to run in the 1994 election for the *Partido de Social Democracia Brasileira* PSDB (Power, 2002).¹⁰⁶ The PSDB had traditionally allied themselves with Brazil's socialist and left-wing parties, but in order to gain support in the conservative Northeast, they shocked the Brazilian system by announcing an electoral alliance with the right of centre *Partido de Frente Liberal* (PFL) (Power, 2002: 623-624).¹⁰⁷ This was one of the first indications that Cardoso and the PSDB were preparing to shift the traditional social democrat platform of the party to a more market-friendly platform.¹⁰⁸ During the election, Cardoso successfully played on the fear generated by the increasing popularity of the left, particularly Lula and the PT (Weyland, 1998), and frequently ridiculed the policy positions of these politicians as *atrasados* (backwards) (Power, 2002: 624).

The resounding success of the Real Plan had endeared Cardoso to the electorate, and he won the election outright, avoiding a run-off (Power, 2002: 624). Cardoso's economic policy was based on 'economic pragmatism,' a new perspective on policy-making that had emerged in the Brazilian state following the fiasco of the *Cruzado Plan*. Economic pragmatism was heavily critical of 'economic populism,' and continually questioned the inability of governments to deal effectively with inflation (Faro de Castro & Valladão de Carvalho, 2003: 478). This policy gave emphasis to monetary stability and external constraints and a core tenet of this pragmatism was privatisation (Faro de Castro & Valladão de Carvalho, 2003: 481; Goldstein, 1999: 685).

The performance of the Brazilian economy improved dramatically after the implementation of the Real Plan. During Cardoso's first term in office, there was, on average, an annual inflation rate of 8.2 per cent, an expansion of GDP of 2.7 per cent per annum and an investment rate of 17.1 per cent of GDP (Pinheiro & Giambiagi, 2000: 16). The main achievement of the Real plan was the extraordinary price stability that it brought to the Brazilian economy.¹⁰⁹ However, there was a downside to this low level of inflation. When Cardoso assumed office in January

¹⁰⁶ Popularly known as the *Tucanos*, because of their party insignia (Power, 2002).

¹⁰⁷ Now known as the *Democratas* (Democrats).

¹⁰⁸ For a good overview of the shift in the PSDB's ideology, and some of the reasons behind this shift, see Power (2002).

¹⁰⁹ Between 1983-94 annual inflation fell below 100 per cent in only one year (65 per cent in 1986) (Pinheiro & Giambiagi, 1999: 16).

1995, the government was in a rather precarious position, as without the ‘crutch’ of inflation, ‘deficits could no longer be finessed, and the election-driven deficits of most state governments came due in harsh real terms’ (Fleischer, 1998: 123). Realising that there may be some knock-on effects from the Mexican crisis, the Central Bank was forced to intervene in Brazil’s two largest state-owned banks, the Bank of São Paulo and the Bank of Rio de Janeiro and in 1995, instigated the emergency programme, *Programa de Estímulo à Reestruturação e ao Fortalecimento do Sistema Financeiro Nacional* (PROER), in order to rescue private banks. Once in power, the Cardoso government were facing progressively worse deficits (Fleischer, 1998: 123). One policy that could alleviate this pressure was privatisation, as this ‘would generate resources needed to sustain the Real Plan during this crucial transition period’ (Fleischer, 1998: 123). Cardoso wasted little time in instigating the longest, most important and most difficult phase of privatisations in Brazil. This phase was to have such a profound effect that it would inevitably ‘change the role of the public and private sectors in the economy to an extent not anticipated in earlier stages’ (Pinheiro & Giambiagi, 2000: 18).

However, before Cardoso could begin this wave of privatisations, he needed to reform a number of political institutions. Firstly, in January 1995, provisional measure 841 replaced the Privatisation Directive Committee, with the National Privatisation Council (CND), which was to be permanently composed of five ministers, as well as by ministers with sector competencies, and the President of the Central Bank when privatisations in the financial sector were being discussed (Goldstein, 1999: 682). This in effect, brought the management of privatisation closer to the central government, although the PND and the role of BNDES remained intact (Pinheiro & Giambiagi, 2000: 18). Secondly and more importantly, if Cardoso was truly to widen the scope of the PND, he needed to alter the constitution. As noted earlier, the 1988 constitution mandated for state monopolies in a number of key areas, and essentially served as an institutional barrier to any large-scale programme of privatisation.

The constitutional revision proposed to transfer to federal states the right to distribute gas directly or through a concession; to abolish Article 171 of the Constitution, eliminating any distinction between foreign and domestic owned firms; to modify Article 21 of the Constitution to allow private investment in telecommunications; and to alter Article 177 allowing private investors to operate in

the oil and gas industries (Goldstein, 1999: 682). Furthermore, the enactment of the Concessions Law (Law 8,987) regulating Article 175 of the Constitution, introduced new rules for the governing of public services. The most significant of these was the right of large consumers to choose their own suppliers, ending the local monopolies imposed by law (Pinheiro & Giambiagi, 2000: 18). The amendments to the Constitution were quickly passed by the Chamber of Deputies and were ratified, with no changes, by the Senate after the July recess (Fleischer, 1998). At a crucial point in the Chamber deliberations on the revisions, there was a national strike by petroleum workers. This was to be of enormous benefit to Cardoso, who utilised this event to reduce opposition to his proposed constitutional amendments. As Fleischer (1998: 124) notes:

A well-organised media campaign painted the workers as enemies of the people, especially the lower classes and inflamed public opinion in favour of the reforms, while the government orchestrated emergency oil imports from Argentina and the armies occupied the refineries to secure them from ‘destruction.’

The state monopolies on telecommunications, subsoil resources, electricity, coastal shipping and gas distribution were essentially broken, while the monopoly in petroleum was severely damaged. Foreign investors were no longer discriminated against and were free to participate in forthcoming privatisations. The constitution no longer served as an institutional barrier to privatisation, and Cardoso was free to significantly widen the scope of the programme.

This was achieved with the delegation of privatisation to the state level, and the extension of the PND to other sectors.¹¹⁰ Once the sale of all the manufacturing state enterprises had been completed, privatisation was extended to public enterprises in mining, electricity, railways, ports, roads, telecommunications, water, sanitation and banking. During this period, ‘privatisation had to overcome a series of life or death obstacles’ (Pinheiro & Giambiagi, 2000: 20) and was subject to intense negotiations among legislators (Velasco, 2006: 250-258).¹¹¹ The process began with the sale of *Light* in 1996, one of the largest state enterprises in the electricity sector and reached its apogee with the sale of *Telebrás* in 1998, holder of the state

¹¹⁰ For example, Ribeirão Preto privatised its telephone company, Rio the concession of a freeway and Limeira its sewage system (Pinheiro & Giambiagi, 1999: 19).

¹¹¹ The sale of CRVD attracted 135 lawsuits, *Vale* 217. The first privatisation that was completely free of lawsuits was *Enersul* in November 1997 (Goldstein, 1999: 685).

monopoly in telecommunications and the largest privatisation carried out in the world that year (Pinheiro & Giambiagi, 2000: 20).¹¹²

At the same time, Cardoso and his government were moving to establish independent regulators in the areas that had been newly privatised. Following the approval of the General Telecommunications Law in 1997, the Brazilian telecommunications agency (Anatel) was established. In the electricity sector Aneel, the sector regulator was created, together with the Energy Wholesale Market (MAE) and the National Systems Operator (ONS), while Anp became the sector regulator for the petroleum industry (Pinheiro, 2000: 22-24). These three main agencies all have rules that provide the directors with stability of tenure, so they can be only be removed with judicial condemnation (Mueller, 2001: 636). They are considered independent, given that they have their own source of income, and they must follow rules that ensure their actions remain transparent.¹¹³ More importantly, as Mueller (2001: 637) notes, these agencies ‘were created by a specific coalition (Cardoso – PSDB/PFL) that...established their structure and process so as to assure outcomes favourable to groups that support the coalition,’ ensuring any subsequent administration would be hampered in altering regulatory policy.

Privatisation had clearly entered a new phase, one that reflected a desire to substantially remove the state from the economy. The Asian Crisis in 1997 ensured that privatisation once again became a central policy issue for the government, and particularly for the success of the Real Plan (Pinheiro & Giambiagi, 2000: 20-21). The amounts received as a result of the privatisation process had become macro-economically significant for the first time and privatisation would also give Brazil the edge over countries that might become susceptible to speculative attacks in the wake of the Asian crisis. As such, ‘privatisation was seen as a kind of safety net or bridge to stability, affording the country some leeway for resolving its two main disequilibria, the current account and fiscal deficits’ (Pinheiro & Giambiagi, 2000: 21). By the end of Cardoso’s first term in office, the Brazilian state had divested itself of 136 state enterprises (Programa Nacional de Desestatização, 2005), generating nearly US\$75 billion in revenues (Tomic, 2006:58). By 1998 ‘the entire telecommunications and railway sectors, the largest ports, some of the main

¹¹² For a good discussion on the support Cardoso received for his reforms in the Chamber, see Power (1998).

¹¹³ For a review of the independence of the Brazilian regulatory agencies see Pires (1999).

highways, much of the electricity distribution and generation sectors, and some water and sanitation services had been transferred to private control' (Treisman, 2003: 94).

Cardoso was able to run in the 1998 general election as a result of his earlier endeavours to revise the constitution to allow presidents to run for a second consecutive term (this amendment was passed in 1997). Cardoso replicated the 1994 ticket and alliance with the PFL, and was elected with 52 per cent of the popular vote in the first round of elections in October 1998 (Power, 2002: 624-625). However, Cardoso's second term was beset by economic woes. Rising interest rates as a result of the Asian Crisis placed severe pressure on government debt and this, coupled with the exit of US\$30 billion belonging to risk-averse investors from the economy in 1999, led to the devaluation of the Real (Heymann, 2001: 16; Bulmer-Thomas, 1999: 731; Kaminsky et al., 2003: 51).¹¹⁴ This produced a change in outlook for the economy in general and for privatisation in particular. 'The drop in government credibility, the contraction of the GDP, and a perception of increased risk all contributed to depress real asset values and make privatisation a difficult endeavour in 1999' (Pinheiro & Giambiagi, 2000: 24). Consequently, the pace of privatisation slowed significantly, and there was a shift in priorities in terms of the utility of this policy. In particular, privatisation was utilised during the second Cardoso term as a means to strengthen the stock market through the use of large flotations in order to sell the shares of former state enterprises. During the sale of *Petrobrás* shares in August 2000, 337,000 individuals bought shares, a record in Brazil (Pinheiro, 2000: 20).

By the end of Cardoso's second term only 31 companies had been sold, albeit generating nearly US\$17 billion in revenue. The majority of these privatisations were in the infrastructure sector (roads, water, sanitation, ports and electricity), with some in financial services and energy (Programa Nacional de Desestatização, 2005; World Bank Privatisation Database, 2007). With the sale of the container terminal in Port Suape in 2002, Cardoso's privatisation drive came to an end. In the space of eight years he had managed to privatise 167 state enterprises, and generate over US\$90 billion in revenue (Programa Nacional de Desestatização, 2005; World Bank Privatisation Database, 2007), ensuring that Brazil's privatisation programme was

¹¹⁴ For good overviews of the Brazilian Devaluation in 1999, see Heymann (2001) or for the early stages, Bulmer-Thomas (1999).

one of the largest in Latin America (Tomic, 2006). Cardoso had significantly widened the scope of the existing PND, created independent regulators in a number of sectors to ensure policy continuity, and altered existing institutional arrangements, all in order to achieve this level of privatisation.

Several factors contributed to the success of Cardoso's privatisation drive. Firstly, the success of the Real Plan in finally applying the brakes to inflation gave the government the political leverage it badly needed to ensure that the necessary constitutional revisions were passed by Congress. Secondly, when Cardoso widened the privatisation process beyond the federal level, the states saw in privatisation an important source of funding, which would become crucial in allowing them to reduce their debt to the federal government. Finally, the success of the privatisations carried out in 1991-1994 and the resultant increased efficiency of these firms, helped widen support for privatisation among the electorate (Pineiro, 2000: 17-18).

Again, there are a number of important points to note about this period of privatisation. Cardoso, in altering the 1988 constitution, essentially removed the main institutional barrier to privatisation in Brazil. Furthermore, by the end of Cardoso's tenure in government, the PND constituted a legal and institutional framework for privatisation, managed by BNDES, which enjoyed a significant level of autonomy from the government. The creation of industry regulators in telecommunications, electricity and petroleum, ensured that regulation remained favourable to those in support of privatisation (Mueller, 2000: 637). These actions have ensured that privatisation in Brazil now exists within an institutional framework that enjoys relative autonomy from the Executive (Mueller, 2001).

Although opposition to this period of privatisation was fierce, mainly from public sector worker's unions allied with the PT, Cardoso continued to follow the divide and conquer method introduced by BNDES in the last phase of privatisation. He appeased them with short-term spending and higher salaries (Treisman, 2003: 102), and continued to encourage workers to benefit individually from the privatisation process through the *moedas sociais* scheme. By 1999, almost 150,000 employees had become shareholders in privatised enterprises (Treisman, 2003: 102). Cardoso reduced the support of the public sector workers among the general electorate by vilifying them. When the oil workers went on strike in May 1995, Cardoso fired the ringleaders and labelled them as 'enemies of the people,' a move augmented by a sophisticated media campaign (Treisman, 2003; Fleischer, 1998:

124). All this had the cumulative affect of ensuring that, ‘although various unions and the PT did protest privatisations actively, they were too isolated to have much effect’ (Treisman, 2003: 102).

Finally, the effect of economic globalisation and international capital can be clearly witnessed in this period in maintaining the importance of privatisation as a policy. Privatisation in Brazil had always been closely related to macroeconomic stabilisation (Pinheiro, 2000; Treisman, 2003), but with the onset of the Asian Crisis in 1997, privatisation acted as a sign of commitment to fundamental reforms to an already jittery market. Privatisation ensured that Brazil continued to attract large volumes of foreign direct investment, which, in turn, helped to finance the high current account deficit (Pinheiro, 2000: 19; Pinheiro & Giambiagi, 2000: 22).¹¹⁵

3.5 The Legacy of Privatisation in Brazil

After nearly two decades, a transition to democracy and the stewardship of four civilian Presidents, Brazil had divested itself of approximately 210 public enterprises at the federal and state level, in a process that had generated over US\$105 billion (Programa Nacional de Desestatização, 2005: 5). The entire telecommunications and railway sectors, the largest ports, the main highways, the majority of the electricity distribution and generation sectors, practically all the former state-owned enterprises in the manufacturing sector, and some water and sanitation services had been transferred to private control. More importantly, this process occurred within the framework of the PND, which now had institutional and legal backing and a manager, in the form of BNDES, that enjoyed relative autonomy from the executive. Independent regulators had been established in a number of sectors, and opposition to privatisation, mainly from the unions and the PT, had been neutralised through the use of a number of clever carrot and stick tactics. Privatisation had become generally accepted by both the policy-makers and the Brazilian electorate.

However, by 2002, approximately 50 state enterprises still existed at the federal level, with a further 200 at the state level.¹¹⁶ Brazil still controlled some enterprises in the electricity sector, some state banks, and the reinsurance monopoly, a large part of the sewage and water sanitation sectors, substantial assets in the oil

¹¹⁵ In 1997-2000, the percentage of FDI inflows associated with privatisation and the current account deficit averaged almost 25% (Pinheiro, 2000: 19).

¹¹⁶ Author’s own estimates based on data from BNDES (2005)

and gas sectors, together with the transportation and banking sectors. This is not to mention the outsourcing of activities in the public sector, such as mail, vehicle inspection, garbage etc. However, privatisation has completely altered the traditional role of the state in Brazil, and by the time Lula came to power in 2002, the majority of the large federally controlled enterprises had been sold, with an increasing number at the state level. In two decades, privatisation had become an integral part of Brazilian stabilisation and macro-economic management, a process which had evolved to such an extent, that it would be very difficult for subsequent governments to halt or reverse (Mueller, 2001; Pinheiro, 2000).

Chapter Four – Privatisation under Lula

The victory of Lula and the PT in October 2002 was widely seen as a major departure from traditional politics in Brazil. The PT emerged from a series of major strikes in the 1970s that undermined the military government and was widely seen as the only true ideological party in Brazil, with extensive links to ‘new unionism’ (Branford & Kucinski, 2005; Flynn, 2005). Lula had contested three elections before 2002 and had contested all three on an anti-poverty, anti-elitist and anti-privatisation platform (Branford & Kucinski, 2005). His platform for 2002, while more moderate, still encompassed those three key elements and his victory was hailed as a victory for change. Indeed, Lula started his inaugural speech with the word *mudança* (change) and proposed an end to privatisations in Brazil (Flynn, 2005: 1222). The previous chapter demonstrated that privatisation in Brazil from the mid-1970s until 2002 occurred within an institutional and legal framework. It remained to be seen whether Lula could actually change this policy.

This chapter is the analysis of privatisation policy during Lula’s Presidency. It will attempt to determine if Lula and the PT managed to completely halt or rollback privatisation once they were in power. It is divided into two main parts. The first part takes the form of a narrative and briefly outlines the 2002 election and the transition to power. This section is important as it will establish the motivations and preferences of Lula’s government. The second section of the narrative actually examines the policy of privatisation once Lula is in power. The second part of this chapter is the analysis, and this analysis is grouped around the independent variables identified in chapter two. The final section will present the conclusion.

The Narrative

4.1 The 2002 Election

Lula and the PT traditionally opposed all privatisations in Brazil, and in previous election campaigns had advocated the re-nationalisation of privatised enterprises. In the initial stages of the 2002 Presidential election campaign, the position of Lula was not vastly different. Cardoso and his market-friendly policies were the subject of much of Lula’s scorn, with Lula claiming that Cardoso’s policies had left an *herança maldita* (accursed legacy), which was the root cause of the 1999 devaluation of the

Real (Samuels, 2006: 6).¹¹⁷ As such, privatisation had been a central component of Cardoso's reforms and from the outset, Lula clearly displayed his hostility to this policy. Lula, who compared privatisation to economic rape,¹¹⁸ began his campaign by urging the Cardoso government to halt all planned privatisations in the electricity sector, scathingly claiming that the government should not 'sell off electricity companies for the price of a banana.'¹¹⁹ In a letter to *Folha de São Paulo*, Lula threatened to review all privatisations in the electricity sector,¹²⁰ before claiming that, if elected, he would renationalise all privatised electricity generating companies: 'The PT has already manifested its desire to nationalise *Furnas* if the government decides to privatise it. We will do the same with all privatisations.'¹²¹ Luiz Pinguelli Rosa, Lula's main energy advisor,¹²² re-iterated Lula's stance, proclaiming: 'We are not planning on carrying out any privatisation if a Lula government is elected.'¹²³

The PT's programme for government, *Concepção e Diretrizes do Programa de Governo do PT para o Brasil* (Conception and Direction of the Programme for Government of the PT for Brazil), although a more moderate programme than previous years, clearly demonstrated that the PT would not be willing to follow the economic policies of Cardoso.¹²⁴ Highly critical of Cardoso and his market model, the document was entitled '*A Ruptura Necessária*' (the Necessary Break), and emphasised government intervention and poverty reduction as the cornerstone of PT policy (Partido dos Trabalhadores, 2002a). In fact, the strengthening of the state and an increased role for the government was seen as complementary to poverty reduction. The document also clearly indicated the PT's sentiments as regards privatisations:

The programme of privatisation...debilitated the infrastructure, compromising the systemic competitiveness and growth potential of the economy. It provoked also, a rise in the price of essential public goods...In short, the programme of privatisation, sponsored by the

¹¹⁷ For a complete overview of the 1999 devaluation of the *Real*, see Bulmer-Thomas (1999).

¹¹⁸ Associated Press Worldstream, August, 21st, 2001

¹¹⁹ Business News Americas, September 4th, 2001

¹²⁰ Folha de São Paulo, September 4th, 2001

¹²¹ AFX European Focus, September 4th, 2001

¹²² The specific focus on the energy sector was due to the fact that, in 2001, as a result of a severe drought, Brazil suffered a crippling shortage of electricity during July to December of that year (OECD, 2005: 101).

¹²³ Business News Americas, May 10th, 2002

¹²⁴ This document was even a departure from initial policy positions in the 2002 election. The *Carta de Recife* (Letter from Recife), articulated even more radical positions (Samuels, 2006: 7).

Federal government, was only good for the transference of wealth, accumulated by Brazil over decades, to private and foreign groups [Partido dos Trabalhadores, 2002a: parágrafo 6].

It explicitly stated that ‘the programme of privatisation will be halted, and existing privatisations will be evaluated and audited, especially where there exists any indication of bad use of public resources, or in areas that relate to national strategic resources’ (Partido dos Trabalhadores, 2002a: parágrafo 57). The PT programme suggested that Lula would attempt to modify the regulatory agencies in the newly privatised industrial sectors under Cardoso, and stated that ‘in areas where the presence of state-owned companies is still excellent (oil, energy, sanitation and banks), this presence will be conserved and consolidated’ (Partido dos Trabalhadores, 2002a: parágrafo 57). This document was a stark refutation of privatisation, indicating that the PT would halt all privatisations, even suggesting the possibility of nationalisation. This was a position generally supported by the Brazilian electorate. Support for privatisation had dropped to just 33 per cent among the electorate by 2003, from a previous high of 51 per cent in 1998 (Latinobarómetro, 2003).

However, following the release of the PT’s election manifesto, the markets displayed considerable nervousness with the prospect of a Lula government. Merrill Lynch and Morgan Stanley downgraded Brazilian bonds from ‘marketweight’ to ‘overweight,’¹²⁵ and Fitch, the risk classification agency, lowered Brazil’s credit rating,¹²⁶ while the *Bovespa*, the Brazilian stock index, fell to three-year lows.¹²⁷ Lula, in an effort to quell market anxieties, stated that he would not default on Brazil’s debts, and would honour Brazil’s commitments to foreign markets.¹²⁸ In order to portray a more moderate image, the new ‘Lula Light,’ announced his ideologically diverse electoral coalition consisting of two left-wing parties, *Partido Comunista Brasileiro* (PCB) and *Partido Comunista do Brasil* (PC do B), one centrist party, *Partido da Mobilização Nacional* (PMN), and one centre-right party, *Partido Liberal* (PL) (Flynn, 2005: 1234). He also chose wealthy businessman, José Alencar of the centre-right PL as his running mate.¹²⁹ The PT’s programme for

¹²⁵ AFX European Focus, May 1st, 2002

¹²⁶ Gazeta Mercantil, June 21st, 2002

¹²⁷ United Press International, June 21st, 2002

¹²⁸ Gazeta Mercantil, May 13th, 2002

¹²⁹ World Markets Analysis, July 24th, 2002

government was edited, and the title '*A Ruptura Necessária*' was dropped. However, the revised *Programa de Governo do PT* continued to clearly indicate that the PT did not support privatisation, scathingly arguing that: 'The privatisations and the financial embrittlement of the State have debilitated the economic and social infrastructure, compromising the competitiveness and potential growth of the economy' (Partido dos Trabalhadores, 2002b: parágrafo 13). It still advocated government intervention in the economy, and explicitly blamed privatisations for the increase in poverty in Brazil, by raising utility tariffs among sectors that could least afford them (Partido dos Trabalhadores, 2002b: parágrafo 21 & 22). Shortly afterwards, José Dirceu, the PT's President and Lula confidant, reiterated the PT's stance towards privatisation in an interview with the *Financial Times*: 'Privatisations have been a complete failure. We will review them but that does not mean re-nationalisation.'¹³⁰ Lula suggested that he would probe controversial privatisations such as telecom firm *Telebras* and *Cia Vale do Rio Doce*¹³¹ and even José Alencar of the PL expressed concern about the pace and extent of privatisations of state-owned enterprises.¹³²

As the election drew nearer and a Lula victory began to look increasingly likely, the *Bovespa* continued to drop in value.¹³³ During the election campaign, Brazil's currency lost more than one-third of its value, its stocks lost more than half their value in dollar terms, and its sovereign bonds were trading at default levels.¹³⁴ Lula, in a last attempt to assuage investor confidence, wrote the *Carta ao Povo Brasileiro* (Letter to the People of Brazil). This three-page letter was conciliatory in tone, but contained no actual policy positions. It continued to criticise the market-friendly policies of Cardoso:

If at one time during the 1990s the current model was able to awaken hope of economic and social progress, today we are left with an enormous feeling of deception. Now after eight years of this model, the Brazilian people have determined that the fundamental promises have not been fulfilled and their hopes only frustrated.

The dominant feeling in all classes and in all regions is that the

¹³⁰ The Financial Times, July 24th, 2002

¹³¹ O Estado de Sao Paulo, May 10th, 2002

¹³² The New York Times, April 13th, 2003

¹³³ By the end of September, 2002, a month before the election, the Bovespa was at a three-year low of 9,264 (United Press International, September 25th, 2002).

¹³⁴ The Financial Times, October 5th, 2002.

actual model has exhausted itself [Partido dos Trabalhadores, 2002c: 1].

Although the PT's stance had moved from the wholesale re-nationalisation of privatised companies that it had advocated in the 1990s, they still clearly indicated that there would be no more privatisations under a Lula government and would even investigate the validity of existing privatisations, suggesting possible re-nationalisation in extreme cases.

Lula's mixture of interventionist policies, criticism of Cardoso and toned down rhetoric ensured he gained the support of a wide swathe of the electorate, who had tired of the market-friendly model under Cardoso, and the resultant *Real* devaluation, energy crisis and social inequality, and in the run-off election on October 27th Lula became the President of Brazil, earning over 61 per cent of the vote giving him a 20 per cent lead over his rival, José Serra of the PSDB.

4.2 Privatisation with Lula in Power

Once Lula was elected, the markets continued their downward spiral in response to the uncertainty surrounding the new government's economic proposals. Cardoso, in an effort to ensure a smooth transition and motivated by the threat of a financial crisis, established an Office of Government Transmission, and instructed all his Ministers to prepare a *livro de transição* (book of transition), for the incoming PT (Flynn, 2005: 1246). However, this ideal of a smooth transition was soon disrupted by Cardoso's attempt to privatise a number of government banks. The banking sector was an area that Lula had categorically claimed would not be privatised in the election campaign. He had actually suggested that he would increase the government presence in this sector (Partido dos Trabalhadores, 2002a: parágrafo 57). Cardoso was planning to sell a minority stake in the *Banco do Brasil*,¹³⁵ Brazil's most profitable bank, and also the state banks of *Santa Catarina*, *Maranhão*, *Piauí* and *Ceará*.¹³⁶ However, the Central Bank, which is responsible for the divestiture of financial institutions under the PND, largely ignored PT pressure and continued with the planned sales.¹³⁷ The sale of these banks was, however, prevented before Lula assumed office. The Supreme Court granted an injunction to prevent the sale of

¹³⁵ The Financial Times, November 5th, 2002

¹³⁶ The Financial Times, November 7th, 2002

¹³⁷ Business News Americas, November 6th, 2002

Banco de Estado Santa Catarina (Besc), due to its very low tender price,¹³⁸ while the Central Bank decided to postpone the sale of *Piauí* state bank (Bep), due to injunctions filed by the state and worker's unions.¹³⁹ The auction for the *Banco do Brasil* continued, but, as a result of market uncertainty, there were no bidders forthcoming and the sale was shelved. In this initial transition period, Lula clearly demonstrated his aversion to privatisation.

Lula assumed office on January 1st 2003 and although his governing coalition, consisting of eight ideologically diffuse parties 'was one of the most fragmented coalitions ever formed in a democratic regime' (Amorim-Neto & Coelho, 2007: 72), it still failed to provide him with a legislative majority.¹⁴⁰ Lula's new cabinet reflected his desire to calm market jitters. Antonio Palocci Filho, an advocate of fiscal discipline and good relations with the IMF, was chosen as the new Finance Minister. Palocci, previously mayor of Ribeirão Preto, was the only PT municipal leader to have experimented with privatisation.¹⁴¹ In February, Palocci signed a letter of intent with the IMF that promised to 'tighten fiscal policy further, targeting a primary surplus of 4.5 per cent of GDP in 2003' (International Monetary Fund, 2003a: 2). The IMF also continued to provide the government with instalments of a US\$20 billion loan. As a result of political uncertainty, portfolio investment had fled the country in 2002, and the net capital inflow had declined from US\$28 billion in 2001 to US\$12 billion by 2002.¹⁴² As such, the IMF loan was essential in order to shore up Brazil's faltering financial system. Surprisingly, Lula also appointed a former PSDB deputy, Henrique Meirelles, as head of the Central Bank.¹⁴³ However, despite this seemingly market-friendly shift, the new administration appeared to remain resolute when it came to privatisation. Luiz Pinguelli, Lula's new appointment as head of the state electricity firm *Eletrobrás*, announced that there would be no more privatisations while Lula was in office,¹⁴⁴ a sentiment echoed by José Dirceu, the PT's Chief of Staff, and a member of Lula's inner circle.¹⁴⁵

¹³⁸ *Gazeta Mercantil*, November 11th, 2002

¹³⁹ *Business News Americas*, December 23rd, 2002

¹⁴⁰ Lula's coalition consisted of the PT, PL, PCdoB, PDT, PPS, PSB, PTB and PV.

¹⁴¹ *The Economist Intelligence Unit*, December, 23rd, 2002, p.2

¹⁴² *Brazil Review*, September 29th, 2003.

¹⁴³ *The Economist Intelligence Unit*, December, 23rd, 2002, p.2

¹⁴⁴ *Business News Americas*, January 3rd, 2003

¹⁴⁵ *World Market's Analysis*, June 16th, 2003

These sentiments appeared to be reflected in the actions of the government when Robert Jefferson, leader of the PT bloc in the Chamber of Deputies, announced the submission of a bill to congress ordering a review of the regulatory agencies created during the privatisations under Cardoso. Jefferson accused these agencies of having a parallel power with the government that ‘even the President can’t dismiss.’¹⁴⁶ Lula also publicly criticised the agencies, blaming them for utility tariff hikes that were fuelling inflation, while holding back up to 50 per cent of the agencies’ budget in an effort to exert pressure on the heads of the agencies to resign.¹⁴⁷ Lula, through *medida provisória* 144/03, proposed altering the regulatory model of the electricity sector. Specifically, this decree stipulated that ANEEL would no longer have the power to offer concessions; secondly, it would create two separate electricity markets, one where prices are set freely and a second government-regulated market; and thirdly and more importantly, it proposed that the state electricity company, *Eletrobrás*, and its subsidiaries *Eletronorte*, *Chesf*, *Furnas* and *Eletrosul* would be exempt from the PND.¹⁴⁸ The opposition immediately challenged this decree in the Supreme Court as it contradicted the PND, but the government managed to get it passed in Congress at the end of January 2004 before the court had finished their deliberations. It was only passed as Lula, six days earlier, had brought the PMDB into his governing coalition ensuring that he had the necessary majority in Congress. Lula submitted his final bill to reform the remaining regulatory agencies to Congress in April 2004, but this bill did not drastically reduce the power of the regulators.¹⁴⁹ Moreover, it was praised by the World Bank as an advance on previous regulatory designs and was not considered ideological in nature (Lock, 2005: 55).

During this period when Lula was attempting to gain greater control in the electricity sector, AES, the US firm which bought *Eletropaulo*, one of Brazil’s main electricity generators in 1998, announced in January 2003 it would be unable to repay an US\$85 million instalment of a US\$1.2 billion loan it had received from BNDES to finance this privatisation.¹⁵⁰ Amid rumours of re-nationalisation, and nervous trepidation on the parts of investors and portfolio markets, Luiz Pinguelli

¹⁴⁶ Latin America Weekly Report, February, 25th, 2003

¹⁴⁷ Newsweek, March 17th, 2003

¹⁴⁸ Latin America News Digest, January 30th, 2004

¹⁴⁹ World Markets Analysis, April 13th, 2004

¹⁵⁰ Latin America Regional Reports: Brazil, March 18th, 2003

Rosa, the Lula appointed head of *Eletrobrás*, suggested federalising the company,¹⁵¹ while Dilma Rousseff, Minister of Energy, told the *Financial Times* that ‘if they don’t pay, we’ll take the assets back.’¹⁵² After AES had missed another payment deadline, the government announced that it would take over control over *Eletropaulo*.¹⁵³ However, following a legal challenge filed by *Eletronet*, a subsidiary of AES in Brazil, a judge issued an injunction on May 29th, preventing BNDES from taking over the shares.¹⁵⁴ In the face of a lengthy legal challenge, the government and BNDES agreed to a debt-for-equity deal in order to settle the matter.¹⁵⁵ The Lula government, which had in the early days of the election campaign said it would renationalise companies in the electricity sector, when presented with a reasonable opportunity to do so, decided to forgo this measure.

While Lula’s legislative activities, attempting to reform the regulatory agencies and preventing the remaining state energy companies from being privatised, appeared to indicate that he was determined to halt privatisations in Brazil, the *Programa Nacional de Desestatização* (PND) continued to quietly operate. The previous delegation of privatisation to the PND somewhat protected this policy from Lula. Decree 1,068 of March 1994, authorised all minority shareholdings of any entities controlled by the federal government to be included in the privatisation process and accordingly, under this law the National Privatisation Council (CND) privatised the state’s interests in five firms in 2003. Brazil’s shares in *Liasa* were sold in June, while the state’s shares in *Celpe*, *Enersul*, *Celpe* and *BeP* were privatised in December of that year (Programa Nacional de Desestatização, 2003: 10). Meanwhile in September, the CND and ANEEL, the electricity regulatory agency, began the process of privatising seven electric transmission facilities across Brazil. The privatisation of electric transmission facilities, and the right of ANEEL to offer these concessions, had been included in the PND under Decree 4,426 of October 2002, and Decree 4,023 of November 2001 (Programa Nacional de Desestatização, 2003: 11). In February 2004, the CND began the privatisation of a

¹⁵¹ Gazeta Mercantil Online, February 19th, 2003

¹⁵² The Financial Times, February 23rd, 2003, Companies and Finance, pg. 26

¹⁵³ The Financial Times, May 10th, 2003, Companies and Finance, pg. 3

¹⁵⁴ World Markets Analysis, June 2nd, 2003

¹⁵⁵ In return for writing off US\$600 million of the debt, BNDES received 49.9 per cent of a new company owning AES’s interests in *Eletropaulo*, as well as generators *Uruguaiana* and *Tiete*. See Business News Americas, September 9th, 2003.

further fourteen facilities,¹⁵⁶ followed by the privatisation of nine more facilities in May.¹⁵⁷ By November 2005, ANEEL had completed another auction, selling seven more transmission facilities throughout Brazil.¹⁵⁸ The same year also witnessed ANEEL supervise the sale of the concession contract for the *Campo Novos* power plant, and the sale of the Cuiaba to Itumbiara transmission line for US\$60 million (Programa Nacional de Desestatização, 2005).

Even the Transport Ministry began to consider privatisations. As a result of the recommendations of the CND, BNDES and also ANTT, the land transport regulator, the Ministry agreed to privatise eight lots of federal railroads in June 2005, amounting to nearly 3,000 kilometres of railway,¹⁵⁹ while lines on the Rio metro system were sold for US\$408 million (Programa Nacional de Desestatização, 2005). The privatisation of federal highways had begun under Cardoso, but was halted in 2000, when the CND recommended revising the programme. Once this revision was finished in 2003, the CND recommended the next stage of the federal highways privatisation programme and Lula, lacking legislative support and desperately needing investment in infrastructure, agreed.¹⁶⁰ The CND approved the model for the sale of nearly 3,000 kilometres of highway, and the management privatisation process began in April 2006.¹⁶¹ A further surprising move came in 2004, when the state water sanitation company *Companhia de Saneamento Basico do Estado de São Paulo* was privatised for US\$210 million. Water and sanitation were an area that the PT had specifically stated would not be privatised both in their manifesto and in campaign speeches.

All this came amid an announcement by the Social Security Minister, Ricardo Berzoini, that ‘credit cooperatives and the private pension fund sector have been overlooked by previous administrations,’¹⁶² followed by the introduction of a pension fund reform bill to Congress that would allow private companies to operate in the pension sector.¹⁶³ Pension reform was a priority for the government. The previous administration had managed to have amendments to the pension system passed,

¹⁵⁶ Valor Economico, February 19th, 2004

¹⁵⁷ Gazeta Mercantil, May 7th, 2004

¹⁵⁸ Valor Economico, November 18th, 2005

¹⁵⁹ O Estado de São Paulo, November 19th, 2004

¹⁶⁰ Business News Americas, June 19th, 2003

¹⁶¹ Agencia Radiobras, April 1st, 2006

¹⁶² Gazeta Mercantil, October 28th, 2003

¹⁶³ Gazeta Mercantil, July 1st, 2003

before the Supreme Court deemed them unconstitutional. Furthermore, the PT had previously been one of the main sources of opposition to any reform of the social security system (Alston *et al.* 2006: 69). However, by the time Lula arrived in power, the public sector deficit had grown to nearly US\$14 billion¹⁶⁴ and by 2002, about 3.5 million public servants and dependents, a tiny proportion of the entire population, were absorbing R\$39 billion in retirement benefits, an amount larger than the total federal health budget (Flynn, 2005: 1229). Lula proposed to cap retirement benefits, extend public sector service time, levy pensions to retired civil servants and limit the pensions to widows and orphans (Flynn, 2005: 1229-1230). Lula attempted to build a broad consensus for his reform through the Council for Economic and Social Development (CDES) and through negotiations with the twenty-seven governors,¹⁶⁵ but even the support of his own party began to look dubious as members of the radical wing of the PT began criticising the government's proposed reforms before they had even been submitted to Congress.¹⁶⁶ Worker's unions also attacked the government, claiming that the creation of complementary pension funds would ultimately end up privatising public pensions,¹⁶⁷ forcing Lula to seek support for his reforms among the opposition PSDB.¹⁶⁸

The financial markets reacted extremely favourably to Lula's orthodox and conservative approach to economic management, and also to his proposed social security reforms. By the end of April, the benchmark C-Bond had risen to nearly 1.5 per cent, contributing to a 4% reduction in Brazil's country risk (the spread between Brazilian bond yields and comparable US treasuries – EMBI+).¹⁶⁹ The markets favourable perception of the Lula administration was further bolstered with the successful issue of Lula's first sovereign bond issue, and in response to the fact that demand for the sovereign exceeded the US\$750 million issue threefold, the Bovespa index rose by 2 per cent.¹⁷⁰ Within hours of the bond launch, Standard & Poor's revised the sovereign's long-term outlook to stable from negative, and *Real* strengthened on expectations of renewed foreign investment.¹⁷¹ In fact, by the end of

¹⁶⁴ World Markets Analysis, 24th February, 2003.

¹⁶⁵ World Markets Analysis, 13th May, 2003.

¹⁶⁶ Agencia Estado, 17th April, 2003.

¹⁶⁷ Gazeta Mercantil, October 28th, 2003

¹⁶⁸ Jornal do Brasil, June 6th, 2003.

¹⁶⁹ Gazeta Mercantil, April 1st, 2003

¹⁷⁰ Gazeta Mercantil, April 29th, 2003

¹⁷¹ Gazeta Mercantil, May 2nd, 2003

Lula's first year in power, mainly as a result of his orthodox economic strategy, Standard & Poor's upgraded the outlook on Brazilian bonds from stable to positive, and the Bovespa had reached a 43 month high.¹⁷²

Lula, reluctant to allow the CND to carry out any large-scale full privatisations and desperately needing foreign investment, unveiled his plans for a public-private partnership initiative. The generic concept of public-private partnerships first appeared in Brazil in 1996 under Cardoso and the pluri-annual plan of 1996-1999, and gained in importance between 2000 and 2003 when private partners accounted for nearly 28 per cent of all investments.¹⁷³ Due to his lack of support in Congress, Lula issued a provisional decree on the issue in order to move the bill to the top of the legislative agenda,¹⁷⁴ but in August 2004, Congress refused to deal with any of Lula's executive decrees, and the situation was compounded when his own government allies refused to back his initiative. Their main complaint was the fact that the government had promised the allied parties R\$874 million in order to fund their own projects, but Lula had only provided them with R\$46 million. Eventually, in November, he instructed the finance ministry to release R\$600 million in order to end the three month impasse in Congress.¹⁷⁵ A month later the Senate approved the law followed shortly afterwards by the lower house.¹⁷⁶ Under the new law, partnerships would be managed by specially created companies consisting of both private and public enterprises. More importantly, it mandated for the creation of a *fundo garantidor* (guaranteed fund), which would ensure a minimum return to investors on all projects.¹⁷⁷ The states soon followed suit, with Minas Gerais offering 250 kilometres of highway under the new programme, and Bahia tendering an underwater pipeline in the city of Salvador, despite virulent opposition from unions who viewed the public-private partnership bill as privatisation in disguise.¹⁷⁸ Indeed, this was a sentiment echoed by industry observers. As one commentator noted: 'the

¹⁷² World Markets Analysis, October 15th, 2003.

¹⁷³ Inside Brazil, January 10th, 2005

¹⁷⁴ Gazeta Mercantil, September 2nd, 2004

¹⁷⁵ Latinnews Daily, November 10th, 2004

¹⁷⁶ Gazeta Mercantil, December 23rd, 2004

¹⁷⁷ Law 11,079 (*Institui normas gerais para licitação e contratação de parceria público-privada no âmbito da administração pública*). Available at https://www.planalto.gov.br/ccivil_03/_Ato2004-2006/2004/Lei/L11079.htm

¹⁷⁸ Mondaq Business Briefing, March 23rd, 2007

PPP does not represent alternatives or even a retreat from the privatisation programme implemented in the 1990s.’¹⁷⁹

However, the biggest surprise came in November 2003, when it was announced, much to the chagrin of the opposition and the left-leaning wing of Lula’s PT party that the privatisations of the state and federal banks, which Lula had opposed during the transition period, were to go ahead.¹⁸⁰ The four banks were federalised in 1996 and according to the law under the PND were placed under the control of the Central Bank in readiness for their privatisation. The National Privatisation Council (CND) had already approved the privatisation of these banks under Resolution CND 24 of 2001. Furthermore, the sale of the state banks was also encouraged by a financial report released by Merrill Lynch that suggested that the sale of these banks, would not only be a positive development for Brazil, but would also represent good value for investors.¹⁸¹ The independent *Conselho Monetaria Nacional* (National Monetary Council – CMN), under Resolution 3,154 of December 2003, established the procedures through which this stock would be sold (Programa Nacional de Desestatização, 2003: 17). So, they were ready to be sold even before Lula came to office. Consequently, on February 10th 2004, *Bradesco*, Brazil’s largest private bank, bought the *Banco do Estado de Maranhão* (BEM).¹⁸² Despite opposition from labour unions and from members of the opposition and parts of the PT, the Central Bank announced its intention to continue privatising the *Banco Estado do Ceará* (BEC), *Banco do Estado de Santa Catarina* (BESC), and the *Banco do Estado do Piauí* (BEP),¹⁸³ and shortly afterwards *Bradesco* purchased BEC at an auction held on the *Bovespa* stock market,¹⁸⁴ while the Central Bank announced that the limit on foreign capital in the federal monolith *Banco do Brasil* was being lifted from 5.6 per cent to 12.5 per cent in preparation for its privatisation.¹⁸⁵ Lula had strongly opposed the privatisations of these banks and on numerous occasions had made statements indicating that he would not privatise either BEM or BEC.¹⁸⁶ Furthermore, the PT’s election manifesto explicitly stated that ‘in areas where the

¹⁷⁹ Gesner Oliveira in *Inside Brazil*, January 10th, 2005

¹⁸⁰ *Gazeta Mercantil*, November 10th, 2003

¹⁸¹ *Business News Americas*, March 3rd, 2003

¹⁸² *Noticias Financieras*, February 13th, 2004

¹⁸³ *O Globo*, September 28th, 2005

¹⁸⁴ *Valor Economico*, December 25th, 2005

¹⁸⁵ *Global Insight*, June 2nd, 2006

¹⁸⁶ *Gazeta Mercantil*, November 7th, 2002

presence of state-owned companies is still excellent (oil, energy, sanitation and banks), this presence will be conserved and consolidated' (Partido dos Trabalhadores, 2002a: parágrafo 57). However, although the unions and members of his own PT opposed his economic policies, the markets lauded his actions. Foreign investors began to return to Brazil in large numbers, and by the end of 2004, foreign investors had purchased some US\$700 million in initial public offerings of shares in Brazilian firms, and some US\$1 billion in corporate bonds issued by Petrobrás and the Banco do Brasil.¹⁸⁷

More surprises were to follow when Finance Minister, Antonio Palocci, in an interview with the *Financial Times* announced that the government planned to submit a bill to Congress that would end the state monopoly in the reinsurance industry and would allow for the privatisation of the *Instituto de Resseguros do Brasil* (IRB).¹⁸⁸ The privatisation of IRB had begun under Cardoso when its regulatory powers were handed to SUSEP in 1999 in preparation for privatisation. An auction was planned in 2000 that would have witnessed the privatisation of a 50 per cent stake in the company. However, this auction was prevented when a Federal Judge issued an injunction blocking the sale in response to a court petition filed by the PT. Although the bill was not actually approved until Lula's second term, it does indicate, in something of a remarkable about-turn, the intent to privatise a major state asset,¹⁸⁹ something which Lula had sternly stated that he would not do.¹⁹⁰

This was followed by the announcement in February 2005 that São Paulo state, controlled by Geraldo Alckmin and the PSDB, was planning to privatise one of their largest electricity companies, *Companhia de Transmissao de Energia Eletrica Paulista* (CTEEP).¹⁹¹ Under Cardoso, reforms had extended the PND to the state level, and delegated the responsibility for these privatisations to the state government. Despite Lula's categorical claims that no major electricity company would be privatised in Brazil while he was President, there was little he could actually do. CTEEP was soon included in the state privatisation programme and in

¹⁸⁷ The Associated Press, September 15th, 2004.

¹⁸⁸ The Financial Times, January 27th, 2005, pg. 12

¹⁸⁹ When the bill was finally passed, it did not indicate any intent to privatize IRB, but rather just allowed for the deregulation and opening of the reinsurance market. See Gazeta Mercantil, January 15th, 2007.

¹⁹⁰ Noticias Financieras, January 28th, 2005

¹⁹¹ Valor Economico, February 4th, 2005

June 2006 was sold to the Colombian firm *Interconexión Eléctrica* for nearly US\$1.2 billion.

In December of 2005, at a specially called ministerial meeting, Antonio Palocci announced that the government was to repay its entire US\$15.5 billion debt to the International Monetary Fund.¹⁹² Lula, in a rather triumphal public proclamation, claimed: ‘we want to announce to the world: the time of colonisation of this country is finished.’¹⁹³ More was to follow. Only a few days later, Antonio Palocci indicated that the government would be repaying the US\$5.8 billion it owed to the Paris Club, officially freeing the country of any further obligations to multilateral creditors,¹⁹⁴ precipitating a 12 point fall in the country’s risk.¹⁹⁵

By the last year of Lula’s first term in office, nearly 3,000 kilometres of railways had been privatised, over 3,000 kilometres of federal highways, 37 electricity transmission facilities had been sold, one major sanitation company, part of the Rio metro, the *Campo Novos* power plant, the São Paulo state-owned CTEEP, and two high-profile state banks. This was apart from the plans for a further two state banks to be sold, and the most profitable federal bank in the state to be prepared for privatisation. The process had also begun to end the state reinsurance monopoly of IRB, as well as introducing private funds to the pension sector, which was generally seen as a step towards the privatisation of public pensions. Granted, the national privatisation programme significantly slowed, but what makes this remarkable is that these privatisations occurred under the leadership of a President and party who had advocated wholesale re-nationalisation for over a decade, and the end of all privatisations in Brazil up to and after the election. The PT had campaigned on a platform in the 2002 election that specifically stated that there would be no more privatisations under a Lula government, something reaffirmed by the speeches of Lula and his closest advisors on numerous occasions. What is more, Lula’s conservative economic policies were well received by the markets. In 2006, foreign investment in Brazilian capital markets had increased by 91 per cent, the Bovespa index had climbed 32.9 per cent,¹⁹⁶ market capitalisation rose by 37 per cent, and

¹⁹² *Gazeta Mercantil*, December 20th, 2005

¹⁹³ *Gazeta Mercantil*, December 21st, 2005

¹⁹⁴ *Noticias Financieras*, December 23rd, 2005

¹⁹⁵ *Noticias Financieras*, December 23rd, 2005.

¹⁹⁶ *Latin Finance*, March, 2007.

IPOs of Brazilian firms jumped to 26, higher than any other emerging market exchange bar Shanghai and Hong Kong.¹⁹⁷

This thesis argues that the political institutional structure in each state will either enable a partisan government to implement their preferences, by increasing their institutional control over policy, or to inhibit a partisan government from implementing their preferences, by leaving them with little institutional control over the policy in question. The policy in question in this instance is privatisation and clearly, from the narrative above, we can see that in Brazil, while privatisation did slow significantly, it did not stop. Throughout this narrative, the constraining effect of the political institutional structure on Lula is clear. Lula's decree power did enable him to protect the state electricity companies from privatisation, but this legislation only passed as it was during the brief interval (January to March 2004) when he had established a cohesive coalition. Cardoso had delegated the policy of privatisation to a number of autonomous institutions and consequently, the privatisation of infrastructure and the federal banks could continue. Lula's strong executive power had the ability to curb the power of these institutions, but this was only functional if he could form a cohesive coalition but he was unable to do so. As such, Lula's policy preferences were constrained by the institutional structure in Brazil. The next section will analyse the privatisations of Lula according to the independent variables identified in chapter two.

The Analysis

4.3 The Political Institutions

The Brazilian political system is a Presidential system with three branches: the Executive, Congress and the Judiciary (Mueller, 2001: 623). The 1988 constitution defined the political institutions in Brazil and the powers of the political actors in the policy-making process. The driving force behind policies in Brazil is the strong set of powers conferred upon the Executive by the Constitution (Alston *et al.* 2006: 3). However, this does not mean that the Executive has unbridled powers. The multi-party system forces Brazilian executives to forge unstable multi-party coalitions, to such an extent that the political system has been called 'coalition presidentialism'

¹⁹⁷ The Economist, April 7th, 2007.

(see Pereira & Mueller, 2002; Figueiredo & Limongi, 1999; Amorim-Neto, 1994; Abranches & Hudson, 1988).

The Executive

After more than twenty years of military rule, the 1988 Constitution was an attempt to move towards a more balanced political system, emphasising principles such as decentralisation, transparency, participation, social control and redistribution (Alston *et al.*, 2006: 12). Although the constitution represented an attempt to break away from Brazil's authoritarian past, a number of institutional arrangements suggested an element of continuity (Amorim-Neto & Coelho, 2007: 75; Alston *et al.* 2006: 13; Mueller, 2001: 623; Mainwaring, 1997: 65). Foremost among these was the presupposition of a strong presidency, including prerogatives such as *medida provisória*, veto power, the exclusive right to initiate legislation in certain areas, and the power to initiate new legislation (Alston *et al.* 2006: 13; Pereira, 2002: 11). As such, 'the new constitution continued to allow incommensurate power to the Executive relative to other branches of government' (Mueller, 2001: 623).

Article 62 of the 1988 Constitution allows Presidents, in cases of 'urgency and relevance,' to decree provisional measures with the force of law (*medida provisória com força de lei*) (Pereira *et al.*, 2005: 184; Mainwaring, 1997: 62), allowing the President to enact new legislation promptly and without congressional approval (Alston *et al.*, 2006: 18). These decrees would have immediate legal effect, but would expire after 30 days if Congress did not convert them into law (Pereira *et al.*, 2005: 184). In effect, the Executive previously used this instrument without restraint. Between 1998 and 2000, 4,422 decrees were issued and Congress rejected only 21 of them (Mueller, 2001: 623). If Congress fails to act on the decree within this timeframe, it automatically goes to the top of the legislative agenda; replacing items the Congress may currently have been debating (Alston *et al.*, 2006: 18). This allows the Executive to force legislation onto the Congressional agenda. Furthermore, a number of quasi-constitutional initiatives by the Sarney Presidency set the parameters for the use of the *medida provisória*. The first was to self-servingly interpret the requisite of urgency; the second was to observe few limits as to the policies that could be initiated or altered by decree; while the third was to reissue decrees that Congress did not consider within the 30 day timeframe (Pereira

et al., 2005: 184), a practice that was generally tolerated by the Supreme Court (Alston *et al.* 2006: 19).

However, following major disagreements in Congress as regards the use of decree power, an agreement was reached with Cardoso in September 2001 that amended Article 62 of the Constitution (Pereira *et al.*, 2005: 184; Alston *et al.* 2006: 19). This amendment limited Presidents to a single reissue of a lapsed decree, and reduced ambiguity by specifying a list of areas in which decree power may not be utilised. These areas include criminal and electoral law, citizenship rights and judicial power.¹⁹⁸ This has altered the executive/legislative relations that existed prior to 2001 and effectively amounts to a ‘partial rollback of Presidential decree authority’ (Alston *et al.* 2006: 19).

The President can resort to the ‘package veto,’ with which entire legislation can be rejected, or the ‘partial veto,’ whereby the President can approve articles of a bill that he may agree with, while rejecting articles in the same bill that he does not (Alston *et al.* 2006: 19; Mueller, 2001: 624). The 1988 Constitution allows for Congress to override this veto relatively easily, given that it only requires an absolute majority in the joint chambers (Alston *et al.* 2006: 19). The fragmentation of the Brazilian party system, however, has hampered opposition attempts to form a cohesive unit to override the veto (Mainwaring, 1997: 60-61).

The Constitution also specifically defines a number of policy areas such as budgetary and public administration matters where the Executive has the exclusive right to initiate legislation (Alston *et al.* 2006: 19-20; Mueller, 2001: 624). Furthermore, Article 10 provides the Executive, through the *Mesa Diretoria* (Steering Body) and *Colégio de Líderes* (Board of Leaders), a central role in the definition of the committee system (Alston *et al.* 2006: 20). The Executive, roughly speaking, has the power to determine the members of any committee and can even bypass the committee system by ‘strategically creating special committees to consider specific issues’ (Mueller, 2001: 624). Although there is obviously an element of self-selection in many committee appointments, ‘there is evidence of significant interference by party leaders in the process of appointing and substituting committee members’ (Alston *et al.* 2006: 20). Clearly, the Executive in Brazil has a central and powerful role in the legislative process. For example, between 1984 and

¹⁹⁸ Emenda Constitucional No. 32, available at:
http://www.planalto.gov.br/ccivil_03/Constituicao/Emendas/Emc/emc32.htm

1999, 86 per cent of the laws promulgated in Brazil were done so on the authority of the executive, indispensable proof of the ‘centrality of this organ of the state in national political life’ (Amorim-Neto & Coelho, 2007: 75).

As such, ‘it is no surprise that the executive has largely dominated the legislative process in Brazil’ (Pereira, 2002: 12). However, the Executive is far from omnipotent (Amorim-Neto & Coelho, 2007: 75). While the President may have recourse to very strong powers, support of the legislature is essential for the President’s legislative agenda.¹⁹⁹ In fact, where presidents have attempted to use their powers to by-pass the legislature to implement unpopular policies, such as Sarney and Collor and privatisation, a lack of legislative support has stymied their initiatives (see Mainwaring, 1997: 91-98). What is important then, is the degree to which the Executive can impose its preferences on Congress, a function of the unity of the governing coalition (Mueller, 2001: 623; Mainwaring, 1997).

Lula, who had traditionally criticised the use of Executive power in Brazil, was forced to rely heavily on the powers granted to the Executive by the constitution. Due to the lack of unity within his own party and the ideologically diverse nature of his governing coalition, he found it very difficult to successfully impose his preferences upon Congress. In terms of privatisation policy, Lula had at his advantage a strong set of presidential powers, but this was offset by his poor support base in both houses. Due to this, he was forced to utilise his decree power excessively in order to promote his legislative agenda. He issued *medida provisória* 144/03 in his attempt to redesign the regulatory structure surrounding the electricity sector and to protect the state electricity firms from privatisation. Initially, the PT had hoped to introduce congressional legislation, but at this time, Lula’s coalition controlled only 41 per cent of the lower house, so in order to ensure his reform proposals had legislative priority he relied upon decrees (Tavares de Almeida, 2006). Although the legislature eventually approved his initiative,²⁰⁰ the new regulatory system is extremely precarious as it consists largely of decrees and executive orders rather than a congressional law and as such, can be easily challenged or altered.²⁰¹

¹⁹⁹ The constitution also prohibits the *medida provisória* from being utilised to amend the Constitution (Alston *et al.* 2006: 14).

²⁰⁰ The decree was approved mainly because of large-scale electoral discontent with Cardoso’s model, due to the 2001 electricity shortage.

²⁰¹ Latin Finance, April/May 2004

Likewise, when Congress refused to consider his public-private partnership programme, Lula was forced to issue an executive decree to force it to the top of the legislative agenda. Even then however, Congress in August 2004, refused to consider any of his legislation, primarily because the parties in his own coalition refused to budge until they had been granted R\$600 million that Lula had promised them in return for their support. Lula was forced to release the funds in order to confirm this support, but this took over three months rather than the constitutionally mandated 30 days. As a result, the public-private partnership bill did not become law until January 2005, nearly two years after Lula had first proposed it. During these two years, with no alternative programme to attract much-needed investment, the PND continued to quietly operate.

This lack of legislative support ensured that he could do little to halt the processes of privatisation that were already in motion, or had been set in motion due to the delegation of this policy under Cardoso. He could, theoretically, have halted the ongoing privatisations of the CND in early 2003 and the proposed privatisation of the state banks, but this was during the period when his coalition had only 41 per cent of the seats in Congress (and even then it was not guaranteed that all 41 per cent would support him). A presidential veto in the early stages of Lula's presidency could easily have been overturned. He simply did not have the political support to curtail the power of the CND. Likewise, when São Paulo announced the sale of their state electricity company in 2005, a priority sector for Lula that he had struggled to protect, there was little he could do. Geraldo Alckmin of the PSDB was in control of São Paulo and the PSDB were also the largest opposition party in Congress, and any move against them would be fiercely challenged. All Lula's government could do was to tacitly accept the privatisation. In fact, Lula used his veto power only once when it came to privatisation. A bill was presented to Congress in 2005 that proposed floating the state-run airline management company *Infraero* on the *Bovespa*, and Lula decided to veto this proposal.²⁰²

Although Lula had strong presidential powers, his lack of support in Congress and the fragmented nature of his coalition were serious obstacles to his initiatives. He used his strong powers to protect the state-owned electricity companies, but his lack of support ensured that there was little he could do to

²⁰² Valor Economico, September 20th, 2006

completely halt the day-to-day actions of the CND, Central Bank or National Monetary Council, or indeed to prevent individual state governors from privatising their assets.

Legislative Support

Despite strong constitutional powers, the President, in order to successfully advance his/her legislative agenda needs co-ordinated, cohesive support within the legislature. A fragmented multi-party system, requiring the President to forge ideologically diffuse, multi-party coalitions, combined with low levels of party discipline however, hamper the Executive in this endeavour, ensuring that Presidents in Brazil 'face constant and crippling difficulties in moving their agendas through the legislature' (Ames, 2002: 213). The open-list proportional representation system, with a low threshold and high district magnitude has encouraged the emergence of Brazil's multi-party system. As such, the President rarely holds an outright majority in Congress, and must forge some form of multi-party coalition in order to govern (Mueller, 2001: 635; Mainwaring, 1997: 69). Although the Executive has potential preponderance over the congress, typically, this preponderance will only be successful if a cohesive coalition is forged. In 2003, Brazil had an effective number of 8.5 legislative parties, among the highest in the world (Samuels, 2006: 26). The myriad party nature of the Brazilian system ensures that at least one party in any coalition will have interests in favour of privatisation,²⁰³ drastically reducing Executive discretion (Mueller, 2001: 635).

The open-list and proportional representation system allows citizens to select candidates rather than parties. This ensures that voters are more attracted to a candidate's personal qualities, encouraging candidates to develop links with his/her constituency rather than the party. This system also pits members of the same party against one another in direct electoral competition, which in turn, tends to promote factions within parties. The Brazilian system allows unlimited re-election, and the *candidato nato* obligates parties to re-nominate incumbents, regardless of whether they towed the party line in the previous legislative term (Pereira, 2002: 8). This of course, reduces the reliance of legislators on the party leadership and these factors have the cumulative effect of severely undermining party discipline in Brazil

²⁰³ In general, votes in the Brazilian Congress are ideologically consistent. Of 221 cases analysed, 64.7% were ideologically consistent (Figueiredo & Limongi, 1995).

(Mainwaring, 1995, 1997; Ames, 1995, 2001, 2002; Figueiredo & Limongi, 1995). This is exacerbated by low levels of party loyalty and frequent party-switching. In addition, federalism has further dispersed power in an already fragmented party system. Loyalty to powerful governors or mayors rather than the federal party has further contributed to factionalism and discipline problems in some of the larger parties (Mainwaring, 1997: 83; Samuels, 2003).²⁰⁴

Recently, a number of scholars, rather than stressing the decentralising effect of electoral rules, have begun to emphasise informal institutional rules and structures that may serve to discipline individual legislators (Figueiredo & Limongi, 1995, 1999, 2000; Meneguello, 1998; Nicolau, 2000; Amorim-Neto & Santos, 2001). Foremost among these structures is the President's ability to control the distribution of political and financial resources, which in turn, 'provides colossal electoral responses for those who have the chance to exploit them appropriately' (Alston *et al.* 2006: 20).²⁰⁵ Although individual legislators may propose amendments to the budget, it is the President who determines which amendments to accept. Evidence suggests that the President will reward those legislators who vote consistently in his favour, leading to pork-barrel politics (Alston *et al.* 2006: 20).²⁰⁶ The Executive can negotiate support on a vote-by-vote, deputy-by-deputy basis, in exchange for these clientelistic resources (Samuels, 2006: 17). For example, in a survey of 1,317 roll-call votes taken in the Brazilian legislature, only in 33 cases did deputies actually go against the party line (Limongi & Figueiredo, 1999).²⁰⁷

The reality however, is that the Brazilian system is neither a centralising nor a decentralising one (Alston *et al.*, 2006: 17; Pereira, 2002: 4-5). The electoral rules provide incentives for deputies to act individualistically, while the informal rules (*fisiologismo* - pork-barrel) also provide deputies with the incentive to support the Executive. For Samuels (2002: 316), deputies actively pursue pork-barrel because it serves their *progressive* ambition to further their future non-congressional career paths. So, as Pereira (2002: 26) argues:

²⁰⁴ Governors have the ability to impede the electoral careers of legislators at the state level (Samuels, 2003), but as a result of privatisation in the 1990s, the pork-wielding power of the governors has diminished significantly (Alston *et al.* 2006: 28-32).

²⁰⁵ For example, Cardoso significantly centralised the budgetary process, by centralising demands and the distribution of assets through the System of Legislative Performance (SIAL), created by Decree 1,403 (Pereira, 2002: 13).

²⁰⁶ For a detailed study supporting this evidence see Pereira & Mueller (2002).

²⁰⁷ Ames (2002) cautions that roll-call votes will not capture Executive initiatives that are abandoned before they reach the voting floor.

Legislators must satisfy constituencies' demands in order to survive politically. Simultaneously, the legislators are compelled to follow their party leader indication and thus to gain access to political and financial benefits, so that they can use them, in turn, to satisfy constituencies' demands in order to have electoral returns.

This institutional configuration ensures that the equilibrium point for a cohesive governing coalition rests on the Executive's ability to distribute economic and political incentives to maintain the support of the coalition.

After the 2002 election, the PT became the largest party in the Chamber of Deputies, but they still only had 17.7 per cent of the seats.²⁰⁸ Lula's electoral coalition could only boast 25.3 per cent of the seats in the lower house, and 29.7 per cent in the upper house (Samuels, 2006: 13). This was well short of the 60 per cent of seats that was effectively needed to pass constitutional amendments and unpopular legislation. Lula's first governing coalition encapsulated eight parties and did not give him a majority in either house, due to his refusal to include the PMBD (Samuels, 2006: 13).²⁰⁹ This earned Lula the dubious accolade of creating 'one of the most fragmented coalitions ever formed in a democratic regime' (Amorim-Neto & Coelho, 2007: 72). This coalition was ideologically diffuse and contained a number of parties (PTB and PL) who were nominal supporters of privatisation. Indeed, the constellation of this particular coalition was very similar to the one that had supported Cardoso and his privatisation drive in the 1990s (Tavares de Almeida, 2006).

For his first year in office, Lula led a minority coalition controlling only 41 per cent of the seats in the lower house and as a result, he had very little control in congress. The fragility of this coalition was soon exposed when Lula attempted to introduce social security reform legislation. He only managed to have this legislation passed by reaching out to the opposition PSDB and PFL, and this resulted in one of the left-wing parties in his coalition withdrawing from government and the PT expelling several members who had stubbornly opposed the legislation (Samuels, 2006: 14). This severely eroded the modicum of legislative prowess that Lula already

²⁰⁸ The PT itself was divided into a number of different factions (*tendências*), among them the *Campo Majoritário*, the *Articulação de Esquerda*, *Movimento PT* and the *Democracia Socialista*. The *Campo* was the largest wing and was led by Lula's mentor and advisor, José Dirceu (Flynn, 2005: 1226).

²⁰⁹ The government only managed to forge a coalition due to the tradition of *governismo*, a pragmatic desire in Brazilian politics to be in power that enticed several deputies to switch parties (Samuels, 2006: 13).

commanded, and ensured his strong executive powers were virtually negated in his first year in office. Furthermore, when the Central Bank announced the sale of the *Banco do Estado de Maranhão*, Lula's strongest opposition came from within his own party. However, there was little he could do due to his precarious position in Congress.²¹⁰

In January 2004, Lula was forced to invite the PMDB into his government, ostensibly providing him with more than the 60 per cent of seats needed. For the first few months of the year it appeared as if Lula was finally able to boast a legislative majority, ensuring he could actively pursue his legislative agenda. This new coalition enabled him in January 2004, to pass his electricity sector reforms and to protect the state-owned electricity companies from privatisation, while avoiding the pending challenge to this legislation from the Supreme Court. However, it soon became clear that Lula had lost control of the Congress. In October and November 2004, the 'lower clerics' boycotted Chamber activities, and effectively stalled government business (Flynn, 2005: 1225).²¹¹ However, despite including the PMBD in his new coalition, due to the proportionality of the distribution of portfolios, the government's control of the legislature actually weakened (Amorim-Neto, 2006: 11-16; Samuels, 2006: 15). The PT controlled only 29 per cent of the coalition's seats but managed 60 per cent of the ministries compared with the 50 per cent of the seats controlled by the PMBD, PL and PTB who only held 12 per cent of the portfolios (Amorim-Neto, 2006: 16). For Lula, this ensured 'his policies angered his leftist base, but the disproportional distribution of cabinet portfolios angered his partners to the right' (Samuels, 2006: 15). As Amorim-Neto (2002: 76) has proved, Presidents who appoint more proportional cabinets tend to oversee more stable and unified coalitions. Lula failed to reach the necessary equilibrium point described above in order to establish a cohesive governing coalition by refusing to distribute the requisite political and economic benefits to his government allies.²¹²

This was clearly illustrated in August 2004, when Congress refused to deal with any of Lula's executive decrees. His own government allies refused to back his initiatives, particularly his public-private partnership bill. Their main complaint was

²¹⁰ Business News Americas, March 5th, 2003

²¹¹ The lower clerics are those with little access to posts and little success for winning federal support for projects in their respective states (Flynn, 2005: 1225).

²¹² Traditionally, the PT and Lula had rejected *fisiologismo* (pork-barrel politics), but in this instance it wasn't a moral stance on behalf of the PT, but simply a refusal to share power (Flynn, 2005).

the fact that the government had promised the allied parties R\$874 million in order to fund their own projects, but Lula had only provided them with R\$46 million. Eventually, in November, he instructed the finance ministry to release R\$600 million in order to end the three-month impasse in Congress.²¹³ This essentially delayed his public-private partnership bill by over a year.

By 2005, discipline within the PT had broken down, Lula's governing coalition was incredibly fragmented, and it appeared as if he had completely lost control of Congress. In January, at the World Social Forum, 100 members of the PT announced that they were leaving the party, among them 42 members of the *Democracia Socialista tendência* bloc, who moved to the *Partido Socialismo e Liberdade* (P-Sol) (Flynn, 2005: 1227). Indeed, between January 27th and February 17th, 45 deputies switched parties, an average of two a day, further highlighting the lack of any party loyalty within the Brazilian legislature (Flynn, 2005: 1230-1231). In February, the government suffered its biggest defeat in Congress during the election for the President of the Chamber of Deputies,²¹⁴ further underlining Lula's inability to impose his preferences upon Congress.²¹⁵ Luiz Eduardo Greenhalgh, the official candidate of the PT, was beaten by Severino Cavalcanti, an independent, by 190 to 300 votes.²¹⁶ This was the first time that a candidate backed by the President had failed to win the post, which is key in setting the legislative agenda in Congress. Sections of Lula's own PT rejected the candidate, and a rebel wing even proposed an opposing PT candidate, further exacerbating fragmentation within the party.²¹⁷ Not only had Lula lost control of Congress, but the appointment of Cavalcanti seriously undermined his ability to pursue his own legislative agenda.

In May 2005, Lula vetoed a bill that would have granted congressional workers a 15 per cent pay rise. This created further damaging divisions within the PT and ensured that Lula lost an extremely powerful ally in Renan Calheiros, President of the Senate.²¹⁸ All this came amid a vote at the PMDB's national convention that favoured its formal departure from the PT-led government.²¹⁹ An entire wing of the

²¹³ Latinnews Daily, November 10th, 2004

²¹⁴ The President of the Chamber of Deputies controls the chamber's agenda and voting procedures, and traditionally went to the largest party in the house (Flynn, 2005: 1227).

²¹⁵ Folha de Sao Paulo, February 15th, 2005

²¹⁶ The Financial Times, February 16th, 2005

²¹⁷ Latin America Monitor, June 2005

²¹⁸ Latin America Monitor, June 2005

²¹⁹ Business News Americas, December 22nd, 2004

PMDB favoured this move due to divergences between the PT and PMDB in the municipal elections in November 2004. Although the party remained in the coalition, it was now split, further weakening the governing coalition. For Samuels (2006: 16) this ‘illustrated that Lula could not even control the moderates within his own party, much less organise a coherent majority coalition.’

Lula’s refusal to distribute cabinet seats continued to cause controversy. Severino Cavalcanti, the President of the Lower Chamber, publicly accused the PT of unilateralism. Both Cavalcanti and other government allies contested that the PT had been extremely inflexible in accommodating other parties, seeking to concentrate power and govern alone.²²⁰ In fact, in what was the most damaging blow to the PT yet, it emerged in May 2005, that the reason Lula did not equitably distribute resources or posts was because he did not rely on the traditional, legal but inefficient, pork-barrel method to govern (Samuels, 2006: 16). Instead, the PT constructed its coalition not through pork-barrel, but through illegal monthly allowances (*mensalão*), and under-the-table campaign financing (*caixa dois*) (Samuels, 2006: 17-18).²²¹ The resultant corruption scandal further ruptured the PT and forced José Dirceu, Lula’s mentor and confidant, to resign from the administration. For Lula’s legislative agenda the results of this crisis were far-reaching.²²² Essentially, Lula and his government were hamstrung, and it became a ‘government of cohabitation, dependent on the PSDB and the PFL’ (Flynn, 2005: 1235). For the remainder of Lula’s term not only was he reliant upon his coalition allies, but also the opposition.

The corruption scandal, and Lula’s failure to provide sufficient pork-barrel for his allies, ensured that his own PT and his ideologically diffuse governing coalition were highly fragmented. Only for a brief three months in early 2004 did Lula ever fully control the Congress. It was during this period that he passed his legislation on the electricity sector and protected the national energy companies from privatisation. However, aside from this brief interval, Lula’s coalition was highly fragmented and as a result, he was unable to impose his preferences as strongly as he might have wished upon Congress.

²²⁰ Latin America Monitor, June 2005

²²¹ In a now infamous interview, Lula when questioned about the illegal payments could only reply: ‘The PT has only done what other Brazilian parties have always done’ (O Globo, July 18, 2005).

²²² For a complete overview of the corruption scandal see Amorim-Neto & Coelho (2007) or Flynn (2005).

Policy Delegation

When Brazil started its privatisation programme there was an urgent need to signal to the market that the government would not rescind the contracts or act opportunistically once the companies were sold (Mueller & Pereira, 2002: 79). Essentially, the government needed to make a credible commitment to privatisation. The main method to achieve this was to delegate this policy to other institutions, which would remain relatively free of Executive interference. This would ensure that if an Executive came to power who held contradictory views on privatisation, this policy could be somewhat insulated.

Law 8,031 established the *Programa Nacional de Desestatização* (The National Program of Destatisation – PND) (Tavares de Almeida, 1999: 18). The PND established a clear and transparent legal and regulatory framework for state retrenchment. A special Privatisation Directive Committee (DC) was established in order to supervise the programme and provide some autonomy for the process, with the President of BNDES at its head.²²³ The DC would also decide on key issues such as the methods and conditions of sale and the minimum auction price (Montero, 1999: 28). When Cardoso came to power, he did alter the PND somewhat. Provisional measure 841 replaced the Privatisation Directive Committee with the National Privatisation Council (CND), which was to be permanently composed of five ministers as well as by ministers with sector competencies and the President of the Central Bank when privatisations in the financial sector were being discussed (Goldstein, 1999: 682). The PND, and the appointment of BNDES to run the programme, effectively delegates the day-to-day decisions concerning privatisation to an autonomous institution. For example, when Itamar Franco came to power in 1992, he initially froze the PND for three months, during which all procedures of the PND were fully examined. But, mounting fiscal and inflationary pressure, together with the continued activity of BNDES staff supportive of privatisation, prompted Franco to continue the PND (Goldstein, 1999: 684; Montero, 1999).

Consequently, in early 2003, the PND continued to operate. Minority shares, railroads, roads and electricity transmission facilities were privatised as they had been included in the PND as a result of a *medida provisória* issued by Cardoso, and

²²³ BNDES is one of the few large bureaucratic sections of the Brazilian state known as *ilhas de excelência* (islands of excellence). These are key insulated bureaucracies that are free from Executive and Congressional manipulation (Alston *et al.* 2006: 42).

the PND merely followed the existing decree orders. Lula could have perhaps have halted this activity, but in the first year of his Presidency he was politically weak and lacked majority support in Congress. Also, Cardoso's reforms of the PND had placed the privatisations of financial institutions in the hands of the Central Bank and the National Monetary Council. It was their decision to forge ahead with the state bank privatisations during the transition period despite PT opposition.²²⁴ Likewise, it was their decision to re-initiate proceedings to privatise these banks once Lula came to power, and they oversaw the sale of the *Banco do Estado de Maranhão* and the *Banco Estado do Ceará*. Furthermore, Cardoso also extended the PND to the state level, and it was solely São Paulo's decision to privatise CTEEP. The PSDB, the largest opposition party in Congress, controlled São Paulo and Lula could not afford to challenge the decision to sell the state-electricity company. The same situation occurred when São Paulo also decided to sell the *Companhia de Saneamento Basico do Estado de São Paulo*.

The BNDES also continued to have an important role.²²⁵ They continued to manage the privatisation programme and to recommend certain sectors to the CND for privatisation. For example, in 2005, BNDES produced a report which recommended that Brazilian port authorities privatise all dredging works at their ports.²²⁶ Furthermore, BNDES, through BNDESpar, was solely responsible for the decision to begin privatising *Brasiliiana de Energia* and *Telemar*.²²⁷ Both these companies belonged to BNDESpar, and the decision to ready them for privatisation was purely an internal BNDES decision, a situation similar to the early privatisations in the Sarney period.

Secondly, the creation of regulatory agencies in a number of sectors intimated to the market that the government was making a credible commitment to privatisation. The main motivation for the regulatory agencies was 'the government's need to tie its own hands, providing a commitment to reassure investors, and thus guarantee a successful privatisation programme' (Mueller & Pereira, 2002: 67). They are important as they are political actors with strong influence over the policy-making process in important sectors of the economy and 'their design provided them

²²⁴ The banks were also mentioned in the 2003 letter of intent with the IMF (International Monetary Fund, 2003a: 4).

²²⁵ Lula did appoint the protectionist Carlos Lessa from the PMBD as head of the bank in 2003.

²²⁶ Business News Americas, July 29th, 2005

²²⁷ Business News Americas, June 12th, 2006 and Business News Americas, May 28th, 2007

with considerable policy-making clout and a high degree of independence from the Executive and Congress' (Alston *et al.* 2006: 37). Since 1997, ten regulatory agencies have been created in Brazil: ANEEL (electricity), ANP (oil), ANATEL (telecommunications), ANTT (land transport), ANTAQ (water transport), ANS (private health insurance), ANVISA (health and sanitary surveillance), and ANA (surface water resources) (OECD, 2005: 114). Mueller (2001: 635) argued that an important institutional restraint on a new Executive expropriating existing contracts or halting privatisations is built into the structure and process of the regulatory agencies at the time they were created. For Mueller (2001) and Mueller & Pereira (2002), Cardoso designed the main regulatory agencies (ANEEL, ANP, ANATEL), so as to favour the policy of privatisation. This 'deck-stacking effect of the administration will restrain the ability of a new Executive to drastically alter policy' (Mueller, 2001: 636). The main powers of the agencies include the power to set tariffs, and the power to grant the concessions through which the right to provide a public service is conferred to the private sector. The rules that were developed at the inception of the agencies ensure stability for the directors, as they can only be removed with judicial condemnation. The directors are appointed by the President and approved by the Senate, and their mandates were staggered so they were non-coincidental (Alston *et al.*, 2006: 37-38; Mueller & Pereira, 2002: 82). A new Executive would have to wait a number of years before they could appoint a director. For example, Lula attempted to replace the market-friendly director of ANATEL, Luiz Guilherme Schymura, with his own representative, Pedro Jaime Ziller. However, this move was successfully challenged by the opposition PSDB in court and ANATEL remained for nearly a year without a director until a suitable replacement could be found.²²⁸

One of Lula's first goals was to reform the regulatory model surrounding the electricity sector. The focus on the electricity sector was mainly a product of the dissatisfaction with Cardoso's model that arose in Brazil following the energy crisis of 2001. After heated legal and legislative challenges, Lula did succeed in reforming this sector, but he maintained the independence of the regulators in the other sectors. As such, ANTT were free to submit proposals for the privatisations of the railway lines and federal highways to the PND. Likewise, ANEEL, before the success of

²²⁸ Total Telecom, January 9th, 2004

Lula's reforms, could continue to offer concessions on the electricity transmission facilities, maintain utility tariffs and protect concessionaires.

As a result of Cardoso's decision to delegate the policy of privatisation to numerous independent and autonomous agencies, the PND could continue to operate relatively peacefully. Lula had the power at his disposal to curb these bodies and agencies, but he lacked the necessary political support in Congress to do so. Policy delegation of privatisation under Cardoso ensured that while Lula significantly slowed down the PND, privatisations already approved could effectively continue mainly as a result of the path dependent effect of previous policy design.

Judicial Independence

In Brazil, it is generally accepted that the judiciary is independent of the Executive and the Legislature (Amorim-Neto & Coelho, 2007: 75; Alston *et al.*, 2006: 27; Mueller, 2001: 624).²²⁹ The court is composed of eleven judges, appointed for life terms by the President and confirmed by the Senate. The composition of the court changes very slowly, so typically each President can only appoint a small number of judges who may hold interests in their favour (Mueller, 2001: 624). However, due to the rule requiring mandatory retirement for judges once they reach the age of 70, Lula was able to appoint three new Supreme Court judges in the first six months of his Presidency (Alston *et al.*, 2006: 25). Once the Supreme Court has made a decision, Congress and the Executive have no recourse to appeal or alter this decision. In effect, they must pass a new law. 'The Supreme Court is afforded considerable insulation from the other branches of government by this rule' (Mueller, 2001: 625).²³⁰ The 1988 constitution further removed potential leverages of political control over the Court, by establishing that the annual budget of the judiciary was to be elaborated by itself and the courts have the sole power to appoint lower court judges (Amorim-Neto & Coelho, 2007: 75; Alston *et al.*, 2006; Mueller, 2001: 625).²³¹ In November 2004, Lula did manage to pass a judicial reform bill. This bill

²²⁹ This only applies at the Federal level and particularly the Supreme Court. At the state level there are large levels of corruption and nepotism (Amorim-Neto & Coelho, 2007: 75-76).

²³⁰ The independence of the judicial system, and its role as an important political actor, is further enhanced by the *Ministério Público* (MP – Public Prosecutors). They have become important actors and further act as a check on Executive Power. For a full discussion on the role of MPs, see Alston *et al.* (2006) and Arantes (1999).

²³¹ Two main instruments can be used by a wide array of actors to force judicial review: *ação direta de inconstitucionalidade* (ADIN), which nullifies a decision or legal norm due to unconstitutionality;

stated that decisions reached by eight of the eleven judges had to be followed by the lesser courts.²³²

The Supreme Court has on numerous occasions contradicted the interests of the Executive and Congress.²³³ In 1996, with the social security system in tatters, Cardoso attempted to tax retired workers. The survival of the government depended upon solving the social security crisis and this tax appeared to be a means to achieve this, albeit a highly unpopular one. The Executive managed to pass this initiative through Congress, but a number of workers brought the issue to the Supreme Court who duly declared the measure unconstitutional, much to the chagrin of the government and its supporters in Congress (Alston *et al.*, 2006: 26; Mueller, 2001: 625-626). This even prompted calls from Cardoso's supporter to alter the Constitution. Castro (1997: 153), in a study of 1,247 Supreme Court judgments, discovered that the courts ruled in favour of private interests versus public interests in 75 per cent of cases demonstrating that even in routine business the Court 'has ruled against the initiatives of the government.' What this serves to demonstrate is that, as Mueller (2001: 627) argues:

Investors who purchased public service concessions through the privatisation programme could have an expectation that the Supreme Court would uphold the concession contracts in an unbiased manner with high probability. Should the circumstances arise that the government would attempt to implement policy that went against these contracts, both the investors and the government could predict relatively safely that the Court would uphold these contracts.

The independence of the Supreme Court from the Executive, and the Court's adherence to the concession contracts, ensured that Lula would be unable to pursue a policy of nationalisation. If he did, the concessionaire would revert to the Supreme Court, who in all likelihood would uphold the concession contract. This is because the Court, despite its many failings, views cases purely legalistically (Alston *et al.*, 2006: 27).

and the *ação declaratória de constitucionalidade*, which confirms the constitutionality of a decision or legal norm. See Alston *et al.* (2006: 15).

²³² Latinnews Daily, November 18th, 2004

²³³ For a list of cases where the Executive and Supreme Court clashed see Castro (1997).

This is exactly what happened in the case of the AES-owned *Eletropaulo* when the firm was unable to meet its debt repayments to the BNDES. When the BNDES moved to take control of the firm, *Eletronet*, a subsidiary of AES in Brazil, brought the case to court and as a result, a judge issued an injunction preventing BNDES from taking over the company. In the face of a lengthy and costly legal challenge, the government and BNDES agreed to a debt-for-equity deal in order to settle the matter. The court also proved important in protecting the design of the regulatory agencies. When Lula dismissed the Cardoso-appointed head of ANATEL, Luiz Guilherme Schymura, and attempted to replace him with the former trade unionist, Pedro Jaime Ziller, the PSDB challenged this move in court as it contradicted the rules created to protect the regulatory agencies.²³⁴ As a result, the court prevented Ziller from assuming the role as head of ANATEL. The agency actually remained for nearly a year without a director until the more market-friendly Plinio de Aguiar, who had previously been head of ANATEL, was appointed to the post. Lula's attempt to reform the regulatory framework for the electricity sector was also challenged by the PSDB and it was only as a result of his new governing coalition in early 2004 that the reforms were passed before the Supreme Court could challenge them. His bill to reform the other agencies was submitted to Congress in April 2004, but this bill did not drastically reduce the power of the regulators mainly because the judiciary would challenge any deviations from the regulatory law.

The independence of the Supreme Court ensured that nationalisation without sufficient monetary compensation was impossible once Lula came to power. The judiciary also acted as a significant barrier in his attempts to reform the regulatory agencies, and replace the existing heads of the agencies with his supporters. As such, it acted as a significant check on the Executive's power.

4.4 Labour support

Since its inception in 1983, the *Central Unica dos Trabalhadores* (Central Workers Union – CUT) has been closely linked to Lula and the PT (Ellner, 2004: 24). Lula himself was a former trade unionist and leader of the metalworkers union of São Bernardo do Campo and Diadema (Flynn, 2005: 1222). Although the CUT and the PT were closely linked, there was never any formal links between the two and the

²³⁴ Total Telecom, January 9th, 2004

PT, unlike other labour parties, is not funded by union contributions (Branford & Kucinski, 2005: 29).²³⁵ The CUT did however formally endorse Lula's candidacy in the 1989, 1994, 1998 and 2002 elections (Branford & Kucinski, 2005). While the CUT is the *de facto* umbrella organisation of the Brazilian trade union movement, unionism in Brazil however, is far from united (Cook, 2002). The growth of rival unions, such as *Central Geral dos Trabalhadores* (General Workers' Union – CGT) and *Força Sindical*, together with the labour reforms and divisive privatisations of the Cardoso era, further weakened and fragmented the Brazilian labour movement (Boito, 1998).

In 1991, shortly after Collor came to power, conservative members of the Brazilian labour movement established *Força Sindical* to act as a counterweight to the representation of the CUT. *Força Sindical* brought together a huge mass of small unions with fewer than 500 members each.²³⁶ The union leaders, rather surprisingly, espoused support for market-friendly policies rooted in a general political conservatism (Boito, 1998: 73-74). The effect of this new union was to draw support from CUT and decisively split the labour movement in Brazil. Furthermore, the privatisations carried out during Collor and Franco's reign exacerbated the divisions within the labour movement. The CGT, CUT and the PT were active in opposing these initial privatisations, but in response to this, BNDES established the FGTS scheme, which allowed workers to participate in the privatisations (Montero, 1999: 47-48).²³⁷ By June 1995, more than 105,000 workers in the public sector had purchased shares, averaging 10 per cent of the total shares for each public firm up for sale (Montero, 1999: 48). This BNDES scheme had the desired effect of splitting the PT/CUT/CGT alliance against privatisation. For example, union leaders opposed the sale of *Embraer* in 1994, but rank and file members, wishing to gain from the FGTS, threatened to leave the union. Likewise, during the privatisation of *Acesita*, local leaders of the metallurgical union sided with the investors against the wishes of the national union, which opposed all steel privatisations (Montero, 1999: 49).

When Cardoso came to power, the influence of the union movement continued to decline. Liberalisation and privatisation particularly affected the auto

²³⁵ In fact members of the *Partido Comunista do Brasil* (PCdoB), and the *Partido Comunista Brasileiro* (PCB) are also associated with CUT (Boito, 1998: 74).

²³⁶ There are actually seven central unions in Brazil. 71% are in CUT, 9% in *Força*, and the remainder in the other five (Martin, 2006).

²³⁷ See Chapter Three

and textile sectors, as well as banking and the civil service. Increased unemployment in these traditionally highly unionised sectors severely reduced union membership levels and consequently, union influence (Cook, 2002: 18). By 2001, only 23.6 per cent of the labour force held trade union membership, while 26 per cent of all employed workers had union membership (Martin, 2006). Cardoso also attempted to undertake extensive labour reforms and despite his best efforts, the corporatist provisions of the constitution remained, although they were significantly watered down (Cook, 2002: 17-23). *Força Sindical* became willing to accept many flexible provisions in their collective agreements, and became the *de facto* union ally of the Cardoso government. They supported labour reform and privatisations and further undermined the cohesiveness of Brazilian labour (Cook, 2002: 19). Public sector worker's unions allied with the PT continued to oppose Cardoso's proposed privatisations, but Cardoso continued to follow the divide and conquer method introduced by BNDES. He appeased them with short-term spending and higher salaries (Treisman, 2003: 102) and continued to encourage workers to benefit individually from the privatisation process.

The CUT endorsed Lula in the 2002 election, and when Lula won the election, one-third of his cabinet were former activists in the CUT (Flynn, 2005: 1252) and nearly two-thirds of the PT's congressional representatives had links to unions or social movements (Branford & Kucinski, 2005: 47). However, by this stage, labour support in Brazil had been significantly weakened. Union membership had declined, the labour movement was fragmented between the CUT and *Força*, and the employee participation scheme during privatisation had further divided the unions. More importantly, those former CUT trade unionists now in power with Lula came from a small nucleus that had their roots in the famous *Clubes de Investimentos* (Investment Clubs) from the Collor era that had actively supported and participated in the privatisation process in the nineties (Flynn, 2005: 1251-1252). This was exemplified during the sale of the *Banco do Estado de Maranhão*, when the government continued the divisive tactics employed during Collor's tenure by offering 10 per cent of the bank's shares to employees.²³⁸ Lula even introduced legislation that would deregulate the labour market and reform 'corrupt' trade

²³⁸ Latinnews Daily, December 18th, 2003

unions.²³⁹ Unions continued to actively oppose privatisations and were specifically active during the sale of the state banks and the Rio metro line.²⁴⁰

Ironically, rather than a PT government strengthening left-labour power, it exacerbated tensions and heightened divisions. Fragmentations within Lula's own PT caused further tensions among the labour movement. As such, labour support in Brazil was divided and somewhat rudderless and had little impact in preventing privatisations from continuing.

4.5 Conclusion

Lula was elected in 2002 with a mandate to change the market-friendly model adopted under Cardoso. Part of this mandate was a categorical pledge to halt all privatisations in Brazil. Once in power, Lula did manage to significantly slow down the PND begun under Cardoso, but nonetheless, privatisations did continue. More to the point, privatisations continued in sectors (banking and electricity) where Lula had specifically stated his intention to halt privatisations. The reason for this was clearly a confluence of institutional factors that shaped policy once Lula was in power. The Executive has extremely strong powers in Brazil, but this power is a function of the Executive's ability to control Congress. Controlling Congress requires a cohesive governing coalition (necessary due to the multi-party system in Brazil), and the adoption of pork-barrel politics to satisfy this coalition. Lula did use his executive power extensively to force the legislative agenda and his decree power enabled him to protect the state electricity companies from privatisation, but this legislation only passed as it was during the brief interval (January to March 2004) when he had established a cohesive coalition.

In general however, it was a self-replicating cycle of institutional factors that ensured he was unable to implement his preferences and halt privatisation. Cardoso had delegated the policy of privatisation to a number of autonomous institutions. Lula's strong executive power had the ability to curb the power of these institutions, but this was only functional if he could form a cohesive coalition, but electoral rules and his inability to achieve the required equilibrium as regards pork-barrel prevented him from doing so. Policy delegation ensured that privatisation could continue while the judiciary could successfully prevent him from completely overhauling these

²³⁹ The Financial Times, January 27th, 2005

²⁴⁰ Mondaq Business Briefing, March 23rd, 2007

institutions or engaging in a policy of nationalisation, even if he had of so wished. Therefore, as hypothesised in Chapter Two, Brazil would be the least likely of the three case studies to halt all privatisations due to the configuration of the specific political institutions in place in that country.

Chapter Five – The Evolution of Privatisation in Argentina

The second of the three chosen case studies is Argentina. In April 2003, Néstor Kirchner of the left-wing *Frente Para la Victoria* (The Front for Victory) was elected President. Kirchner, like Lula, campaigned on a platform that attacked the economic policies of his predecessors, particularly privatisation. When Kirchner assumed office, privatisation had been an acceptable policy for over a decade. In fact, so large was Argentina's privatisation programme that it was labelled as 'one of the broadest and most rapid in the Western Hemisphere (World Bank, 1993: ix).

The purpose of this chapter is to provide historical context for the analytical narrative of Kirchner's Presidency. This chapter will trace the evolution of privatisation policy in Argentina until the election of Kirchner in 2003. The first section will briefly outline the development and role of public enterprises in Argentina. The second section will discuss the implementation of privatisation policy in Argentina during the transition to democracy, while the third will examine the Presidency of Raul Alfonsín. The fourth section will examine the Presidency of Carlos Menem, while the fifth section will briefly examine the 2001 crisis. The final section will outline the extent and legacy of the Argentine privatisation experience by the time Kirchner came to power.

5.1 The Development of State-Owned Enterprises in Argentina

The expansion of state enterprises in Argentina is the result of a series of decisions made in response to varied economic imperatives, rather than as a result of a coherent strategy for the state sector in the economy (Enrique Andrieu, 1999: 282). Before World War II, public enterprises in Argentina had little role in the economy, but after the war, with the development of an alliance between a nationalistic military and the working class when Perón assumed power in 1946, import substitution industrialisation became the central platform of economic policy, leading to a large increase in state ownership (Goldstein, 1998: 59; Alexander & Corti, 1993: 1; Enrique Andrieu, 1999: 283). Once Perón was in power, the military instigated a campaign pushing for the nationalisation of what they perceived as vital strategic sectors (Goldstein, 1998: 59) and Perón, with access to large foreign reserves accumulated during World War II, used this money to nationalise the telephone company, the electricity industry, railroads and several bankrupt private industries

(Alexander & Corti, 1993: 1; Molano, 1997: 90). The surpluses produced by the agricultural sector were utilised to subsidise industrial expansion and major public companies were established under Perón in the gas, power and steel sectors (Alexander & Corti, 1993: 1; Molano, 1997: 90). The government significantly increased the scope of its interventions, but no central holding was ever established to manage the proliferation of state enterprises (Goldstein, 1998: 59). Because of this, no definitive survey was ever carried out to map the extent of state enterprises in the Argentine economy, but from a number of different sources, it can be estimated that by the 1966 military coup, the state-owned or held a minority interest in some 560 enterprises (see Table 5.1).

Table 5.1: Extent of State Enterprise in Argentina (Early 1960s)

Ownership	Banco Nacional de Desarrollo & National Bank for Savings and Insurance			At Federal, State and Municipal Level		Total Enterprises
Share	>20%	≤20%≤15%	<15%	Non-Financial Sector	Financial Sector	
Total	97	39	130	260	37	563

Source: Alexander & Corti (1993), Di Tella (1983) and Enrique Andrieu (1999)

Following the ousting of Perón in 1955, a number of state enterprises were either closed down or privatised under the government of President Frondizi (Alexander & Corti, 1993: 2), but when Perón returned as President in 1973, he adopted expansionist economic policies and once again enlarged the public sector (Murillo, 2001: 131). In order to maintain low levels of unemployment, he absorbed large numbers of workers into the state enterprises (see Table 5.2) (Di Tella, 1983). Perón also established the *Corporación Nacional de Empresas del Estado* (National Corporation for State Enterprises - CNEE) in an attempt to provide unified management for the enormous public sector, but the formation of the CNEE ‘constituted more of a declaration of intent, rather than a real political instrument’ (Di Tella, 1983, 175), and it was eventually disbanded after the appointment of Alfredo Gómez Morales as Minister of Economy in 1974 (Di Tella, 1983: 180),

Table 5.2: Percentage Variation in Employment in State Enterprises

Year	Variation in Employment in State Enterprises (Each Year as Base Year)
1967	-3.53
1968	-5.61
1969	-2.83
1970	-1.27
1971	-0.37
1972	2.32
1973	10.89
1974	20.33
1975	5.29
1976	0.99

Source: Di Tella (1983)

Because no effective survey of state ownership has ever been carried out in Argentina, it is impossible to state with certainty exactly how many state enterprises actually existed before the 1976 coup. However, taking into account the 560 enterprises in state hands at the beginning of the 1960s, and accounting for closures and privatisations that occurred under successive military governments, it has been generally estimated that by the beginning of the Alfonsín administration some 400 state enterprises were in existence in Argentina, holding monopolies or near-monopolies in areas as diverse as gas, steel, mining, oil, electricity, air travel, railroads, port management, postal services, water, sanitation, roads and banking (Manzetti, 1999: 72; Corrales, 1998: 26; Molano, 1997: 92).

5.2 The Beginning of Privatisation: José Martínez de Hoz

Although there were incidental privatisations in the 1960s, the beginning of privatisation in Argentina can be traced to the return of military rule in 1976 and the appointment of José Martínez de Hoz as Minister of the Economy (Müller & Rapetti, 2000; Azpiazu & Schorr, 2001). By 1976, mainly due to the expansionary economic policies of Perón, the economy was in recession, with the fiscal deficit constituting 15.1 per cent of GDP, wholesale price inflation peaking at 499 per cent and the external public debt crisis placing enormous fiscal restraints on economic policy (Molano, 1997: 79; Müller & Rapetti, 2000: 1; Murillo, 2001: 131). Fiscal discipline, together with liberalising reforms and attempts at privatisation, modelled on General Augusto Pinochet's policies in Chile, became the core tenet of de Hoz's economic programme (Corrales, 1998: 25; Goldstein, 1998: 60). Martínez de Hoz attempted to liberalise the financial and foreign exchange markets, considerably reduce the tariffs on imports and undermine the bases of the populist coalitions created under Perón

(Müller & Rapetti, 2000: 3-5).²⁴¹ The role of state-owned enterprises also began to change. Consumer tariffs were left low to avoid inflation, and when external sources of financing for the private sector began drying up due to an increase in the perception of Argentina's country risk, state enterprises, as in Brazil, were used as lines for external credit (Goldstein, 1998: 60).

Furthermore, there were widespread staff rationalisations in state-owned enterprises, and lucrative (and often bloated) sub-contracts with the private sector were curtailed, while oil exploration was opened to private domestic firms in 1977 (Müller & Rapetti, 2000: 3; Goldstein, 1998: 60). Although Martínez de Hoz wished to conserve the nucleus of state-owned enterprises in the industrial and service sectors, he did initiate a process of privatisation (Müller & Rapetti, 2000: 3-4). A list of state-owned enterprises created by the Inter-ministerial Commission for Privatisation, coupled with companies in which the *Banco Nacional de Desarrollo* (National Development Bank - BANADE) held a minority stake or shareholding, were considered eligible for sale (Ministerio de Economía y Producción, 2007). Law 22,177 of March 1980 attempted to create a legal framework for this process, and this initiative led to the re-privatisation of a number of small or medium sized firms that had previously come under state management due to bankruptcy (Müller & Rapetti, 2000: 3-4).²⁴² However, as a result of fervent opposition from a wide variety of actors, privatisations were extremely limited and due to the fact that the new firms found themselves in a monopsony market situation, the hoped for gains in efficiency failed to materialise (Molano, 1997: 79).

Opposition to Martínez de Hoz's privatisation initiatives came from an active and strong anti-privatisation coalition consisting of the *patria contratistas*,²⁴³ the rent-seeking private sector, and the Peronist controlled labour unions (Corrales, 1998: 35). Ironically, after the military coup of 1976, a number of high-ranking military leaders who had been given control of state enterprises, joined this coalition, further impeding government attempts at reform. They actively lobbied for the removal of Martínez de Hoz and 'ultimately precluded the government from enacting

²⁴¹ For the policies of José Martínez de Hoz, see Canitrot (1980, 1981).

²⁴² Ley 22,177 (*Privatización de empresas*). Available at <http://mepriv.mecon.gov.ar/Normas/22177.htm>.

²⁴³ The *patria contratistas* were the largest holding groups in the country, and made enormous fortunes through multimillion dollar public works contracts with the state (see Corrales, 1998: 28-29).

any meaningful reduction in state-owned enterprises. By 1982, even the technocrats in office had given up their efforts to shrink the state' (Corrales, 1998: 36).

During this period there were also two major nationalisations of companies in a critical condition and in fact, the nationalisation of *Italo* alone, constituted more than all other privatisations combined (Müller & Rapetti, 2000: 3; Goldstein, 1998: 60). Financial liberalisation increased interest-rate differentials between Argentina and the rest of the world and this, coupled with high interest rates and an appreciation of the domestic currency, placed enormous pressure on manufacturing firms in the import competing sector, forcing firms to acquire dollar denominated debt to keep afloat (Murillo, 2001: 131-132). Foreign debt grew three times between 1978 and 1981 (Murillo, 2001: 132), and the share of total public expenditure as a percentage of GDP rose from 27.6 per cent in 1971-75 to 38.7 per cent in 1981-83. The external debt of state-owned enterprises had reached a massive US\$12 billion (approx) by 1982 (see Table 5.3) (Goldstein, 1998: 60-61).

With the Mexican debt moratorium and the subsequent debt crisis, the government was forced to take over a number of struggling banks, ensuring 'reserves dwindled as it tried to sustain the financial system' (Murillo, 2001: 132). The military government decided to divert attention from the economic woes of the state, and generate an upsurge in nationalistic sentiment by invading the Malvinas/Falkland Islands in April 1982, provoking a war with the United Kingdom. Following the defeat of the Argentine armed forces, and the ultimate de-legitimation of the regime, the military government was forced to accept a democratic transition and elections were called for October 1983.²⁴⁴

²⁴⁴ For a comprehensive account of Argentina's transition to democracy see, for example, Levitsky (2005).

Table 5.3: Foreign Debt by Company in Argentina in 1980

Company	US\$ millions
YPF	2,906.0
GAS	452.3
YCF	118.0
Water and Electricity	1,496.6
SEGBA	661.2
Hidronor	281.6
FFAA	439.5
Airlines	515.5
AGP	33.0
Elma	663.5
ENTel	293.0
Encotel	9.3
Total	7,869.5

Source: Manzetti (1999: 82)

5.3 The Election of Raul Alfonsín: Reluctant Privatisation

The first Argentine election in over a decade surprisingly returned Raúl Alfonsín, of the social democratic *Unión Cívica Radical* (Radical Party – UCR), as the new civilian President (Manzetti and Dell’Aquila, 1988: 3; Murillo, 2001: 132).²⁴⁵ When Alfonsín took office, he found himself in a precarious position. Not only was he tasked with consolidating democracy in Argentina after half a century of political turmoil, but the country was also in the throes of its deepest economic recession since the 1930s (Manzetti and Dell’Aquila, 1988: 3). Although GDP growth had actually marginally increased by 2.8 per cent, inflation had peaked at 343 per cent and unemployment had grown to 4.2 per cent by 1983 (Murillo, 2001: 132).

The primary concern of Alfonsín and his Economy Minister, Bernardo Grinspun, was to combat inflation and they initially adopted a heterodox stabilisation programme, a policy that conflicted with the IMF plan for stabilisation (Molano, 1997: 91; Manzetti & Dell’Aquila: 1988: 3). Alfonsín was reluctant to implement privatisations, as this policy was considered too closely associated with the military regime, and also contrary to the social democratic ideology of the UCR (Corrales, 1998: 25-26). The new measures increased government revenues by 18.6 per cent, but the main problem was still the level of fiscal spending (Molano, 1997: 91). By the end of 1983, Argentina could no longer repay its principal debt or even make timely interest payments and the lack of available external credit forced Grinspun to sign an agreement with the IMF in September (Manzetti & Dell’Aquila: 1988: 4). The

²⁴⁵ Alfonsín won the election with 51.75 per cent of the vote, beating the strongly favoured Peronist candidate, Italo Luder.

stringent measures requested by the IMF prompted Grinspun and the Central bank Governor, Enrique García Vázquez, to resign. They were replaced by Juan Sourrouille and José Luis Machinea respectively, although this new team did not significantly alter the economic policy of their predecessors. This breach of the September agreement led to the IMF suspending all loans and by spring 1985, Argentina was on the verge of hyperinflation (Manzetti & Dell'Aquila: 1988: 4).²⁴⁶ Alfonsín was finally forced to reject this heterodox stabilisation plan, paving the way for the return of privatisation onto the Argentine policy agenda.

The government began to realise that it could not continue to service the external debt, let alone subsidise domestic capital, without a considerable reduction of public sector spending (Azpiazu & Schorr, 2001: 5). As had happened in Brazil under Sarney, Alfonsín began to consider privatisation, not as a result of any ideological about-turn, but simply as a response to fiscal imperatives. Privatisation had been initially considered in 1984, when Alfonsín created a commission whose purpose was to analyse and report upon the financial health of all existing state-owned enterprises, and recommend which state companies could be divested through the re-activation of Law 22,177.²⁴⁷ A concerted effort to privatise state enterprises only occurred when Sourrouille launched the 'Austral Stabilisation Plan' in June 1985 to combat the spectre of hyperinflation (Molano, 1997: 91). The Austral Plan was essentially 'an anti-inflationary programme aimed at economic reform' (Manzetti & Dell'Aquila: 1988: 5). Following the signing of a letter of intent with the IMF in July 1985, the third and fourth phases of the programme contained a number of structural reforms, (Manzetti & Dell'Aquila: 1988: 8-15). Privatisation was integral to these proposed reforms. As part of this process, the *Directorio de Empresas Públicas* (DEP) was created, in order to divest Argentina of burdensome companies, enabling debt repayments and reducing public sector deficits (González-Fraga, 1991: 78; Goldstein, 1998: 65). The Ministry of Growth was also established in order to provide incentives for private firms to invest in areas traditionally monopolised by state enterprises, such as oil, ports and natural gas (Manzetti & Dell'Aquila: 1988:

²⁴⁶ In 1985, inflation was running at 29.5 per cent for April, 25.1 per cent for May, and 30.5 per cent in June (see Manzetti & Dell'Aquila: 1988: 3).

²⁴⁷ Decreto No. 414/84 - available at: <http://mepriv.mecon.gov.ar/Normas/414-84.htm>.

15). Initially, the programme was slow to start and in 1988, only *Austral*, a small domestic airline carrier, was sold for US\$28 million.²⁴⁸

By 1988, Argentina had plunged into a deep recession, with the fiscal deficit accounting for nearly 21.8 per cent of GDP, the balance of payments deficit widening to US\$1.4 billion and interest payments on commercial bank debt going into arrears (Molano, 1997: 92-94), and in April 1988, the government had no choice but to suspend all service payments on debt to creditors (Azpiazu & Schorr, 2001: 4). In this economic climate, the government was desperate for short-term revenue, so it decided to carry out two major privatisations: the state telephone company ENTel, and the state airline *Aerolíneas Argentinas*. The sale of both it was hoped, would ease fiscal pressure (Molano, 1997: 94).

However, when these plans were publicly announced, just as had happened during the de Hoz era, a large anti-privatisation coalition began to mobilise against the sales. Alfonsín sent his privatisation package to Congress on January 2nd 1989 and fearing that it would be rejected, opened the topic up for public debate. Public support for the sale of ENTel jumped to 85 per cent, but the Peronist bloc, allied with the anti-privatisation coalition and under the leadership of Eduardo Menem, decided to reject all three of the proposed privatisation programmes (Treisman, 2003: 95; Corrales, 1998: 34; Molano, 1997: 99).²⁴⁹ Alfonsín's attempts at privatisation were stymied before they could even properly begin and by the end of Alfonsín's tenure, only four state enterprises had actually been transferred to private hands (Treisman, 2003: 95).

There are a number of important points to note about both these early attempts at privatisation in Argentina. Firstly, as occurred in Brazil under Sarney, the initial decision to move towards privatisation under Alfonsín was not the product of an ideological re-evaluation, but rather was brought about due to fiscal constraints and the pressure to control inflation. As in Brazil (see Pinheiro, 2000), early privatisation attempts were an integral part of stabilisation plans, and later privatisations in Argentina were to have 'the primary objective of price stabilisation' (Machinea *et al.* 2003: 4).

²⁴⁸ World Bank Privatisation Database, 2007

²⁴⁹ In September 1987, a general election saw the Peronists gain substantially at the expense of the Radicals (see Manzetti & Dell'Aquila, 1988: 21).

Secondly, while the initial privatisation forays in Brazil were not subject to external pressure, in Argentina they were heavily influenced by the International Monetary Fund. The enormous levels of Argentine debt forced Alfonsín to turn to the IMF on a number of occasions. After the failure of the Austral Plan to rectify the country's economic problems, Alfonsín and Sourouille were forced to sign a new letter of intent with the IMF in 1985 that ultimately led to the decision to implement structural reforms including privatisation and the creation of the *Directorio de Empresas Públicas* (Manzetti & Dell'Aquila: 1988, 15).

Thirdly, privatisations during the military period were essentially halted as a result of a large and mobilised anti-privatisation coalition and during Alfonsín's tenure, this coalition, consisting of the military, business leaders, members of the Radical party and most importantly, labour allied with the Peronists, once again managed to prevent any privatisation programmes from taking root (Goldstein, 1998; Treisman, 2003; Murillo, 2001; Molano, 1997; Corrales, 1998). Alfonsín alienated the military by instigating tribunals to punish military officers guilty of human rights abuses during the 'dirty war' (Manzetti, 1993: 188). This coupled with defence budget cuts ensured that the military were unwilling to support any of Alfonsín's initiatives (Goldstein, 1998: 65).²⁵⁰ Opposition to Alfonsín's plans came not only from the rent-seeking *patria contratistas* or *capitanes de la industria* who benefited enormously from lucrative contracts with the public sector, but also from other areas of domestic industry, who feared that privatised state firms would provide unfair competition to their own businesses (Corrales, 1998: 30; Treisman, 2003: 95). One effective tactic they employed to prevent privatisations was to simply refuse to buy the firms that were up for sale (Corrales, 1998: 28). Large industrialists, in the form of the Industrial Union of Argentina (UIA) together with the *Grupo de los 9* refused to support the government's privatisation initiatives (Goldstein, 1998: 68).

The most virulent opposition to privatisation came from labour allied with the Peronist opposition. Alfonsín had attempted to dismantle the traditional link between the Peronists and the *Confederación General del Trabajo* (General Worker's Union – CGT), and this initiative galvanised the unions and Peronists into action (Molano,

²⁵⁰ In April 1987, Lieutenant Colonel Rico led the first of a series of military coups that attempted to overthrow the government. The main motivation of these coups was to secure a general amnesty for the military from prosecution (Molano, 1997: 97).

1997: 89).²⁵¹ While the Peronists had cooperated with the Radicals on a number of legislative issues, they now began to systematically oppose all Radical legislation on privatisation. At the same time, the unions launched thirteen paralysing general strikes and called more than 2,300 smaller strikes between 1984 and 1988, leading to a total loss of 95 million days (Goldstein, 1998: 65). Meanwhile, the Peronist-controlled Senate ensured that every piece of legislation relating to privatisation introduced by Alfonsín was defeated (Molano, 1997: 98). This large anti-privatisation coalition ensured that ‘most of Alfonsín’s privatisation deals died in Congress, at the negotiating table, or in the streets’ (Corrales, 1998: 34).

5.4 The Election of Carlos Menem

It was not until the election of Dr. Carlos Saúl Menem of the Peronist Party as President on May 15th 1989, that privatisation finally became a standard policy instrument in Argentina. Menem set out to ‘privatise everything that was privatisable’ (Corrales, 1998: 27), and under Menem’s leadership, ‘a massive privatisation programme virtually reversed the tide of state ownership that had overrun the country throughout the twentieth century’ (Llanos, 2001: 74). Menem had campaigned in the 1989 election on traditional Peronist doctrine, emphasising economic nationalism and strong state regulation (Manzetti, 1999: 71).²⁵² While Menem avoided concrete details concerning his policy, his Peronist rhetoric appealed to the large working class and members of the middle class (Manzetti, 1999: 71), and on polling day the Peronists not only gained the presidency but also control of both houses of Congress (Molano, 1997: 100).

Argentina during the 1989 election campaign was a country in the midst of an economic depression, with high interest rates and a large external debt. By July, Argentina was in the grip of hyperinflation with the inflation rate running at almost 200 per cent per month, prompting a serious social crisis and frequent food riots (Goldstein, 1998: 66; Menin & Cerdá, 2006: 11; Treisman, 2003: 94). It now appeared as if the Alfonsín administration was facing the possibility of another military coup, without the resources to withstand it (Molano, 1997: 100). Alfonsín, realising his government could not survive and continue to protect the nascent

²⁵¹ This move also provided a catalyst for the two factions of the CGT to unite: the CGT-Azopardo headed by Jorge Triaca and CGT-RA headed by Saul Ubaldini. See Molano (1997) or Murillo (2001).

²⁵² Menem had previously been the three time governor of La Rioja, one of Argentina’s most impoverished regions (Manzetti, 1999: 71).

democracy, offered to resign and on July 9th 1989, five months before the constitutionally mandated date of succession (December 10th), Carlos Menem assumed power (Menin & Cerdá, 2006: 11). Menem, assuming power in the midst of a veritable economic meltdown, called for the resignation of Congress and new elections, but the Radicals, fearing a humiliating electoral defeat, refused (Molano, 1997: 100). In order to convince Menem to assume power early, the Radicals, who still held a plurality in the lower house, agreed to support any legislation presented by Menem in the remaining six months of the Congressional term, including any legislation that would confer special decree powers on the President in order to deal with the economic crisis (Treisman, 2003: 98; Molano, 1997: 100). It was this extraordinary deal that granted Menem the enormous executive power to pursue his policy of privatisation.

Once in power, ‘in the most stunning policy reversal in Argentina’s modern history, Menem reached the conclusion that turning the economy around no longer rested in the traditional populist, nationalistic, redistributive approach. The key to success was instead the establishment of a free-market economy...worthy of Thatcher and Reagan’s applause’ (Manzetti, 1999: 71). Menem began to move towards market-friendly reforms, with the intention of rapidly combating hyperinflation and to restrain the exorbitance of the public accounts (Menin & Cerdá, 2006: 11).²⁵³ The first indication of Menem’s economic direction came with the appointment of Miguel Roig, a senior executive from the powerful *Bunge y Born* food export conglomerate as Minister of the Economy, (Molano, 1997: 2) and the incorporation of several members of the market-friendly *Unión del Centro Democrático* (Union of the Democratic Centre - UCEDE) into his administration (Murillo, 2001: 135).²⁵⁴ Menem was desperate to gain credibility in the eyes of the business community, particularly considering his Peronist past, and one of the main methods he utilised to signal his commitment to a reformist course was through privatisation (Gerchunoff *et al.* 2003: 8; Azpiazu & Schorr, 2001: 12).

Forty-six days after assuming office, Menem initiated his privatisation programme by demanding approval from Congress for the State Reform Law and the Law of Economic Emergency (Manzetti, 1999: 72). Both these laws were highly

²⁵³ For an excellent discussion on Menem’s policy reversal, see Stokes (2001).

²⁵⁴ The *Bunge y Born* corporation were traditionally derided by Peronists as ‘local puppets of the oligarchy’ (Goldstein, 1998: 68).

significant as they concentrated power in the hands of the Executive and placed the Executive, rather than Congress, in complete control of the process of privatisation (Llanos, 1998: 749, 753). The Law of Economic Emergency was directed at the cleansing of the public sector, specifically by conferring upon the President the right to suspend industrial promotion subsidies and tax breaks (Llanos, 2001: 76; Manzetti, 1999: 72). The State Reform Law on the other hand, was concerned with privatisation, and Article 1 declared a state of emergency in the public sector, while the appendix also contained a list of state enterprises, which the Executive would have full power to privatise immediately.²⁵⁵ Most importantly however, Articles 15 and 18 granted to the Executive a number of legislative functions that ultimately 'delegated to the Executive the power to privatise through decrees, and unlimited discretion on the means and criteria to be implemented' (Manzetti, 1999: 72).

The State Reform Law ensured that privatisation policy in Argentina would be initiated by executive decrees rather than law, enabling Menem to implement privatisation 'without major institutional interference' (Llanos, 2001: 76). Because of the economic conditions of the time which led to the agreement reached between Menem and the Radicals, Congress through the State Reform Law and the Law of Economic Emergency, delegated to the Executive an inordinate amount of power that replaced law with delegated executive decrees (Llanos, 2001: 71). Within two months of taking office, 'Menem had established the legal instruments for expediting privatisation without any independent oversight' (Manzetti, 1999: 72-73).²⁵⁶

The first stage of Menem's privatisation programme was launched in conjunction with the IMF sanctioned Bonex stabilisation plan (Molano, 1997: 81), beginning with the sale of ENTel, and followed by *Aerolíneas Argentinas*, a number of YPF (state oil company) drilling operations and refineries, 10,000 kilometres of roads, six radio stations, two television channels, a chemical company, and a food and detergent manufacturer.²⁵⁷ Menem was able to achieve all this as a result of the decree power delegated to him by Congress (Rubio & Goretti, 1996: 448).

In order to combat the very real threat of hyper-inflation, in 1991, the new Economy Minister, Domingo Cavallo, launched the Convertibility plan which, based upon stringent fiscal control, initiated a range of structural reforms and fixed the

²⁵⁵ Ley 23,696, Available at <http://mepriv.mecon.gov.ar/Normas/23696.htm>

²⁵⁶ At the time of the vote for these laws, some wary Peronists and Radicals did refuse to attend (see Manzetti, 1999: 72).

²⁵⁷ World Bank Privatisation Database, 2007

value of one dollar at the value of one Argentine peso (Manzetti, 1999: 73; Goldstein, 1998: 62; Murillo, 2001: 135).²⁵⁸ In conjunction with this new stabilisation plan, the second stage of Menem's privatisation programme began (Llanos, 2001: 77),²⁵⁹ and in this respect 'privatisation was no longer an ad hoc policy but was incorporated as an integral part of the administration's economic plan' (Manzetti, 1999: 73). Cavallo made explicit his intention to depart from the first stage through more rigorous planning of privatisations, improvements in the actual procedures and also to increase legal guarantees for investors (Llanos, 2001: 77). Also during this stage, Executive-Congress relations changed, mainly due to the fact that the Radicals now returned to the traditional role of opposition (Llanos, 1998: 755), and the government wished to expand the privatisation of state enterprises beyond the list mandated for in the appendix of the State Reform Law (Llanos, 2001: 78).

During this period Menem submitted ten new privatisation bills to Congress widening the State Reform Law to a number of new areas, and Congress in an effort to re-assert their authority, attempted to amend all of these bills during their passage through the house (Llanos, 1998: 755).²⁶⁰ However due to the concentration of executive power, Menem still had the ability to re-amend these bills according to his wishes through the use of the partial veto (see Table 5.3). Nonetheless, this particular period of privatisation was characterised by 'intense negotiations' with legislators (Treisman, 2003: 98-99). However, these ten bills only served to widen the existing State Reform Law to incorporate other potential areas of privatisation, and 'even under Cavallo, privatisations were implemented via the so-called decrees of necessity and urgency' (Manzetti, 1999: 92). By the end of his first term in office in 1995, Menem had sold nearly 140 state enterprises, generating US\$18,446 million in revenue, in diverse areas that included the majority of the state oil industry, all passenger and cargo rail operators, the entire gas industry, the principal generation, distribution and transmission facilities of the electricity industry, the

²⁵⁸ The Convertibility Plan had considerable success in reducing inflation. Inflation, which had peaked at 4,923 per cent in 1989, had dropped to 3.7 per cent by 1994. Added to this, in 1992 Argentina had a fiscal surplus for the first time in decades (see Manzetti, 1999: 74).

²⁵⁹ Domingo Cavallo had previously been Central Bank Governor in 1982, and he had written a best-selling book in 1985 *Volver a Crecer*, which advocated a reduction in the size of the public sector (Goldstein, 1998: 66).

²⁶⁰ The Peronists remained loyal to Menem and agreement was usually made with some of the smaller parties, and only twice with the Radicals (Llanos, 2001: 82).

telecommunications industry, the national airlines, the major state petrochemical and chemical plants, the ports, radio and television channels and a chunk of the national pension system (Azpiazu & Schorr, 2001: 12; Murillo, 2001: 142).

Table 5.3 - Privatisation Bills in Menem's First Term

Privatisation Bills	Approval	Congressional Amendment	Partial Veto
Ministry of Defence Assets	Yes	Yes	No
AHZ (defence)	Yes	Yes	No
Electricity Industry	Yes	Yes	Yes
Gas Industry	Yes	Yes	Yes
YPF (oil industry)	Yes	Yes	Yes
Cattle Market	Decree	-----	-----
Ports	Yes	Yes	Yes
Banks	Yes	Yes	No
Pensions	Yes	Yes	Yes
YPF (2 nd round)	Yes	Yes	No

Source: Llanos (2001: 86; 1998: 750)

Following a number of secret meetings between Raul Alfonsín and Menem in November 1993, the pair signed an agreement, the Pact of Olivos, in which Menem managed to secure Alfonsín's backing to allow Menem run for a second consecutive term. In return, Menem agreed to a number of reforms that 'Alfonsín felt would limit the power of the president, benefit the UCR, and restore Alfonsín to a more prominent role in Argentine politics' (Jones, 1997: 291). So, as a result of the 1994 amendment to the constitution, Menem was now free to run for a second consecutive term in the 1995 elections, and the success of the Convertibility Plan in taming inflation had endeared the electorate to Menem's economic package. Furthermore, in 1994 the Tequila Effect and the general fear of instability 'helped Menem to get re-elected in 1995, under the idea that the President and his team were the best pilots in stormy waters' and Menem won the Presidential election with nearly 48 per cent of the vote (Bambaci *et al.* 2002: 76).²⁶¹ Added to this, in the legislative elections, the Peronists secured a majority in both the lower and upper houses, but this advantage was offset by an increase in conflict within the Peronists themselves as internal

²⁶¹ The Tequila Effect was the name given to the devaluation of currencies in the Southern Cone as a result of the crisis in Mexico in 1994, following a sudden devaluation of the peso in the early days of the Presidency of Ernesto Zedillo.

competition to secure the candidate for the next Presidential election in 1999 began (Llanos, 2001: 92).²⁶²

Once elected, Menem continued his policy of privatisation, and so began the third stage in this process, a stage that was characterised by increased conflict between the Executive and the Legislature (Llanos, 1998: 759). As in the second stage, Menem initially attempted a more consensual approach when implementing privatisations and submitted five bills to that end to Congress during this period (Llanos, 1998: 759-765; Llanos, 2001: 92-96). As can be seen from Table 5.4 however, Congress was less willing to support Menem's privatisation programme and actually rejected three of the proposed five bills and in response to this lack of support, Menem simply bypassed Congress by exercising his Executive power. Even in those cases where the legislature accepted the proposed bills, but with amendments, Menem used his partial veto power in order to bring them back into line with his own policy. Consequently, due to the hostility of Congress towards his reforms, particularly after the 1997 legislative elections, in this stage of privatisation, Menem increasingly relied upon his decree powers (Llanos, 1998: 765).

During Menem's second term in office, he privatised a further thirty-two state enterprises, generating revenue of nearly US\$23 billion and by the time Menem finally left office in 1999, he had managed to sell 165 state-owned enterprises, generating over US\$40 billion in revenue, earning nearly US\$15 billion in foreign exchange, and transferring US\$25 billion to both internal and external debt titles (Azpiazu & Schorr, 2001: 13).²⁶³ Menem, within a very short period of time, had privatised nearly 90 per cent of all state enterprises in Argentina (Tresiman, 2003: 94).

Table 5.4 – Privatisation Bills in Menem's Second Term

Privatisation Bills	Approval	Congressional Amendment	Partial Veto
Post Office	No (delegated decree)	----	----
Nuclear Plants	Yes	Yes	Yes
Airports	No (necessity and urgency decree)	----	----
Yacyretá dam	No (administrative decree)	----	----
Mortgage Bank	Yes	Yes	Yes

Source: Llanos (2001: 93)

²⁶² The majority the Peronists enjoyed, only lasted until the 1997 legislative elections when Frepaso allied with the Radicals shifted the balance of power in the lower house towards the opposition (Llanos, 2001: 81).

²⁶³ World Bank Privatisation Database, 2007

One of the major factors that enabled Menem to implement privatisation so quickly and so effectively, was the 1989 hyperinflation crisis, which ‘helped forge a political agreement between the two major parties’ (Bambaci *et al.*, 2002: 80). This agreement led to the delegation of significant powers to the Executive, which Menem utilised cleverly in order to circumnavigate political opposition in the early stages of privatisation (Bambaci *et al.*, 2002: 80; Rubio & Goretti, 1996: 447-448). In the context of this crisis and the debilitating prospect of continued hyperinflation, privatisation was presented as an integral part to the solution of this problem (Gerchunoff & Cánovas, 1995: 483; Gerchunoff *et al.* 2003: 8; Machinea *et al.* 2003: 4). Privatisation was also utilised as a signal to international capital that Menem had left his Peronist past behind and was committed to a reformist course (Gerchunoff *et al.* 2003: 8; Azpiazu & Schorr, 2001: 12).

Secondly, the role of the international financial institutions in placing pressure on the government to privatise is also clearly evident. Menem, in contrast to Alfonsín’s heterodox stabilisation programme, launched an IMF-sanctioned plan in the form of the *Reforma del Estado* and within a month, following the suspension of all loans to Argentina under Alfonsín, the IMF approved a new US\$150 million loan package (Molano, 1997: 96). For the IFI’s, privatisation permitted the re-establishment of service payments on the country’s external debt, and as such reflected ‘the interest of external creditors’ (Azpiazu & Schorr, 2001: 10). Privatisation was also an integral part of the Brady Plan negotiations, which facilitated Argentina’s return to international finance (Azpiazu & Basualdo, 2004: 3; Menin & Cerdá, 2006: 8).²⁶⁴ As such, ‘the multilateral lending agencies played a significant role in guiding Argentina toward privatisation’ (Molano, 1997: 96).

Thirdly, Menem, like Martínez de Hoz and Alfonsín before him, also faced strong opposition to privatisation from a number of important actors, but Menem cleverly used privatisation, through patronage, negotiation and sometimes force, as a means to neutralise this opposition (Azpiazu & Basualdo, 2004: 2; Gerchunoff *et al.* 2003: 16; Etchemendy, 2001: 5). As Molano (1997: 101) argues: ‘While privatisation was an end in itself to the other national executives in the Southern Cone and the Alfonsín administration, the Menem administration used privatisation as a means to

²⁶⁴ The Brady Plan was the brainchild of US Treasury Secretary Nicholas Brady in 1989. It was an emergency economic package that provided debt relief to debtor countries, which ‘showed concrete efforts towards market-orientated reform policies’ (see Manzetti, 1999: 142).

garner the approval of key interest groups.’ Etchemendy’s (2001: 1-2) supports this view, arguing that market transformation in Argentina was ‘founded on coalitions cemented in more or less formal bargains with a variety of sectoral interests anchored in the old model.’

In order to overcome the opposition of the *patria contratistas*, who had benefited enormously as a result of lucrative contracts with the public sector, and opposition from other rent-seeking indigenous industry, Menem began to involve them in the privatisations on highly preferential terms (Treisman, 2003: 97).²⁶⁵ Suppliers of state enterprises were given preference in their sale, with the state often assuming the enterprise’s debt, and in many cases oligopolistic or monopolistic conditions were preserved for years (Treisman, 2003: 97). These benefits convinced the *patrias* to part with their lucrative service contracts in exchange for the opportunity to become the new owners of cheap state enterprises (Treisman, 2003: 97).

In the case of the military, shortly after his inauguration, Menem issued over 200 pardons to military officers and personnel who had been convicted of human rights abuses under Alfonsín (Molano, 1997: 103; Treisman, 2003: 97). When he announced the privatisation of the national defence industries (DGFM), he promised the military that they would benefit from these sales, primarily in the form of increases in officers’ salaries and also through the purchase of much-needed equipment (Molano, 1997: 103; Treisman, 2003: 97). The military, which had provided such strong opposition to privatisation under Martínez de Hoz and Alfonsín, soon fell in behind Menem’s reforms.

While individual legislators opposed Menem’s reform policies, particularly privatisation, he actually received ‘surprisingly little intra-party resistance’ (Levitsky, 2003: 149).²⁶⁶ Those who did oppose Menem were ‘compensated’ through the windfall generated by the Convertibility Law and provincial bosses were provided with pork and excused from replicating the economic reforms being carried out at the national level (Levitsky, 2003: 155-156; Treisman, 2003: 98-99). Levitsky (2003) convincingly argues that Peronist acquiescence to the Menem reforms is best

²⁶⁵ The *patria contratistas* continued to oppose privatisation for the first two years of Menem’s Presidency. Supposedly, during the first months of the administration, they would frantically barge into Cabinet meetings and demand that privatisations be halted (see Corrales, 1998: 27).

²⁶⁶ For an excellent analysis of how Menem managed to receive his party support for neoliberal reforms, see Levitsky (2003).

understood within the context of the PJ party structure. Due to the lack of secure tenure patterns and routinised career paths, PJ leaders, wishing to preserve or advance their careers, have a strong incentive to 'bandwagon' with the winning side and PJ party leaders in the non-Menem camp opportunistically established alliances with Menem despite their opposition to his liberalising reforms. The weakly institutionalised nature of the PJ and PJ leadership bodies meant that internal critics were largely unable to use party vehicles to critique or question Menem's neoliberal strategy (see Levitsky, 2003: 144-185) and as a result, there was only a minor splinter in the party, with eight legislators defecting who would ultimately join Frepaso (Murillo, 2001: 137).

The last group with the potential to provide major opposition to privatisation in Argentina was labour, but Menem, in a manner similar to both Franco and Cardoso in Brazil (see chapter three), utilised both carrot and stick tactics in order to neutralise this opposition. The *Confederación General del Trabajo* (General Worker's Union – CGT) was the 'most prominent labour federation and a pillar of political power in Argentina' and since the time of Perón, it had also become a bastion of Peronist power (Molano, 1907: 89). However, privatisation caused a division within the CGT between October 1989 and March 1992, and the government manipulated the competition among factions by rewarding the loyal segment of the union, CGT-San Martín led by Saul Ubaldini, in order to induce defections from the rebel CGT-Azopardo, led by Jorge Triaca (Murillo, 2001: 142-150).²⁶⁷ This split in the union, coupled with depressed labour market conditions particularly in manufacturing, significantly weakened the bargaining position of the unions (Goldstein, 1998: 67). On the political side, Menem dismantled the labour arm of the PJ, the '62 Organisations' and abandoned the traditional, but informal mechanism of placing union members on the party lists, the *tercio*, and without these institutional channels, union influence in the party quickly eroded (Levitsky, 2003: 24-25). This weak position and lack of patronage for the CGT-Azopardo led to its leaders modifying their demands and they had slowly moved towards the pro-privatisation position of the CGT-San Martín by the end of 1991 (Murillo, 2001: 151).

²⁶⁷ A small group of unions did split from the CGT in order to create the Congress of Argentine Workers (CTA), which eventually participated in the creation of Frepaso (see Murillo, 2001: 137).

Menem also employed a number of strong-arm tactics to neutralise labour. When FOETRA, the only major union associated with the Radicals, called a strike to protest against the proposed privatisation of ENTel, Menem dissolved the union by force and its headquarters were physically taken over by the police (Goldstein, 1998: 67). When workers from the railway and oil industries went on strike, 'Menem fired many of them, prosecuted ringleaders, and even threatened at one point to call out the military' (Treisman, 2003: 96). But the carrot was also evident. During the election, Saul Ubaldini joined Menem's team, while after the reunification of the CGT, Jorge Triaca was appointed as Minister of Labour, and Julio Gullian, leader of the telephone workers, was appointed as Secretary of Communications (Molano, 1997: 89). In return for their support, the unions were also allowed to maintain their main sources of power: the regulation of collective bargaining and *Obras Sociales* (Bambaci *et al.*, 2002: 82).²⁶⁸ Most importantly however, as the BNDES had in Brazil, Menem introduced a scheme whereby the workers could participate in purchasing some of the newly privatised enterprises. The *Programa de Propiedad Participada* (PPP) enabled workers to buy up to ten per cent of the shares in privatised firms, and this scheme also provided a further incentive to the unions, as workers had to nominate a legal entity to act as their representative in these transactions (Gerchunoff *et al.* 2003: 16). Because of these tactics, and because of the partisan loyalty of the unions to a Peronist President, Menem managed to successfully neutralise the opposition of labour to privatisation in Argentina (Murillo, 2001: 149-150).

The final and most important to note, is the institutional context within which privatisation occurred under Menem. In Brazil, privatisation was carried out within the context of a comprehensive legal and institutional framework. In Argentina in contrast, privatisation was carried out under the auspices of the State Reform Law, which due to the severity of the economic problems at this time, delegated a large amount of power to the Executive (Bambaci *et al.*, 2002: 80; Rubio & Goretti, 1996: 447-448). This created a concentration of power in the hands of the Executive, and privatisation was carried out nearly entirely at the discretion of the President, and primarily implemented by means of executive power in the form of delegated

²⁶⁸ *Obras Sociales* are union-administered welfare funds (Bambaci *et al.*, 2002: 82).

decrees, decrees of urgency and necessity and administrative decrees, bypassing Congress and all other state institutions.

The entire Menem administration 'is characterised, from an institutional perspective, by a concentration of power in the hands of the Executive' (Rubio & Goretti, 1996: 443). Between 1853 and July 1989, only 35 decrees of necessity and urgency were ever issued by Argentine Presidents, but between July 1989 and August 1994, Menem issued 336 decrees of urgency and necessity in order to implement his reforms (Rubio & Goretti, 1996: 444, 451). As such, the policy of privatisation in Argentina remained very much in the hands of the President and was a product of the high-level of Executive power in this state. Menem could not even be checked by the courts. At the beginning of Menem's Presidency a law was introduced that increased the members of the Supreme Court from five to nine, and as a result of this move, Menem was able to appoint his political allies to the bench (Helmke, 2005: 144; Bambaci *et al.*, 2002: 78-79; Manzetti, 1999: 93). This favourable disposition of the Supreme Court was clearly evident when, in 1990, Deputy Moisés Fontela asked a federal judge to halt the sale of *Aerolíneas Argentinas*, due to the questionable legality of the decree used to begin this privatisation. The Supreme Court, in an unprecedented move called *per saltum* procedure, assumed jurisdiction over this case, and 'within a few minutes...ruled against Fontela's request' (Helmke, 2005: 147-148; Manzetti, 1999: 93).²⁶⁹ The early and quick privatisation of some national symbols (telecoms, gas, air transport and highways) ensured that these newly privatised industries were left with weak regulation (Murillo & Finchelstein, 2004: 140; Bambaci *et al.*, 2002: 77; Goldstein, 1998: 69-70).

Therefore, in contrast to events in Brazil, privatisation was not carried within a comprehensive legal and institutional framework, but rather remained a function of executive discretion, nor was this policy delegated to an independent body, but remained in the hands of the Executive, and the creation of regulators to guarantee investor security in Brazil, was in many cases, sorely lacking in Argentina.

²⁶⁹ In the *Peralta* (1990) decision the Court also upheld the government's controversial Bonex stabilisation plan freezing private savings accounts (see Helmke, 2005: 148).

5.5 The 2001 Crisis

By 1999, the rigidity of the Convertibility Plan had left the government with few reserves in the event of hard times and following the 1995 Mexico crisis and subsequent Tequila effect, this lack of reserves meant the government could do little to soften the loss of investor confidence in developing world markets, a situation exacerbated by the Asian Crisis of 1997 and the devaluation of the Brazilian Real in 1999 (Grugel & Pia Riggirozzi, 2007: 8-9). The national debt, denominated in dollars, tripled between 1992 and 1999, but Argentina, hailed as an example of free market reforms, had access to easy credit to finance the widening fiscal deficit (Ocampo, 2003: 22-25). In the midst of rising dissatisfaction with growing levels of poverty and stagnant growth, Fernando de la Rúa, of the *Alianza por el Trabajo, la Justicia, y la Educación*²⁷⁰ won the 1999 Presidential election (Grugel & Pia Riggirozzi, 2007: 9), but once in power, was faced with the prospect of cutting government spending in the midst of a depression in order to tackle the budget deficit (Bambaci *et al.* 2002: 86).

In early 2000, the government began implementing spending cuts and tax increases, but the increases inadvertently drove the economy further into stagnation (Saxton, 2003: 10). De la Rúa brought Cavallo back as Minister of Finance in March 2001 (Grugel & Pia Riggirozzi, 2007: 9), but Cavallo was able to do little to solve the economic problems. As Bambaci *et al.* (2002: 86) comment:

He fiddled with tariffs and, fatally, with the currency board itself, so that the peso was pegged for exporters half to the dollar, half to the euro. This was, in itself, a good idea, but the timing was disastrous. By raising the idea of devaluation, it spooked foreign investors. They demanded a higher risk premium for holding Argentine bonds, driving up interest rates and deepening the recession.

Amidst a general lack of confidence in the economy, a run to the banks was triggered (Bambaci *et al.* 2002: 87) and by late 2001, capital flight had reached 6 percent of GDP, and the government found itself unable to meet debt payments (Kaminsky *et al.*, 2003: 63). On November 30th, \$1.3 billion fled the banks and the central bank's net reserves slumped by \$1.7 billion.²⁷¹ The government effectively froze bank accounts on December 1st in a last ditch effort to prevent money leaving the banking

²⁷⁰ An alliance of the Radical Party and Frepaso

²⁷¹ The Economist, December 8th, 2001.

system. In November 2001, the IMF withdrew its support for the government and the capital flight continued at an alarming rate (Grugel & Pia Riggirozzi, 2007: 9). The crisis spilt out into the streets and 20 people were killed in clashes with the government, eventually forcing Cavallo to resign, followed closely by De la Rúa (Grugel & Pia Riggirozzi, 2007: 9). During this period, De la Rúa continued to privatise, but due to the fact that the major and most valuable state companies had previously been sold, the generated revenues could do little to prevent the growing budget deficit. During this period, De la Rúa sold four railways stations, the water service for Buenos Aires and Neuquen Airport.²⁷²

It was not until Peronist Eduardo Duhalde assumed office on January 1st 2002 that the government managed to reassert some control over the economy (Menin & Cerdá, 2006: 22; Grugel & Pia Riggirozzi, 2007: 10).²⁷³ On January 6th Duhalde introduced the law of *Emergencia Pública y Reforma del Regimen Cambiario*,²⁷⁴ which unpegged the peso from the dollar, triggering a burst of inflation (Azpiazu & Basualdo, 2004; 40). Following intense negotiations, a 70 per cent reduction in debt to private creditors was agreed upon, and the IMF consented to a US\$3 billion loan deal in January 2003 (Grugel & Pia Riggirozzi, 2007: 13). Once the economy began to stabilise, Duhalde resumed privatisations in early 2003, mainly in the area of infrastructure. Duhalde, mainly in an effort to keep tariff prices low to combat inflation, through Decree 293 established a formal procedure, the *Comisión de Renegociación*, for the renegotiation of contracts with companies who had purchased privatised public services (Menin & Cerdá, 2006: 22). This was a clear example of how the policy of privatisation, and investor security, remained very much in the hands of the Executive.

By 2003, real GDP had fallen by 28 per cent, real wages by 23.7 per cent, while unemployment had increased to 23.6 per cent. In 2002, the poverty rate doubled to 60 per cent, while growth contracted by 4.4 per cent, setting the scene for the 2003 election and the victory of the left-wing candidate, Néstor Kirchner.²⁷⁵

²⁷² World Bank Privatisation Database 2007

²⁷³ Before Duhalde became President, De la Rúa was succeeded by Ramón Puerta, who was in office just two days when succeeded by Adolfo Saá. Saá initially declared a debt moratorium, but a few days later Argentina announced the biggest default in history. Saá was in office for only one week before he was replaced by Eduardo Camaño, who lasted just three days.

²⁷⁴ Law 25,561

²⁷⁵ The Economic Intelligence Unit – Country Report: Argentina, January 2002

5.6 The Legacy of Privatisation in Argentina

By the time Kirchner won the Presidential election in 2003, Argentina, roughly within the space of a decade, had divested itself of approximately 180 state enterprises and generated over US\$44 billion in revenue. The entire telecommunications, gas, oil, steel and railway sectors, the largest ports, the main highways, the state television and radio stations, the majority of the electricity distribution and generation sectors, practically all the former state-owned enterprises in the manufacturing sector, and some water and sanitation services, not to mention the vast majority of the military monolith DGFM, had been transferred to private control. Importantly however, unlike Brazil, where privatisation occurred within the context of a comprehensive legal and institutional framework, privatisation in Argentina primarily occurred at the discretion of the Executive. This policy had not been delegated to an independent body capable of operating freely from political interference, and the haste with which early privatisations were carried out meant that guarantees of investor security were lacking, and regulation of some of the newly privatised industries remained weak. Menem had neutralised opposition to privatisation from the *patria contratistas*, Peronists, the military and labour by building a pro-privatisation coalition through patronage, force, and pork-barrel.

By 2003, when Kirchner came to power, some 5 to 10 per cent of state-owned enterprises still remained, including a small number of banks, and some former military companies, not to mention service provision in terms of water, sanitation and toll roads in different parts of the country, coupled with the large number of enterprises that still remained in state hands at the provincial level. Nonetheless, Menem's privatisation drive, within a single decade, had completely altered the role of the Argentine state, and this initiative remains one of the largest and fastest privatisation programmes ever instigated, one that completely redefined the nature of the Argentine economy.

Chapter Six – Privatisation under Kirchner

The 2003 elections in Argentina were held as the country was gradually emerging from the worst economic crisis it had suffered in recent memory. Amidst fears of voter apathy and abstention, the little-known Néstor Kirchner of the *Frente Para la Victoria* wing of the *Partido Justicialista* won the Presidential election. Kirchner's platform for the 2003 election was based upon a harsh critique of the market-friendly policies implemented in Argentina in the 1990s under Menem, and advocated a greater role for the state in the economy and a rejection of privatisations (Sanchez, 2005: 462-463). Kirchner promised change and began his acceptance speech by claiming that 'a new era is about to begin.'²⁷⁶ The previous chapter documented the extent and size of the Argentine privatisation programme, and it remained to be seen whether Kirchner could actually introduce a new direction for this particular policy.

This chapter therefore, is the analysis of privatisation policy during Kirchner's Presidency. It will attempt to determine if Kirchner managed to completely halt privatisation once he was in power. It is divided into two main parts. The first part takes the form of a narrative and briefly outlines the 2003 election. This section will establish the motivations and preferences of Kirchner's government. The second section of the narrative actually examines the policy of privatisation once Kirchner is in power. The second part of this chapter is the analysis, and this analysis is grouped around the independent variables identified in chapter two. The final section will present the conclusion.

The Narrative

6.1 The 2003 Election

In December of 2001, the first candidates for the Presidential election in 2003 began to emerge amidst growing social unrest, voter apathy and anger towards the political classes (Vives Segl, 2006: 112; Sanchez, 2005: 461).²⁷⁷ The Peronist *Partido Justicialista* (PJ) was highly fragmented and appeared as if it would not unite behind a single leader for the elections. The former governor of Buenos Aires, Carlos Ruckauff, the governor of Córdoba, José Manuel de la Sota, the former governor of Santa Fe, Carlos Reutemann, former President, Carlos Menem, short-term President,

²⁷⁶ The Financial Times, May 15th, 2003.

²⁷⁷ This anger towards politicians, and political parties in general, was captured by the now famous slogan, 'Que se vayan todos (get them all out).' See Vargas Llosa (2004:72).

Adolfo Rodríguez Saá, and the governor of Santa Cruz, Néstor Kirchner, all emerged as potential PJ candidates (Vives Segl, 2006: 112). The lack of unity within the party was primarily a product of the intense political rivalry that existed between two PJ heavyweights: the former President Carlos Menem, and the current interim President Eduardo Duhalde.²⁷⁸ Duhalde had opted out of running in the 2003 election, but he actively sought a surrogate candidate who he perceived would be easily malleable (Sanchez, 2005: 461). Initially, he favoured the former racing-car driver, Carlos Reutemann,²⁷⁹ but eventually, Duhalde and his influential political machine in Buenos Aires decided to throw their weight behind the little-known governor of Santa Cruz, Néstor Kirchner (Sanchez, 2005: 461).²⁸⁰ Due to increasing social unrest, Duhalde decided to bring forward the date of the election to April 27th 2003 and at the same time, tendered his resignation to become effective on May 25th, six months ahead of the constitutionally mandated date (Vives Segl, 2006: 111).

Traditionally, the PJ had chosen their presidential candidate through party primaries, but Duhalde, fearing that Menem's support and control within the party would lead to the defeat of his candidate, sparked an intense political wrangle to prevent these primaries from occurring (Vives, Segl, 2006: 110; Sanchez, 2005: 461). Internal party elections were not held and the PJ, for the first time in its history, agreed to let three different candidates run for President. As none of the candidates were allowed to use PJ symbols, all three were forced to establish new political movements within the PJ itself: Menem created the *Frente por la Lealtad*, Rodríguez Saá headed the *Movimiento Nacional y Popular*, while the left-wing Néstor Kirchner became the Presidential candidate representing the *Frente para la Victoria* (FpV) (Vives Segl, 2006: 110; Sanchez, 2005: 461). In total, eighteen candidates announced their intention to run for the 2003 election, ensuring that this election would be one of the most hotly contested since Argentina's return to democratic rule.

Néstor Kirchner was the least well-known of the three PJ candidates. Kirchner had been governor of the oil-rich province of Santa Cruz for eleven years, and while governor had utilised a mix of interventionist policies and state investment

²⁷⁸ Duhalde was Menem's vice-President for his first term in office and appeared to be the likely PJ candidate for the 1995 election. However, Menem's constitutional reforms enabled him to run for a second term, denying Duhalde his chance at the Presidency and creating a bitter split in the party between the *Duhaldistas* and the *Menemistas*. See Sanchez (2005: 460-461).

²⁷⁹ Latin America Regional Reports: Southern Cone, July 30th, 2002.

²⁸⁰ Before Duhalde had opted to support Kirchner, Kirchner had threatened to leave the PJ as he felt he was being ignored by the party hierarchy. See The Washington Post, September 4th, 2002.

in the economy in order to maintain fiscal balance and low levels of poverty (Vargas Llosa, 2004: 73; Sanchez, 2005: 462).²⁸¹ As a youth, Kirchner had been a member of the left-wing *Montenaro* revolutionary group, and was one of the few dissenters within the ranks of the PJ who had criticised Menem's economic model in the 1990s, particularly the privatisations. He also supported the establishment of the *Corriente Peronista*, a political space within the party for those who did not subscribe to the market-friendly policies of Menem (Vargas Llosa, 2004: 73; Sanchez, 2005: 462).

During the election campaign, Kirchner scathingly attacked the market model of Menem, claiming that 'people cannot bear any more austerity. They have sold everything. Some want to go back to that economic model of exclusion, austerity and unemployment.'²⁸² Privatisation was an essential component of Menem's policies and Kirchner clearly displayed his preferences towards this policy from the outset. He called for an end to all future privatisation contracts, particularly with regard to utilities²⁸³ and suggested that 'there is a need to recuperate the instruments of the state, the essential macroeconomic tools for driving Argentina. It is not a question of nationalising everything, but regaining strategic control.'²⁸⁴ In an interview with *El País*, Kirchner stated that 'he would recover the railways, the petrol rents and the commercial airlines,'²⁸⁵ while also stating that if elected he would 'analyse the [privatisation] contracts.'²⁸⁶ Kirchner urged the Duhalde government to renegotiate the contracts of privatised rail services²⁸⁷ and this coupled with his call to 'recover the railways,' prompted the government to commission a report investigating the state of the nation's rail services,²⁸⁸ and forced the Production Minister, Aníbal Fernández, and Kirchner's campaign manager, Alberto Fernández, to clarify that he was not talking of nationalisation, only for Kirchner to rebuke them, claiming that he needed no interpreter for his words.²⁸⁹ When questioned about his views on the Duhalde government's possible privatisation of the state-owned banks, Kirchner

²⁸¹ Kirchner had also altered the state constitution to allow him to run for governor indefinitely, raised the number of Supreme Court judges in the province, and had been criticised for attempting to control the media. See *The Buenos Aires Herald*, April 24th, 2003.

²⁸² *The Buenos Aires Herald*, February 21st, 2003.

²⁸³ *Latin America Regional Reports: Southern Cone*, April 15th, 2003.

²⁸⁴ *El País*, September 29th, 2002.

²⁸⁵ *El País*, February 6th, 2003.

²⁸⁶ *The Buenos Aires Herald*, April 1st, 2003.

²⁸⁷ *El País*, February 10th, 2003.

²⁸⁸ *Clarín*, February 13th, 2003.

²⁸⁹ *The Buenos Aires Herald*, February 20th, 2003.

responded: 'We need a strong *Banco Nación*, not a privatised one.'²⁹⁰ He was also highly critical of the privatisation of the state-oil company, YPF, under Menem and called for greater state-involvement in the energy sector.²⁹¹

Kirchner's 152 page *Plan de Gobierno* (Plan for Government) and the FpV's *Plataforma Electoral* (Electoral Platform), both clearly indicated his preferences as regards the economy and the policy of privatisation. Highly critical of Menem's market-friendly policies, the platform accused Menem of engendering the 2001 economic crisis by 'dismantling the national productive sector,' and 'selling the national patrimony' (Frente Para la Victoria, 2003a: La Economía). It also proposed a 'neo-Keynesian plan of public works to generate a strong and immediate growth in the levels of employment and production, through the construction of housing, the provision of drinkable water and the expansion of infrastructure' (Frente Para la Victoria, 2003a: La Economía). The *Plan de Gobierno* promised to construct a 'national capitalism,' and it proposed to halt and review all privatisations, 'in order to recover the wealth for the Argentine peoples' (Frente Para la Victoria, 2003b: Estado). While the document stated that it was not suggesting nationalisation, it advocated a renegotiation of all privatised utility contracts, so that the 'state would have control over these macroeconomic instruments' in order to direct the efficient usage of these services (Frente Para la Victoria, 2003b: Estado). It also proposed greater state involvement in the rail and commercial airline industries, the recovery of the 'golden share' in the state oil company and the creation of a new hydrocarbon law to regulate the petroleum industry, while explicitly rejecting the privatisation of any of the remaining state banks (Frente Para la Victoria, 2003b: Estado).

Kirchner's pro-statist and anti-privatisation stance was a position generally supported by the Argentine electorate. By 2003, only 15 per cent of the Argentine public were satisfied with the market economy, while support for privatisation had dropped to just 12 per cent among the electorate, from a previous high of 32 per cent in 1998 (Latinobarómetro, 2003). Consequently, in the first round of voting on April 27th, Menem won with 22.2 per cent of the vote, with Kirchner second, garnering 21.9 per cent of the vote, ensuring both qualified for a second round election to be

²⁹⁰ Clarín, March 9th, 2003.

²⁹¹ El País, February 10th, 2003.

held on May 18th (Sanchez, 2005: 465-466).²⁹² The prospect that Kirchner might actually win the run-off election sent jitters through the financial markets, with share prices on the Argentine *Bolsa* plummeting by 8.6 per cent in one day and initiating a run on the sale of Argentine sovereign bonds.²⁹³ Kirchner, in response to this turmoil and in an attempt to calm the markets, announced that he would re-appoint Roberto Lavagna as Minister of the Economy, a respected economist and former Minister of the Economy under Duhalde.²⁹⁴

However, it soon began to appear as if a second round election would not be necessary. Even before the first round results were known, polling had indicated that 58 per cent of the Argentine electorate would not vote for Menem under any circumstances, and while his first round voters would constitute a definite core in the second round, it became apparent that Menem would face a resounding defeat by Kirchner, with polls indicating that Kirchner, buoyed by the anti-Menem sentiment, commanded about 70 per cent of the vote (Vives Segl, 2006: 114-115; Sanchez, 2005: 470). After days of uncertainty, Menem finally announced on May 14th that he was pulling out of the second round, forcing the legislative assembly to rule that the candidate with the second highest total, Néstor Kirchner, was the winner and therefore by default, the new President of Argentina (Vives Segl, 2006: 114-115; Sanchez, 2005: 470-471).

4.2 Privatisation with Kirchner in Power

Néstor Kirchner was inaugurated as President of Argentina eleven days later on May 25th 2003. From the outset, it appeared as if Kirchner was facing a number of serious obstacles in his ability to govern successfully. Menem's final act in the 2003 elections forced Kirchner to enter the *Casa Rosada* with the lowest electoral mandate in Argentinean democratic history.²⁹⁵ Furthermore, although the Peronists had a majority of the seats in the Senate and a near majority in the lower house,²⁹⁶ the decision to allow three different PJ candidates to run for President had bitterly divided the party. Kirchner, elected under the aegis of Eduardo Duhalde who

²⁹² Ballotage had been introduced by Menem during his constitutional reforms in 1994, but it had never been necessary to revert to a second round election until now.

²⁹³ The Buenos Aires Herald, April 29th, 2003.

²⁹⁴ Latin News Daily, May 16th, 2003.

²⁹⁵ The Economist Intelligence Unit, Country Report: Argentina, July 2003, p. 1.

²⁹⁶ After the legislative elections of October 2001, the PJ held 110 seats of the 257 seats in the lower house (42.8 per cent), and 41 out of 76 seats in the upper house (53.94 per cent).

controlled the powerful Buenos Aires section of the party, would have to rely upon Duhalde's support in order to get any legislation through the lower house, leading to widespread speculation that he would be little more than a Duhalde puppet.²⁹⁷ To exacerbate issues, Kirchner had also inherited a country which had defaulted on debts worth some US\$77 billion, and an economy that was still suffering the legacies of the 2001 crisis.²⁹⁸ The economic situation, the impatient clamouring of creditors and the IMF to receive payment on the defaulted debt and capital markets that had remained jittery since the first round elections, fuelled further speculation that Kirchner would be hamstrung while in office. Added to this, companies that had purchased privatised utilities during Menem's tenure were placing intense pressure on the new government to allow a raise in tariff prices. During the 2001 crisis, the Economic Emergency Law converted the tariffs of all privatised utilities into devalued pesos and froze them at this level.²⁹⁹ This law was utilised by Duhalde to impose the rate freeze on privatised utilities, and no move had been made on this issue by the time Kirchner came to power.³⁰⁰ The IMF had included the introduction of tariff hikes as an essential part of any agreement regarding the defaulted debt.³⁰¹

When Kirchner announced his new cabinet just days after Menem pulled out of the run-off election, the composition of this cabinet appeared to reflect the impediments that Kirchner was facing. The twelve posts were shared out between members of the PJ who were loyal to Duhalde (*Duhaldistas*), and members of Kirchner's inner circle from Santa Cruz,³⁰² while the decision to re-appoint the economically conservative Lavagna as Economy Minister was widely interpreted as an effort to placate the financial markets and the IMF.³⁰³

However, once in office, Kirchner soon appeared intent on asserting his authority and implementing his preferences regardless of any obstacles. In his acceptance speech he continued his campaign rhetoric vowing that he would not be 'a prisoner of the big corporations,'³⁰⁴ while in his inauguration speech he called for

²⁹⁷ The Economist, May 24th, 2003.

²⁹⁸ The Economist, August 9th, 2003.

²⁹⁹ This was a process that became known as 'Pesification,' to prevent price rises in key sectors and reduce the threat of inflation. See The Economist, January 29th, 2005.

³⁰⁰ Noticias Financieras, October 29th, 2004.

³⁰¹ The Economist, August 9th, 2003.

³⁰² The Economist, May 24th, 2003.

³⁰³ Lavagna had dealt with both creditors and the IMF as Economy Minister under Duhalde, and was generally respected by both groups.

³⁰⁴ The Economist, May 24th, 2003.

a central role for the state, and rebuffed IMF pressure by stating that the government would not restart debt payments at the ‘price of the hunger and exclusion of Argentines.’³⁰⁵ Within days, in a move designed to distance himself somewhat from Duhalde, he began a purge of high-ranking police officers in the Duhalde controlled province of Buenos Aires, before turning his attention to the military, where he replaced 52 senior officers.³⁰⁶ His next move was to tackle the ‘automatic majority’³⁰⁷ of the Menem-friendly Supreme Court, urging Congress to investigate the Menem-appointed judges for corruption and conflicts of interest.³⁰⁸ Impeachment processes began in June against the President of the Supreme Court, Julio Nazareno, eventually forcing his resignation a month later.³⁰⁹ At the same time, Kirchner issued a decree which would transform the manner in which justices were selected for the Supreme Court, ostensibly in a move to reduce executive interference in the process.³¹⁰ Kirchner, in order to cement his own support base in Congress and reduce his reliance upon Duhalde, adopted what became known as the ‘transversal strategy,’ a process that involved winning support from the non-Kirchner aligned sections of the PJ and other parties (Vives Segel, 2006: 118). It was a strategy that was to prove relatively successful.³¹¹

With regard to privatisation, Kirchner appeared no less determined to assert his authority and implement his preferences. On July 4th, he issued Decree 311, which established the *Unidad de Renegociación y Análisis de Contratos de Servicios Públicos* (UniRen – The Commission for the Renegotiation and Analysis of Public Service Contracts).³¹² The commission would be directed by Lavagna’s economy ministry and the planning ministry of Julio de Vido, and its mandate was the analysis and possible renegotiation of 63 utility concessions that were privatised in the 1990s in areas such as electricity, gas, water, telecommunications, roads, rails, ports and mail.³¹³ Specifically, the commission would be responsible for investigating the

³⁰⁵ The Economist, May 31st, 2003.

³⁰⁶ The Economist Intelligence Unit, Country Report: Argentina, July 2003, p. 1.

³⁰⁷ Menem, in order to place his own supporters on the bench, had increased the number of Supreme Court judges from five to nine. See chapter five.

³⁰⁸ Clarín, June 5th, 2003.

³⁰⁹ Latin American Weekly Report, July 1st, 2003.

³¹⁰ World Markets Analysis, June 20th, 2003.

³¹¹ One of the most successful examples of this strategy occurred only days after Kirchner took office, when Eduardo Lorenzo ‘Borocotó,’ elected as a deputy for the Federal Capital under the banner of the PRO, joined the *Frente para la Victoria*. See Vives Segl (2006: 118-119).

³¹² Clarín, July 4th, 2003.

³¹³ Clarín, July 4th, 2003.

impact of these contracts on the economy in general, the level of investment, the quality of service, public access to these services and the profits generated by these privatised utilities.³¹⁴ As he issued the decree creating UniRen, Kirchner also introduced a bill to Congress that proposed extending the deadline for the renegotiation of utility contracts until December 2004, whereupon Congress would then have 90 days to accept or reject the revised contracts. This law would also enable the executive to renegotiate the contracts without congressional interference.³¹⁵ This was extremely significant, as it meant that not only was Kirchner scrutinising utilities that had profited from privatisation in the 1990s, something he had proposed to do during the election, but also that the earliest possible date whereby tariff hikes would even be considered would now be March 2005.³¹⁶ This move established a relationship between Kirchner and the privatised utility companies that was to become fraught with acrimony. Kirchner was indicating that he was unwilling to bow to the pressures of the IMF or the privatised utility companies to raise tariffs immediately. In fact, at the end of July, Kirchner's administration signed a letter of intent with the IMF that although committed the government to a consolidated primary surplus of 2.5 per cent of GDP, contained no mention of utility tariffs (International Monetary Fund, 2003b).

Further exacerbating tensions with the privatised utilities, Kirchner appointed Daniel Azpiazu of the *Facultad Latinoamericana de Ciencias Sociales* (FLASCO) as a special technical advisor to the commission. Both FLASCO and the *Instituto de la Central de Trabajadores Argentinos* (CTA) were to provide technical assessments on the regulation of privatised utilities and provide analyses as regards the benefits of the existing contracts.³¹⁷ Both FLASCO and Azpiazu were well known for being highly critical of the privatisation process under Menem,³¹⁸ and had produced a number of damning reports which had attacked this process for engendering much of the social inequities within Argentina (see for example Azpiazu, 2002; Azpiazu & Schorr, 2001).³¹⁹ Then, in July, in a clear demonstration of his statist tendencies,

³¹⁴ Clarín, July 4th, 2003.

³¹⁵ Business News Americas, July 7th, 2003.

³¹⁶ Clarín, July 4th, 2003.

³¹⁷ Clarín, July 12th, 2003.

³¹⁸ Clarín, July 12th, 2003.

³¹⁹ One of the things that Azpiazu recommended was a 'social tariff,' which would be applied to sectors of the population that could not afford to shoulder the eventual rise in utility prices. See Clarín, July 12th, 2003.

Kirchner established a new state-owned passenger carrier by decree, *Lineas Aereas Federales* (LAF).³²⁰

In September, Kirchner's administration signed a 36 month stand-by agreement with the IMF, that allowed Argentina to refinance the amortisation of the principal due to the fund over three years (International Monetary Fund, 2003c: 1), enabling Kirchner to begin dealing with bilateral creditors.³²¹ The IMF placed pressure on the administration to adopt a conventional re-structuring programme but Kirchner held fast, and eventually the fund reluctantly agreed that mandatory fiscal and monetary targets would only apply for six months.³²² As part of this agreement, the IMF insisted that the government finish negotiations with privatised utilities and allow tariff hikes, but the September letter of intent rather ambiguously stated that 'the government will act pursuant to the provisions of Law 25,561 (emergency law allowing renegotiation of contracts)' (International Monetary Fund, 2003c: 13).³²³ Twenty-three privatised utility companies, in an attempt to step up the pressure on the Kirchner government, also lodged claims worth US\$16 billion with the World Bank's International Centre for the Settlement of Investment Disputes (ICSID),³²⁴ arguing that they should be compensated by the Argentine government for 'pesification,' the subsequent rise in their dollar-denominated debts, and the refusal of the government to allow tariff increases.³²⁵ Also Argentina's refusal to adopt a conventional re-structuring programme sent share prices on the MerVal plummeting by 3.66 per cent.³²⁶

Despite this pressure, Kirchner remained resolute, refusing to allow any increases in utility rates and continuing his combative stance towards the privatised utilities, stating that he 'won't negotiate under pressure from anyone.'³²⁷ After an electricity blackout in Buenos Aires, Kirchner accused the privatised electricity companies of engineering the blackout in order to place pressure on the government, and a week later, Julio de Vido of the Planning Ministry, announced that the firms

³²⁰ Aviation Daily, July 14th, 2003.

³²¹ The Economist Intelligence Unit, Country Report: Argentina, December 2003, p. 19.

³²² The Economist Intelligence Unit, Country Report: Argentina, December 2003, p. 19.

³²³ The Economist Intelligence Unit, Country Report: Argentina, December 2003, p. 20.

³²⁴ In total, a third of all cases were against the Argentine government. See The Financial Times, October 28th, 2003.

³²⁵ World Markets Analysis, October 29th, 2003.

³²⁶ Gazeta Mercantil, September 10th, 2003.

³²⁷ The Financial Times, October 28th, 2003.

involved, Edenor and Edesur, would be fined for this blackout.³²⁸ Indeed, when Daniel Scioli, the Vice-President, suggested that he would be in favour of a utility rate increase in an interview, Kirchner publicly rebuked him by dismissing German Perez of the tourism ministry and eleven members of Perez's staff as they were all appointed by Scioli.³²⁹ Likewise, when Lavagna told an assembly of businessmen that he was in favour of perhaps allowing some tariff hikes, the Interior Minister, Aníbal Fernández, was quick to announce to the press that there would be no utility tariff increases until all negotiations were finished, and warned that any company not fulfilling its obligations would have its contract rescinded.³³⁰ Issues began to come to a head in October, when Kirchner accused the privatised companies of using the issue of tariff raises as a smokescreen to disguise the fact that they had failed to invest in the services they had purchased. Kirchner announced that 'from now on they [privatised utility firms] are going to have to fulfil their obligations. Argentines will not be extorted.'³³¹

Following a series of staggered gubernatorial and legislative elections during October and November, Kirchner's support base was significantly strengthened with most gubernatorial candidates backed by Kirchner winning their elections.³³² As a result, the PJ could now boast a majority in both houses, including a quorum in the lower house.³³³ This accumulation of political and institutional power significantly strengthened Kirchner's ability to pursue his preferences and, after months of tension, Kirchner issued a decree at the end of November rescinding the contract of *Grupo Macri*³³⁴ to run the national postal service *Correo Argentino*.³³⁵ The postal service was privatised under Menem in 1997, and Kirchner's excuse for rescinding the contract was a product of the analysis of UniRen, which documented the fact that the company had run up a debt of over \$450 million pesos and had failed to meet

³²⁸ World Markets Analysis, October 21st, 2003.

³²⁹ The Financial Times, August 21st, 2003.

³³⁰ Latin American Weekly Report, November 18th, 2003.

³³¹ World Markets Analysis, October 22nd 2003.

³³² The PJ won a total of 69 seats in the lower house out of a possible 130, 14 seats in the senate out of 24, and 14 governorships out of a possible 22. See *Elecciones en Argentina*, available at: <http://www.towsa.com/andy/site.html>.

³³³ The Economist Intelligence Unit, Country Report: Argentina, December 2003, p. 7.

³³⁴ The owner of Grupo Macri was Francisco Macri, who interestingly, lost the mayoral elections against the Kirchner backed candidate in Buenos Aires during the summer. See Noticias Financieras, November 21st, 2003.

³³⁵ Noticias Financieras, November 21st, 2003.

semi-annual royalties to the state, agreed to in the 1997 contract.³³⁶ Initially, it was announced that a new state enterprise, *Correo Oficial de la Republica Argentina* (Corasa), would run the postal service for six months before it was to be re-privatised.³³⁷ However, within three months, the government announced that it was considering nationalising the postal service, with Cabinet Chief Alberto Fernández stating: ‘We need to get away from false dogmas. Not everything that is private is good, nor everything that is public bad.’³³⁸ Consequently, Corasa remained in state hands, successfully posting profits of \$99 million pesos between November 2003 and November 2004.³³⁹

The successful nationalisation of the postal service provided Kirchner with momentum and in January 2004, shortly after he lambasted utility companies once again for failing to maintain adequate investment levels,³⁴⁰ Kirchner announced that he was cancelling the contract of the French defence firm, *Thales Spectrum*, to operate the Argentine radio-electric spectrum.³⁴¹ *Thales* had purchased the 15 year concession for US\$500 million in 1997, granting the firm the right to operate airwaves used by mobile phone companies, radio and television stations.³⁴² The decision to cancel the contract and nationalise the radio spectrum was sparked by an article in the French news magazine, *Le Point*, in October 2003 that suggested that the purchase of the concession by the French firm in 1997 was plagued with corruption. It also alleged that *Thales* had paid up to US\$25 million in bribes to Argentine officials to win the contract.³⁴³ Kirchner issued a decree cancelling the contract and nationalising the service on the basis of these corruption allegations and also because *Thales* had failed to invest the requisite \$300 million pesos in the service that they were obligated to do.³⁴⁴ Kirchner issued the decree claiming that control of the radio-electric spectrum was ‘an integral function of the state,’³⁴⁵ a

³³⁶ El Cronista, January 26th, 2006.

³³⁷ Noticias Financieras, November 21st, 2003.

³³⁸ World Markets Analysis, February 9th, 2004.

³³⁹ La Nación, August 27th, 2006.

³⁴⁰ The Financial Times, January 27th, 2004.

³⁴¹ La Nación, January 26th, 2004.

³⁴² La Nación, January 26th, 2004.

³⁴³ Le Point, October 3rd, 2003. Story available at <http://www.lepoint.fr/content/monde/article?id=41071>.

³⁴⁴ La Nación, January 27th, 2004.

³⁴⁵ La Nación, January 27th, 2006.

sentiment echoed by Alberto Fernández, who stated: ‘This service can’t be conceded to the private sector. The results of the privatisation have not been positive.’³⁴⁶

In May 2004, the government introduced an energy bill to the legislature that reflected Kirchner’s desire to increase the role of the state in the economy. The central component of this energy plan was the establishment of a new state-owned energy company, *Empresa Nacional de Energia* (Enarsa).³⁴⁷ This bill was introduced in the face of a looming energy crisis, which Kirchner argued was due to a lack of investment from privatised energy companies.³⁴⁸ Enarsa’s activities would involve exploration, as well as distribution and transport, which would place the company in direct competition with the former Argentine oil company YPF.³⁴⁹ The energy plan also included a state investment scheme designed to expand the country’s energy infrastructure, and the imposition of higher taxes on gas and oil exporters.³⁵⁰ Taken as a whole, this new energy plan was viewed as significantly increasing state involvement in the energy sector.³⁵¹

Following a report on the metropolitan railways by the Secretary of Transport in May 2004 that indicated that more than one person a day was killed on trains in Buenos Aires during 2003, Kirchner now turned his attention to those companies who had purchased rail concessions during the 1990s.³⁵² After repeated warnings from the government to the rail operators to improve safety and service,³⁵³ Kirchner signed Decree 798 in June, rescinding the contract of *Metropolitano* to operate the San Martín rail line.³⁵⁴ *Metropolitano*, owned by Argentine businessman Sergio Tasselli, had purchased the 30 year concession to operate the railway lines between Buenos Aires and the surrounding areas in 1994.³⁵⁵ Kirchner rescinded the contract due to the company’s failure to improve conditions on the San Martín line.³⁵⁶ Control and operational management of the line was handed to the newly created *Unidad de*

³⁴⁶ The Financial Times, January 27th, 2004.

³⁴⁷ Clarín, April 30th, 2004.

³⁴⁸ As Argentina began to economically recover under Kirchner, there was an increased demand for energy from the industrial sector, but supply could not meet this increased demand, due to a lack of investment by energy firms since privatisation and a reduction in hydroelectric power caused by very dry weather conditions. See World Markets Analysis, May 12th, 2004.

³⁴⁹ Clarín, May 9th, 2004.

³⁵⁰ World Markets Analysis, May 12th, 2004.

³⁵¹ The Financial Times, June 22nd, 2004.

³⁵² La Nación, May 13th, 2004.

³⁵³ La Nación, May 13th, 2004.

³⁵⁴ Clarín, June 24th, 2004.

³⁵⁵ Clarín, June 24th, 2004.

³⁵⁶ La Nación, June 24th, 2004.

Gestión Operativa Ferroviaria de Emergencia (UGOFE – The Emergency Rail Operational Unit), run by the state and the concessionaires on the other Buenos Aires' lines.³⁵⁷

Shortly after the *Metropolitano* affair, the Argentine Communications Secretariat announced that it was revoking the satellite licence held by *Nahuelsat* S.A. The consortium purchased the licence in 1999 and had proposed to launch a satellite servicing Argentina by 2003.³⁵⁸ However, they had failed to invest the US\$200 million necessary to do so and for this reason, their contract was rescinded.³⁵⁹ A new state controlled enterprise, *Empresa Nacional de Soluciones Satelitales* (Arsat S.A.), owned by the state and the provincial governments, was established to assume control of the licence.³⁶⁰ The Communications Secretariat resolution that cancelled the contract and nationalised the licence stated that this was a 'resource that should be used in the public interest.'³⁶¹

Riding high approval ratings, Kirchner entered 2005 eager to consolidate his position and began by tackling the issue of Argentina's debt. During the previous summer, Kirchner had suspended the September 2003 agreement with the IMF, due to his refusal to meet the demands of the fund, particularly concerning the issue of tariff increases.³⁶² In January, Argentina finally issued its offer to holders of the US\$81 billion worth of bonds on which the country defaulted in 2001. Creditors were presented with a choice of sixteen different bonds in six currencies, but the offer itself was barely above thirty cents for every dollar that was invested.³⁶³ Creditors were given until the end of February to accept or reject the thirty cents in the dollar offer, with the Argentine government vowing not to pay a cent to those that rejected this deal.³⁶⁴ Despite the paucity of the offer, nearly 78 per cent of creditors accepted the deal by the end of February, freeing the Kirchner administration from one of the largest debt defaults in history.³⁶⁵ The decision of the government to address the defaulted debt also raised confidence in the markets and

³⁵⁷ *Unidad de Gestión Operativa Ferroviaria de Emergencia, ¿Qué es UGOFE?* Available at <http://www.ugofe.com.ar/>.

³⁵⁸ La Nación, August 24th, 2004.

³⁵⁹ La Nación, August 24th, 2004.

³⁶⁰ El Cronista, August 27th, 2004.

³⁶¹ Resolución 188/2004, Boletín Oficial, 18/08/2004, No. 30465.

³⁶² The Economist, March 5th, 2005.

³⁶³ The Economist, January 15th, 2005.

³⁶⁴ The Economist, January 15th, 2005.

³⁶⁵ The Economist, March 5th 2005.

after an announcement that nearly 78 per cent of creditors were participating in the swap, the MerVal index shot up by 3.21 per cent.³⁶⁶

The IMF continued to place enormous pressure on the government, not only to resolve issues with the privatised utilities, but also to formulate some type of plan for dealing with those creditors that did not participate in the debt swap.³⁶⁷ However, Kirchner, needing access to funds and unwilling to agree to the IMF conditions, instead turned to his left-wing counterpart in Venezuela, Hugo Chávez, and following negotiations, Venezuela agreed to purchase US\$4500 million of Argentine sovereign bonds once the new paper to be issued as a result of the recent swap is in circulation.³⁶⁸

The New Year also witnessed Kirchner continuing to target privatised utility companies, fining the water company, *Aguas Argentinas*, and the power supplier *Edenor*, for ‘unjustifiable cuts in service.’³⁶⁹ Kirchner, citing the Rossati doctrine,³⁷⁰ also urged the companies to drop their cases against Argentina at the World Bank and to submit their cases to an Argentine court.³⁷¹ In March, Kirchner even called for a national boycott of Shell oil after the company raised fuel prices by 4.2 per cent.³⁷² Kirchner’s combative rhetoric and aggressive actions proved popular with the electorate, and a poll conducted shortly after the Shell affair, indicated that 78 per cent of Argentines believed that foreign-owned utilities should be nationalised.³⁷³ However, Kirchner’s interventionist policies and the hostile business environment convinced a number of utility companies that it was time to leave, culminating in *Electricité de France’s* (EDF) announcement that they were going to sell their 90 per cent share in power company *Edenor*.³⁷⁴ Despite Lavagna’s attempts to calm investors by stating that he was not in favour of re-nationalisation in an interview

³⁶⁶ World Markets Analysis, February 9th, 2005.

³⁶⁷ World Markets Analysis, April 15th, 2005.

³⁶⁸ El Cronista, November 24th, 2005 & El Nacional, December 1st, 2005.

³⁶⁹ World Markets Analysis, January 12th, 2005.

³⁷⁰ The Rossati doctrine was published in a law magazine in 2004, and suggested that those operating in Argentina should only resort to international arbitration after they have exhausted the domestic judicial system.

³⁷¹ La Nación, March 3rd, 2005.

³⁷² Shell’s revenue dropped by 70 per cent as a result of the boycott and the company agreed to lower prices by 3.3 per cent further bolstering Kirchner’s support. See The Economist, March 19th 2005 and April 30th 2005.

³⁷³ World Markets Analysis, April 19th, 2005.

³⁷⁴ El Cronista, April 27th, 2005.

with the Financial Times,³⁷⁵ EDF were soon followed by *Gaz de France*, *France Telecom* and *Vivendi*.³⁷⁶

Compounding problems, in May, the World Bank's arbitration tribunal, ICSID, ordered the Argentine government to pay US\$133 million in compensation to US firm CMS Gas Transmission for the process of pesification and the subsequent tariff freeze.³⁷⁷ Kirchner refused to pay, and demanded that all companies withdraw their claims from the ICSID as a prerequisite to signing new contracts, which would include the long-awaited tariff increases.³⁷⁸ This decision did set the tone for a slightly more conciliatory relationship however, with companies such as *Telefonica* and *Gas Natural* withdrawing their claims from the ICSID.³⁷⁹ Consequently, for the first time since Kirchner assumed office, progress was made on the utility contracts and by November, UniRen had signed 23 letters of understanding with concessionaires.³⁸⁰

Despite these problems, mid-term legislative elections held in October resulted in a resounding victory for Kirchner, with the *Frente Para la Victoria* wing of the PJ now holding 108 of 257 seats in the lower house, and 40 of 72 seats in the upper house.³⁸¹ In total, the PJ had a clear majority in both houses. With his political and institutional power consolidated, Kirchner, in a clear sign of the direction he wished his economic policy to take, dismissed his Economy Minister Roberto Lavagna and Finance Secretary, Guillermo Nielson. Relations between Kirchner and Lavagna had begun to sour over economic policy, particularly over the issue of utility rate increases and expropriations.³⁸² Lavagna was replaced with Felisa Miceli, who previously had worked in the state-owned *Banco de la Nación*, and who was considered to be more supportive of Kirchner's economic policies.³⁸³ However, the replacement of Lavagna with Miceli was not favourably received by the markets, with the MerVal tumbling by 4.5 per cent on the announcement of the news.³⁸⁴ Riding the crest of his popular support, Kirchner, in his last action of the year,

³⁷⁵ The Financial Times, March 24th, 2005.

³⁷⁶ World Markets Analysis, May 2nd, 2005.

³⁷⁷ The Financial Times, May 14th, 2005.

³⁷⁸ World Markets Analysis, May 16th, 2005.

³⁷⁹ Business News Americas, July 20th, 2005.

³⁸⁰ El Cronista, November 29th, 2005.

³⁸¹ The Economist Intelligence Unit, Country Report: Argentina, April 2006, p. 1.

³⁸² The Financial Times, November 29th, 2005.

³⁸³ El Cronista, November 29th, 2005.

³⁸⁴ World Markets Analysis, November 28th, 2005.

announced on December 15th 2005 that his government would repay its entire debt of US\$9.8 billion to the IMF, freeing the country of any further obligations to the fund.
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With this consolidation of power and with the issue of the defaulted debts addressed, Kirchner was now in an even stronger position to pursue his preferences and in March 2006, following numerous disputes with the company, he issued Decree 303, cancelling the contract of water firm *Agua Argentinas* and renationalising the service.³⁸⁶ The company, controlled by French firm *Suez*, won the concession to provide water to Buenos Aires and the surrounding province in 1993,³⁸⁷ and Kirchner cancelled the contract citing the company's failure to meet its contractual obligations.³⁸⁸ The decree also mandated for the establishment of a new state enterprise to run the water service, *Aguas y Saneamientos Argentinos* (AySA), in which the state would hold a non-transferable 90 per cent stake, with the employees owning the remaining 10 per cent.³⁸⁹ Shortly after this move, it was announced that the Argentine government were in negotiations to increase their share in *Aerolineas Argentinas* (AA) from 1.21 per cent to 20 per cent.³⁹⁰ AA, owned by the Spanish group *Marsans*, was one of the most infamous and unpopular privatisations during Menem's tenure and had occurred with questionable legal authority (see chapter five). The new state share in the company would grant the government greater control of AA, by providing it with a board-level veto.³⁹¹

In February 2007, Kirchner submitted to the legislature a bill, which proposed the reform and partial re-nationalisation of the Argentine pension system. In 1994, Argentina partially privatised its pension system by establishing a mixed public and private, two pillar system.³⁹² Under the old system, employees had three months to choose between the public system and the private *Administradoras de Fondos de Jubilaciones y Pensiones* (AFJPs). If employees did not make this choice within the required timeframe, they were automatically assigned to a private AFJP, and were subsequently prohibited from switching back to the public system.³⁹³ The new law

³⁸⁵ The Economist, December 24th, 2005.

³⁸⁶ Clarín, March 22nd, 2006.

³⁸⁷ Latin News Daily, March 30th, 2006.

³⁸⁸ Clarín, March 22nd, 2006.

³⁸⁹ Clarín, March 22nd, 2006.

³⁹⁰ El País, June 14th, 2006.

³⁹¹ Latin America News Digest, November 27th, 2006.

³⁹² Business News Americas, February 2nd, 2007.

³⁹³ Inter Press Service, March 1st, 2007.

proposed to allow all 12 million affiliates of the private AFJPs 180 days to switch to the public system, should they so wish. This option would then be provided to AFJP customers every five years. Furthermore, if an employee fails to choose a pension scheme within the required three month timeframe, they would now automatically be assigned to the public rather than the private system.³⁹⁴ By June, nearly 500,000 Argentines had switched back to the state-run pension scheme.³⁹⁵

Kirchner also announced the re-nationalisation of the small shipyard *Tandanor*, which had been privatised in 1991³⁹⁶ and the nationalisation of the Buenos Aires' *Hospital Francés*, after the charity who ran the hospital went bankrupt.³⁹⁷ Following the temporary closure of a Buenos Aires rail line, angry commuters set fire to the *Constitucion* station and looted nearby shops. In response, Kirchner urged the rail operators to address the service deficiencies on their lines, warning that otherwise 'the state is going to give a swift kick where it counts.'³⁹⁸ Following further commuter protests, Kirchner decided to act and revoked the rail concessions for *Metropolitano General Roca SA* and *Metropolitano Belgrano Sur*. Both these companies were owned by Sergio Tasselli, and this move followed Kirchner's earlier decision to rescind *Metropolitano's* contract to run the San Martín line.³⁹⁹ Both the *Belgrano* and *General Roca* lines were re-nationalised and handed over to the state-run UGOFE for management.⁴⁰⁰

Kirchner, like Lula in Brazil, had advocated the end of all privatisations and even suggested the possibility of re-nationalisation in Argentina. In Brazil, although privatisations significantly slowed, they did not stop. In contrast, by Kirchner's last year in office, no privatisations had occurred.⁴⁰¹ In fact, not only did privatisations stop, but Kirchner had also created two new state enterprises that would directly compete with previously privatised state firms, he had re-nationalised the Argentine postal service, cancelled and nationalised a US\$500 million contract to run the radio-

³⁹⁴ Business News Americas, February 2nd, 2007.

³⁹⁵ Business News Americas, June 4th, 2007.

³⁹⁶ La Nación, April 2nd, 2007.

³⁹⁷ Global Insight, April 24th, 2007.

³⁹⁸ Noticias Financieras May 18th, 2007.

³⁹⁹ El Cronista, May 23rd, 2007.

⁴⁰⁰ Latin News Daily, May 23rd, 2007.

⁴⁰¹ There was one incidence of re-privatisation. The Duhalde government took control of *Belgrano Carga*, which had been run by the *Union Ferroviaria* trade union since 1991 after it went bankrupt. After initially deciding to hold on to the company, Kirchner then allowed for its re-privatisation, in which 68 per cent of the company was sold to private investors, with the state retaining a 10 per cent 'golden share,' and workers controlling the other 22 per cent. See La Nación, June 23rd, 2004; Clarín, July 11th, 2005 and Clarín, February 17th, 2006.

electric spectrum in Argentina, re-nationalised three major rail lines, a shipyard, a satellite licence and a hospital, returned to state hands a major water provision service and partially re-nationalised the Argentine pension system (see Table 6.1).⁴⁰² What is more, the Argentine economy grew at over 7.5 per cent per annum between 2003 and 2006, although this is partly explained by the increase in agricultural exports and market prices.⁴⁰³ However, throughout Kirchner's tenure, Argentina's credit rating languished well below investment grade. In June 2005, Standard & Poor's improved its rating for Argentina's long-term debt from SD (Selective Default) to B-, while the country's short term rating moved from SD to C.⁴⁰⁴ In September 2007, these ratings were raised once more, long-term debt to B+ and short-term debt to B, ratings still well below investment grade, and S & P refused to countenance any further ratings increase because of what they perceived to be the excessive concentration of power in the hands of the executive and Kirchner's unorthodox approach to economic policy-making.⁴⁰⁵

Both Lula and Kirchner expressed similar preferences concerning privatisation before they were elected, but in one instance, privatisation continued, while in the other, not only did privatisations halt, but there was also a series of re-nationalisations, as well the establishment of new state enterprises. So what explains this difference? This thesis argues that the political institutional structure in each state will either enable a partisan government to implement their preferences, by increasing their institutional control over policy, or to inhibit a partisan government from implementing their preferences, by leaving them with little institutional control over the policy in question. Lula was hampered by the institutional structure in his state from pursuing his preferences, whereas in Argentina, the institutional structure enabled Kirchner to pursue his preferences by increasing his institutional control over the policy of privatisation. Kirchner utilised his decree power to establish UniRen, and nearly of all the nationalisations that occurred in Argentina during this period were initiated by executive decree. Kirchner's ability was to draw upon his

⁴⁰² In fact, Kirchner's economic model is such a departure from the market-friendly policies of the 1990s that authors have begun to suggest it represents a new, post-neoliberal economic strategy. See for example Grugel & Pia Riggirozzi (2007), who have called this economic strategy *neodesarrollismo*.

⁴⁰³ World Markets Analysis, February 20th, 2004, The Economist, October 1st, 2005 & Noticias Financieras, February 17th, 2006.

⁴⁰⁴ World Markets Analysis, June 2nd, 2005.

⁴⁰⁵ Global Insight, September 27th, 2007.

decree power without major opposition was due to his ability to build his own support in the legislature and to significantly alter the composition of the Supreme Court. Privatisation had never been delegated to an autonomous body as it had in Brazil. In fact, in Argentina, privatisation was initially implemented by executive decree. As such, Kirchner was able to roll-back these privatisations through recourse to the same institutional mechanisms. The next section will analyse the actions of Kirchner according to the independent variables identified in chapter two.

Table 6.1: Kirchner's Privatisation Policy

Utility (Company Name in Brackets)	Action	Outcome
Airlines	Creation of new enterprise Líneas Aérea Federales (LAF)	Will absorb the workers from bankrupt carriers LAPA and Dinar
National mail service (Correo Argentino)	Contract rescinded	Nationalised - new state enterprise Corasa
Radio-electric spectrum (Thales Spectrum)	Contract rescinded	Nationalised
Energy Sector	Establishment of new state energy company	Creation of Enarsa - direct competition with Repsol YPF
San Martín rail line (Metropolitano San Martín)	Contract rescinded	Nationalised - new state controlled body UGOFE
Satellite licence (Natuelsat SA)	Contract rescinded	Nationalised - new state controlled enterprise Arasat SA.
Water provision (Aguas Argentinas)	Contract rescinded	Nationalised - new state enterprise AySA
Airlines (Aerolineas Argentinas)	State increased its share in company to 20 per cent	State now has a board level veto over company actions
Pension system (Administradoras de Fondos de Jubilaciones y Pensiones)	Reform of pension system and partial nationalisation	Allow private pension customers to return to state system. New employees, unless other wise directed, now automatically assigned to state system.
Shipyard (Tandanor)	Contract rescinded	Nationalised
Health (Hospital Francés)	Contract rescinded	Nationalised - state social welfare system for retirees PAMI
Belgrano rail line (Metropolitano Belgrano SA)	Contract rescinded	Nationalised – UGOFE
General Roca rail line (Metropolitano General Roca SA)	Contract rescinded	Nationalised – UGOFE

Source: Derived from author's own analysis.

The Analysis

6.3 The Political Institutions

As in Brazil, the Argentine political system is a Presidential system with three branches: the Executive, Congress and the Judiciary (Llanos, 2001: 68). The 1853 constitution defined the political institutions in Argentina and the powers of the

political actors in the policymaking-process. This constitution conferred a large amount of power to the Executive, and the Executive in Argentina remains at the heart of policy-making, to such an extent that the Argentine system has been described as ‘hyper-presidentialist’ (see Nino, 1992, 1996).

The Executive

The Executive in Argentina has two extraordinarily powerful legislative tools at its disposal to enable it to implement its preferences by avoiding congressional opposition: the *decretos de necesidad y urgencia* (decrees of urgency and necessity – DNU) and the item veto (De Luca, 2004; Mustapic, 2000, 2002; Peruzzotti, 2001). While the 1853 Constitution ‘conceived the Presidency as the motor of the government,’ by granting the Executive the power to present its own legislative initiatives and the power of veto after congressional approval, it was a succession of democratic, semi-democratic and authoritarian regimes that reduced the power of checks and balances enshrined in the constitution (Congress and the Judiciary), resulting in the ‘accumulation of prerogatives in the office of the Presidency’ (Llanos, 2001: 68-69).

With the return of democracy in 1983, a subsequent decade of economic and social turmoil re-enforced authoritarian conceptions ‘about the proper exercise of political authority that lead in the direction of delegative...democracy (O’Donnell, 1994: 56). The nature of this delegative democracy is a product of historical authoritarian legacies and an atmosphere of crisis which acts as a catalyst for its re-emergence, but the end result is a democracy characterised by an extremely strong Executive, with a weak legislature and judiciary (O’Donnell, 1994). Subsequent Executives (particularly Menem) used these periods of crisis to cement their own power and sideline other institutions in the policy-making process. Since the return to democracy, the increasing power of the Executive in Argentina, relative to the legislature and the judiciary, to such an extent that it forecloses opportunities for opponents to veto policy, has led to the characterisation of the Argentine political system as ‘hyper-presidentialist’ (see Nino 1992, 1996; Serrafiero, 1993; Kay, 1999). It is the item veto and the decrees of necessity and urgency that form the central tenet of this ‘hyper-presidentialism.’

Decrees of necessity and urgency essentially enable the executive to pass legislation and bypass Congress (Mustapic, 2002: 29). The 1853 Constitution did not

authorise their usage as everyday legislative tools, because the only exceptional measures that it recognised, which would justify the use of such tools, were a state of emergency and federal intervention (Rubio & Goretti, 1996: 449; Mustapic, 2000: 584).⁴⁰⁶ Consequently, between 1953 and 1989, executives only issued 35 decrees of necessity and urgency, with ten of these belonging to Alfonsín alone (Rubio & Goretti, 1996: 444; Mustapic, 2002: 585). It was Menem who set the precedent for their usage as a common legislative tool and between July 1989 and August 1994 Menem issued 336 decrees of urgency and necessity in order to implement his own legislative agenda (Rubio & Goretti, 1996: 444, 451).⁴⁰⁷ The strategic values of these decrees are clear. The executive issues a decree, and if Congress introduces an act that repeals this decree, the executive can simply veto their decision (Mustapic, 2002: 39). The costs of forming a parliamentary coalition to reverse the executive decision are extremely high and require a two-thirds majority. Therefore, the executive only needs the support of one third of all legislators to unilaterally impose his will upon Congress (Mustapic, 2000: 585). When the executive decides to utilise these decrees ‘the Congress becomes a marginal actor’ (Mustapic, 2002: 41).⁴⁰⁸

Coupled with the ability to pass bills and by-pass Congress through the use of decrees of necessity and urgency, the Argentine President also has the power of total veto or partial veto. The total veto can be used most effectively to protect decrees of necessity and urgency, while the partial veto, again under Menem, became another strong legislative resource (Llanos, 2001: 72; Mustapic, 2000: 583, 2002: 30-31). Specifically, the partial veto enables the executive ‘to move forward by obtaining a necessary piece of legislation which, after congressional amendments, could still be corrected to adjust it to the presidential view, and then promulgated’ (Llanos, 2001: 72). Under Alfonsín and Menem, the number of presidential vetoes increased significantly compared to the historical average, with Alfonsín issuing 49

⁴⁰⁶ This was designed to face the main potential threat at this time: resistance by provincial powers. See Mustapic (2002: 29).

⁴⁰⁷ A Supreme Court ruling on DNUs in 1990 declared: ‘The decrees of necessity and urgency are valid as long as they are dictated in response to situations of extreme gravity that endanger the continuity of the state or imply social breakdown.’ This ambiguous wording has left the usage of DNUs open to interpretation and therefore subject to presidential discretion. See Mustapic (2002: 30).

⁴⁰⁸ The 1994 Constitutional Reform mandated for the establishment of a *Comisión Bicameral Permanente*, which is responsible for reviewing each DNU in a ten day timeframe before the DNU is submitted to Congress. But, the Constitutional Reform stipulates that the composition of this commission should reflect the proportion of party representatives in each chamber, meaning that if the President has a majority or near majority, the commission will follow the executive line. See Constitución de la Nación Argentina, Artículo 99.3.

veto and Menem 109 (Peruzzotti, 2001: 151). In fact, the 1853 Constitution did not explicitly recognise the partial veto and it was only after the 1994 Constitutional Reform that Executives were explicitly allowed to resort to the partial veto (Mustapic, 2000: 582; Llanos, 2001: 72).⁴⁰⁹ Essentially, the veto allows the Executive to amend any legislation in order to reflect its own preferences.

Despite these institutional prerogatives, a number of authors have recently challenged the characterisation of the Argentine political system as ‘hyper-presidentialist,’ arguing that the role of Congress in the legislative process is still significant and therefore, the Argentine system could be better characterised as one of ‘limited centralism’ (see Llanos, 2001; Mustapic, 2000, 2002; Peruzzotti, 2001; Eaton, 2002). Specifically, they suggest that situations in which Presidents issue large numbers of decrees and vetoes could actually indicate institutional conflict between the Executive and the legislature, with Congress refusing to act as a mere rubber-stamp body (Peruzzotti, 2001; Llanos, 2001). They also suggest that such scenarios could reflect the lack a governing party majority in either chamber, or perhaps in-fighting within the governing party itself (Llanos, 1998, 2001). The Executive therefore resorts to these measures to avoid ‘gridlock’ (Mustapic, 2002; Llanos, 2001).⁴¹⁰

However, these arguments do not diminish the fact that the balance of powers in the Argentine political system is detrimental to the legislature. Even if the Executive is facing ‘gridlock,’ he/she still has recourse to decrees of necessity and urgency and veto power, enabling the executive, once they can rely upon the support of one third of legislators, to effectively impose their preferences upon Congress.

This extensive executive power was to prove crucial in Kirchner’s ability to implement his preferences. Not only did Kirchner make wide use of the powers at his disposal, but he also attempted to increase and strengthen these prerogatives, resulting in one of the greatest concentrations of power in the hands of a single President since 1853.⁴¹¹ When Kirchner arrived in power, as part of his UniRen package to deal with public utility contracts, he managed to convince Congress to extend the Economic Emergency Law, passed during Duhalde’s tenure to enable him

⁴⁰⁹ To override a veto, a two thirds majority is required in both chambers, and so consequently, veto overrides are extremely rare, with only 12 overrides occurring between 1862 and 1985. See Mustapic (2002: 34).

⁴¹⁰ See Eaton (2002) for an excellent account of the role of the legislature in the economic reform process.

⁴¹¹ Latin American Weekly Report, November 23rd, 2004.

deal with the 2001 crisis, until December 2004. The Economic Emergency Law, besides implementing ‘pesification,’ delegated significant powers to the Executive, such as the ability to re-arrange by decree the financial, banking and exchange sectors, and to renegotiate public utility contracts and set utility tariffs without congressional approval.⁴¹² In essence, it granted the Executive significant leeway in managing the economy without having to concern himself with congressional opposition.⁴¹³ In November 2004, Congress agreed to extend this law for another year,⁴¹⁴ which was then extended twice more in 2005 and 2006,⁴¹⁵ ensuring that Kirchner had the use of these delegated powers for his entire presidency.

Furthermore, Article 14 of the 2004 Budget Act increased the power of the executive over the budget,⁴¹⁶ by granting special powers to the cabinet chief to increase spending above the ceilings set and to re-allocate spending without Congressional approval.⁴¹⁷ In May 2004, Kirchner significantly increased taxes on export revenues, which are exempt from the ‘co-participation’ system under which a proportion of federal tax is automatically distributed to the provinces.⁴¹⁸ The provinces share of tax revenue fell from 39 per cent in 2001, to 34 per cent in 2005, increasing the dependence of the governors on Kirchner, leading to five of the opposition Radical Party governors allying with Kirchner.⁴¹⁹ In July 2006, the government managed to have Law 26,122 passed through both houses, which although still mandated that decrees of necessity and urgency had to be approved by Congress, eliminated any fixed time within which these decrees had to be approved, significantly strengthening the Executive’s legislative prowess (Bonvecchi & Giraudy, 2007: 36). Finally, in August 2006, Kirchner gained approval for legislation that further strengthened Executive discretionary spending powers. This legislation allows the cabinet chief virtually unrestricted authority to alter the federal budget without Congressional approval (Levitsky & Murillo, 2008: 19; Bonvecchi & Giraudy, 2007: 37). The cumulative effect of these initiatives was to ‘contribute, in distinct ways, to the fortification of the power of the Executive over Congress, and

⁴¹² Latin American Weekly Report, November 23rd, 2004 and Noticias Financieras, November 12th, 2004.

⁴¹³ Latin News Daily, October 28th, 2004.

⁴¹⁴ Noticias Financieras, October 29th, 2004.

⁴¹⁵ World Markets Analysis, December 22nd, 2005 and Global Insight, November 21st, 2006.

⁴¹⁶ The Economist Intelligence Unit, Country Report: Argentina, September 2004, p. 17.

⁴¹⁷ The Economist Intelligence Unit, Country Report: Argentina, December 2003, p. 22.

⁴¹⁸ The Economist, August 12th, 2006.

⁴¹⁹ The Economist, August 12th, 2006.

more generally, the national government over the provinces' (Bonvecchi & Giraudy, 2007: 36).

Kirchner deployed this executive power regularly in order to implement his preferences. In fact, Kirchner's record of issuing decrees of necessity and urgency echoed that of Menem. In his first year alone, Kirchner issued 67 decrees of necessity and urgency,⁴²⁰ while over his four years in power, as Table 6.2 indicates below, Kirchner issued a total of 249 decrees of necessity and urgency, compared to just 176 laws introduced by the Executive to Congress over the same period. Kirchner was also not reticent when it came to using his veto power. As Table 6.3 shows below, Kirchner issued a total of 35 vetoes (full and partial) during his tenure, with 77 per cent of these vetoes being promulgated in his first two years, enabling him to bring legislation which had passed through Congress back to a position that more reflected his preferences.⁴²¹

Table 6.2 Kirchner and the use of Decree Power

Type of Legislative Initiative	Year 1	Year 2	Year 3	Year 4	Total
Decrees of Necessity and Urgency	67	73	61	48	249
Laws	56	43	35	40	176

Source: *La Nación*, September 10th, 2007.

Table 6.3 Kirchner and the use of Veto Power

Type of Veto	2003	2004	2005	2006	2007
Total	4	8	---	---	---
Partial	7	8	3	2	3
Number	11	16	3	2	3

Source: *Boletín Oficial* (various) and *Información Legislativa* at <http://www.infoleg.gov.ar/>.

Kirchner also utilised this Executive power to implement his preferences with regards to privatisation. He established UniRen through a decree of necessity and urgency,⁴²² and as a result of the powers delegated to him by the Economic Emergency Law, he was able to conduct all negotiations and re-negotiate contracts with the privatised utility companies without Congressional interference.

⁴²⁰ *La Nación*, June 22nd, 2004.

⁴²¹ This was during the period when Kirchner had no directly elected support base in Congress and was reliant upon Duhalde. Llanos (2001), Mustapic (2000, 2002) and Peruzzotti (2001) argue that the Executive resorts to such measures in order to impose his preferences upon Congress when he cannot boast a legislative majority of his own.

⁴²² Decreto 311/2003, *Boletín Oficial*, 04/07/2003, No. 30185.

Furthermore, as Table 6.4 indicates below, the majority of his actions in this particular policy area were through unilateral executive initiatives. Kirchner used his decree power to rescind and nationalise (bar one) the contracts of the privatised utility companies. In fact, he only introduced legislation to Congress for his energy plan establishing Enarsa and for the partial re-nationalisation of the pension system.

As such, in Brazil, the Executive has significant power, but this can be checked by the judiciary or by Congress, particularly if the governing party fails to form a cohesive coalition, as happened to Lula. In Argentina however, the Executive has recourse to even more powerful legislative tools, some of which can enable the Executive to sideline an uncooperative legislature. Whereas Lula was prevented from utilising his Executive powers to successfully implement his preferences, Kirchner was able to utilise the wide array of Executive tools available in Argentina in order to implement his preferences.

Table 6.4 Executive Power and Kirchner's Privatisation Policy

The Action	Legal Norm (source in brackets)
Airlines: Creation of LAF	Decreto 337/2003 Boletín Oficial, 08/07/2003, No. 30187
National mail service: Nationalisation of Correo Argentino contract	Decreto 1075/2003 Boletín Oficial, 20/11/2003, No. 30281
Radio-electric spectrum: Nationalisation of Thales Spectrum contract	Decreto 340/2004 Boletín Oficial, 23/03/2004, No. 30366
Energy Sector: Creation of Enarsa	Ley 25,943 Boletín Oficial, 03/11/2004, No. 30519
Rail: Nationalisation off San Martín rail line (Metropolitano San Martín)	Decreto 798/2004 Boletín Oficial, 25/06/2004, No. 30429
Satellite: Nationalisation of Nahuelsat satellite licence	Resolución 188/2004 Boletín Oficial, 18/08/2004, No. 30465
Water provision: Nationalisation of Aguas Argentinas contract	Decreto 303/2006 Boletín Oficial, 22/03/2006, No. 30871
Airlines (Aerolineas Argentinas)	State increased its share in company to 20 per cent
Pension system: Reform and partial nationalisation of Administradoras de Fondos de Jubilaciones y Pensiones	Ley 26,222, Boletín Oficial 08/03/2007, No. 31111
Shipyard: Nationalisation of Tandanor	Decreto 315/2007 Boletín Oficial, 03/04/2007, No. 31128
Rail: Nationalisation of General Roca rail line (Metropolitano General Roca SA)	Decreto 591/2007 Boletín Oficial, 23/05/2007, No. 31161
Rail: Nationalisation of Belgrano rail line (Metropolitano Belgrano SA)	Decreto 592/2007 Boletín Oficial, 23/05/2007, No. 31161

Source: Derived from *Boletín Oficial* (various). Relevant *Boletín Oficial* listed in brackets.

Legislative Support

The extensive power granted to the Executive however, does not render the legislature impotent (Llanos, 2001; Mustapic, 2000, 2002; Eaton, 2002; Peruzzotti,

2001; Corrales, 2000, 2002; De Luca, 2004). The Argentine Congress, ‘while certainly more of a reactive blunt veto player than a proactive agenda setter, is nevertheless an important actor in the policy process’ (Jones, 2004: 1). As Llanos (2001) and Mustapic (2000: 2002) have argued, when an Executive is forced to use the full array of powers (DNUs and veto) available to them, this is an indication of Executive-Congress tension. It signifies an active Congress that is unwilling to act as a mere rubber-stamp body for Executive initiatives, and so the Executive must rely heavily upon these powers to impose a legislative agenda (Peruzzotti, 2001: 152). No Executive can rule by decree alone. Decrees must be accepted and ratified by Congress, and rarely can permanent and lasting decisions be made through decree (Mustapic, 2002: 32).⁴²³ Furthermore, Congress controls the parliamentary agenda and while it gives priority to the initiatives of the Executive, it does not neglect those of the legislators themselves (Mustapic, 2002: 43). Congress can therefore thwart, delay and prevent an Executive from implementing its preferences.

This is where party fragmentation and party discipline becomes relevant. Since the return to democracy, the Argentine political system has been dominated by two major parties,⁴²⁴ the *Partido Justicialista* (PJ) and the *Unión Cívica Radical* (UCR), while at several times a third party has achieved a degree of national prominence (Jones, 2004: 2; 2002; 149).⁴²⁵ Most importantly however, the level of party discipline in the Argentine Congress is very high (Jones, 1997; 2002; 2004; Molinelli, 1991). In fact, for the four legislative periods between 1989 and 1997, the level of relative discipline for the PJ in each period never dropped below 94 per cent (Jones, 2002: 156). Indeed, it is extremely rare for a deputy of either of the two main parties to vote against his/her party in the Chamber (Jones, 2002: 157).

Firstly, deputies are elected via closed party lists (using the d’Hondt divisor form of proportional representation), and thus the votes for this office are pooled, encouraging deputies to engage in behaviour that enhances the electoral prospects of the party (Jones, 2002: 159). Furthermore, legislator’s access to the list is controlled by the internal party hierarchy and hence the opportunity for re-election (Jones,

⁴²³ The prime example here is the policy of privatisation under Menem. Menem implemented privatisation primarily through decree and because of this; Kirchner was then able to reverse this policy.

⁴²⁴ For a general overview of the Argentine party system, see for example, Manzetti (1993).

⁴²⁵ Parties such as FREPASO, ARI, PI and UCEDE have all achieved this level of national prominence.

2002; 159; Kay, 1999; 415-416).⁴²⁶ Secondly, the career pathways of deputies are extremely party-orientated, and those that go against the party line will generally be expelled or forced to defect (Jones, 2002, 2004; De Luca, 2004). Thirdly, parties resort to the distribution of selective incentives, such as committee positions and budgetary resources to engender party unity (Mustapic, 2002: 35).⁴²⁷ Importantly, when the party is in power, the national leadership has strong resources at its disposal to strengthen the support coalition and conversely, when in opposition, the party leadership tends to be weak, due to the lack of these selective incentives (Mustapic, 2002: 38).

The locus of politics in Argentina however, is at the provincial level (Spiller & Tommasi, 2003: 295; De Luca, 2004; 3; Jones, 2004; 3). The provincial governor is an extremely powerful actor in Argentine politics, and generally tends to dominate parties at the provincial level (*caudillo*) (Jones, 1997, 2004; Spiller & Tommasi, 2003; De Luca, 2004). The governor's power is derived from a group of political and institutional resources, such as control over jobs in the provincial public sector, the provincial budget and the provincial party organisation, and is based upon patronage, pork-barrel and clientelism (De Luca, 2004: 3). Because the principal nucleus of electoral competition is at the provincial level, the governors exercise strong control over access to the lists and in turn, they can then influence representatives' conduct once in office (De Luca, 2004; Jones, 2004; Spiller & Tommasi, 2003).

In turn, the President has ample discretion over budgetary design and implementation (Abuelafia *et al.*, 2005: 4; Spiller & Tommasi, 2003; 292). In fact, as Abuelafia *et al.* (2005: 4) have discovered: 'the executive power...has a de facto role that is much more important than what the laws and institutions of the budget process stipulate,' and given the financial dependence of the provinces (and therefore the pork-barrel politics of the governors) on the centre, the Executive engenders discipline among the governors by distributing positions in the national government, discretionary federal funds, threatening federal intervention in the provinces and simply backing a rival candidate for the next gubernatorial election (De Luca, 2004: 30). The Executive disciplines the governors with federal pork, while the governors,

⁴²⁶ Access to the list is controlled by the national party organisation, the district-level party organisation and rank and file members. The methods employed for candidate selection include elite arrangement, assembly election and direct primary (Jones, 2002; 159-164).

⁴²⁷ All legislators receive a base disbursement of US\$5,000 to pay staff, which is generally insufficient. The Executive however can be of great assistance in increasing this base amount through the allocation of budgetary resources or committee appointments. See Jones (2002: 180).

reliant upon the centre for funding, disciplines legislators from their province with provincial pork. This engenders party unity and discipline, but the key is for the Executive to correctly court and control the governors.

When Kirchner was elected, the PJ was highly fragmented as it was the first time that the party had contested a general election divided (Sanchez: 2005: 461; Vives Segl, 2006: 112).⁴²⁸ Initially, Kirchner was reliant upon Duhalde for support in Congress, but as a result of his clever use of the selective incentives available to him, and the disciplining effects of the Argentine political system, Kirchner was soon able to boast a support base of his own. Kirchner began distributing resources to members of the PJ and other left-of centre political parties, in order to cultivate his own support base, in a policy that came to be known as the 'transversal strategy' or the '*concertación plural*' (Bonvecchi & Girudy, 2007: 31; Vives Segl, 2006: 116).

Kirchner began distancing himself from Duhalde, and following a series of staggered gubernatorial and legislative elections during October and November 2003, Kirchner's support base was significantly strengthened with most gubernatorial candidates (including non-PJ candidates) backed by Kirchner winning their elections. The PJ won a total of 69 seats in the lower house out of a possible 130, 14 seats in the senate out of 24, and 14 governorships out of a possible 22. Those gubernatorial candidates that Kirchner backed formed the backbone of his own support base, and legislators began drifting towards the *Frente para la Victoria* bloc in order to take advantage of the resources on offer. This strategy proved crucial, for it was this support base, coupled with his high levels of popular support, which enabled him to have the Economic Emergency Law and also his energy plan passed by Congress and the Senate.⁴²⁹ This early nucleus of support also enabled Kirchner to proceed with his reform of the judiciary and to pass the 2004 Budget Act, which increased the power of the executive over the budget,⁴³⁰ and to increase taxes on export revenues.⁴³¹ This resulted in the provinces' share of tax revenue falling from 39 per cent in 2001 to 34 per cent by 2005, increasing the

⁴²⁸ Perón once claimed that Peronists fighting were like cats having sex. 'It may seem like they are fighting, but they are really just reproducing. In the end, Peronism survives and expands. The Washington Post, September 4th, 2002.

⁴²⁹ Kirchner's position was threatened following a dangerous split in the PJ in March 2004, when a number of anti-Kirchner politicians were elected to prominent positions within the PJ. It was only after significant pressure from Kirchner that a number of these new appointees agreed to resign. See Latin News Daily, March 29th, 2004.

⁴³⁰ The Economist Intelligence Unit, Country Report: Argentina, September 2004, p. 17.

⁴³¹ The Economist, August 12th, 2006.

dependence of the governors on Kirchner, leading to five of the opposition Radical Party governors allying with Kirchner.⁴³² Kirchner also managed to pass the *Ley de Responsabilidad Fiscal*, which placed more stringent control on spending by provincial governments.⁴³³ Kirchner used the ‘transversal strategy’ to build an initial coalition in Congress but the transversal movement, while initially successful, did not prove to be a viable long-term strategy. Kirchner, who had alienated many of the PJ bosses, eventually realised he needed their support to deliver votes and so made his peace with the party machine (Levitsky & Murillo, 2008: 21). Also, Kirchner’s legislative support strengthened as he slowly saw off the threat of Duhalde. This was mainly due to internal PJ party rules. As Levitsky (2003: 157-158) argues, the lack of secure tenure patterns and routine career paths within the PJ, forces PJ members and leaders who wish to maintain and/or advance their careers to remain on good terms with the leadership. So you witness bandwagon effects where party members who previously opposed a PJ leader or faction will switch sides when a clear winner begins to emerge. The end result was strengthened legislative support, enabling Kirchner to call upon this support for initiatives that would strengthen his control over the governors, which in turn would serve to widen his support base and engender discipline and so on. While Kirchner was establishing this base, he still had recourse to his Executive powers should Congress balk at his initiatives, and he used this power widely during this period (see tables 6.2 and 6.3 above).

When Kirchner first came to power he had no independent support base, but as Table 6.5 and 6.6 shows, during the legislative session that spanned the first two years of his presidency, Kirchner was able to establish the FpV as the majority bloc in the lower and upper house. This, coupled with the discipline of PJ members, the support he fostered among non-PJ members (such as the five Radical governors), and his return to the party machine and peace with party bosses, ensured that Kirchner had a cohesive governing coalition after only a year in power.

The mid-term legislative elections held in October 2005 resulted in a resounding victory for Kirchner, with the *Frente Para la Victoria* wing of the PJ winning 108 of 257 seats in the lower house, and 40 of 72 seats in the upper house.⁴³⁴ Also, it signalled Kirchner’s definitive victory over Duhalde. Kirchner’s wife,

⁴³² The Economist, August 12th, 2006.

⁴³³ The Economist Intelligence Unit, Country Report: Argentina, September 2004, p. 20.

⁴³⁴ The Economist Intelligence Unit, Country Report: Argentina, April 2006, p. 1.

Cristina Fernández, ran as the senatorial candidate for the FpV in Buenos Aires, directly competing against Duhalde's wife, Hilda ('Chiche'), and her victory confirmed Kirchner as the undisputed leader of the PJ.⁴³⁵ The PJ now had a clear majority in the lower house, with the FpV alone boasting a majority in the upper house (see Table 6.6). This strong cohesive legislative support, comprised of the PJ and non-PJ provincial governors, enabled Kirchner to present successful reforms aimed at increasing executive discretion over the budget and reducing congressional control of decrees of necessity and urgency.⁴³⁶ These moves strengthened his control over the governors, which in turn, strengthened his own support base. They also highlighted the weakness of the opposition. In terms of privatisation, Kirchner's majority in both houses ensured that he could introduce legislation and pass decrees safe in the knowledge that they would be accepted. For example, the lower house voted 209-10 in favour of Kirchner's pension system reforms.

In Brazil, the electoral rules hampered Lula. The electoral rules in Argentina however, engender a high level of discipline and Kirchner used his selective distribution of resources carefully, in order to create a cohesive coalition that enabled him to strengthen his position over the provincial governors, which in turn, further strengthened his legislative support. In fact, by the second half of Kirchner's presidency, he could boast a clear majority in both the upper and lower houses.

Table 6.5 Deputies in the Lower House 2003-2005 and 2005-2007

Party Blocs	No. of Deputies	% of Deputies	No. of Deputies	% of Deputies
	(2003-2005)		(2005-2007)	
PJ Kirchner	88	34.24	114	44.36
PJ Duhalde	36	14.01	18	7.00
PJ non- aligned	5	1.95	5	1.95
UCR	45	17.51	41	15.95
ARI	11	4.28	13	5.06
Regional Parties	19	7.39	18	7.00
Other	53	20.62	48	18.68
Total	257	100	257	100

Source: Bonvehchi & Giraudy (2007: 39-40) and Vives Segl (2006:118)

⁴³⁵ The Economist Intelligence Unit, Country Report: Argentina, April 2006, p. 1.

⁴³⁶ The Economist Intelligence Unit, Country Report: Argentina, January 2007, p. 1.

Table 6.6 Deputies in the Upper House 2003-2005 and 2005-2007

Party Blocs	No. of Senators	% of Senators	No. of Senators	% of Senators
	(2003-2005)		(2005-2007)	
PJ Kirchner	37	51.39	41	56.94
PJ Duhalde	1	1.39	1	1.39
PJ non- aligned	0	0	4	5.55
UCR	16	22.22	13	18.06
UCR - Separated	4	5.55	2	2.78
Other	12	16.67	10	13.89
Vacant/Suspended	2	2.78	1	1.39
Total	72	100	72	100

Source: Bonvehchi & Giraudy (2007: 39-40) and Vives Segl (2006:118)

Judicial Independence

In Brazil, the judiciary is considered independent of the Executive (see chapter four), and for Lula this ensured that it would be nearly impossible for him to pursue a policy of re-nationalisation, as concessionaires would have recourse to a judiciary that would view the cases purely legalistically. In Argentina however, when Kirchner came to power, the judiciary was not considered independent of the Executive (Helmke, 2005; Smulovitz, 1995, 2005; Peruzzotti, 2001; Manzetti, 1999). The subjugation of the Supreme Court to the Executive was sown by a Court in 1930, which submitted to the authority of a government installed by a military coup, subsequently legitimising the ensuing acts of government.⁴³⁷ Although the Constitution includes a provision for tenure protection, in practice this rule has been ignored and since 1930, subsequent Executive's have removed justices for political purposes. In fact, between 1946 and 1983, the average tenure of justices was only four years (Chávez, 2007: 42). The Supreme Court has endured purges in 1946, 1955, 1966, 1973 and 1976, with 33 per cent of justices between 1946 and 1983 having been removed by the politically expedient tool of impeachment (Chávez, 2007: 42).

When Menem came to power, he maintained this tradition of transforming the Supreme Court to suit his own political ends. At the beginning of his Presidency, he introduced a bill that reformed the Supreme Court, increasing the number of justices from five to nine, and filling the bench with his own political supporters (Helmke, 2005: 144; Bambaci *et al.*, 2002: 78-79; Goldstein, 1998: 66; Manzetti, 1999: 93). This granted Menem the now infamous pro-government majority in the

⁴³⁷ Latin American Special Reports, September 6th, 2005.

Court, known as the *mayoría automática menemista* (the automatic Menem majority) (Chávez, 2007: 37). This majority proved essential in the implementation of Menem's plans, particularly privatisation, and on numerous occasions passed dubious judgements enabling privatisation to proceed apace (see chapter five and the case of *Aerolíneas Argentinas*). The judiciary under Menem became such a central actor in political processes that this phenomenon was labelled the 'judicialisation' of politics (see for example Smulovitz, 1995, 2005). The 1994 Constitution, in compliance with the Olivos Pact,⁴³⁸ raised the Senate approval for Supreme Court justices from a simple majority to two-thirds, and the 1994 reform also mandated for the establishment of a *Consejo de la Magistratura* (Judicial Council), which was supposed to reduce Executive interference in the process of appointing lower court judges (Chávez, 2007; 40).⁴³⁹

So, when Kirchner arrived in office, the Supreme Court provided a major obstacle for him to pursue his preferences, particularly as regards privatisation, as Menem's pro-privatisation automatic majority still sat on the bench. In fact conflict seemed inevitable, when, shortly after Kirchner assumed power, the court began to consider ordering the re-dollarisation of bank deposits converted into pesos by Duhalde after the 2001 crisis.⁴⁴⁰ Not only would this place enormous pressure on the Central Bank, but it would also raise issues for the administration with privatised utility companies concerning the legality of utility tariffs converted into pesos.⁴⁴¹ Not surprisingly then, after only a week in office, Kirchner began a process of judicial reform. Firstly, in a move to ostensibly bolster a discredited institution and reduce Executive interference, Kirchner introduced a decree which altered the manner in which Supreme Court justices would be selected. Under the new process, non-governmental organisations would now have two weeks to voice criticism about the Executive's selection before the Senate vote.⁴⁴²

⁴³⁸ The 1993 Olivos Pact was an agreement reached between the Alfonsín and Menem. See chapter five.

⁴³⁹ Menem prevented the judicial council from assuming its duties, and it did not actually function until 1998, after the PJ lost control of both houses in the 1997 legislative elections. Congress passed Law 24,937 which established a twenty member council (see Chávez, 2007: 41).

⁴⁴⁰ During the crisis, the Court, in the *Smith* decision, overruled a government freeze on bank deposits (see Helmke, 2005: 139).

⁴⁴¹ Inter-Press Service, June, 5th, 2003.

⁴⁴² The Financial Times, July 3rd, 2003.

Secondly, he urged Congress to consider the impeachment of judges appointed by Menem due to misconduct while on the bench,⁴⁴³ initiating a series of congressional investigations into the activities of the Menem-appointed justices, beginning with the President of the Court, Julio Nazareno. Before impeachment proceedings could begin proper, Nazareno resigned,⁴⁴⁴ leaving a vacancy on the bench, enabling Kirchner to appoint the respected jurist, Eugenio Zaffaroni, as his replacement.⁴⁴⁵ In December, the Senate voted to remove justice Eduardo Moline O’Conner, after finding him guilty on two charges of misconduct,⁴⁴⁶ and in the same month, Justice Guillermo Lopez announced his resignation in order to avoid the inevitable impeachment hearings.⁴⁴⁷ Kirchner replaced Lopez and O’Conner with the respected jurists, Carmen Argibay and Elena Highton de Nolasco.⁴⁴⁸ Then, in August 2004, facing a Senate impeachment hearing, the fourth Menem-appointed justice, Guillermo Vazquez, resigned,⁴⁴⁹ enabling Kirchner to appoint Ricardo Lorenzetti as his successor.⁴⁵⁰ By June 2005, the purge of the court was complete. Justice Antonio Boggiano⁴⁵¹ was suspended by Congress and subjected to impeachment proceedings,⁴⁵² while the aging Justice Augusto Belluscio retired during the same month.⁴⁵³ Of the seven justices now remaining on the bench, Kirchner was responsible for the appointment of four of them (see Table 6.3 below).⁴⁵⁴ Finally, in 2006, Law 26,183 reduced the number of Supreme Court justices from nine to five, finally removing the last vestiges of Menem’s majority once and for all (Bonvecchi & Giraudy, 2007: 37).

Kirchner’s judicial reform did not stop there however. In December 2005, Law 26,080 modified the composition of the *Consejo de la Magistratura*, established as part of the 1994 constitutional reforms (Bonvecchi & Giraudy, 2007: 36). The 20 member judicial council was established to reduce Executive interference in the

⁴⁴³ The Financial Times, June 6th, 2003.

⁴⁴⁴ Latin American Weekly Report, July 1st, 2003.

⁴⁴⁵ World Markets Analysis, October 9th, 2003.

⁴⁴⁶ Noticias Financieras, December 5th, 2003.

⁴⁴⁷ Brazil Report, October 28th, 2003.

⁴⁴⁸ Noticias Financieras, February 20th, 2004.

⁴⁴⁹ Noticias Financieras, September 3rd, 2004.

⁴⁵⁰ La Nación, December 22nd, 2004.

⁴⁵¹ Kirchner did not support the impeachment proceedings against Boggiano. However, Congress insisted that they were only completing the process that Kirchner initiated. See Noticias Financieras, September 30th, 2005.

⁴⁵² Latin American Weekly Report, June 28th, 2005.

⁴⁵³ Noticias Financieras, June 10th, 2005.

⁴⁵⁴ Kirchner’s wife, Cristina Fernández, was appointed as President of the Senate’s constitutional affairs commission in 2005, granting the administration greater control of the appointment process.

appointment and removal of lower court federal judges and regulate judicial power. This law however, reduced the number of council members to thirteen, and granted the Executive control of 38.5 per cent of the council, enabling Kirchner to deny the body a quorum, and effectively providing him with veto power, ensuring that in practice, no federal judge can be appointed or removed without the approval of the Executive (Bonvecchi & Giraudy, 2007: 36).

Initially, Kirchner's reforms of the judiciary were welcomed, but soon questions began to arise over the extent of Executive manipulation in the process. Elisa Carrió, the left-of-centre deputy, described the new justices as 'of poor quality and above all agents of the governments,'⁴⁵⁵ while Alfredo Bisordi,⁴⁵⁶ the head of the Court of Cassation for Criminal Law, accused Kirchner of reforming the judiciary to enable the Executive to have 'overall control of power.'⁴⁵⁷ However, Kirchner's appointments did improve the quality of the Supreme Court, as most of the new judges were well-qualified and well-respected jurists (Levitsky & Murillo, 2008: 21), but undeniably, Kirchner's judicial machinations did increase Executive control over the judiciary (Bonvecchi & Giraudy, 2007: 36), and his purge of the Supreme Court fashioned a bench that was undeniably more favourable to the government than the bench he inherited when he arrived in power.⁴⁵⁸

For example, by the time Kirchner had replaced three of Menem's appointees, the Court had ruled in favour of pesification, removing the threat of domestic lawsuits from utility companies, whose tariffs had been converted into pesos and frozen after the 2001 crisis.⁴⁵⁹ The Court ruled that the freezing of tariffs was a matter of public policy, and by invoking a civil code provision (Article 872), they effectively foreclosed the opportunity for utility companies to bring compensation cases against the government in Argentine courts.⁴⁶⁰ Likewise, when Kirchner rescinded the contract of *Metropolitano* to run the San Martín rail line, the company obtained an injunction from a Buenos Aires judge suspending the decree.⁴⁶¹

⁴⁵⁵ Latin American Weekly Report, October 4th, 2005.

⁴⁵⁶ After these comments, Kirchner asked the magistrates council to investigate Bisordi for delaying human rights cases from the period of the Dirty War.

⁴⁵⁷ Latin News Daily, March 28th, 2007.

⁴⁵⁸ The Supreme Court did not always rule in favour of the government. The 2006 *Badaro* case forced the government to index pensions and the 2007 *Rosza* case prohibited the governments from using interim appointments on the bench (see Levitsky & Murillo, 2008: 21).

⁴⁵⁹ Latin News Daily, September 2nd, 2004.

⁴⁶⁰ Mondaq Business Briefing, December 21st, 2004.

⁴⁶¹ Business News Americas, July 13th, 2004.

However, when the government appealed this ruling, the Supreme Court overturned the suspension granted by the district judge and the nationalisation of the line was able to continue.⁴⁶²

The independence of the Supreme Court in Brazil effectively ensured that nationalisation was impossible once Lula came to power, but in Argentina, Kirchner was able to alter the composition of the Court (favourably with respect to the composition of the preceding bench) by encouraging the legislature to impeach sitting justices, weakening judicial tenure (Levitsky & Murillo, 2008: 19) and increasing Executive control over judicial appointments. This ensured that *de facto* judicial independence was further weakened, enabling Kirchner to rescind the contracts of privatised utilities and re-nationalise public services, with a greater degree of confidence that the Court would support his actions, in comparison to Lula in Brazil.

⁴⁶² Business News Americas, September 21st, 2004.

Table 6.7 Kirchner's Supreme Court

Supreme Court Justice (May 2003)	Julio Nazareno (Appointed by Menem)	Eduardo Moline O'Conner (Appointed by Menem)	Guillermo Lopez (Appointed by Menem)	Adolfo Vazquez (Appointed by Menem)	Juan Carlos Maqueda (Appointed by Duhalde)	Enrique Petracci (Since 1983)	Antonio Boggiano (Appointed by Menem)	Carlos Fayt (Since 1983)	Augusto Belluscio (Since 1983)
Event	Congressional investigation begin and resigns June 2003	Impeached and removed from office, December 2003	Congress moves for impeachment proceedings, so resigns December 2003	Impeachment proceedings begin and resigns September 2004			Removed from office by Senate, September 2005		Retires at age 75
Kirchner's Replacements	Eugenio Zaffaroni	Elena Highton de Nolasco	Carmen Argibay	Ricardo Lorenzetti	Remains in office	Remains in office	Vacant	Remains in office	Vacant

Source: Derived from author's own analysis

Policy Delegation

In Brazil, the policy of privatisation was initiated within the context of a comprehensive legal and institutional framework that delegated this policy to a relatively independent body, which could continue to operate without excessive Executive interference (see chapter four). In Argentina on the other hand, the State Reform Law ensured that privatisation policy was initiated by executive decrees rather than law, ensuring that Menem could implement privatisation ‘without major institutional interference’ (Llanos, 2001: 7). Indeed, within two months of taking office, ‘Menem had established the legal instruments for expediting privatisation without any independent oversight’ (Manzetti, 1999: 72-73). While Menem used the powers delegated to him to implement the policy of privatisation in Argentina, Kirchner in a similar manner, simply utilised the powers delegated to him to reverse this policy and sideline the regulatory agencies.

Regulators were established in various industries such as electricity (ENRE), gas (ENARGAS), telecommunications (CNT), and water provision (ETOSS), but the early and quick privatisation of some national symbols (telecoms, air transport and highways) ensured that these newly privatised industries were left with weak regulation, and in some cases, regulators were only created after privatisation and often in an ad hoc manner (see Abdala & Spiller, 2000; Bambaci *et al.*, 2002; Goldstein, 1998). While ENARGAS and ENRE were established by international best-practice, the vast majority of the regulators in Argentina suffered from problems of transparency and lack of independence (World Bank, 1997).⁴⁶³

Most importantly however, by the time Kirchner arrived in power, the 2002 Economic Emergency Law had halted the effective functioning of all Argentina’s regulatory agencies (Laffont, 2005: 9). The establishment of UniRen, and the promulgation of the Economic Emergency Law under Kirchner, delegated to him the power to re-negotiate all privatised utility contracts unilaterally, essentially vitiating any remaining role for the regulatory agencies.

While in Brazil, the delegation of privatisation to an independent body and the design of the regulatory agencies protected this policy from excessive interference by subsequent executives thereby preventing Lula from implementing his preferences, in Argentina on the other hand, the decision to implement

⁴⁶³ Argentina also opted for the establishment of regulatory commissions, rather than a single agency for each industry, further complicating matters (World Bank, 1997).

privatisation through executive decrees rather than through a comprehensive legal and institutional framework ensured that there was no such protection for this policy. This resulted in Kirchner's ability to reverse privatisations, by employing the same tools that Menem utilised in order to implement this policy in the first place.

6.4 Labour support

Menem's policy of privatization caused a division within the CGT, Argentina's main union confederation (see chapter five) between 1989 and 1992, and the government manipulated the competition among factions by rewarding the loyal segment of the union, CGT-San Martín led by Saul Ubaldini, in order to induce defections from the rebel CGT-Azopardo, led by Jorge Triaca (Murillo, 2001: 142-150).⁴⁶⁴ This split in the union, coupled with depressed labour market conditions particularly in manufacturing, significantly weakened the bargaining position of the unions (Goldstein, 1998). The weakening of the unions was exacerbated by political developments. Menem, due to the lack of institutionalisation in union-PJ linkages, successfully reduced the influence of the unions in the party, transforming the PJ from a unionist-based party to a patronage-based political machine (Levitsky, 2003: 24-25). This weak position and lack of patronage for the CGT-Azopardo led to its leaders modifying their demands and they had slowly moved towards the pro-privatisation position of the CGT-San Martín by the end of 1991 (Murillo, 2001: 151). Through the usage of carrot and stick tactics, Menem managed to neutralise the opposition of the main unions to his policy of privatisation, particularly the re-united CGT, and during Menem's second term, the union movement's relationship with the government shifted towards cooperation and support (Murillo, 2001: 168).

In 2000, the CGT split once more over disagreements concerning a proposed new labour law that, amongst other things, would increase labour market flexibility and a rebel faction, led by Hugo Moyano, left the confederation.⁴⁶⁵ With the 2001 crisis, the main unions became discredited due to their support of Menem's market-friendly policies and the rise in unemployment, coupled with their replacement as a vehicle for social action by *piqueteros*,⁴⁶⁶ meant that by the time Kirchner came to

⁴⁶⁴ A small group of unions did split from the CGT in order to create the militant Congress of Argentine Workers (CTA) (see Murillo, 2001: 137).

⁴⁶⁵ Inter Press Service, July 15th, 2004.

⁴⁶⁶ The *Piqueteros* (those that picket – movement of the unemployed), first emerged in Salta after the 1993 privatisation of the oil company, and during the 2001 crisis, they quickly spread to all areas of

power the union movement was discredited, fractured and significantly weakened (Grugel & Pia Riggirozzi, 2007: 103).⁴⁶⁷ ‘The locus of social conflict and labour policy debates seemed no longer to reside in the formal working class but in the growing informal sectors’ (Etchemendy & Collier, 2007: 364).

Once in power, Kirchner established links with many of the *piquetero* movements, who in turn had strong links to the militant Congress of Argentine Workers (CTA).⁴⁶⁸ In particular, Kirchner nurtured relations with the *piquetero* movement, the Federation for Land and Housing (FTV), led by a pro-Kirchner deputy, Luis D’Elia.⁴⁶⁹ The FTV were part of a pro-Kirchner *piquetero* bloc, which included elements of the CTA, but the *piqueteros*, while an important social force, were also highly unpredictable and frequently violent, such as the clashes that occurred between rival blocs at the 188th Independence Day Celebrations in Tucuman.⁴⁷⁰ Consequently, Kirchner soon began to court the larger unions, particularly the CGT⁴⁷¹ in order to find more reliable social organisations to deal with.⁴⁷²

In March 2004, Kirchner introduced a new labour reform bill, granting more power to the unions, increasing the cost of dismissing workers and improving the rights of workers with regards to permanent employment,⁴⁷³ and introducing a number of initiatives that increased labour’s non-wage social benefits (Etchemendy & Collier, 2007: 382). Then in July, it was announced with Kirchner’s support, that the CGT was to re-unite, establishing a tripartite leadership consisting of Moyano, the leader of the former rebel faction, José Lingeri of the federation of water and sanitation workers and Susana Rueda, leader of the *gordos*⁴⁷⁴ (the fat ones).⁴⁷⁵

the country. The *piqueteros* were not part of the traditional union movement, but they were not hostile to the unions. They numbered over two million and became a powerful actor in Argentine politics. See, for example, Dinerstein (2003).

⁴⁶⁷ Although the unions’ leverage did begin to increase under Duhalde as a result of the establishment of the *Mesas de Diálogo*. See Grugel & Pia Riggirozzi (2007: 96).

⁴⁶⁸ Telam News Agency, June 22nd, 2004.

⁴⁶⁹ The Washington Post, April 11th, 2005.

⁴⁷⁰ Latin American Weekly Report, July 13th, 2004.

⁴⁷¹ Etchemendy & Collier (2007: 390) argue that the alliance with the CGT was enabled by the government’s macroeconomic policy. A depreciated exchange rate strengthened traditional industrial sectors and a low-interest rate policy prioritising growth set the stage for a return to collective bargaining. This was bolstered by the Kirchner administration’s lenient attitude towards industrial action and resumed intervention in wage policy.

⁴⁷² Latin Daily, October 30th, 2003.

⁴⁷³ Noticias Financieras, March 5th, 2004.

⁴⁷⁴ The *gordos* are the unions with the largest memberships.

⁴⁷⁵ Inter Press Service, July 15th, 2004.

Kirchner was hoping that a re-united CGT would act to channel the demands of the *piqueteros* movements.⁴⁷⁶ Kirchner began a process of signing collective wage agreements with the CGT and the Minimum Wage Council was re-established, combining the government, the CGT and the UIA, in order to establish a consensus on a new minimum wage level (Etchemendy & Collier, 2007: 380). Following a meeting with the tripartite leadership in September,⁴⁷⁷ the government announced a \$34 peso salary increase to the monthly wages of most public and private sector workers.⁴⁷⁸

Then, in January 2005, Kirchner announced the establishment of a tripartite social agreement between the government, employer organisations and unions, which would serve as a guide to future pay negotiations. This has led to what Etchemendy & Collier (2007: 366) have defined as ‘segmented neocorporatism.’⁴⁷⁹ The move was motivated by Kirchner’s desire to conduct wage increases in an orderly fashion in order to avoid inflationary pressures, but it also significantly increased the power of the union movement.⁴⁸⁰ In April of 2005, both the CGT and the CTA began agitating for new wage increases, but while Lavagna categorically said no to these demands, Kirchner appeared more willing to accommodate the unions.⁴⁸¹ When the *gordos* announced they would support Duhalde in the upcoming legislative elections, Kirchner struck a deal with Moyano for his support and in July, Moyano orchestrated a coup within the CGT, taking over as sole leader and forcing Rueda to resign.⁴⁸² This deal served to further strengthen the ties between the CGT and the Kirchner administration. The unions were assured posts on the FpV lists for the October elections,⁴⁸³ and Moyano’s union received an increase in government payments to its social welfare scheme, while one of its lawyers was named head of a federal credit agency with an annual budget of US\$110 million.⁴⁸⁴ This newly strengthened relationship was reflected in the decision of rail workers to stop striking in August

⁴⁷⁶ The Economist Intelligence Unit, Country Report: Argentina, September 2004, p. 7.

⁴⁷⁷ Noticias Financieras, September 17th, 2004.

⁴⁷⁸ Noticias Financieras, December 10th, 2004.

⁴⁷⁹ Segmented neocorporatism is a pattern of peak-level negotiation among monopolistic unions, business associations and the government targeting inflation-wide, sector-wide wage agreements (see Etchemendy & Collier, 2007: 366).

⁴⁸⁰ The Economist Intelligence Unit, Country Monitor, February 21st, 2005, p. 4.

⁴⁸¹ Brazil Report, May 3rd, 2005.

⁴⁸² Latin News Daily, July 19th, 2005.

⁴⁸³ Latin American Weekly Report, July 12th, 2005.

⁴⁸⁴ The Economist, April 22nd, 2006.

after a request from Kirchner,⁴⁸⁵ and also in Kirchner's desire to continue to meet union demands. Following another meeting with Moyano in November,⁴⁸⁶ Kirchner announced an increase in the non-taxable minimum wage that would cost the state US\$487 million a year, and an increase of 19 per cent for the salaries of public administration workers.⁴⁸⁷

Under Kirchner, the unions began to re-gain credibility and as a result of the collective wage agreements, favourable labour reform and the tripartite council (segmented neocorporatism), the power of the unions significantly increased also. Kirchner nurtured and maintained strong links with the CGT and with elements of the CTA, and was highly amenable to union demands. Consequently, and hardly surprisingly, the unions were also very supportive of Kirchner's tough stance with privatised utilities and his nationalisation initiatives. For example, the pension system reform was something the unions had been clamouring for and it received their full support.⁴⁸⁸ Kirchner's decision to involve the unions in some of the nationalisation programmes also increased their support for his administration. For example, when Kirchner nationalised *Agua Argentina*, the new state company established to assume control over the water service, AySA, was to have a 10 per cent stake belonging to the unions.⁴⁸⁹ Ironically, Menem had used a similar ploy to induce union support for privatisations, by offering employees the opportunity to purchase 10 per cent of many of the privatised companies. The unions also received seats on the board of the re-nationalised postal company (Etchemendy & Collier, 2007: 383). In May 2006, when Kirchner called for a demonstration celebrating the third year of his Presidency, the CGT supplied 'the bulk of the lower-class support in the street demonstrations' (Etchemendy & Collier, 2007: 391).

As a result, the level of left-labour power significantly increased in Argentina during Kirchner's presidency. In Brazil, labour remained fractured and antagonistic towards Lula, whereas in Argentina, this high level of labour support contributed to Kirchner's ability to implement his preferences.

⁴⁸⁵ Latin America News Digest, August 5th, 2005.

⁴⁸⁶ Latin News Daily, November 30th, 2005.

⁴⁸⁷ Latin America News Digest, April 20th, 2006.

⁴⁸⁸ Business News Americas, February 2nd, 2007.

⁴⁸⁹ Clarín, March 22nd, 2006.

6.5 Conclusion

Kirchner was elected in 2003 with a mandate to alter the market-friendly model adopted under Menem. Part of this mandate was a categorical pledge to halt all privatisations in Argentina. Once in power, not only did all privatisations cease, but there were also a number of high-profile re-nationalisations. Whereas in Brazil, Lula was unable to implement his policies due to a confluence of institutional factors, Kirchner was able to implement his preferences in Argentina due to the configuration of institutions in that state. The Executive has extremely strong powers in Argentina (stronger than Brazil), and in periods where Congress is hostile, the Executive can sideline this institution in the policy process. The electoral system and the high-level of party discipline it engenders enabled Kirchner to slowly establish his own power base in Congress. He used this power base to support initiatives that would strengthen Executive power, which in turn, he then used to further enlarge his support base. Kirchner's ability to control both Chambers in Argentina and the high level of Executive power at his disposal meant that he could implement his preferences, particularly with regard to privatisation. Privatisation had not been delegated to an independent body as it had been in Brazil, so Kirchner could simply utilise his Executive power to halt and reverse this policy. The high level of support he had in Congress, ensured that they were willing to allow him to do this. The lack of *de facto* judicial independence ensured that Kirchner could rescind contracts with a higher level of confidence than Lula in Brazil, that the judiciary would support his actions.⁴⁹⁰ Therefore, as hypothesised in Chapter Two, Argentina would be the most likely of the three case studies to halt all privatisations due to the configuration of the specific political institutions in place in that country. As in Brazil under Lula, policy outcome in Argentina under Kirchner in the area of privatisation was primarily a product of the constellation of the political institutions within that state.

⁴⁹⁰ Interestingly, until 2005, the country was heavily in debt, but the multilateral institutions had little influence. This was most likely because of the scale of Argentina's default, coupled with the IMF's acceptance of some of the blame.

Chapter Seven – The Evolution of Privatisation in Uruguay

The last of the three chosen case studies is Uruguay. In October 2004, Tabaré Vázquez of the left-wing alliance, *Encuentro Progresista - Frente Amplio - Nueva Mayoría* (EP-FA-NM), became the first left-wing candidate in Uruguay's democratic history to win the Presidency. When Vázquez assumed office, privatisation had not been implemented to the same extent in Uruguay as it had been in Argentina and Brazil. This was mainly as a result of a specific institutional configuration that allowed for mechanisms of direct democracy.

The purpose of this chapter is to provide historical context for the analytical narrative of Vázquez's Presidency. This chapter will trace the evolution of privatisation policy in Uruguay until the election of Vázquez in 2004. The first section will briefly outline the development and role of public enterprises in Uruguay. The second section will discuss the transition to democracy and the first attempt at privatisation in Uruguay during the Presidency of Julio Sanguinetti. The third section will examine the Presidency of Luis Lacalle and his ill-fated 1992 privatisation law, while the fourth section will briefly discuss the second Sanguinetti Presidency. The fifth section will examine Jorge Batlle's attempt to introduce privatisation in Uruguay, while the final section will outline the legacy of this policy in Uruguay by the time Vázquez came to power.

7.1 The Origins and Role of Public Enterprise in Uruguay

The size and extent of state-owned enterprises in Uruguay was a product of the Presidencies of José Batlle y Ordóñez and the first period of *batllismo* (1903-1916) (Nahum, 1993: 12; Yaffé, 2001: 5-6). When Batlle came to power, the growth and expansion of the state's role in the economy accelerated. Batlle, influenced by the Liberal reforms of Lloyd George and Joseph Chamberlain, established the state banks, the *República* and *Hipotecario*, nationalised all foreign insurance firms, monopolised the state's production of electrical energy and the ports service, and between 1911 and 1915, he created further state monopolies in alcohol, merchant shipping, telephones and refrigeration (Nahum, 1993: 13-17; Yaffé, 2001: 7). Batlle's decision to create a large number of state enterprises was not motivated by ideology, but a desire for industrialisation that was simply not forthcoming from the Uruguayan populace (Nahum, 1993: 15). The importance of state-enterprises in

Uruguay was solidified with the 1917 constitution and the policy of co-participation. Co-participation ensured proportional access among the two main political parties to public goods and as a result, the state enterprises became integral for the two traditional parties, for rents, patronage and clientelism (Bergara *et al.* 2005: 23; Filgueira & Papadópulos, 1997: 374).

With the 1930s, a new relationship between the state, the economy and society began, but the growth of state enterprises continued (Yaffé, 2001: 11; Azar & Yaffé, 2003: 3-5; Lanzaro, 2004: 119-120). The numbers employed in state-owned companies grew by 22,000, and new state monopolies were created in railways, transport, water and sanitation (Nahum, 1993: 65). Despite the economic crisis of the mid-1950s, the expansion of the state enterprises did not halt. Instead, the political parties used the state to employ any workers that remained unabsorbed by the private sector, a practice that continued until the bureaucratic authoritarian regime came to power in the 1970s (see Table 7.2 below) (Filgueira & Papadópulos, 1997: 375-376; Sondrol, 1997: 110).

The end result of this uninterrupted growth of state enterprises for nearly six decades was the domination of the Uruguayan economy by public companies. As Table 7.1 shows, by the time the military came to power in 1973, the Uruguayan state held a monopoly, or near monopoly in a number of strategic areas. Furthermore, state enterprises had grown to employ nearly 60,000 workers (see Table 7.2 below) (World bank, 1994: 10-11; Bensión, 2006: 40). But, this unbridled growth of the public sector produced two major dysfunctions. Firstly, public sector growth led to a large middle class dependent upon the state. This group relied upon the public sector to maintain their position and would passionately resist any attempt to alter the status quo. Secondly, the hyper-politicisation of state enterprises ensured that they were crucial for the clientelistic politics practised by the two main political parties.

Table 7.1: The Dominance of State Enterprises in the Economy

Sector	Dominance of Sector
Farming	○
Fishing	○
Pits and Mines	○
Rail	●
Combustibles	●
Aviation	●
Manufacturing	□
Electricity, Gas	●
Building	●
Telecoms	●
Transport, Storage	□
Financial Institutions and Securities	●
Ports	●
Water Supply	●

● fully or predominantly public sector; □ mixed sector; ○ fully or predominantly private sector

Source: Bensi3n (2006: 39) & World Bank (1994: 10)

Table 7.2: The Growth of Public Sector Employment ('000s)

Year	Population	Employees of State Enterprises
1938	1870	7.5
1941	1970	11.1
1955	2400	49.7
1961	2590	55.7

Source: Nahum (1993: 65)

7.2 The Transition to Democracy and the Election of Sanguinetti

The beginning of liberalisation in Uruguay can be traced back to the bureaucratic authoritarian military regime that took power after the 1973 coup (Bensi3n, 2006: 14; de Sierra, 1992: 248). Between 1974 and 1975, due to severe balance of trade problems, all the financial restrictions on imports were lifted and levels of import tax reduced, combined with a policy of fiscal austerity and reduced social spending (Bensi3n, 2006: 14-15). Although privatisation was discussed, it was never seriously attempted and the government limited themselves to simply reducing the number of employees in some state enterprises (de Sierra, 1992: 248). These reforms not only managed to address the balance of trade deficit, but also led to rapid growth (World Bank, 1994: 3). However, by the early 1980s, Uruguay was suffering a serious recession (Blake, 1998: 9) and by the time of the Naval Club pact in 1984 and the transition to democracy, Uruguay had witnessed a 'general restoration of a status quo ante: government giganticism, presidentialism and factionalised party politics' (Sondrol, 1997: 114).

In 1980, the military government attempted to institutionalise their rule through a highly repressive constitution, which was resoundingly rejected by the Uruguayan electorate in a referendum held in the same year. This defeat, coupled with the military's inability to rectify the country's economic ills, set in motion the process of democratic transition (Blake, 1998: 9; Sondrol, 1997: 114). Eventually, in March 1984, after nearly four years, the military offered to hold democratic elections, and in the six months before the elections, the main political parties and the major interest groups established the *Concertación Nacional Programática* (CONAPRO), which designed a shared platform for the Uruguayan government that would be implemented regardless of who won the actual election (Molano, 1997: 71; Blake, 1998: 9).⁴⁹¹ In this manner, a framework for co-operation was established between the two major Uruguayan political parties, the *Partido Colorado* (PC – Colorado Party) and the *Partido Nacional* (PN – National Party),⁴⁹² and in the November 1984 elections, Julio Sanguinetti of the PC became the first civilian Uruguayan President in over 12 years (Molano, 1997: 71).

After the election, Sanguinetti attempted to forge the government envisioned by CONAPRO, but the PN and the left-wing *Frente Amplio* refused to co-operate (Blake, 1998: 9-10). Although unemployment had fallen, it still remained high at 10 per cent and inflation was now running at an annual average rate of 84.1 per cent (World Bank, 1994: 3; Blake, 1998: 10). The new government's main economic objective was to reduce the fiscal deficit and bring the public finances to order, mainly through reduced spending on social welfare and privatisation (Filguiera & Papadópulos, 1997: 364; Molano, 1997: 69). By the early 1980s, widespread clientelism and patronage in the state enterprises had rendered many of these companies highly inefficient. These enterprises had become a significant burden on the state, with the deficit generated by Uruguayan state companies representing 18.4 per cent of GDP by 1982 (Molano, 1997: 69).

Sanguinetti's initial attempt at privatisation occurred in September 1986, when he sent to the legislature a bill to partially privatise the national airline, *Primeras Líneas Uruguayas de Navegación Aérea* (PLUNA). However, mainly as a result of opposition from the trade unions and from all three political parties, not only was the bill rejected, but the legislature even refused to debate the issue (Bensión,

⁴⁹¹ For comprehensive accounts of the democratic transition, see Gillespie (1991) or Filguiera (1985).

⁴⁹² The *Partido Nacional* is also known as the *Blancos*.

2006: 44; Filguiera & Papadópulos, 1997: 377). Despite this initial failure, Sanguinetti remained undeterred and one year later he turned his attention to the national railroad operator, *Administración de los Ferrocarriles del Estado* (AFE). The company was re-organised, the number of personnel was reduced and certain services previously offered by AFE, such as large cargo transport, the restaurant in the general station and medical assistance services, were privatised (Bensión, 2006: 43).⁴⁹³

The lack of political support for privatisation ensured that Sanguinetti's initial foray in this direction had petered out by 1988. In fact, not only were there practically no privatisations during the first Sanguinetti administration, the state actually ended up assuming control over a number of private companies. As a consequence of the banking crisis of 1982, the state, between 1985 and 1987, through the *Banco de la República* and the *Corporación Nacional para el Desarrollo* (CND),⁴⁹⁴ assumed control of three private banks that had fallen into insolvency: the *Banco Pan de Azúcar*, the *Banco Comercial* and the *Caja Obrera* (Bensión, 2006: 40).

Furthermore, Sanguinetti's attempts to reduce social spending also proved futile. The retiree organisation, the *Organización Nacional de Jubilados y Pensionistas del Uruguay* (ONJPU), blocked a 1987 social spending reform favoured by the World Bank, by sponsoring a plebiscite on a constitutional reform that would incorporate an automatic indexation of benefits (Filguiera & Papadópulos, 1997: 365). The plebiscite, which ran concurrently with the general election in 1989, was approved by 82 per cent of voters, significantly raising the fiscal burden on the state (Filguiera & Papadópulos, 1997: 376; Filguiera & Moraes, 1999: 12).

Although Sanguinetti attempted to alter the state's role in the national economy, his initiatives were limited to only minor changes 'that did not significantly trim the state apparatus, nor lead to significant institutional reforms' (Narbondo & Ramos, 1999: 38). There are a number of important points to note. Firstly, in Brazil under Sarney and in Argentina under Alfonsín, privatisation was driven by fiscal constraints and the need to control inflation. Uruguay however, did

⁴⁹³ In the same year, Sanguinetti did manage to have a law passed allowing for the de-concentration in the health care system (Filguiera & Moraes, 1999: 29).

⁴⁹⁴ The CND was established in 1985, in order to provide finance and advice to private enterprises so as to stimulate their growth. It was also responsible for assuming control of businesses that were in financial trouble (seeensión, 2006: 40).

not suffer the hyperinflation experienced by Brazil and Argentina during the same period and the inflation rate, albeit a rate of nearly 80 per cent, actually remained relatively constant for most of the 1980s (Blake, 1998: 10; Molano, 1997: 69). Also, Uruguay did not experience a single recessionary year in the first six years following the transition to democracy.

Secondly, the Sanguinetti administration experienced practically no external pressure to privatise. Uruguay had signed a standby agreement with the IMF in 1985, and while this agreement stipulated that the government must reduce spending to 1.5 per cent of GDP, it did not mention privatisation (Molano, 1997: 70). Thirdly, opposition from well-organised interest groups to any proposed privatisation was fierce. The attempt to partially privatise PLUNA was derailed mainly as a result of strident union opposition, allied not only with the two main left-wing parties, the *Frente Amplio* and the *Nuevo Espacio*, but also with members of the two traditional political parties (Filguiera & Papadópulos, 1997: 377).

Finally, during the democratic transition, the military intentionally weakened the new civilian government and they remained a constant threat to the new democracy. The military continued to harangue the administration, limiting the policy options available to Sanguinetti in his first years in office. It was only with the 1986 *Ley Caducidad*, which granted a military amnesty, that the threat began to recede. As such, 'with political issues absorbing most of the administration's resources and focus, it was unable to implement many economic reforms' (Molano, 1997: 71).

7.3 The Election of Luis Alberto Lacalle

With the election of Luis Alberto Lacalle of the *Partido Nacional* in 1989, privatisation once again appeared on the political agenda. By the late 1980s, the fiscal deficit had grown to nearly 5.5 per cent of GDP, triggering a resurgence of inflation (Bergara *et al.* 2005: 59; Molano, 1997: 69). The 1989 election therefore, was primarily concerned with economic issues, and Luis Lacalle campaigned on a platform of market-orientated reform that proposed privatisation (Filguiera & Papadópulos, 1997: 378; Blake, 1998: 10). Lacalle, once in power, faced a legislature that was controlled by the opposition *Colorados*. However, the worsening economic situation convinced Jorge Areco and Jorge Battle of the *Colorados*, to sign a bi-partisan pact with the *Blancos*, the *Coincidencia Nacional*, that committed

congressional support for Lacalle's economic reforms (Filguiera & Moraes, 1999: 15; Molano, 1997: 72). This alliance set three major goals for economic reform: reform of the social security system, fiscal reform and the privatisation of state-owned enterprises (Molano, 1997: 72).

The new Economy Minister, Enrique Braga, and Lacalle sent a privatisation initiative to Congress in the form of Resolution no. 1122, and after a period of intense negotiations, Law 16,211, the Privatisation of National Public Services, was passed in October 1991 (Molano, 1997: 72; Blake, 1998: 12; Filguiera & Papadópulos, 1997: 378). This law attempted to create a legal and institutional framework within which a policy of privatisation could operate. Law 16,211 proposed the partial privatisation of PLUNA, the closure of the state fishing firm, ILPE, while most importantly, articles 10 to 14 allowed for the partial privatisation of the flagship telecommunications firm, ANTEL.⁴⁹⁵

Once this law was passed, Lacalle moved quickly to begin the sale of 51 per cent of ANTEL. However, opposition to the sale soon began to ferment. These disparate groups, led by the left-wing *Frente Amplio* and comprising the public sector trade unions, factions of the traditional political parties, and the powerful pensioner associations that had successfully thwarted Sanguinetti and initiated the 1989 plebiscite, came together to form a united front against privatisation through the establishment of the *Comisión de Defensa del Patrimonio Nacional y Reforma del Estado* (de Sierra, 1992: 253; Filguiera & Papadópulos, 1997: 378; Bensión, 2006: 46). This group managed to collect enough signatures to hold a referendum on articles 10 to 14 (Bensión, 2006: 46). This vote was also publicly supported by Sanguinetti and the *Foro Batllista* faction of the *Colorados*, and on December 13th 1992, the sale of ANTEL was overwhelmingly rejected by nearly 70 per cent of the electorate (Panizza, 2004: 10; Bensión, 2006: 46; Filguiera & Papadópulos, 1997: 378).

Although the result of the plebiscite only prevented the privatisation of ANTEL, it was to sap the momentum, not only for economic reform during Lacalle's remaining two years, but also for any future attempts at privatisation (Sondrol, 1997: 117). The legacy of this plebiscite ensured that Lacalle and future administrations, not only had to consider the chance of any state reform legislation being accepted by

⁴⁹⁵ Ley 16,211 available at <http://www.parlamento.gub.uy/leyes/AccesoTextoLey.asp?Ley=16211&Anchor>

Congress, but also the likelihood that opposition groups would mobilise and campaign for a public vote against it (Panizza, 2004: 10).

Privatisation during Lacalle's tenure did continue, but it was now limited to peripheral public services and bankrupt state-enterprises. The state-owned fishing company, *Industria Lobera y Pesquera del Estado* (ILPE), was closed and in July of 1994, 49 per cent of PLUNA was sold to a consortium of Uruguayan and Argentine investors.⁴⁹⁶ The Lacalle administration also oversaw the re-privatisation of the *Banco Comercial* and the *Banco Pan de Azúcar*, two of the three banks that fell into state hands due to insolvency during Sanguinetti's tenure (Bensión, 2006: 44-47).

Law 16,211 also allowed concessions for certain services to be offered to the private sector, but the threat of opposition to any major privatisation ensured that Lacalle could do little but offer concessions for services that were relatively peripheral to the functioning of the state. Consequently, only five such concessions were offered during his tenure in areas such as roads, hostelry, sanitation and the management of passenger terminals (see Table 7.3 below). In August 1990, Lacalle also introduced a bill that provided for the abrogation of the legal state monopolies in alcohol, insurance, port services, telecommunications and casinos. Due to the unfavourable political climate towards state reform, Lacalle only dismantled the state's monopolies in two sectors: port services and insurance (Bensión, 2006: 51-52).

Lacalle's attempts to rectify the fiscal deficit by reducing social spending were also severely hampered, mainly because the opposition framed any of Lacalle's social security proposals as covert privatisation (Filguiera & Moraes, 1999: 15). Lacalle submitted five different social spending bills to the legislature between 1992 and 1994 and all five bills were quickly rejected (Filguiera & Papadópulos, 1997: 367; Coelho, 2002: 52). The *Frente Amplio* successfully portrayed all these initiatives as the first step towards privatisation and as a consequence, very few of the political party factions were willing to be associated with any legislation that resembled privatisation of the social security system. The failure of Lacalle's social security bills testify to the incredibly hostile atmosphere that existed at this time towards any type of privatisation in Uruguay.

⁴⁹⁶ Further souring the public perception of privatisation, the sale of PLUNA was considered highly unsatisfactory, as until 2005, the state had to continue subsidising the airline to prevent it from becoming insolvent (see Bensión, 2006: 45).

Table 7.3: Lacalle's Concessions to the Private Sector

Concession	Details	Date	Cost
Casino at Punte de Este	20 year concession to construct and manage a five star hotel and casino at Punte de Este	Aug 1992	Initial cost of US\$217 million, followed by a fee of US\$3.2 million upfront, \$3.3 million between 1998 and 1999 and \$6.5 million by 2016.
Water and Sanitation in Maldonado	25 year concession to provide water and sanitation to the tourist zone of Maldonado	Sep 1993	<i>Aguas de la Costa</i> S.A. obliged to invest US\$9 million in service.
Motorway between Montevideo and Punte de Este	13 year concession to build and manage a motorway from Montevideo to Punte de Este.	Sep 1993	Cost of US\$65 million.
Airport Laguna del Sauce	16 year concession, with the support of World Bank, to run and expand the airport at Laguna del Sauce	Dec 1993	Initial US\$40 million investment, followed by yearly fee
Maritime Passenger Terminal in Montevideo	10 year concession to manage maritime passenger terminal in Montevideo, and also to build and manage a duty free shop within the terminal	Sep 1994	Initial investment of US\$9 million, and 30% tax on profits from terminal and 7.5% on profits from the duty-free

Source: Bensión (2006: 60-65)

By the end of Lacalle's term in office, he had failed to substantially reform the public sector. Again, there are a number of important points to note. Firstly, as during Sanguinetti's term, the international financial institutions played little or no role in encouraging Lacalle to adopt a policy of privatisation. Uruguay was not dependent upon the World Bank or the IMF for financial assistance as most of the country's borrowing was conducted with other institutions such as the Inter-American Development Bank (IADB), and as Molano (1997: 70) notes, the IADB 'was mainly interested in promoting social programmes, not the type of structural reforms pursued by the IMF and World Bank. Hence, the major multilateral lending organisations had little impact on Uruguayan privatisation policies.'

Secondly, while part of Menem's success at implementing privatisation in Argentina was predicated upon his ability to build a diverse coalition in support of such measures, part of Lacalle's failure to implement privatisation in Uruguay, was based upon his inability to build a similar winning reformist coalition (Filguiera & Moraes, 1999: 7). In theory, Lacalle should have found it easier than his predecessor to build a coalition in favour of privatisation, mainly as a result of the propitious evolution of the system of co-participation. As a result of the emergence of the *Frente Amplio*, the two traditional parties could no longer legitimately utilise state enterprises as mass patronage tools, and so political resistance to privatisation should

have diminished somewhat by Lacalle's Presidency (Panizza & Philip, 2005: 673; Bergara *et al.* 2005: 23).⁴⁹⁷ However, the opposite was actually the case.

The opposition of the *Colorados* was not based upon any ideological grounds or defence of the system of co-participation, but rather on worries over political competition. The law stipulated that the proceeds of the sale of ANTEL be spent on social security and welfare, and the opposition were worried that the *Blancos* would use this money in order to build support for their party through the distribution of favourable resources (Molano, 1997: 73).

Furthermore, business organisations were weak and poorly organised in Uruguay, and the *Camara de Industrias del Uruguay* only supported Lacalle's privatisation initiative after the government promised to slow down the pace of tariff cuts in the Mercosur. Also, as a result of Lacalle's attempt to reduce the fiscal deficit, he had significantly curtailed the military budget, and therefore was forced to placate a temperamental and recalcitrant military that refused to support any of his economic reforms (Molano, 1997: 73-76).

Compounding Lacalle's lack of support, the anti-privatisation coalition appeared to be growing in strength and numbers. In 1992, a strike by ANTEL's workers in opposition to privatisation paralysed the telecommunications industry. This strike was then followed by a 72 hour general strike (Filguiera & Papadópulos, 1997: 370-371; Molano, 1997: 68). Workers in state enterprises earned nearly double that of their counterparts in the private sector and in other parts of the public administration, providing a major incentive for public sector union mobilisation against privatisation (Bensión, 2006: 42).

The emergence of powerful pensioner associations, which had been created during the Sanguinetti Presidency, also played an important role in resisting the privatisation of ANTEL. Pensioner associations viewed privatisation as part of larger reform efforts to dismantle the state's role in the economy, justifying their participation in the anti-privatisation coalition (Molano, 1997: 75; Filguiera & Papadópulos, 1997: 363-368). While all these different groups had an interest in opposing privatisation, it was the leadership of the *Frente Amplio* that forged these disparate groups into a unified and mobilised anti-privatisation coalition (Filguiera & Papadópulos, 1997: 378; de Sierra, 1992: 253; Molano, 1997: 75-76). The

⁴⁹⁷ Although the success of some of the larger state enterprises was still essential in transferring rents to the state treasury as mandated by Law 16,170 of 1990 (seeensión, 2006: 41).

establishment of the *Comisión de Defensa del Patrimonio Nacional y Reforma del Estado* provided a clearly identifiable political movement that served as a rallying point for all those interest groups opposed to privatisation in Uruguay.

Finally, it was the specific institutional mechanism of direct democracy that allowed these interest groups access to a major veto point in the Uruguayan political system, providing them with the ability to derail privatisation policies. When Congress passed Law 16,211, the *Frente Amplio* and the anti-privatisation coalition utilised the mechanisms of direct democracy to hold a plebiscite proposing the derogation of articles 10 to 14 of this law. The success of this plebiscite was to sap the momentum, not only for economic reform during Lacalle's remaining two years, but also for any future attempts at privatisation. Future administrations, not only had to consider the chance of any state reform legislation being accepted by Congress, but also the likelihood that opposition groups would mobilise and campaign for a public vote against it. This institutional mechanism ensured that as long as the electorate did not support privatisation, any future privatisation attempt could be vetoed by recourse to a referendum sponsored by organised interest groups.

7.4 The return to power of Sanguinetti

The 1994 election witnessed Julio Sanguinetti, the leader of the largest faction within the *Partido Colorado*, the *Foro Batllista*, returned as President for a second time. Sanguinetti, who campaigned on a platform of state reform that attempted to distance himself from the 'scorched earth policies' employed by other Southern Cone leaders, failed to capture a majority in either the upper or lower house. In order to ensure governability, Sanguinetti crafted a well-structured *Colorado-Blanco* coalition by allocating 50 per cent of all cabinet seats to the opposition *Blancos* (Panizza, 2004: 14; Panizza & Philip, 2005: 678; Sondrol, 1997: 120). The *Colorado-Blanco* coalition had developed a programmatic agenda of reforms that was drafted by working groups comprised of technocrats and politicians from the two parties (Filguiera & Moraes, 1999: 17; Panizza & Philip, 2005: 678). This agenda consisted of major state administrative reform, reform of public education, the alteration of the regulatory system for the electricity sector, the modernisation of state-owned enterprises and social security reform (Narbondo & Ramos, 1999: 39; Panizza & Philip, 2005: 678; Coelho, 2002: 52-53).

Privatisation of state-owned enterprises appeared to be off Sanguinetti's policy agenda, mainly because of Lacalle's failed attempt to privatise ANTEL, but Sanguinetti was proposing the partial privatisation of the social security system. Lacalle, and Sanguinetti in his first term in office, had both attempted social security reform, and both had been prevented from doing so as a result of the mobilisation of organised interest groups and their recourse to mechanisms of direct democracy. Despite the certainty of fevered opposition, Uruguay's pay-as-you-go single pillar pension system was approaching a fiscal meltdown, lending an urgent imperative to Sanguinetti's attempt at reform. The disbursements of the social security system administrator, *el Banco de Previsión Social* (BPS), had grown from 10.4 per cent of GDP in 1990 to 15.1 per cent of GDP by 1994 (Forteza *et al.* 2005: 10; Bensión, 2006: 33).

Shortly after assuming power, Sanguinetti sent his proposals for social security reform to congress in the form of Law 16,713, which was passed on the 3rd of September 1995.⁴⁹⁸ This law mandated for the partial privatisation of the pension system in Uruguay, through the creation of a mixed, public and private system (Luján, 2002: 97; Filgueira & Moraes, 1999: 18). Workers under the age of 40 would now have the option of contributing half of their taxes on earnings to a private pension fund administered by an *Administradora de Fondos de Ahorro y Previsión* (AFAP). Retired persons were left in the existing pension pillar and the 1989 constitutional amendment remained in force (Bensión, 2006: 35-36; Filgueira & Moraes, 1999: 18; Kay, 1999: 408-409). The reform did not exclude anyone from contributing to the state pay-as-you-go system, and while AFAPs can be in the hands of private agents, the state was also represented in the AFAP pillar.⁴⁹⁹ In order to reduce opposition to the initiative, the military, police, notaries, bank-workers and university professionals were exempted from the reform (Luján, 2003: 97-99; Filgueira & Moraes, 1999: 18-19; Kay, 1999: 408-409).⁵⁰⁰

Although Law 16,713 partially privatised the social security system, Sanguinetti had replaced the privatisation of state-owned enterprises on the policy agenda, with the modernisation of these enterprises. The defeat of Lacalle's 1992

⁴⁹⁸ Ley 16,713 available at

<http://www.parlamento.gub.uy/leyes/ AccesoTextoLey.asp?Ley=16713&Anchor>

⁴⁹⁹ In fact, the state's AFAP represents nearly 40 per cent of the market share (see Bensión, 2006: 37).

⁵⁰⁰ For greater detail on the social security reform under Sanguinetti, see for example, Luján (2002) or Filgueira & Moraes (2000).

privatisation law had significantly raised the political cost of attempting to implement privatisation in Uruguay, and so the focus had shifted from privatisation to modernisation (Traversa, 2004: 43; Bergara, 2005: 56). The focus was now on new forms of management within the public sector, and maximising transfers to the treasury from the state companies, rather than on the overall size of the state (Traversa, 2004: 43; Bergara, 2005: 56).

Nonetheless, Sanguinetti did continue to offer concessions on minor public services as provided for by the 1992 privatisation law, and he also continued the process of dismantling the state's legal monopolies begun by Lacalle. The public services offered to the private sector were limited to the construction and management of three motorways; one between Montevideo and Libertad, one between Montevideo and Mendoza, and one between Pando and Minas (Bensión, 2006: 63). Sanguinetti also ended the legal monopoly of the state in the alcohol and drinks market. What was to prove more controversial however, was Sanguinetti's legislation to reform the regulatory framework of the electricity industry.

Law 16,832 of June 1997, allowed for the possibility of private investors to compete in the electricity generating market.⁵⁰¹ However, the state electricity firm, *Usinas y Teléfonos del Estado* (UTE), would retain a monopoly in the distribution and transmission of electrical energy. This law never contemplated the privatisation of UTE, but it did allow for both private competition in the generation market and for UTE to associate with private firms (Bergara *et al.* 2005: 55;ensión, 2006: 55-56). Despite the fact that this law only proposed de-monopolisation in one aspect of the electricity market, opposition groups began mobilising to hold a referendum to derogate the law (Bergara *et al.* 2005: 55). Eventually, this attempt was abandoned and the law was ratified, although the regulations did not actually come into force until 2000, when the new regulatory agency, the *Unidad Reguladora de la Energía Eléctrica* (UREE) was established (Bergara *et al.* 2005: 55;ensión, 2006: 55-56). As of 2006 however, UTE remained the only company operating in the generation, distribution and transmission of electricity in Uruguay (Bensión, 2006: 56).⁵⁰²

⁵⁰¹ Ley 16,832 available at

<http://www.parlamento.gub.uy/leyes/AccesoTextoLey.asp?Ley=16832&Anchor>

⁵⁰² The state actually ended up taking over private enterprises teetering on the brink of insolvency. In 1996, the Central Bank was forced to take control over the *Banco Pan de Azúcar* (BPA) and the *Banco Crédito* (Bensión, 2006: 47).

Sanguinetti's other major endeavours to reform the state included an attempt to reform the public health care system that was eventually rejected by Congress, and a wide-ranging civil service re-structuring law, '*La reforma administrativa del estado*' (administrative reform of the state) (see Panizza & Philip, 2005; Panizza, 2004; Narbondo & Ramos, 1999). The civil service reform was only supported by the political parties because it exempted state-enterprises and left untouched the practice of appointing political supporters to high-level posts within the civil service (*cargos de particular confianza*) (Panizza, 2004: 20).

So, by the end of Sanguinetti's second term in office, no state enterprises had actually been privatised. Sanguinetti concentrated on state reform and modernisation rather than privatisation. During this period, the legacy of Lacalle's failed privatisation law and the subsequent opposition referendum can be clearly witnessed. Now, not only an actual referendum, but also the threat of a referendum to derogate a government law acted as a major veto point. The potential of opposition groups to derail any government attempt at privatisation through mechanisms of direct democracy had significantly raised the political cost of attempting to implement this policy. Consequently, Sanguinetti shifted the political focus from the privatisation of state-owned enterprises, to the modernisation of these enterprises (Traversa, 2004: 43; Bergara, 2005: 56).

The potential for mass interest group mobilisation and the threat of a subsequent public referendum was also evident throughout Sanguinetti's preparations for the partial privatisation of the social security system. Ironically, social security privatisation was given a major political impetus by the rise in popularity and success of the left-wing *Frente Amplio* in the 1994 elections (Luján, 2002: 104; Forteza *et al.* 2005: 15; Filguiera & Moraes, 1999: 8). This imminent threat to the traditional parties' duopoly on power led the *Colorados* and the *Blancos* to realise that 'coalitions to pass broad reforms and sustain them were needed if the traditional parties wanted to hold on to their hegemony over the political system for the last 150 years' (Filguiera & Moraes, 1999: 8). For the first time since the return to democracy, a significant reform could occur under the wing of a stable, programmatic political coalition between the two major parties.⁵⁰³

⁵⁰³ In fact, the threat of the left also encouraged the two traditional parties to sponsor a reform of the electoral system. If the electoral system remained unchanged, the FA would have most likely come to power in the 1999 elections. On December 8th 1996, a plebiscite was held that approved the

When a referendum petition was actually issued, the electoral court dictated that such a move was unconstitutional, since the Executive had a legal monopoly over social security legislation. Such an argument could not be used to prevent the 1989 plebiscite, as this referendum proposed an amendment to the constitution rather than the derogation of an existing law (Filguiera & Moraes, 1999: 20). Opponents would now only have recourse to a constitutional amendment by means of a plebiscite to derail the reform. However, plebiscites can only be held alongside national elections and Sanguinetti, by pushing the reform through in his first year in office, was assured 'of more than four years in which to organise the new system before it can be put to the test of a plebiscite' (Forteza *et al.* 2005: 16). The struggle to have the social security reform passed as early as possible in 1995 was based on this rationale (Forteza *et al.* 2005: 16; Bergara *et al.* 2005: 52). Consequently, by 1999, the new two-pillar system had created new stakeholders in the reform; nearly half a million people had signed up to an AFAP, diminishing the potential support for a plebiscite (Filguiera & Moraes, 1999: 20).

7.5 The Election of Jorge Batlle

Although the first round of the 1999 elections was won by the left-wing *Frente Amplio* candidate, Tabaré Vázquez, with 39 per cent of the vote, the 1996 electoral reform promoted by the *Colorado* and *Blanco* parties (see footnote 481 above), forced a second-round run-off that witnessed the two traditional parties allying with each other in the face of the leftist threat.⁵⁰⁴ Consequently, the run-off returned Jorge Batlle of the *Partido Colorado* as the new President, who promptly forged a coalition government of the *Colorados* and *Blancos*. Although inflation in 1999 was at its lowest point in fifty years and the Uruguayan economy had grown over the last three years, the early contagion effects of the *Real* devaluation in Brazil and the deepening recession in Argentina were beginning to widen cracks in the Uruguayan economy.⁵⁰⁵ Batlle had run on a free-market ticket that promised to further reduce the role of the state in the economy.⁵⁰⁶

constitutional reform of the electoral system. The main change was the introduction of the majority run-off system, in order to improve the chances of the traditional parties remaining in power (see Bergara *et al.* 2005: 46-48).

⁵⁰⁴ The Economist, December 4th, 1999.

⁵⁰⁵ The Economist, December 4th, 1999.

⁵⁰⁶ The Economist Intelligence Unit, Country Monitor: Americas, January 19th, 2000.

Within a few months of assuming office however, Batlle was facing the prospect of a serious economic downturn, as the widespread fears about the negative effects of contagion appeared to become reality. Low prices for agricultural exports and Argentina's economic woes were slowly driving the Uruguayan economy into recession.⁵⁰⁷ The budget deficit amounted to 4.2 per cent of GDP in 2001 and Uruguay lost its investment-grade rating, raising the cost of borrowing for the state.⁵⁰⁸ Uruguay's economic slide was accelerated by the financial collapse of Argentina in 2001. Argentines with money in Uruguayan banks began rapidly withdrawing their deposits. The country's foreign reserves fell by US\$200 million a month and Uruguayans, witnessing the actions of the Argentines, began a run on the banks.⁵⁰⁹ With reserves slowly disappearing, Uruguay was forced to abandon its currency-band system and let the peso sink freely.⁵¹⁰ As the value of the Uruguayan peso slowly slid downhill, the value of Uruguay's debt, denominated in dollars, steadily rose uphill and by the start of 2002, the debt represented 52 per cent of GDP.⁵¹¹ The economy shrank by 11 per cent in 2002 and the rate of unemployment hit 20 per cent.⁵¹² The return of the fiscal deficit led to the resurgence of inflation, which was soon back in double figures, reaching 14 per cent in 2002 and 20 per cent in 2003.⁵¹³

The government response to this crisis was a fiscal squeeze involving tax rises and spending cuts, but disagreement remained as to where the axe should fall.⁵¹⁴ These disagreements intensified and in October 2002, four ministers from the minority *Partido Nacional* quit, leaving Batlle with the prospect of a minority government in the middle of one of the worst economic crises the country had ever faced.⁵¹⁵ With the debt increasing steadily, default began to appear highly likely,⁵¹⁶ prompting the IMF to eventually step in with a US\$3.8 billion rescue loan in August

⁵⁰⁷ The Economist, 3rd February, 2001.

⁵⁰⁸ The Economist, April 6th, 2002.

⁵⁰⁹ The Economist, March 1st, 2003.

⁵¹⁰ The Economist, July 27th, 2002.

⁵¹¹ The Economist, April 6th, 2002.

⁵¹² The Economist, December 13th, 2003.

⁵¹³ The Economist Intelligence Unit, Country Monitor: Uruguay, November 10th, 2003.

⁵¹⁴ The Economist, June 8th, 2002.

⁵¹⁵ The Economist Intelligence Unit, Country Monitor, Americas, November 4th, 2002.

⁵¹⁶ Although Uruguay did not technically default on their debt, they did so in all but name by eventually opting for a debt swap plan in April 2003. For more details see Latin America Financial Alert, April 21st, 2003.

2002.⁵¹⁷ In return for this loan, the IMF insisted that the government widen the tax base, cut pension fund deficits, offer certain public services to the private sector and end the state monopolies in energy and telecoms.⁵¹⁸

Unable to initiate any outright privatisations due to the likelihood of intense public opposition, but subscribing to the argument that privatisations would boost the economy by attracting foreign investment, aiding the fiscal deficit and lowering costs, Batlle began offering concessions to the private sector for public services, as provided for by Law 16,211 (see Table 7.4 below).⁵¹⁹ Batlle's strategy of offering concessions to the private sector did not lead to wide repercussions politically because the concessions tended to be a localised phenomenon and because most of these concessions did not require a sectoral law (except for Carrasco and ANP), mechanisms of direct democracy could not be utilised to halt their sale (Bergara *et al.* 2005: 58).⁵²⁰

Table 7.4: Batlle's Concessions to the Private Sector

Concession	Details	Date	Cost
Drinking Water in Maldonado	30 year concession offered by state enterprise OSE to Uruagua SA, to invest in and provide drinking water for Maldonado	Oct 2000	US\$12 million investment required
Container Terminal in Montevideo	30 year concession to operate and manage the 80% of the container terminal in Montevideo	June 2001	US\$17.1 million paid for management contract
National race track in Maroñas	A 30 year concession for the operation and management of the betting shops in the Maroñas race track.	May 2002	Annual fee of US\$500,000 to be paid to the state.
Radio electric spectrum	20 year concession to maintain and operate the radio electric spectrum	Oct 2002	Abiatar paid US\$6 million for concession
Carrasco Airport	20 year concession, to repair, operate and manage carrasco airport terminal	Aug 2003	A fee of US\$34 million paid to the government for operating company.

Source: Bensión (2006: 64-67)

Following the success of the early public service concessions and with the necessity for fiscal severity, Batlle turned towards the more politically risky subjects of further dismantling the state's legal monopolies and the partial privatisation of state-enterprises. In February 2001, the legislature passed a law that allowed Spanish investors to operate and run the port of Mbopicuá on the Río Uruguay. By 2005,

⁵¹⁷ The Economist, March 1st, 2003.

⁵¹⁸ The Economist, April 6th, 2002.

⁵¹⁹ The Economist, February 3rd, 2001.

⁵²⁰ Although the main trade union in ANTEL, did vociferously oppose the sale of the radio-electric spectrum. See El Observador, April 11th, 2004.

foreign investors were also operating with the co-operation of local government in two other ports (Bensión, 2006: 49). In the same month, the legislature also passed a law that ended ANCAP's legal monopoly in the production and sale of asphalt in Uruguay (Bensión, 2006: 57). Neither of these laws generated much opposition, but this was to change when Batlle turned his attention to the state telecommunications firm ANTEL.

In 2000, Batlle, through Articles 612 and 613 of the national budget, Law 17,296, attempted to dismantle the monopoly of the state firm ANTEL in the provision of mobile phone services and long-distance calls (Bergara *et al.* 2005: 55; Forteza, *et al.* 2005: 25; Bensión, 2006: 57-58). These articles re-iterated ANTEL's monopoly in the provision of basic telephone services, but they also allowed for the partial privatisation of ANCEL, ANTEL's mobile phone division, and for private competition in the long-distance market.⁵²¹ Following the introduction of this law, the telecommunications union, the *Sindicato Único de Telecomunicaciones* (Sutel), and the *Comisión de Defensa del Patrimonio Nacional*, led by the *Frente Amplio*, began the process of collecting signatures to hold a referendum on Articles 612 and 613 and in January 2001, they announced that they had collected enough signatures to hold a referendum on the issue.⁵²² Batlle and his government announced in March 2002 that they themselves would derogate Articles 612 and 613 in order to prevent a referendum.⁵²³ The law that Batlle sent to congress to derogate these articles, re-affirmed ANTEL's monopoly in the provision of basic telephone services.⁵²⁴ However, in the intervening period before Batlle repealed this law, ten private companies had entered the long-distance market, and although new firms could no longer enter the market, Batlle's administration successfully argued that the licences already granted to these firms while the law was in place were still valid (Forteza *et al.* 2005: 25; Bergara *et al.* 2005: 55).

In 2001, Batlle turned his attention to the state oil company, ANCAP, and its legal monopoly in the area of combustibles. Following intense negotiations that even involved members of the *Frente Amplio*, the legislature agreed to pass Law 17,448 in December 2001 (Forteza *et al.* 2005: 25; Bergara *et al.* 2005: 55). This law proposed

⁵²¹ Ley 17,296 available at

<http://www.parlamento.gub.uy/leyes/AccesoTextoLey.asp?Ley=17296&Anchor>

⁵²² *Cronicas*, January 25th, 2001.

⁵²³ *Cronicas*, March 22nd, 2002.

⁵²⁴ *Cronicas*, March 22nd, 2002.

to allow ANCAP to associate with private investors in the refining, distribution and sale of oil, and also to dismantle ANCAP's monopoly on the importation of combustibles into Uruguay.⁵²⁵ Unsurprisingly, the main umbrella union organisation, the PIT-CNT, quickly began to voice opposition to this proposed initiative, and with the support of the *Frente Amplio*, they began to collect signatures to hold a referendum to repeal this law in March 2002.⁵²⁶ With the leader of the *Frente Amplio*, Tabaré Vázquez, insisting that reform of ANCAP was needed rather than any type of privatisation,⁵²⁷ over 60 per cent of the electorate voted to repeal this law in December 2003 (Bensión, 2006: 51).

During Batlle's term in office, the need for fiscal austerity and price stabilisation, combined with pressure from the international financial institutions, placed privatisation once again on the political agenda. However, despite these external and macro-economic pressures, it was ultimately the institutional structure that allowed for mechanisms of direct democracy that shaped the policy outcome. While Batlle did succeed in introducing foreign firms into the long-distance telephone market, in order to avoid an imminent referendum on the issue, he was forced to derogate his own law and in doing so, re-iterated ANTEL's monopoly in the provision of telephone services in Uruguay. His attempt to dismantle ANCAP's monopoly in the combustibles market and allow the company to associate with foreign investors was resoundingly defeated in a referendum on the issue. As long as interest groups who opposed privatisation could mobilise public support, any major attempt at privatisation would be vetoed through recourse to institutional mechanisms.

7.6 The Legacy of Privatisation in Uruguay

After numerous attempts at privatisation, Uruguay had failed to divest itself of any significant state enterprises. By 2004, only 13 public service concessions had been offered to the private sector, one bankrupt state enterprise had been closed and another partially privatised. The state's monopolies in a number of areas had been dismantled and the social security system had been partially privatised, but all major privatisation attempts had failed. Lacalle's attempt to partially privatise ANTEL was

⁵²⁵ Ley 17,448, available at <http://www.parlamento.gub.uy/leyes/ AccesoTextoLey.asp?Ley=17448&Anchor>

⁵²⁶ *Cronicas*, March 22nd, 2002.

⁵²⁷ *El Observador*, December 2nd, 2003.

repealed by referendum, the legacy of which was to overshadow any of Sanguinetti's attempts at state reform. Batlle's attempt to allow ANTEL to associate with private investors eventually resulted in him derogating his own law in order to prevent a referendum on the issue, while his attempt to partially privatise ANCAP was also struck down by public referendum.

Privatisation policy in Uruguay for these two decades therefore, has been primarily shaped by the institutional structure that allows for mechanisms of direct democracy. Well-organised interest groups, under the leadership of the *Frente Amplio*, managed to forge a militant anti-privatisation coalition that consistently opposed any attempts to introduce privatisation in Uruguay. The historical development of the Uruguayan state produced an electorate that was hostile to any attempt at state reform or privatisation. Each time an administration attempted reform of this kind, the anti-privatisation coalition mobilised public opinion on this issue and by exploiting mechanisms of direct democracy, they simply vetoed these initiatives.

Chapter Eight – Privatisation under Vázquez

The 2004 Uruguayan elections were held against the backdrop of a country slowly beginning to regain its feet after the crippling effects of economic depression. Social unrest and economic turbulence as a result of the 2002 crisis, prompted the electorate to reject the duopoly on power held by the two traditional political parties, who turned to the candidate of the left-wing coalition, *Encuentro Progresista - Frente Amplio - Nueva Mayoría* (EP-FA-NM), Tabaré Vázquez. Vázquez was elected President of Uruguay in October 2004, marking the first time in Uruguay's 178-year history that a candidate from a party other than the *Partido Colorado* or *Partido Nacional* had won a national election (Panizza, 2008: 178; Arocena, 2005: 147). Vázquez, like his counterparts in the Southern Cone, Kirchner and Lula, campaigned on a platform that attacked Neoliberalism and the primacy of the market-model for engendering much of the social and economic turmoil in the state. Vázquez proposed a model that was predicated upon greater state involvement in the economy and that specifically rejected all privatisations. Like Kirchner and Lula, Vázquez's entire campaign was centred upon the idea of change and transformation. Campaign materials referred to an EP-FA-NM government as '*El Gobierno del Cambio*' (the government of change) (Frente Amplio, 2004a, 1), while the motto of the left's campaign was the simple '*cambiamos*' (let's change) (Altman & Castiglioni, 2006: 150).

This chapter is the analysis of privatisation policy during Vázquez's Presidency. It will attempt to determine if there was any major change in privatisation policy once Vázquez came to power. It is divided into two main parts. The first part takes the form of a narrative and briefly outlines the 2004 election. This section will establish the motivations and preferences of Vázquez's government. The second section of the narrative actually examines the policy of privatisation once Vázquez is in power. The second part of this chapter is the analysis, and this analysis is grouped around the independent variables identified in chapter two. The final section will present the conclusion.

The Narrative

8.1 The 2004 Election

The 2002 crisis had nearly precipitated the collapse of the Uruguayan economy (see chapter seven), but by the time of the national election in October 2004, the economy had already begun the slow path towards recovery. The peso had appreciated in value, inflation had fallen to below 8 per cent, bank deposits had risen, the country's risk premium had been reduced and growth was now exceeding 10 per cent.⁵²⁸ But this recovery was tempered by persistently high unemployment and indigence, and a public debt that had jumped from 41 per cent of GDP in 1999 to 111 per cent of GDP by the end of 2003 (Banco Central del Uruguay, 2005: 69). The winner of the 2004 election would be presented with the immediate task of having to refinance US\$2.1 billion of maturing debts, an amount equivalent to 14 per cent of GDP.⁵²⁹

The grim reality of this economic situation encouraged voters to become increasingly disillusioned with the two traditional political parties and their mismanagement of the economy (Altman & Castiglioni, 2006; Arocena, 2005; Luna, 2004). The left-wing EP-FA-NM coalition in contrast,⁵³⁰ having never been in government, remained untainted by the country's economic woes (Queirolo, 2006: 43). Offering the dissatisfied electorate an alternative set of economic proposals and buoyed by their support for the successful 2003 referendum rejecting the partial privatisation of the state oil firm ANCAP (see chapter seven),⁵³¹ the left-wing coalition began the 2004 campaign as favourites to win the election.⁵³² Indeed, for Panizza (2008: 181), the EP-FA-NM:

[w]as in an ideal position to capitalise on popular opposition to the programme of neoliberal economic reforms implemented by successive Blanco and Colorado governments during this period. It did so by presenting itself as the guardian of the Batllista state, which had allegedly been dismantled by the traditional parties' neoliberal reforms.

⁵²⁸ Brazil Report, December 21st, 2004

⁵²⁹ Brazil Report, December 21st, 2004

⁵³⁰ The coalition was a broad based movement comprising communists, socialists, former *tupamaro* guerrillas and Christian democrats. The main factions of the FA included the Partido Socialista (PS), the Partido Comunista (PC), Asamblea Uruguay (AU), Movimiento Participación Popular (MPP), Alianza Progresista (AP), Vertiente Artiguista (VA), Nuevo Espacio (NE) and Liga Federal (LF).

⁵³¹ See NotiSur, December 19th 2004 and Brazil Report, November 23rd, 2004

⁵³² The decline in the support of the two traditional parties was not solely as a result of the 2002 crisis. In fact, this was a process that had begun with the return to democracy in 1985, and which was rooted in 'deep-seated popular dissatisfaction with the status quo' (Panizza, 2008: 178). The two traditional parties were unable to counter this erosion in their support mainly due to the 'decreasing possibilities of using the state as the national employer and as a springboard for pork-barrel politics' (Altman & Castiglioni, 2006: 153).

The EP-FA-NM's position was re-enforced by the unity of the coalition, with Tabaré Vázquez emerging as their sole uncontested Presidential candidate at the party primaries in June 2004.⁵³³ Vázquez, a member of the *Partido Socialista*, was a respected oncologist and formerly mayor (1990-1994) of the *Frente Amplio* administration of Montevideo (Winn & Ferro-Clérico, 1997: 450).⁵³⁴

The *Frente Amplio* had emerged at the beginning of the 1970s to contest the 1971 election, as a coalition of communists, socialists and Christian democrats with strong links to the union movement, opposed to the authoritarian and conservative government of the time.⁵³⁵ Their 1971 programme advocated bank nationalisation and agrarian reform (Yaffé, 2002: 41; Panizza, 2008: 179), and although they had moderated their stance in the intervening years, their economic programme for the 2004 election still sought to 'limit the role of market forces. It favoured a more interventionist, protectionist and socially orientated state, with a bias towards the working class and those working in the state sector' (Panizza, 2008: 1983).

The EP-FA-NM's election manifesto, *Grandes Líneas Programáticas*, agreed at their fourth congress in Montevideo in December 2003, was focused upon increasing the role of the state in the economy and addressing the pressing issues of inequality and indigence (Frente Amplio, 2004b). It was harshly critical of the market model adopted by subsequent *Blanco* and *Colorado* governments, claiming that 'the structural legacy of neoliberalism has left our country with hundreds of thousands of our compatriots in situations of poverty, inequality, emigration' and 'unemployment' (Frente Amplio, 2004b: 1). The economic chapter of the manifesto had an entire section, entitled '*Otorgue un rol activo y orientador del Estado*' (granting an active and directive role for the state), that outlined a new role for the state in the economy and argued that 'to develop the country's productive potential and to distribute the results with social justice, requires an active state, able to orient this process' (Frente Amplio, 2004b, 11). State enterprises were to be essential for this new role, with the manifesto promoting 'a strong and efficient public bank' and a crucial role for state enterprises in the development of infrastructure and tourism

⁵³³ Party primaries are mandatory in Uruguay and they are held on the same day for all parties competing in the Presidential election. The *Partido Colorado* also had only candidate, Guillermo Stirling, while Jorge Larrañaga defeated Luis Lacalle to win the nomination for the *Partido Nacional* (Altman & Castiglioni, 2006: 149).

⁵³⁴ For an analysis of the FA administration of Montevideo, see Winn & Ferro-Clérico (1997).

⁵³⁵ For comprehensive overviews of the growth of the left in Uruguay, see for example the edited volumes of Lanzaro (2004) and Garcé & Yaffé (2004).

(Frente Amplio, 2004b: 12). What is more, the document explicitly stated that ‘the state-owned enterprises, in that they have a strategic role, will be reformed to protect the national patrimony and the state management’ (Frente Amplio, 2004b: 12). The manifesto further proclaimed that ‘the state will assume economic activities where the private sector is reluctant to take risks, and will rescue firms facing closure, when there exists a positive social and/or economic evaluation of their activities’ (Frente Amplio, 2004b: 12). In fact, not once was the word privatisation mentioned in the entire document.

During the election campaign, although Vázquez tried hard to avoid been drawn on substantive economic issues (Panizza, 2008: 183),⁵³⁶ he continued to criticise the neoliberal model and his antagonistic stance towards privatisation remained unequivocal.⁵³⁷ In an interview with the weekly *Búsqueda* he stated that ‘we have received a horrific legacy as a consequence of the politics of neoliberalism, which is the cause and maintenance of this crisis.’⁵³⁸ He continued to focus on the theme of transformation suggesting that ‘the winds of change are blowing...to totally destroy the neoliberal model,’⁵³⁹ and he promoted ‘another model’ that ‘would not privilege finance over the productive model.’⁵⁴⁰ As regards the state-owned enterprises, Vázquez declared that ‘we have a very clear position vis-à-vis privatisations. The strategic sectors should remain in the hands of the state,’⁵⁴¹ and instead argued for the ‘professionalisation and reform of the structures’⁵⁴² of the state-owned companies.

The position of Vázquez and the EP-FA-NM as regards privatisation was further illustrated through their support for the referendum on water provision that was due to be held concurrently with the national election in October 2004. In March 2003, Jorge Batlle submitted a bill to congress entitled ‘*Regulación de los Servicios de Agua Potable y Saneamiento*,’ that aimed to open up the water provision sector to private entities. Immediately, resistance to this initiative began to build and by January 2004, over 280,000 signatures calling for a referendum on the bill had been

⁵³⁶ The FA’s election campaign was organised and led by the *Movimiento de Participación Popular* (MPP), the largest faction within the FA.

⁵³⁷ In personal communication with Alvaro Forteza (March 2008), Daniel Buquet (March 2008) and Daniel Chasqueti (March 2008)

⁵³⁸ *Búsqueda*, September 2nd, 2004

⁵³⁹ *Reforma*, October 31st, 2004

⁵⁴⁰ Agencia EFE, August 4th, 2004

⁵⁴¹ *Morning Star*, August 30th, 2004

⁵⁴² *Búsqueda*, September 2nd, 2004

collected.⁵⁴³ This opposition was spearheaded by the *Comisión Nacional en Defensa del Agua y de la Vida*, comprising members of the water services union, Ffose, the national trade union movement and over twenty other national social organisations.⁵⁴⁴ The referendum proposed amending Articles 47 and 188 of the Constitution.⁵⁴⁵ Article 47 would be altered to classify water as ‘a natural resource essential for life,’ where ‘access to drinking water and sanitation, constitute fundamental human rights.’⁵⁴⁶ Furthermore, the management and operation of water services in Uruguay would be ‘exclusively conducted by state-owned entities.’⁵⁴⁷ From the beginning, the referendum campaign was supported by Tabaré Vázquez and the EP-FA-NM coalition.⁵⁴⁸ Members of the EP-FA-NM were involved in launching the campaign for a public plebiscite,⁵⁴⁹ and when questioned about the upcoming plebiscite, Vázquez stated: ‘We support this referendum and the attempt to change the constitution. We will vote for it. We feel that water is a public good and absolutely essential for a decent standard of living.’⁵⁵⁰

Vázquez’s support for the plebiscite caused some concern among international investors, specifically as the proposed constitutional amendment would raise questions over the positions of two multinational firms, *Uragua* and *Aguas de al Costa*, already operating water provision services in Uruguay.⁵⁵¹ Vázquez, while on a tour to Spain, asserted that the referendum would not be retroactive and that his administration would respect private contracts already in place.⁵⁵² In order to further soothe the nerves of the capital markets, he also announced that Daniel Astori,⁵⁵³ a respected economist with moderate views from the *Asamblea Uruguay*, would be his new Economics Minister.⁵⁵⁴ Astori, while critical of the policies adopted by his predecessors, infused his economic rhetoric with a more moderate tone (Astori, 2004).

⁵⁴³ La República, January 30th, 2004

⁵⁴⁴ La República, January 30th, 2004

⁵⁴⁵ NotiSur, November 12th, 2004

⁵⁴⁶ Clarín, October 24th, 2004

⁵⁴⁷ Clarín, October 24th, 2004

⁵⁴⁸ Clarín, November 1st, 2004

⁵⁴⁹ La República, January 30th, 2004

⁵⁵⁰ Morning Star, August 30th, 2004

⁵⁵¹ El País (Uruguay), November 7th, 2004

⁵⁵² La República, July 6th, 2004

⁵⁵³ Vázquez had initially offered this position to Enrique Iglesias, President of the Inter-American Bank, who declined the offer (Altman & Castiglioni, 2006: 150).

⁵⁵⁴ La República, July 14th, 2004

These moves broadened Vázquez's appeal to include disillusioned centre-left supporters of the traditional parties and on Election Day on October 31st 2004, Tabaré Vázquez was elected President of Uruguay with 50.5 per cent of the vote, defeating his closest rival, Jorge Larrañaga of the *Partido Nacional*, by nearly 17 percentage points (Altman & Castiglioni, 2006: 148).⁵⁵⁵ More importantly, Vázquez won the election outright with over 50 per cent of the vote, therefore avoiding a second-round run-off. This victory was further bolstered by the overwhelming success of the referendum that Vázquez had endorsed and supported throughout the election campaign, proposing to establish water as a basic human right and definitively preventing the privatisation of water provision services in Uruguay.⁵⁵⁶ The EP-FA-NM also won 52 of the 99 seats on offer in the Chamber of Deputies, and 16 of the 30 seats in the Senate, providing the coalition with a narrow majority in both houses.⁵⁵⁷ In fact, not since 1966 had an elected Uruguayan president enjoyed a majority in Congress (Altman & Castiglioni, 2006: 148).

8.2 Privatisation with Vázquez in Power

Tabaré Vázquez was inaugurated as President of Uruguay on March 1st 2005 and his comprehensive outright victory in the first round of the election and the majority he could now boast in both houses placed, Vázquez in a stronger political position than any other administration since the return to democracy in 1985 (Panizza, 2008: 185; Buquet & Chasquetti, 2005: 148). Since 2002, the economy had slowly begun to regain its feet, with GDP growing by a remarkable 12.3 per cent in 2004, inflation stabilising at 8 per cent and unemployment falling to just over 12 per cent from a high of nearly 20 per cent in mid-2002 (Banco Central del Uruguay, 2005: 13-16).

However, there were dark clouds hovering on the horizon. Although Vázquez held a majority in both houses, it was a very narrow one and he did not have the necessary three-fifths majority to appoint supporters to key posts in the administration, let alone the two-thirds majority needed for constitutional reform, heightening the potential importance of party discipline (Altman & Castiglioni, 2006: 153; Buquet & Chasquetti, 2005: 147-150). The buoyancy and optimism in the

⁵⁵⁵ Guillermo Stirling, the candidate for the *Partido Colorado* received only 10 per cent of the vote, the worst election result in the party's history (Altman & Castiglioni, 2006: 148).

⁵⁵⁶ The proposed constitutional amendments were overwhelmingly approved by 64.6 per cent of the valid vote (Altman & Castiglioni, 2006: 148).

⁵⁵⁷ Corte Electoral, Elecciones Nacionales 2004, available at <http://www.corteelectoral.gub.uy/gxpfiles/elecciones/Elecciones%20Nacionales%202004.htm>

economy also masked some serious structural problems. The numbers of those living in poverty in Uruguay had increased from 18 per cent in 2001 to nearly 32 per cent by 2004 (Instituto Nacional de Estadística, 2006), while Uruguay's debt had climbed alarmingly from 41 per cent of GDP in 1999 to 101 per cent of GDP by the end of 2004 (Banco Central del Uruguay, 2005: 69). In order to manage this debt, Vázquez was facing the prospect of prolonged fiscal rectitude. The economy and national infrastructure were also desperately in need of investment, but domestic savings would not suffice and Vázquez and the *Frente Amplio*⁵⁵⁸ had explicitly expressed their opposition to privatisation, ensuring that the administration would have to attract foreign capital in some other manner.⁵⁵⁹

Once in power, Vázquez's main concerns therefore were maintaining a disciplined party in the legislature, addressing the inequality in Uruguayan society, dealing with the unwieldy public debt and attracting much-needed investment. His choice of cabinet reflected his desire to maintain unity within his left-wing party. His new ministers consisted of two main groups: those that were leaders of the main factions within the FA and those that were Vázquez's close confidants (Buquet & Chasquetti, 2005: 150). The leaders of the main factions within the coalition comprised 43 per cent of the cabinet posts and 88 per cent of the legislative weight of the FA (Buquet & Chasquetti, 2005: 150).⁵⁶⁰ The remaining eight posts were shared out among members of his own *Partido Socialista* and trusted independents (Buquet & Chasquetti, 2005: 150).⁵⁶¹ In spreading the cabinet posts among the leaders of the major factions, Vázquez hoped to inspire unity and discipline within the FA.⁵⁶² To tackle the issue of indigence, Vázquez established the Ministry for Social Development (MIDES), and launched an emergency social fund, *Programa de atención nacional a la emergencia social* (Panes), targeted at families living in

⁵⁵⁸ In December 2005, the EP and NM parties officially joined the *Frente Amplio*, so the rest of this chapter will follow Panizza (2008: 178) in referring to the former coalition as simply the *Frente Amplio*.

⁵⁵⁹ Global Insight, Uruguay: Quarterly Review and Outlook, Third Quarter 2005.

⁵⁶⁰ The leaders of the factions were: José Mujica (MPP), Agriculture; Danilo Astori (AU), Economy; Reinaldo Garagano (PS), Foreign Affairs; Mariano Arana (VA), Living and Marína Arismendi (PC), Social Development. Added to these posts were Rodolfo Nin Novoa, (AP), Vice-president and President of the Senate (Buquet & Chasquetti, 2005: 150).

⁵⁶¹ These included: Azucena Berruti (PS), Defence; Jorge Brovetto (Ind), Education and Culture; Jorge Leptra (Ind), Energy and Minerals; José Díaz (PS), Interior; María Julia Muñoz (Ind), Public Health; Eduardo Bonomi (MPP), Employment and Social Security; Víctor Rossi (AP), Transport and Public Works and Héctor Lescano (AP), Tourism and Sports (Chasquetti, 2007: 257).

⁵⁶² This task was aided by the success of the FA in local elections in May.

extreme poverty (Filgueira & Lijenstein, 2006: 64; Panizza, 2008: 189; Chasquetti, 2007: 250).⁵⁶³

In order to deal with the public debt, Vázquez was forced to come to an agreement with the IMF and this was to place pressure on state enterprises and public services. After the crisis of 2002, the previous Batlle administration had made the decision to avoid default at all costs, and in order to do so, they negotiated a re-structuring of the debt with private bondholders (Panizza, 2008: 185). As a consequence of this agreement, the government was left with a heavy interest and principal debt burden, necessitating further support from the IMF. The tacit acceptance of this deal by the FA while in opposition, generated a ‘path-dependent trajectory,’ that required the FA to come to agreement with the IMF once in power (Panizza, 2008: 186). Negotiations with the IMF for a stand-by loan had begun as soon as the election was over, and two months after assuming office in May 2005, the IMF accepted the administration’s letter of intent detailing their economic programme for the next three years (Luján, 2007: 184; Panizza, 2008: 187; Arocena, 2005: 154).⁵⁶⁴ The *Memorandum of Economic and Financial Policies* proposed economic stability and a ‘comprehensive structural reform agenda’ that committed the government to a primary fiscal surplus of 3.5 per cent of GDP (International Monetary Fund, 2005a: 3). Although privatisation was not mentioned in the document, the FA administration did aspire towards ‘improving the efficiency of the public enterprise sector,’ and ‘preparing them for competition with the private sector,’ through the expansion of ‘private sector activities in public utilities and infrastructure’ (International Monetary Fund, 2005a: 3, 8).

However, while privatisation was not mentioned, the letter of intent did commit the government to the re-privatisation of the *Nuevo Banco Comercial* (NBC) (International Monetary Fund, 2005a: 7). NBC was created by the state in the wake of the 2002 banking crisis with the assets of three insolvent private banks, the *Comercial*, *Montevideo* and *Caja Obrera* (Bensión, 2006: 49). Concurrent with the release of the letter of intent in May 2005, Astori announced that NBC was to be re-privatised and by September, an agreement was reached with a consortium headed by investment fund Advent International.⁵⁶⁵ Following the approval of the Uruguayan

⁵⁶³ Panes was modelled on the *Bolsa Família* in Brazil (Panizza, 2008: 189).

⁵⁶⁴ For a comprehensive overview of these negotiations, see Luján (2007).

⁵⁶⁵ *El Observador Económico*, September 7th, 2005

banking superintendent 8 months later,⁵⁶⁶ Advent assumed control of NBD in a deal worth US\$167 million, out of which the state made a profit of US\$67 million to be spent on the development of infrastructure.⁵⁶⁷ The state was also to continue to participate in the decision-making process at the bank, through their seat on the bank's fiscal commission.⁵⁶⁸

To attract much-needed investment, the government was keen to signal stability and continuity to private capital and immediately after the election, Vázquez announced that he would be abandoning his proposal to revise the public service concessions of the previous Batlle government, while also announcing that he would respect all previous contracts signed by private entities with the state (Ibarra, 2006: 152). In fact, on May 20th and contrary to the wishes of a number of powerful interest groups, Vázquez issued a decree stating that: 'The non-state entities that have the capacity to provide public service sanitation or water for human consumption, and have signed contracts before 31st October 2004, can continue to administer the above services until expiration of the original agreed contract date.'⁵⁶⁹ This decree proposed negating the retroactivity of the October referendum and respecting the concessions of *Uragua* and *Aguas de al Costa*. Inevitably, the decree generated opposition, particularly from workers of the state water and sanitation company, OSE, radical elements of the FA and from the *Comisión de Defensa del Agua*, who collected over 3,000 signatures demanding that Vázquez revoke the decree and return all private water and sanitation concessions to state hands.⁵⁷⁰

The conservative economic strategy however, adopted by Vázquez and Astori, significantly reassured international investors. The marked improvement in relations between Uruguay and investors was confirmed when the government successfully issues some US\$300 million in sovereign bonds, covering the country's financing requirement for the whole of 2005.⁵⁷¹

Despite the decree, the state water company, OSE, had already commissioned a report that recommended rescinding the contract of *Uragua* and penalising the

⁵⁶⁶ El Observador Económico, May 16th, 2006

⁵⁶⁷ El País, June 1st, 2006

⁵⁶⁸ El Observador Económico, June 4th, 2006

⁵⁶⁹ Decreto 157/05, Artículo 1: Presidencia de la República Oriental del Uruguay, Mayo 2005, available at

http://www.presidencia.gub.uy/Web/decretos/2005/05/CM%2071_20%20MAY%2005_00001.PDF

⁵⁷⁰ El País (Uruguay), May 31st, 2005

⁵⁷¹ Uruguay Review, July 30th, 2007.

company for breach of contract, including work delays and lack of investment.⁵⁷² Ironically, for its part, *Uragua*, a subsidiary of *Aguas de Bilbao*, argued that the constitutional referendum of October *was* retroactive and as such, it was illegal for the firm to continue to provide water and sanitation services in Uruguay.⁵⁷³ The firm, realising that the referendum had essentially ended any possible future expansion plans in Uruguay, wished to exit the market and hoped that the government would nationalise the contract, thereby ensuring that *Uragua* could leave Uruguay with all its assets and the US\$20 million in contractual guarantees. So, two weeks after Vázquez had issued the decree respecting the water and sanitation concessions signed before the October referendum, a notice appeared on the website of the OSE followed by a government press conference announcing that the state had decided to rescind the contract of *Uragua* for incompleteness of the terms of the concession.⁵⁷⁴ What is more, in rescinding the contract, Vázquez decided to hold on to the valuable contractual guarantees much to the chagrin of the Spanish-owned firm.⁵⁷⁵

In response, the company launched a legal action against the state and lodged a case with the World Bank's arbitration tribunal, ICSID. Following failed attempts at conciliation, the company remained steadfast in its demand for an indemnity of US\$24 million⁵⁷⁶ and eventually, nearly a year after the constitutional reform, *Uragua* and the Vázquez government finally came to an agreement enabling OSE to assume control of the company⁵⁷⁷ and absorb all 115 former employees of *Uragua*.⁵⁷⁸ In exchange for all operations and assets of *Uragua* in Uruguay valued at US\$15 million, the Spanish firm would, in return, get to keep the contractual guarantees worth US\$20 million. In addition, *Uragua* was to pay invoices to creditors worth US\$2.8 million and the concession fees to OSE for April and May (US\$1.5 million).⁵⁷⁹ After the state assumed control of this concession, 97.1 per cent of all water and sanitation services in Uruguay were now in state hands.⁵⁸⁰ When asked to comment on the remaining 2.9 per cent of services in the hands of *Aguas de*

⁵⁷² Business News Americas, March 23rd, 2005

⁵⁷³ El País (Uruguay), August 30th, 2005

⁵⁷⁴ El País (Uruguay), May 31st, 2005

⁵⁷⁵ El Observador, June 14th, 2005

⁵⁷⁶ El País (Uruguay), June 28th, 2005

⁵⁷⁷ *Uragua's* concession in Uruguay served 50,000 households in *Pan de Azúcar*, *Piriápolis*, *Maldonado* and *Punte del Este*.

⁵⁷⁸ El País (Uruguay), October 8th, 2005

⁵⁷⁹ El País (Uruguay), October 8th, 2005

⁵⁸⁰ El Observador, June 2nd, 2005

la Costa, Mariano Arana, the minister responsible, stated: ‘*Aguas de la Costa* has a contract until 2018 and as long as they fulfil the terms of their accord, there will be no problems.’⁵⁸¹

Ironically however, the company in question did not quite share this optimistic outlook. In September 2005, reports began to appear in the Madrid daily, *CincoDías*, that the Spanish firm *Aguas de Barcelona* (Agbar), who owned 60 per cent of *Aguas de la Costa*, was interested in ending their operations in Uruguay and Argentina.⁵⁸² Their desire to leave the Argentinean market was driven by the growing acrimony between the company and Néstor Kirchner,⁵⁸³ while in Uruguay, the company, similar to *Uragua*, believed that the referendum in October not only threw doubts on the sustainability of their existing contract, but that it definitively paralysed the water and sanitation privatisation process in Uruguay, and in doing so, dashed any future hopes the company may have harboured for expansion in this market.⁵⁸⁴ Two weeks later, OSE announced that they would be interested in buying Agbar’s share of *Aguas de la Costa* and with the support of Vázquez,⁵⁸⁵ by February, OSE had reached an agreement to purchase *Aguas de la Costa* for US\$3.4 million to be paid in two instalments of US\$1.7 million each.⁵⁸⁶ Vázquez’s administration was motivated to purchase Agbar’s share of *Aguas de la Costa*, firstly, as this would enable the government to level all tariffs for water services across the country and secondly, as this would complete the constitutional reform of 2004⁵⁸⁷ as all water and sanitation services would now be in state hands.⁵⁸⁸

Legislative approval for the purchase of *Aguas de la Costa* was necessary as the other 40 per cent of the company was owned by a number of local businessmen, who refused OSE’s offer to purchase their share. OSE therefore needed to legally create a new mixed-ownership enterprise in order to manage the concession with private actors until 2018.⁵⁸⁹ The Executive sent a bill to the legislature proposing the

⁵⁸¹ El Observador, June 2nd, 2008

⁵⁸² CincoDías, September 12th, 2005

⁵⁸³ CincoDías, September 12th, 2005

⁵⁸⁴ El País (Uruguay), September 13th, 2005

⁵⁸⁵ El Observador, September 30th, 2005

⁵⁸⁶ La República, February 19th, 2006

⁵⁸⁷ The tariffs of *Aguas de la Costa* were generally 10 to 50 per cent higher than those charged by OSE. See El Observador, September 30th, 2006

⁵⁸⁸ El Observador, September 30th, 2006

⁵⁸⁹ El Observador, February 15th, 2006

transaction in April⁵⁹⁰ and despite the opposition of the *Herrerismo* faction of the PN, who could do little in the face of the FA majority in both houses, OSE assumed control of the operations and assets of *Aguas de la Costa* in September 2006 and received permission from Mariano Arana to lower the water and sanitation tariffs of the homes in Maldonado previously served by this concession.⁵⁹¹

Following an announcement in March 2006 that the government was planning to pay off ahead of schedule debts of US\$130 million and US\$300 million with the World Bank and Inter-American Development Bank,⁵⁹² and in the midst of a fractious and controversial tax reform (Traversa, 2006: 148),⁵⁹³ the government, still desperately in need of infrastructural investment, approved plans for two concessions to be offered to the private sector. In June, the government advertised for concessionaires to manage a landfill in Cañada Grande in order to handle the municipal waste of Montevideo,⁵⁹⁴ while the following month, Vázquez approved plans to tender out the construction and management of a new US\$300 million port at *Puntas del Chileno*.⁵⁹⁵ Astori favoured the idea of using public-private concessions to develop infrastructure⁵⁹⁶ due to a lack of domestic savings and high levels of public debt, combined with the fact that these concessions were not privatisations and did not therefore require any specific legal approval.⁵⁹⁷ Vázquez also agreed to let the state oil firm, ANCAP, operate in a joint venture with the Brazilian and Venezuelan state energy companies, PETROBAS and PDVSA.⁵⁹⁸ This decision was questionable as it could be interpreted to have contradicted the results of the 2003 referendum prohibiting ANCAP from associating with private enterprises.⁵⁹⁹

By the end of 2006, Astori's growth-orientated policies appeared to be a success. GDP growth was an impressive 7 per cent of GDP in 2006, while fixed capital formation represented 16 per cent of GDP in the same year, its highest level

⁵⁹⁰ El País (Uruguay), April 21st, 2006

⁵⁹¹ La República, October 10th, 2006

⁵⁹² Global Insight, Uruguay: Quarterly Review and Outlook, First Quarter 2006, p. 104.

⁵⁹³ The proposed tax reform was included in the May 2005 letter of intent with the IMF (International Monetary Fund, 2005a), and proposed the introduction of a personal income tax, altering corporate tax, reducing VAT and eliminating low-yield taxes in the hope of generating economic growth and improving equity (International Monetary Fund, 2005b: 4).

⁵⁹⁴ Business News Americas, June 6th, 2006

⁵⁹⁵ Business News Americas, July 12th, 2006

⁵⁹⁶ Allowing for private investment in infrastructure was also proposed in Uruguay's letter of intent to the IMF (International Monetary Fund, 2005a: 8).

⁵⁹⁷ In personal communication with Daniel Chasqueti (March 2008) and Daniel Buquet (March 2008)

⁵⁹⁸ In personal communication with Daniel Chasqueti, March 2008

⁵⁹⁹ In personal communication with Daniel Chasqueti, March 2008

since 1998 (Banco Central del Uruguay, 2007: 4-5). The economy's growth, combined with Vázquez's social programmes, also contributed to reductions in poverty and by the end of 2006, the number of those living in poverty had been reduced from a high of 31.8 per cent of the population in 2004 to 25.2 per cent of the population (Instituto Nacional de Estadística, 2006). Astori's fiscal rectitude had also ensured that the total public sector deficit for 2006 was only 0.8 per cent of GDP and this stringency enabled Uruguay to officially cancel its entire debt to the IMF at the end of the year, an amount of US\$2.6 billion (Banco Central del Uruguay, 2007: 7-9). Uruguay's last Letter of Intent to the IMF in December 2006 stated: '...we have paid off all outstanding obligations to the Fund. We do not intend to make any further drawings under the current agreement' (International Monetary Fund, 2006: 1).

However, not everything was bright for the Vázquez administration. Vázquez, as a result of increasing disillusionment with the Mercosur, had pursued a trade and investment framework deal with the United States in early January 2007, a move that had generated widespread public opposition and had threatened to split the FA down the middle (Chasquetti, 2007: 253).⁶⁰⁰ Part of the motivation for this decision was the result of an increasingly ugly dispute with Uruguay's larger Mercosur partner and neighbour, Argentina, over two proposed paper mill plants on the *Río Uruguay*, that had witnessed Argentina bring the dispute to the International Court in The Hague (Chasquetti, 2007: 252).⁶⁰¹ Compounding these problems was the very real threat of an upsurge of inflation at the beginning of 2007. Uruguay's complete dependence on foreign energy sources meant that the risk of higher inflation was correlated closely with higher international oil prices and initial

⁶⁰⁰ Vázquez's initial enthusiasm for the Mercosur had soon waned as a result of what he perceived to be the dominance of the larger states (Brazil and Argentina) in the organisation, a perception compounded by the increasingly ugly paper mills dispute with Argentina.

⁶⁰¹ Uruguay had managed to attract two firms, Metsia-Botnia of Finland and Ence of Spain, to construct two paper mill plants on the *Río Uruguay*, an investment worth US\$1.7 billion to the Uruguayan economy. However, Argentine protesters began to block a bi-national bridge in an effort to halt construction of the plants, as they argued that these plants would pollute the river and harm tourism in the area. The issue became imbued with nationalistic sentiment on both sides, partly as a result of media and political rhetoric. Following a trip to Spain by Kirchner, the Spanish firm Ence announced that they were halting construction and moving their plant 250km away, further worsening relations between the two states. Argentina took the issue to The Hague, began lobbying international creditors financing the investment and Argentine tourist boycotts cost the Uruguayan economy an estimated US\$300 million. Mediation by the Spanish king failed to rectify the matter and although the Finnish plant is now up and running, the dispute continues to quietly simmer (see *El Observador*, November 15th 2007, *Clarín*, December 13th 2006, *The Economist*, March 18th 2006, *Global Insight*, *Monthly Outlook: Uruguay*, December 2006, p. 66 and Chasquetti, 2007: 252-253).

estimates suggested that inflation in 2007 could exceed the target of the Central Bank.⁶⁰²

Amidst these troubles at the beginning of 2007, Vázquez oversaw the second re-privatisation of his administration.⁶⁰³ In 1994, during the Lacalle Presidency, 49 per cent of the state airline, PLUNA, had been privatised (see chapter seven). However by 2006, the Brazilian airline *Varig*, who owned the majority stake in PLUNA, were in dire financial trouble and consequently neglected the management of PLUNA, even refusing to pay the necessary US\$1 million payment to the International Air Transport Association to continue operating.⁶⁰⁴ Following a failed attempt by *Varig* to extricate themselves from PLUNA by selling their share to the Venezuelan state airline *Conviasa*,⁶⁰⁵ the company found itself on the brink of bankruptcy, requiring an immediate cash injection of at least US\$20 million.⁶⁰⁶ After *Varig* flatly refused to inject US\$10 million into the floundering airline,⁶⁰⁷ the national treasury was forced to provide PLUNA with a US\$4 million bailout to continue operating and in September 2006, the Uruguayan government increased its share of the airline to 90 per cent in order to prevent the company from going bankrupt.⁶⁰⁸ The Vázquez administration immediately began actively seeking a partner to rescue the beleaguered airline and by early January, the re-privatisation of the airline was complete, when the Argentine consortium, Leadgate Investment, agreed to purchase 75 per cent of PLUNA.⁶⁰⁹ Leadgate would now own 45 per cent of the airline directly, whilst also owning 40 per cent of *Sociedad Aeronautica Oriental*, a group controlled by the Uruguayan Raul Rodríguez that owned a further 30 per cent of PLUNA. The reason for this convoluted ownership structure was to ensure that at least 51 per cent of the company remained in Uruguayan hands as dictated by the law.⁶¹⁰ The Argentinean consortium agreed to invest US\$177 million in the company over two years and the Uruguayan government, who now owned 23

⁶⁰² Global Insight, Uruguay: Quarterly Review and Outlook, First Quarter 2007, p. 114.

⁶⁰³ Some of Vázquez's problems were offset by internal elections within the FA at the end of 2006 that acted as a plebiscite on Vázquez's government. The results were highly favourable to the administration. See Chasqueti (2007: 254-256).

⁶⁰⁴ El País, May 2nd, 2006

⁶⁰⁵ El Observador Económico, July 4th, 2006

⁶⁰⁶ El País, August 10th, 2006

⁶⁰⁷ El País, August 1st, 2006

⁶⁰⁸ El País, September 14th, 2006

⁶⁰⁹ El Observador Económico, January 9th, 2007

⁶¹⁰ El Observador Económico, June 18th, 2007 & El Cronista, February 16th, 2007

per cent of the company, agreed to immediately inject US\$18 million in order to ensure that the national airline remained solvent.⁶¹¹

As the state was rescuing PLUNA, Uruguay's state rail association, UFE, announced the creation of two new public-private enterprises. Tenders were announced for private investors interested in participating in the *Corporación Ferroviaria de Uruguay* (CFU), a company that would be responsible, in conjunction with AFE and the *Corporación Nacional para el Desarrollo* (CND) (see chapter seven), for the development and repair of 940 km of railway lines⁶¹² at a cost of US\$90 million, a third of which would come from the new private partner.⁶¹³ The second company would be a public-private association, active for 15 years that would be responsible for marketing, planning and coordinating cargo and logistics services in order to increase Uruguayan rail cargo capacity from 1.4 million tons to 3.5 million tons per annum.⁶¹⁴ AFE would remain solely responsible for the cargo trains themselves, and none of AFE's existing operations or responsibilities would be affected.⁶¹⁵ The association of AFE with private investors in the areas of cargo transport and railroad repair was first proposed by the Vázquez administration as early as 2005, as the rail network in Uruguay was in need of investment to the tune of US\$90 million, a sum beyond the resources of the state (International Monetary Fund, 2005b: 5).⁶¹⁶ The *Corporación Andina de Fomento* (CAF) was hired to develop the models for these public-private partnerships and by June,⁶¹⁷ four companies were actively negotiating with the government to invest US\$50 million in a company that would operate Uruguay's rail cargo transport,⁶¹⁸ whilst four bids had been received for the contract to recondition the 940 km of railway by September.⁶¹⁹ The Executive officially approved the creation of these mixed enterprises, in which the private partner would hold the majority share, at the end of February 2008, and all that remained was for the CND to select appropriate private partners for both enterprises from among the bids received.⁶²⁰

⁶¹¹ El Observador Económico, June 18th, 2007

⁶¹² Business News Americas, December 4th, 2006

⁶¹³ El País, February 16th, 2007

⁶¹⁴ El País, February 16th, 2007

⁶¹⁵ Business News Americas, December 4th, 2006

⁶¹⁶ Business News Americas, November 16th, 2006

⁶¹⁷ El País, February 17th, 2007

⁶¹⁸ El País, June 12th, 2007

⁶¹⁹ Business News Americas, November 12th, 2007

⁶²⁰ El País (Uruguay), February 21st, 2008

In response to the initiative to create two new mixed ownership enterprises in the rail sector, the PIT-CNT, at the behest of their communist wing, resurrected the *Comisión en Defensa del Patrimonio*.⁶²¹ The communist sector of the union believed, along with some sectors of the MPP, that there was a danger of future privatisations looming on the horizon in Uruguay. However, the resurrection of the *Comisión* did not generate much support among the majority of the PIT-CNT, with Juan Silveira, the co-ordinator of the socialist wing of the PIT-CNT, dismissing the fears of his communist counterparts and asserting that ‘an association is not a privatisation,’ a sentiment echoed by the co-ordinator of the PIT-CNT, Fernando Pereira.⁶²²

Vázquez, like Lula in Brazil and Kirchner in Argentina, had contested the Presidential election on a platform that criticised the market-friendly policies of his predecessors and like Lula and Kirchner, during the election campaign had rejected the possibility of privatisation in Uruguay. In Brazil, although privatisations significantly slowed, they did not stop. In Argentina, not only did they not stop, but there were also a number of instances of re-nationalisation. In Uruguay in contrast, once in power, the preferences of Vázquez remained constant⁶²³ and by the end of Vázquez’s first three years in power, there had been no actual privatisations, although there had been two instances of re-privatisation: the *Banco Nuevo Comercial*, a re-privatisation encouraged and supported by the IMF; and the re-privatisation of the national airline PLUNA, which the state took control of in order to prevent the company from falling into insolvency. The Vázquez administration had also offered concessions in infrastructure to the private sector and had allowed the state rail operator, UFE, to associate with private partners in the maintenance and repair of rail lines and the management of cargo services in Uruguay. However, the state also reassumed control of two water and sanitation companies; one through reluctant re-nationalisation and the other through formal purchase.

So, of our three cases, Uruguay appears to lie somewhere between the outcome in Brazil under Lula and the outcome in Argentina under Kirchner. So what explains this? This thesis argues that the political institutional structure in each state will either enable a partisan government to implement their preferences, by increasing their institutional control over policy, or to inhibit a partisan government

⁶²¹ El País (Uruguay), March 29th, 2008

⁶²² El País (Uruguay), March 29th, 2008

⁶²³ In personal communication with Daniel Chasqueti (March 2008), Daniel Buquet (March, 2008), Andrés Pereyra (May, 2008)

from implementing their preferences, by leaving them with little institutional control over the policy in question. Chapter four and chapter six demonstrated that the outcomes in Brazil and Argentina were due to the configuration of their political institutions. In Uruguay, it was primarily the institutional device that allowed for mechanisms of direct democracy that shaped the outcome of privatisation policy. The referendum on water and sanitation services in Uruguay in 2005 ultimately forced Vázquez to re-nationalise the two private companies operating in this sector, despite the fact this was contrary to his initial preference. Once the decision had eventually been made to assume control of these firms, it was his executive power and the discipline of his legislative support that enabled the nationalisation and purchase to succeed, despite opposition. There were no actual privatisations, an outcome that was primarily due to the fact that by the time Vázquez came to power, the threat of referenda had nearly completely removed the idea of privatisation from the policy agenda. The next section will analyse the actions of Vázquez in accordance with the independent variables identified in chapter two.

The Analysis

8.3 The Political Institutions

As in Brazil and Argentina, the Uruguayan political system is a Presidential system with three branches: the Executive, Congress and the Judiciary. In Uruguay, as in other Latin American Presidential systems, the Executive has a number of powerful constitutional prerogatives. However, as in many of these other Presidential systems, these powers are heavily dependent upon the ability of the Executive to craft a cohesive and disciplined majority in the legislature (Mainwaring & Shugart, 1997: 394-396). In Uruguay, the Executive does not have the ability to by-pass the legislature as in Argentina and the independence of the Judiciary and the ability of organised interest groups to sponsor popular votes on government initiatives, act as further checks on the initiatives of the Executive (Bergara *et al.* 2005: 39).

The Executive

In the Uruguayan political system, the Executive, as in Argentina and Brazil (and many other Latin American Presidential regimes), has a number of powerful constitutional prerogatives that places the Executive in a potentially dominant

position in the policy-making process (Chasquetti, 2004: 45).⁶²⁴ Since 1930, ‘the Executive branch has gained substantive power vis-à-vis the legislative branch’ (Bergara *et al.* 2005: 16), a process that continued with the 1996 constitutional reform (Buquet, 1997, 1998: 11, 4; Lanzaro, 2001: 299). The potential of the Executive to control the legislative process is derived from a combination of prerogatives including exclusive initiative, veto power and urgent legislation. The Executive has the right to exclusively initiate legislation in areas related to the budget, tax exemptions and minimum wages or prices and also has recourse to a full or item veto in all policy areas (Bergara *et al.* 2005: 16, 36; Chasquetti, 2004: 45; Mainwaring & Shugart, 1997: 458). Added to this, is the right to amendatory observations, a process whereby the President can make counter-proposals or last ditch alterations to an already vetoed piece of legislation (Tsebelis & Aleman, 2005: 411). Legislators then have 30 days to override these amendatory observations and should they fail to do so, the bill, with the Executive’s alterations, then becomes law (Tsebelis & Alemán, 2005: 411).⁶²⁵ The president may also set the legislative agenda by categorising any Executive initiative as a *proyecto de urgente consideración* (project of urgent consideration), thus propelling this legislation to the top of the agenda and providing Congress with a short window within which to reject or amend the bill before it automatically becomes law (Chasquetti, 2004: 45; Mainwaring & Shugart, 1997: 458).⁶²⁶

However, despite ‘the centrality’ of the President in political life in Uruguay (Lanzaro, 2001: 293), the Executive is far from omnipotent. The successful function of Presidentialism is conditioned, again as in many other Latin American Presidential regimes (see Mainwaring & Shugart, 1997), upon the institutional and legislative position of the Executive, i.e. the degree of cohesiveness within the executive’s legislative support (Chasquetti, 2007, 2006, 2004; Buquet, 1998). As Daniel Buquet (1998: 7) notes: in Uruguay, ‘the relationship between the executive and the legislative is the fulcrum upon which the process of government is blocked or

⁶²⁴ The constitution (art. 149) defines the Executive as the President and one or more ministers. Within the Executive there is also the Council of Ministers (arts. 160 & 161), combining all Ministers under the direction of the President and responsible for articulating his/her agenda (Chasquetti, 2007: 256).

⁶²⁵ A three-fifths majority in joint session is needed to override a veto or amendatory observation (Tsebelis & Alemán, 2005).

⁶²⁶ The 1996 constitutional reform also amended this window. Previously Congress had 45 days to consider laws of urgent consideration, and although this time-frame remains, after 30 days the legislation can only be examined in an extraordinary session (Buquet, 1997, 11: 1998, 4; Lanzaro, 2001: 299).

enabled to run fluidly.’ With the emergence of the *Frente Amplio* and the shift from a bi-partisan to a multi-party system, since 1971 every Uruguayan President has presided over a minority government and so has been forced to forge multi-party coalitions to pass legislation. As such, since the return to democracy, Uruguayan executives have been institutionally powerful, but generally political weak (Bergara *et al.* 2005: 17; Chasquetti, 2006: 71; 2004: 45; Buquet, 1998: 7).

Most importantly, in Uruguay, even when congressional support is not forthcoming, ‘executives never by-pass the legislature’ (Bergara *et al.* 2005: 39).⁶²⁷ The Executive simply does not have the institutional ability to do so, such as recourse to strong decree power as in Argentina. Decree power in Uruguay is negligible: allowed only in specific policy areas and only relating to legislation that has already been accepted by Congress (Bergara *et al.* 2005: 39, Chasquetti, 2007: 257). In addition, while laws of urgent consideration could potentially set the agenda in the legislature, they are rarely invoked. In fact, since the return to democratic rule, legislation has only been deemed necessary of urgent consideration four times.⁶²⁸ Furthermore, the independence of the judiciary and the existence of popular initiatives provide major veto points for Executive initiatives (Bergara *et al.* 2005: 36).⁶²⁹ Indeed, the ability of organised interest groups to promote mechanisms of direct democracy has, on a number of occasions, supplanted the preferences of the Executive.

However, the results of the 2004 election signalled a major shift in Uruguayan politics, as Tabaré Vázquez became the first President since 1966 to enjoy a majority in both houses. Vázquez would not be forced to forge a multi-party coalition, ensuring that he was a genuine ‘institutionally and politically strong President’ (Chasquetti, 2006: 73). However, Vázquez’s narrow majority in both houses brought the importance of party discipline to the fore (Altman & Castiglioni, 2006: 153; Buquet & Chasquetti, 2005: 147-150). Despite this, without the burden of attempting to satisfy fractious coalition partners, Vázquez’s ability to dominate the policy-making process and implement his preferences would be vastly improved. In fact, the ability of Vázquez to dominate the legislative agenda vis-à-vis the

⁶²⁷ Not since Pacheco in 1968 has an executive attempted to bypass the legislature (Bergara *et al.* 2005: 39).

⁶²⁸ Sistema de Información Parlamentaria available at <http://www.parlamento.gub.uy/websip/Default.asp>

⁶²⁹ In fact, in order to avoid political stalemate during the policy-making process, the Executive will generally send bills that are ‘far from its best policy position’ (Bergara *et al.* 2005: 36).

legislature in his first three years in power can be clearly witnessed from Table 8.1 below. During this period, Vázquez succeeded in shepherding 76 per cent of all his legislative initiatives into law. The legislative power on the other hand only managed to have 21 per cent of their legislative projects approved within the same period. The majority Vázquez boasted in both houses and his ability to dominate the policy process, rendered many of Vázquez's constitutional prerogatives redundant. As Table 8.2 below shows, on only five occasions in his first three years did Vazquez have to resort to the use of his veto power in order to bring legislation closer to his preferences (and none of this legislation related to public enterprises).⁶³⁰ In contrast, within the first three years of Battle's tenure, he was forced to wield his veto power 17 times.⁶³¹ Likewise, only twice did Vázquez classify legislation as in need of urgent consideration.⁶³²

Table 8.1 Dominance of Executive in Legislative Process 2005-2007

	Executive Power	Legislative Power	Total
Total projects (2005-07)	350	600	950
2005 Approved	105	67	388
2006 Approved	95	40	326
2007 Approved	66	21	255
Total Approved (2005-07)	267	128	395
Total Pending (2005-07)	102	472	574
Rate of Effectiveness	76%	21%	

Source: Sistema de Información Parlamentaria

Note: Modelled on 2005 analysis by Chasquetti (2007), but data updated and revised by author

Table 8.2 Vázquez's use of the Executive Veto

Type	2005	2006	2007
Full Item	1	1	---
Partial	1	1	1
Total	2	2	1

Source: Sistema de Información Parlamentaria

Clearly then, Vázquez was able to stamp his preferences upon the policy process, something that was also evident with regards to the policy of privatisation. Vázquez, desperately in need of investment in infrastructure, favoured associations

⁶³⁰ Sistema de Información Parlamentaria available at <http://www.parlamento.gub.uy/websip/Default.asp>

⁶³¹ Sistema de Información Parlamentaria available at <http://www.parlamento.gub.uy/websip/Default.asp>

⁶³² Both these bills were proposed within the first month of taking office, and they were concerned with the launching of the emergency poverty relief plan PANES and the creation of the Ministry of Social Development, a testament to the pressing urgency of addressing poverty and indigence after the election of 2005. Sistema de Información Parlamentaria available at <http://www.parlamento.gub.uy/websip/Default.asp>

with private enterprise and minor concession contracts. There were no actual privatisations and Vázquez had the institutional power to oppose any suggestion of such. In fact, the *Herrerismo* faction of the *Partido Nacional* introduced their own legislation proposing the privatisation of state enterprises, but Vázquez was able to draw on his legislative support to prevent this law being approved (Ibarra, 2006: 153). Indeed, when Vázquez eventually decided to re-nationalise and purchase *Aguas de la Costa* from *Aguas de Barcelona*, he needed to introduce legislation to authorise the purchase. Luis Lacalle and his conservative *Herrerismo* faction of the PN opposed this legislation, with Lacalle stating in a congressional debate that such legislation was ‘unconstitutional,’ and any claims that ‘it would lower tariffs were nothing but a decoy.’⁶³³ However, despite this opposition, Vázquez could rely upon his majority support in the legislature and this law was duly approved and the purchase of *Aguas de la Costa* completed.

Interestingly however, despite this dominance in the policy process, it was another institutional mechanism, the constitutional referendum declaring water a human right that supplanted the preferences of the Executive and drove the nationalisation of the two water concessions. Vázquez, desperate for investment and wishing to send signals of continuity to the capital markets, issued a decree after the success of the referendum protecting the two existing water contracts in Uruguay.⁶³⁴ However, Vazquez was confronted with the unusual situation whereby the loss-making company running one of the concessions, *Uragua*, was calling for the re-nationalisation of the firm in order to enable its graceful exit from the Uruguayan market with assets and contractual guarantees intact.⁶³⁵ Powerful interest groups who supported and sponsored the referendum also placed enormous pressure on Vázquez to rescind the contracts and even legally challenged the government decree. Eventually, Vázquez, in the face of this pressure, was forced to rescind the contract of *Uragua*.⁶³⁶ A similar situation occurred with *Aguas de la Costa*. Despite the preferences of the government for *Aguas de la Costa* to continue to administer their concession, the company, believing that the referendum in October not only threw

⁶³³ Luis Lacalle, Diario de Sesiones de la Cámara de Representantes, Segundo Período Ordinario de la XLVI Legislatura, 30th Sesión Extraordinaria, July 25th, 2006 available at <http://www.parlamento.gub.uy/sesiones/AccesoSesiones.asp?Url=/sesiones/diarios/camara/html/20060725d0030.htm>

⁶³⁴ Decreto 157

⁶³⁵ El País (Uruguay), August 30th, 2005

⁶³⁶ El País (Uruguay), May 31st, 2005

doubts on the sustainability of their existing contract, but also that it dashed any future hopes they harboured for expansion in this market, announced they wished to sell⁶³⁷ and Vázquez eventually arranged for the state to purchase the firm.

In Argentina, nationalisations under Kirchner were primarily driven by the Executive branch, but in Uruguay in contrast, the two nationalisations during Vázquez's tenure were mainly driven by the institutional structure that allowed for mechanisms of direct democracy.

Legislative Support

While the executive branch may have the potential to dominate the legislative branch in Uruguay, the ability of the President to do so, as in many other Latin American Presidential systems (see Mainwaring & Shugart, 1997), is dependent upon the institutional and legislative position of the Executive (Chasqueti, 2007, 2006, 2004; Buquet, 1998). The legislature, for its part, has a number of constitutional powers that can stymie the initiatives of the Executive, including the power to censure Ministers and decide upon the distribution of posts within the state enterprises (Chasqueti, 2004: 45). As such, the ability of the Executive to implement its preferences is determined by the degree of fragmentation within the governing party and/or coalition. That is, the exercise of Executive power in Uruguay rests upon the President's ability to rely upon cohesive and disciplined support within the legislature.

Traditionally however, this has not always proved easy for Uruguayan Presidents to do. Uruguay has one of the few institutionalised party systems in Latin America (Bergara *et al.* 2005, Mainwaring & Scully, 1995) and since the emergence of the *Frente Amplio*, this system has evolved from a bi-partisan to a multi-party system. As a consequence, the last election in which a party received a majority in parliament was in 1966, forcing successive administrations to forge frequently unstable inter-party coalitions in order to generate simple legislative majorities to govern (Altman, 2000: 279; Bergara *et al.* 2005: 17; Chasqueti, 2007: 260; Buquet, 1998: 7). To compound matters, the Uruguayan party system is also highly factionalised (see Table 8.3 below). In other countries with factionalised party systems, such as Japan and Italy for example, party factions tend to be 'informal

⁶³⁷ El País (Uruguay), September 13th, 2005

actors,’ but in Uruguay in contrast, factions ‘are institutionalised agents within parties and the whole political system’ with ‘their own leaders and organisations’ (Bergara *et al.* 2005: 16). This is primarily because the factionalised party system in Uruguay is a direct consequence of the electoral system (Piñeiro, 2004: 17; Andrés Moraes, 2004: 5; Morgenstern, 2001: 236; Bergara *et al.* 2005: 17).

Table 8.3 Party Factionalisation in Uruguay

	1985-90	1990-95	1995-00	2000-05	2005-10
Frente Amplio	2.6	2.3	3.5	4.8	4.5
Partido Colorado	2.3	2.5	1.9	2.0	1.9
Partido Nacional	1.8	2.9	4.2	1.7	2.7

Source: Buquet & Chasquetti (2005) and Chasquetti (2004)

The Uruguayan electoral system is based upon Double Simultaneous Vote (DSV) and closed-list Proportional Representation (PR). DSV was introduced in 1910 by the leaders of the *Colorados* and *Blancos* in order to prevent the advent of a multi-party system (Piñeiro, 2004: 17; Andrés Moraes, 2004: 4-5; Morgenstern, 2001: 239). In a nutshell, ‘DSV restrains defections that could hurt the electoral performance of parties by allowing intra-party competition. Basically, it allows national elections to operate as party primaries,’ (Andrés Moraes, 2004: 5) and this has led to the emergence of the factionalised party system in Uruguay (Piñeiro, 2004: 17; Andrés Moraes, 2004: 5; Morgenstern, 2001: 236; Bergara *et al.* 2005: 17). The electorate cast their vote firstly for a party (*lemas*) and that party’s presidential candidate. They must then select among factions (*sublemas*) within parties (Andrés Moraes, 2004: 5; Morgenstern, 2001: 240). The ‘faction lists are hierarchies’ with leaders (senate candidates) at the top, followed by national and local deputies (Andrés Moraes, 2004: 5).⁶³⁸ Upper and lower house seats are assigned among parties on the basis of proportional representation (d’Hondt formula) and then seats are distributed among the factions within the party (again on basis of PR) (Bergara *et al.* 2005: 17; Andrés Moraes, 2004: 7). It is here that competition occurs among factions within a single party for these factions must compete with each other for seats within districts (Andrés Moraes, 2004: 7).

⁶³⁸ Before the 1996 constitutional reform, voters had to choose a party and then a presidential candidate from one of the factions within the party. By choosing a candidate, you also choose this faction list. However, the 1996 reform required that parties select a single Presidential candidate at mandatory primaries to be held on the same day by all parties. For more details on all aspects of the 1996 reform see Buquet (1997).

Despite the fact that the electoral rules promote factionalised party politics, these same rules also engender very high levels of discipline among factions and parties in Uruguay (Morgenstern, 2001; Andrés Moraes, 2004; Chasquetti, 2004; Buquet & Chasquetti, 2005). The PR-closed and blocked list system that Uruguay employs requires that aspirants to the legislature be linked to national senators (usually faction leaders) on the same ticket (Andés Moraes, 2004: 8). This means that faction leaders can control the selection of candidates and their order on the lists, engendering loyalty to the faction leader and consequently discipline, since those legislators that do not respect factions decisions will be punished when the next list is created (Altman & Chasquetti, 2005: 239-240; Buquet & Chasquetti, 2005: 150; Andrés Moraes, 2004: 8-9; Chasquetti, 2004: 48).⁶³⁹ In fact, since the 1996 constitutional reform, which prohibited multiple faction lists in a single district, power has been even more centralised in the hands of faction leaders (Andés Moraes, 2004 11).⁶⁴⁰ In turn, the reform also increased party cohesiveness and discipline, as each party can now only present one Presidential candidate (Buquet, 1998: 7). Party unity is encouraged as the President can satisfy faction leaders through the distribution of cabinet posts and budgetary concessions (Morgenstern, 2001: 244) and it is this complicated electoral system that results in the high levels of party discipline witnessed in Uruguay since the return to democratic rule (see Table 8.4 below).

Table 8.4 Discipline in the Uruguayan Legislature (Rice Index)⁶⁴¹

	1985-90	1990-95	1995-00	2000-05	Average
Frente Amplio	100	100	92	96	97
Partido Colorado	91	87	99	100	94
Partido Nacional	94	90	99	94	94

Source: Buquet & Chasquetti (2005) and Chasquetti (2004)

The victory of the FA and Tabaré Vázquez in the 2004 elections was significant as it left Vázquez as the first President since 1966 to have a single party majority in both houses. However, this majority was an extremely narrow one and so

⁶³⁹ See Altman & Chasquetti (2005: 240) who argue that ‘intra-party competition softens the rigidity of closed and blocked lists and transforms the Uruguayan system into a kind of *intrapartisan preferential vote*.’

⁶⁴⁰ Campaign financing is also largely centralised in the hands of faction leaders (Andrés Moraes, 2004: 8).

⁶⁴¹ The Rice Index is based upon the difference between negative and affirmative votes among members of the same party for the same bill. A score of 100 represents perfect discipline, while a score of 0 represents complete division.

consequently, party discipline became a key variable for Vázquez (Altman & Castiglioni, 2006: 153; Buquet & Chasquetti, 2005: 147-150). The FA however, is the most factionalised party in Uruguay (see Table 8.3 above), but paradoxically, it is also the most disciplined (see Table 8.4 above).⁶⁴² This is mainly because the party has ‘the highest level of routinisation in its internal decision making-process’ with a unique leader and ‘solid mechanisms for making decisions beyond factions’ (Bergara *et al.* 2005: 21).⁶⁴³

Vázquez’s cabinet was designed with the objective of developing centralised decision-making and engendering party discipline in the FA (Chasquetti, 2004: 53), by giving each of the main faction leaders a cabinet post. The leaders of the main factions within the coalition comprised 43 per cent of the cabinet posts and 88 per cent of the legislative weight of the FA (see Table 8.5 below). Legislators are extraordinarily loyal to faction leaders and by providing all the faction leaders with cabinet posts, legislators become loyal to the government, therefore engendering discipline across the party.⁶⁴⁴

Table 8.5 Engendering Discipline through the Cabinet

	Ministries	Percentage	Seats	% Seats of FA
Ministers (Leaders of Factions)	6	43%	61	88%
Ministers (Loyalists)	7	50%	---	---
Extra portfolio for largest fraction (MPP)	1	7%	---	---
Total	14	100%		88%

Source: Buquet & Chasquetti (2005)

This tactic proved successful and the unity and cohesiveness of the FA during Vázquez’s first term enabled the Executive to dominate the legislative agenda as can be clearly seen from Table 8.1 above. Three incidents did threaten to fracture the party; Astori and Vázquez came to blows over the five-year budget proposal after Vázquez attempted to force Astori to ensure that at least 4.5 per cent of the budget

⁶⁴² Since 1985, the *Mesa Política* has been organising and managing the FA (Bergara *et al.* 2005: 21).

⁶⁴³ Some factions within the FA, such as the PSU and PCU, select their candidates at local and national congresses. Other factions such as the AU and MPP stipulate that their candidates must be selected democratically, but despite this, all parties have a ‘long history of party manipulation in the nomination process’ (see Andrés Moraes, 2004: 10).

⁶⁴⁴ In March 2007, Vázquez replaced José Díaz, the Minister of the Interior, with the socialist Daisy Tourné and the the Minister of the Office of Planning, Carlos Viera with Enrique Rubio. These moves were interpreted as a signal to the most critical leftist elements of the government (see Chasquetti, 2008: 394).

would go towards education;⁶⁴⁵ the reform of the taxation system caused divisions between those who favoured Astori's significant decrease in corporate tax and those who favoured a more gradual reduction;⁶⁴⁶ while the announcement of a potential free trade agreement with the US angered Communist elements of the FA.⁶⁴⁷ On each occasion, Vázquez, in order to maintain the unity of his governing party, opted for compromise and conciliation and this legislative discipline enabled Vázquez to implement his preferences as regards privatisation. The FA majority was able to successfully oppose the *Herrerismo* faction's proposal for privatisation (Ibarra, 2006: 153), and approve the purchase of *Aguas de la Costa* from *Aguas de Barcelona*, despite opposition from Lacalle and his *Herrerismo* faction.

In brief then, the unity and discipline of the FA majority was a consequence of the electoral rules and a number of strategic decisions made by Vázquez. In turn, this majority enabled Vázquez to dominate the legislative agenda and successfully implement the majority of his preferences.

Judicial Independence

In Uruguay, the Judiciary has a long history of professionalism and independence and there exists a clear separation of powers between the executive branch and the judicial branch (Aloisio & Arboleda, 2006: 97; Bergara *et al.* 2005: 27). A two-thirds majority in the Senate is needed for judicial appointments and given the nature of the multi-party system in Uruguay, this isolates the institution further from political discretion and manipulation (Bergara *et al.* 28). However, the Uruguayan Judiciary is not without its problems and foremost among these is the issue of financing. Members of the Judiciary earn very low salaries hampering the quality of the institution (Aloisio & Arboleda, 2006: 95; Bergara *et al.* 2005: 29). Furthermore, the judiciary does not have complete financial independence. According to the constitution, the Judiciary elaborates its own budget, but in reality depends upon the budget office, which in turn is dependent upon the Executive, and this issue has served as one of the major points of contention between the Executive and Judiciary since the return to democratic rule (Aloisio & Arboleda, 2006: 96-97; Bergara *et al.* 2005: 29).

⁶⁴⁵ Global Insight, Uruguay, Quarterly Review and Outlook, Third-Quarter 2005, p. 99

⁶⁴⁶ Global Insight, Uruguay, Quarterly Review and Outlook, Second-Quarter 2006, p. 108

⁶⁴⁷ NotiSur, September 22nd, 2006

Despite these shortcomings, the independence and professionalism of the institution have earned them widespread respect among the Uruguayan populace (Aloisio & Arboleda, 2006: 95; Bergara *et al.* 2005: 28). Citizens, unhappy with government legislation, have recourse to the *Tribunal de la Contencioso Administrativo* (TCA) as well as to the Supreme Court. In fact, most claims against government decisions are submitted to the TCA⁶⁴⁸ and while the independence of this organisation is not in question, its procedures are notoriously slow (Bergara *et al.* 2005: 28).⁶⁴⁹ The Supreme Court does not have the ability to question the constitutionality of certain legislation once it is under consideration in the legislature, but it can veto a government initiative once it has been approved by Congress and a citizen has challenged its constitutionality (Bergara *et al.* 2005: 29). Crucially, particularly with regards to privatisation, the Judiciary has the ‘ability to make policy reversals when the Executive or the Legislative promote unconstitutional bills’ (Bergara *et al.* 2005: 29). In real terms, this means a policy of nationalisation (unless under exceptional circumstances), would be impossible to pursue in Uruguay. A concessionaire whose concession was nationalised for no apparent reason would have recourse to the Supreme Court and the Court would, in all likelihood, uphold the contract as it views cases purely legalistically.

In fact, when the state did nationalise the water and services concession of *Uragua* and decided not to pay the firm any of the contractual guarantees, the company immediately filed suit with the Supreme Court. Ironically, the company had urged the government to renationalise the concession in the hope that they could exit the Uruguayan market with their contractual guarantees and assets intact,⁶⁵⁰ but when Vázquez finally did decide to assume control over the firm, he refused to pay any of the guarantees (his argument was centred upon their breach of contract).⁶⁵¹ It was only after a year of negotiations, when *Uragua* and the Vázquez administration came to a satisfactory agreement, that the case was eventually dropped.⁶⁵² This one instance of nationalisation was an exceptional circumstance and due to the fact that the company and state reached an amicable agreement, the Judiciary was sidelined in

⁶⁴⁸ The TCA has three members, who are judges appointed by Congress and is an autonomous body with its own financing (specific item of each national budget) (see Bergara *et al.* 2005: 28).

⁶⁴⁹ Providers of cable TV (which was legally not allowed) initiated proceedings in 1994. Preliminary decisions were not forthcoming until 2003 (see Bergara *et al.* 2005: 28).

⁶⁵⁰ El País (Uruguay), August 30th, 2005

⁶⁵¹ El Observador, June 14th, 2005

⁶⁵² El País (Uruguay), October 8th, 2005

this process. The other company that was returned to state ownership during Vázquez's tenure, the water and sanitation firm *Aguas de la Costa*, was returned through a commercial transaction.

In general then, the independence and professionalism of the Judiciary ensured that a general policy of nationalisation without remuneration in Uruguay was simply not a viable policy option, as this institution had the potential to veto any unconstitutional government initiatives.

Policy Delegation

In Brazil, the policy of privatisation was delegated to an autonomous body but in Uruguay in contrast, because subsequent administrations failed to successfully introduce privatisation as policy, there was no necessity for such a body. Also, due to the fact that most state enterprises have retained their respective monopolies, few regulatory bodies have been established, although there has been a move to create regulatory agencies in water and sanitation services and electricity distribution. Sanguinetti did oversee the creation of the *Corporación Nacional para el Desarrollo* (CND), which was established in 1985 in order to provide finance and advice to private enterprises so as to stimulate their growth. It was also responsible for assuming control and re-privatising private businesses facing imminent financial collapse but that were considered vital to the national interest (see Bensi3n, 2006: 40). During Vázquez's presidency, it was the CND that was responsible for re-privatising the *Nuevo Banco Comercial* and *PLUNA*, and the CND was also at the helm in the search for private partners in the new companies to be partly owned by AFE (see section 8.2 above).

There is however, another institutional mechanism that must be examined in the context of Uruguay. It is not strictly delegation, as in the sense of delegating responsibility for a particular policy to a technocratic body, but it does delegate to the general electorate an important role in the policy process. This institutional mechanism is the constitutional device that allows for two distinct types of direct democracy: constitutional plebiscites and referendums on existing legislation (Bergara *et al.* 2005: 19). A constitutional amendment can be introduced by reformers with the support of 10 per cent of the electorate, while 25 per cent of the electorate can vote to revoke a law previously passed by Congress (Bergara *et al.* 2005: 19). As Altman (2002: 620) notes: 'any analysis of the Uruguayan period of

re-democratisation that does not take into account this powerful institutional arrangement ignores a crucial aspect of the country's political reality.' The first application of direct democracy in Uruguay was in 1917 when the country officially decided upon the separation of the church and state and among the 'stable democracies, Uruguay is one of the most prodigious users of direct democratic devices at the national level' (Altman, 2006: 2).

In fact, with regard to privatisation, it has primarily been this institutional arrangement that has shaped this policy in Uruguay, not only during the tenure of Tabaré Vázquez, but since the return to democratic rule. Mechanisms of direct democracy have been invoked frequently since 1989 and as can be clearly seen from Tables 8.6 and 8.7 below (in bold), those concerned with the privatisation of public enterprises or services have all been successful, with Vázquez and the FA supporting each one of these initiatives.⁶⁵³ It was the 1992 referendum on the privatisation of public enterprises that prevented Lacalle from privatising state enterprises at a time when other Southern Cone states were selling their state companies, and the success of this initiative rendered any attempt at privatisation too politically costly. So, privatisation remained off the policy agenda not only for the remainder of Lacalle's term, but also for Sanguinetti's second term in office. When Jorge Batlle ill-advisedly turned his attention to ANTEL and ANCAP, once again it was this institutional mechanism that shaped the policy outcome. Batlle, fearing a referendum was inevitable in the case of ANTEL, derogated the articles of his own legislation, while his attempt to de-monopolise the market of ANCAP failed at the ballot box (see chapter seven). The success of Vázquez's preference for no privatisations in Uruguay was primarily as a result of this institutional mechanism. By the time Vázquez came to power, the threat of referenda had rendered the idea of implementing privatisation among the body politic as nearly unthinkable. As long as interest groups, and in the case of the FA, political parties who oppose privatisation, could mobilise public support, any major attempt at privatisation would be defeated through recourse to institutional mechanisms.⁶⁵⁴

In fact, it was the legacy of the constitutional plebiscite on the right to water and sanitation services in 2004 that ultimately led to the two instances of

⁶⁵³ See Altman (2006, 2002) who shows that the outcomes of popular initiatives are generally determined by political loyalty.

⁶⁵⁴ See Altman (2002) who argues that the instances of direct democracy that have not been successful were primarily as a result of no political party support.

nationalisation during Vázquez's tenure (see Table 8.7 below). Shortly after the plebiscite, Vázquez, in order to send positive signals to the market, issued a decree protecting the existing water concessions in the state. However, the legacies of the popular vote had left both concessionaires eager to exit the Uruguayan market and Vázquez, facing legal challenges and under vociferous pressure from an array of interest groups who had supported the plebiscite, eventually agreed to take over the two water firms (see section 8.2). This institutional mechanism supplanted the preferences of the Executive and essentially forced the state to take over these two companies. Mechanisms of direct democracy have undoubtedly been one of the main institutions shaping the outcome of the policy of privatisation in Uruguay.⁶⁵⁵

Table 8.6 Popular Referendums in Uruguay

Subject	Year	Law	Result
Revoke amnesty to military	1989	Law 15,848	35% - failed
Prevent privatisation of public firms	1992	Law 16,211	79%- succeeded
Opposing deregulation of transmission of electrical energy	1998	Law 16,832	22.4% - did not achieve minimum turnout necessary (25%)
Opposing the restriction of the period of time available to employees to make claims against employers	1998-99	Law 16,906	4.7% (1998) & 9.3% (1999) - did not achieve minimum turnout necessary (25%)
Opposing improvement of public and private services and public security (emergency law)	2001	Law 17,243	20.7% - did not achieve minimum turnout necessary (25%)
Oppose partial privatisation of ANCEL and end of ANTEL's monopoly	2002	Law 17,296	Signatures were collected to hold a referendum and government decided to derogate law themselves rather than face a referendum
Oppose ending of monopoly of ANCAP	2003	Law 17,448	62% - succeeded

Source: Moreira (2004: 30), Altman (2002: 619; 2006: 12) and author's narrative (chapter 7)

Table 8.7 Constitutional Plebiscites in Uruguay

Subject	Year	Result
Link pensions to salary fluctuations	1989	72% - approved
Prohibitions on altering pension benefits through budget	1994	54% - approved
Establish a constitutionally fixed budget for education	1994	28% - not approved
Constitutional reform	1996	50.5% - approved
Financial independence for the judiciary	1999	43% - not approved
Prevent directors and managers of state entities from engaging in political activity	1999	38% - not approved
Enshrine the right to water and the provision of water services as a constitutional human right to be provided only by the state	2004	64% - approved

Source: Moreira (2004: 30), Altman (2002: 619; 2006: 12) and author's narrative (chapter 7)

⁶⁵⁵ In personal communication with Daniel Buquet (March, 2008) and Andrés Pereyra (May 2008)

8.4 Labour support

Since its emergence at the beginning of the 1970s to contest the 1971 election, the *Frente Amplio* has had strong links to the main umbrella union movement in Uruguay, the *Plenario Intersindical de Trabajadores-Convención Nacional de Trabajadores* (PIT-CNT).⁶⁵⁶ This was mainly as a result of the hegemony of the Communist Party within the PIT-CNT and also their dominance within the FA well into the 1990s, preserving union and leftist unity and overcoming partisan splits (Winn & Ferro-Clérico, 1997: 447; Filgueira & Papadópulos, 1997: 373).⁶⁵⁷ As a result, the trade union movement in Uruguay ‘became part of a true party system, linked to the left, in which corporatist aspects and political capital constantly intermingle’ (Filgueira & Papadópulos, 1997: 372). With the advent of the military government in 1973, all trade union activities were declared illegal and it was not until 1984, with the re-establishment of the *Consejo de Salarios* (Wage Councils) and tripartite negotiations, that the central union movement, reunited as the PIT-CNT, once again became a significant political actor (Cassoni, 2000: 1; Panizza, 2008: 179; Casacuberta *et al.* 2004: 10).⁶⁵⁸

However, with the election of Lacalle and his drive towards liberalisation, this was soon to change. Lacalle proposed creating a flexible labour market and radically altering the Uruguayan trade union movement through three measures: regulating their right to strike, regulation of trade union activity and the abandonment of wage negotiations (Filgueira & Papadópulos, 1997: 371). Lacalle only managed to implement the last of these measures. In 1991, the government announced an end to the tripartite wage councils in all sectors bar construction, health care and transportation (Cassoni, 2000: 3). This decision provided an incentive for negotiations between firms and workers at more decentralised levels and the end result was a significant decline in membership of the central union (Cassoni, 2000: 3; Casacuberta *et al.* 2004: 10), a situation exacerbated by de-industrialisation and high un-employment (Panizza, 2008: 179). By 1997, membership of the PIT-CNT numbered only 165,000 (15 per cent of the labour force) in comparison to 250,000 in

⁶⁵⁶ For comprehensive overviews of the growth of the left in Uruguay, see for example the edited volumes of Lanzaro (2004) and Garcé & Yaffé (2004).

⁶⁵⁷ The emergence of trade unions in Uruguay can be traced to the beginning of the twentieth century. In the early 1940s, the economic model facilitated a robust labour movement and they played an active role in wage settings through *Consejo de Salarios* (Wage Councils). In 1964, the first central union, the CNT was established (Cassoni, 2000: 1; Filgueira & Papadópulos, 1997: 369).

⁶⁵⁸ The idea behind re-establishing the Wage Councils was primarily to combat inflation.

1985 (Cassoni, 2000: 6). As a consequence, the movement's 'synchronisation, co-ordination and political bargaining power deteriorated' (Cassoni, 2000: 3). Despite this, during this period, 'the unions played a significant role in blocking privatisation of public utilities through the promotion of referenda' and 'they also maintained strong links with the FA' (Panizza, 2008: 179). The union movement in Uruguay, through recourse to mechanisms of direct democracy, and allied to the FA, proved to be the major veto player during every attempt at privatisation.⁶⁵⁹

The PIT-CNT actively supported Vázquez's electoral campaign in 2004 and once elected, the most significant and controversial political and economic changes Vázquez introduced were related to labour policy (Panizza, 2008: 189; Zurbriggen, 2006: 106). Firstly, Vázquez re-instated tripartite negotiations with the establishment of the *Consejo Superior Tripartito* and the *Consejo Superior Rural*. Wage councils were also re-introduced in 20 sectors and discussions were also begun between employer organisations and trade unions for the purpose of long-term planning in the labour market (Senatore, 2006: 146-147; Panizza, 2008: 189-190). One of the most controversial initiatives was the decision by the government to repeal a decree passed by a previous administration that allowed police to evict workers who occupy a workplace as part of an industrial action (Panizza, 2008: 190; Senatore, 2006: 147). When questioned about this issue, Eduardo Bonomi, the Minister of Labour, stated: 'Occupations are a part of striking.'⁶⁶⁰ Vázquez introduced a Trade Union Rights Act,⁶⁶¹ comprehensively protecting trade union activities (Senatore, 2006: 147) and extended labour rights to domestic workers and sub-contracted workers (PIT-CNT, 2007: 20),⁶⁶² while also proposing legislation to establish a national system of collective bargaining.⁶⁶³

These initiatives attracted much ire from employer organisations who accused Vázquez of bias towards the unions, while opposition parties attempted to derail his labour related legislative initiatives (Zurbriggen, 2006: 106; Panizza, 2008: 190). Despite this opposition, Vázquez's clear support for the unions significantly

⁶⁵⁹ In personal communication with Daniel Chasqueti (March 2008), Daniel Buquet (March 2008) and Andres Pereyra (May 2008)

⁶⁶⁰ Interview with Eduardo Bonomi, Minister of Labour, Regional Latinoamericana de la Unión Internacional de Trabajadores, May 13th, 2008, available at <http://www.rel-uita.org/laboral/con-eduardo-bonomi-eng.htm>

⁶⁶¹ Ley 17,940

⁶⁶² Ley 18,098 and Ley 18,099

⁶⁶³ Interview with Eduardo Bonomi

increased their importance and by 2007, membership of the PIT-CNT had returned to 250,000 workers.⁶⁶⁴ More importantly, the bargaining and political weight of the unions and left-labour power in general in Uruguay was strengthened considerably by these actions.

The relationship of the FA with the union movement was not all bright during Vázquez's tenure. The political stance of the PIT-CNT remained closer to the more radical elements within the FA who questioned central elements of the economic programme and international relations of the state (Zurbriggen, 2006: 107). The PIT-CNT staged a number of general strikes during Vázquez's first three years in power over opposition to a proposed free trade agreement with the US⁶⁶⁵ and in response to some of Astori's economic decisions.⁶⁶⁶

However, in general, the union movement was supportive of Vázquez. The PIT-CNT was highly supportive of the social emergency fund Panes⁶⁶⁷ and in response to a potentially devastating strike by truck drivers,⁶⁶⁸ the PIT-CNT called a general walkout in support of the government, forcing the truck drivers to back down.⁶⁶⁹

In terms of privatisation, the PIT-CNT actively supported the referendum on water and sanitation services with the *Frente Amplio* in October 2004 and trade unions were among the most vocal advocates of nationalising the two existing private water concessions in Uruguay.⁶⁷⁰ It was partly as a result of pressure and opposition from this direction that Vázquez finally relented and made moves to take over both these companies (Ibarra, 2006: 153).⁶⁷¹ When the communist wing of the union proposed re-establishing the *Comisión en Defensa del Patrimonio*, in response to the decision to establish two new mixed-ownership enterprises in the rail sector, the PIT-CNT supported the position of the government.⁶⁷² The resurrection of the *Comisión* did not generate much support among the majority of the PIT-CNT, with Juan Silveira, the co-ordinator of the socialist wing of the PIT-CNT, dismissing his

⁶⁶⁴ Interview with Eduardo Bonomi

⁶⁶⁵ See NotiSur, September 22nd, 2006

⁶⁶⁶ See Latin American Weekly Report, August 30th, 2007 and Latin American Weekly Report, November 1st, 2007

⁶⁶⁷ See NotiSur, October 21st, 2005

⁶⁶⁸ Truck drivers were protesting at a price hike in petrol, which was being used to subsidise public transport. See Latinnews Daily, October 26th, 2006.

⁶⁶⁹ Latinnews Daily, October 26th, 2006

⁶⁷⁰ El País (Uruguay), May 31st, 2005

⁶⁷¹ El País (Uruguay), October 8th, 2005

⁶⁷² El País (Uruguay), March 29th, 2008

communist counterparts and asserting that ‘an association is not a privatisation,’ a sentiment echoed by the co-ordinator of the PIT-CNT, Fernando Pereira.⁶⁷³

As a result, the level of labour support significantly increased in Uruguay during Vázquez’s presidency. In Brazil, labour remained fractured and antagonistic towards Lula, whereas in Argentina and in Uruguay, this high level of labour support contributed to Kirchner’s and Vázquez’s ability to implement their preferences.

8.5 Conclusion

Vázquez was elected in 2004 on a platform that rejected the market-friendly model of his predecessors and during the election campaign, Vázquez was explicit in his rejection of privatisation. By the end of his first three years in power, there had been no actual privatisations, although there had been two instances of re-privatisation: the *Banco Nuevo Comercial* and the national airline PLUNA. Some concessions to the private sector had also been offered and the administration had allowed the state rail operator, UFE, to associate with private partners. However, the state had also reassumed control of two water and sanitation companies; one through reluctant re-nationalisation and the other through formal purchase.

The Executive branch has significant power in Uruguay (although not as much as the Executive in Argentina), but this power is primarily a product of the unity and discipline of the President’s support base in the legislature. The electoral rules in Uruguay engender very high levels of party discipline and this, combined with his single party majority, ensured that Vázquez dominated the legislative agenda during his first three years in power. However, it was another institutional device, the mechanisms of direct democracy that primarily shaped the outcome of privatisation policy in Uruguay. The referendum on water and sanitation services in Uruguay in 2005 ultimately forced Vázquez to re-nationalise the two private companies operating in this sector, despite the fact this was contrary to his initial preference. Once the decision had eventually been made to assume control of these firms, it was his executive power and the discipline of his legislative support that enabled the nationalisation and purchase to succeed, despite opposition. These instances of nationalisation were exceptional and primarily driven by the constitutional plebiscite. A wide-ranging policy of nationalisation would have been

⁶⁷³ El País (Uruguay), March 29th, 2008

impossible in Uruguay mainly due to the independence of the judiciary. There were no actual privatisations and Vázquez was able to implement his preferences in this regard due to a combination of his executive power and disciplined party support, but this outcome was primarily due to the existence of mechanisms of direct democracy. By the time Vázquez came to power, the threat of referenda had nearly completed removed the idea of privatisation from the policy agenda.

As hypothesised in Chapter Two, Uruguay would be more likely than Brazil and yet less likely than Argentina to halt all privatisations due to the configuration of the specific political institutions in place in that country. As in Brazil under Lula and Argentina under Kirchner, policy outcome in Uruguay under Vázquez in the area of privatisation was primarily a product of the constellation of the political institutions within that state.

Conclusion

The purpose of this final chapter is to summarise and draw together the main insights, findings and arguments of this research. Firstly, the main argument of this study will be re-iterated, followed by the summation of the findings of each case study in the context of this argument. These findings will then be drawn together and presented in a comparative context. The implications and context of this research and how this project ‘contributes’ to the literature on globalisation and partisan politics will be explored. Finally, some potential future avenues of exploration, based on the findings of this study will be considered.

Economic Globalisation and Partisan Politics

Globalisation, the general term used to describe increasing integration at the international level, has undoubtedly altered the practice of politics and economics at both the international and national levels. Our understanding however, of the extent of this alteration and the mechanisms through which it may occur, still remain contested. One particular aspect of this phenomenon, increasing economic integration, has, it has been suggested, potentially significant ramifications for political actors within states. Again, our understanding of the causal relationship between economic globalisation and domestic political actors, particularly partisan political actors, remains under-developed.

Initial attempts at deciphering the relationship between economic globalisation and left-wing politics in particular, treated economic globalisation as the sole determining explanatory variable. The increasing mobility of capital as a result of economic integration forced states to compete for this capital if they wish to remain competitive in international markets. Capital prefers a specific policy mix and if governments, regardless of their political orientation, fail to implement this mix, the highly mobile capital will simply move elsewhere, precipitating a policy convergence along lines that internalise the preferences of capital. The preferences of capital are considered to be congruent with the preferences of the political right, rendering left-wing politics somewhat meaningless in the contemporary era.

Those that rejected this argument also rejected the focus on economic globalisation as the sole explanatory variable. Early studies contesting the concept of policy convergence contended that left-wing politics were far from meaningless in

today's world. In fact, they treated left-wing politics as an independent variable and found that, where governments were of the left, the effects of convergence, in areas such as social welfare spending and taxation reform, were lessened or even reversed. The means by which left-wing politics resisted this convergence remained unclear, but it was thought that the answer lay in the relationship of these parties with labour. Later, more sophisticated studies attempted to untangle this relationship and so began the incorporation of institutions as an independent variable into this debate. The focus now shifted to labour market institutions and it was convincingly argued that where left-wing governments were allied with broad and encompassing labour movements, the effects of convergence, again in the areas of social welfare spending or taxation reform, would be either significantly slowed or even reversed. So, the general thrust of the riposte to those initial studies above: left-wing governments can implement their preferences. They matter.

Attention has turned to the domestic-level mechanisms by which left-wing governments resist the pressures of convergence, but the focus still remains on exogenous variables to the detriment of a more complete understanding of the effects of domestic-level variables. In particular, the role of political institutions in mediating convergence warrants further attention. Some studies have incorporated institutional variables such as democracy, party fragmentation, or labour market institutions. Swank (1998b; 2002) has suggested that the institutional access to decision-making, provided to those opposed to the policies of convergence or materially harmed by globalisation, is important. Pierson (1996, 2004) and Campbell (2004) have highlighted the importance of institutional design and path dependence in shaping outcomes. In these studies, specific institutional configurations have mediated or nullified the effect of convergence. Swank (2002: 34) captures the general argument: 'The impacts of international capital mobility should vary substantially across specific configurations of national institutions.'⁶⁷⁴

This research built upon these studies by further contributing to our understanding of the mechanisms by which left-wing governments can resist convergence and implement their preferences. It examined how the different configuration of specific institutional structures impacted the control of partisan actors over decision-making and resulted in different path dependent effects.

⁶⁷⁴ These studies have however, remained focused on the advanced industrialised democracies and on social welfare spending or taxation reform.

Previous studies emphasising the continued ability of left-wing governments to implement their preferences have also iterated the importance of labour institutions. Left-wing governments allied with strong and encompassing labour movements can resist the pressures of convergence.⁶⁷⁵ The role of labour, and labour market institutions, in enabling partisan governments to resist convergence has been well established in this literature. This thesis was interested, not only in the role of labour market institutions, but also political institutions in mediating the pressures of economic globalisation. So, the main research question of this thesis was concerned with what conditions, if any, enable left-wing governments to implement their preferences in the face of increasing economic globalisation.

Which leads us to the main hypothesis of this research: while strong and encompassing unions allied with the left-wing party in power will be important for demanding and providing support for specific policy outcomes, the ability of a left-wing government to achieve this policy outcome will also be predicated upon the institutional control a government has over a particular policy. By institutional control, we are referring to the decision-making power of the government, embodied by a combination of executive power, control over the legislature etc; the ability of important players to veto initiatives, e.g. the judiciary; and the institutional design of policies and their path dependent effects.

So, the central contention of this thesis was simple. The configuration of the political institutions in each state will mediate the effect of economic globalisation on policy outcomes. Where the level of institutional control over policy is high and the union movement is cohesive and well-organised, a left-wing government with close links to labour will have a greater ability to implement their preferences, than one with low-levels of institutional control and weak links to a fragmented and disorganised labour movement.

The Findings

This argument, hypothesis and institutional framework were applied to three left-wing governments in the Southern Cone of Latin America. Latin America has recently witnessed the continent-wide resurgence of left-wing political parties at the polls. The revival of left-wing politics in Latin America provides us with a good

⁶⁷⁵ In fact, capital may even prefer the left-leaning policies produced by the coherence of left-governments allied with encompassing unions (see Garrett, 1998a).

opportunity to examine the relationship between economic globalisation and partisan politics. Latin America has been exposed to international capital and foreign direct investment to a far greater degree than the advanced industrial democracies and generally, it is assumed that the impact of economic globalisation will be magnified in the developing world. So, choosing three Latin American states should provide a more rigorous test of the argument outlined above. These three states have all recently elected to power left-wing governments with similar preferences as regards privatisation. These three states are the most 'developed' in Latin America and their geographical proximity acts a natural control. What is more, they all have similar levels of exposure to economic globalisation and all three should be under similar levels of influence from the IFIs. This enabled all exogenous variables to be held constant across the three cases, providing the research with greater analytical leverage over the main explanatory variable. Finally, these three states varied across this main explanatory variable, the political institutions, and this enabled us to hypothesise on expected outcomes in order to test the central argument.

Privatisation was chosen as the dependent variable. Previous empirical studies in this literature have focused upon social welfare spending or taxation shifting. Choosing privatisation widens the scope of this literature. Also, the globalisation literature provides a clear set of expectations regarding the relationship between privatisation and globalised markets. Increasing trade competition and the multinationalisation of production place downward pressures on the size of the public economy and this leads to the privatisation of state assets. Privatisation is also an effective means for developing world states to attract FDI and to 'signal' stability and orthodoxy to capital markets.

So, why have three left-wing governments, from the same geographical area, with similar preferences as regards privatisation, elected within the same period and with similar exposure to economic globalisation, exhibited three different policy outcomes? The findings of this research appear to confirm the central argument – the left does matter, but this is dependent upon the configuration of domestic political institutional variables that include access to decision-making and path dependence. In Brazil under Lula, while privatisations did slow significantly, they did not cease. More to the point, privatisations continued in sectors (banking and electricity) where Lula had specifically stated his intention to halt all sales of state assets. Labour was fragmented and disorganised and failed to provide cohesive support for Lula, while

the confluence of institutional variables left Lula with little power to exert his authority over the policy of privatisation.

Cardoso had implemented privatisation within a legal and institutional framework and while Lula's strong executive power had the ability to curb the power of these institutions, this was only functional if he could form a cohesive coalition, but electoral rules and his inability to achieve the required equilibrium as regards pork-barrel prevented him from doing so. The path dependent effects of Cardoso's policy design ensured that privatisation could continue (albeit at a much slower pace). The judiciary could veto any attempts to overhaul these institutions or engage in a policy of nationalisation, even if Lula had wanted to do so. So cumulatively, these variables left Lula with little institutional control over the policy of privatisation in Brazil.

In Argentina, Kirchner oversaw the uniting of the labour movement and established strong links between the central union and his *Frente Para la Victoria* faction. Their support and Kirchner's institutional power ensured that in Argentina, not only did all privatisations cease, but there were also a number of high-profile re-nationalisations. The Executive has extremely strong powers in Argentina and during periods when Congress is hostile, the Executive can sideline this institution in the policy process. The electoral system and the high-level of party discipline it engenders enabled Kirchner to slowly establish his own power base in Congress. He used this power base to support initiatives that would strengthen Executive power, which in turn, he then used to further enlarge his support base. Privatisation had not been delegated to an independent body as it had been in Brazil. Menem had instigated this policy by widely employing his executive powers. So, somewhat ironically, Kirchner could simply utilise his Executive power to halt and reverse this policy. The high level of support he had in Congress, ensured that they were willing to allow him to do this. His erosion of *de facto* judicial independence also enabled Kirchner to rescind the contracts of public utilities and re-nationalise public services, with a greater degree of confidence than Lula in Brazil, that the judiciary would support his actions.

Finally, in Uruguay under Vázquez, although there were no actual privatisations, there were two instances of re-privatisation, but the state also reassumed control of two water and sanitation companies. Labour was united, cohesive and well organised and was an integral player in the re-nationalisation of

the water contracts. The Executive branch has significant power in Uruguay, but this power is primarily a product of the unity and discipline of the President's support base in the legislature. The electoral rules in Uruguay engender very high levels of party discipline and this, combined with his single party majority, ensured that Vázquez dominated the legislative agenda. However, it was another institutional device, the mechanisms of direct democracy that primarily shaped the outcome of privatisation policy in Uruguay. Frequent recourse to this mechanism throughout the 1990s had effectively removed privatisation from the policy agenda. This institutional structure has served to repeatedly constrain Executive preferences. For example, the referendum on water and sanitation services in Uruguay in 2005 ultimately forced Vázquez to re-nationalise the two private companies operating in this sector, despite the fact that this was contrary to his initial preference. Once the decision had eventually been made to assume control of these firms, it was his executive power and the discipline of his legislative support that enabled the nationalisation and purchase to succeed, despite opposition. A wide-ranging policy of nationalisation without remuneration would have been impossible in Uruguay, mainly due to the independence of the judiciary. The lack of privatisations, while congruent with Vázquez's preferences, was not a product of his institutional control over this policy, as demonstrated by the case of the two re-nationalisations. The lack of privatisation was primarily a product of the frequent use of mechanisms of direct democracy in the 1990s.

Holding all exogenous variables constant, variation in policy outcome can also be explained by the configuration of political institutions within each state. A left-wing government will have the ability to implement their preferences in situations where the institutional configuration is favourable enabling them to exert influence over the desired policy outcome, and where labour is united and organised. This is what occurred in Argentina under Kirchner. Where the institutional configuration prevents a government from exerting their influence over policy, and where labour is fragmented and disorganised, a left-wing government will not have the ability to implement their preferences – they will be blocked. This is what occurred in Brazil under Lula. Where labour is united and organised, but where the institutional configuration inhibits a government from exerting their influence over a policy, they will not have the ability to fully implement their preferences, nor will

their preferences be entirely blocked – they will be constrained. This is what occurred in Uruguay under Vázquez.

From the analysis of these three case studies then, the variation in policy outcome can be primarily explained by the configuration of the political institutions within each state. This is best illustrated by returning to the typology presented in the introduction (see figure 2 below).

Figure 2: A typology of domestic-level variables – the results

	Strong cohesive labour movement with strong links to party	Weak and fragmented labour movement with weak links to party
High levels of institutional control over policy	Implementation - ARGENTINA	Muted
Low levels of institutional control over policy	Constrained – URUGUAY	Blocked - BRAZIL

Implications for the Literature on Economic Globalisation and Partisan Politics

While it is difficult to make universal generalisations on the basis of three case studies from a distinct geographical area, nonetheless, the findings of this research have implications for the literature on economic globalisation and policy convergence.

Firstly, the findings of this research suggest that the proponents of the globalisation thesis have over-exaggerated the decline of the contemporary left. Increasing economic globalisation and the disciplinary effects of mobile capital have not, it appears, consigned distinct left-wing policies to the dustbin of history. Despite the increasing economic integration of the international system continuing to place pressures on governments to converge along a specific policy mix, left-wing governments can, under certain conditions, implement policies congruent with their

preferences, even if these preferences contradict the policy-mix prescribed by the convergence thesis. For example, in Argentina, Kirchner not only halted all privatisations, but he also re-nationalised a number of high-profile public services and previously privatised state companies. By any reading of the globalisation thesis, nationalisation should be nigh on impossible. While there is a case to be made for increased welfare spending funded by progressive taxation actually proving attractive to mobile asset holders, there is no logic which supports the argument that a climate of expropriations will be in any way attractive to mobile asset holders. Yet, even in this era of increasing economic globalisation, a left-wing government in Argentina re-nationalised a number of entities, while, it must be added, continuing to maintain economic growth. So, left-wing governments can still implement policies congruent with their preferences. In capitalist democracies, they can matter.

Secondly, this research adds to those studies that highlight the importance of including political institutional variables in any attempts to understand the mechanisms that mediate the effects of economic globalisation in the contemporary era. The first wave literature, in condemning the left to an early grave, stressed the effect of exogenous variables on left-wing politics. More sophisticated studies have since incorporated various domestic variables and highlighted the continued relevance of partisan politics. Some scholars have highlighted the importance of institutions in mediating or nullifying convergence in the advanced industrial democracies. This research built upon these studies by further contributing to our understanding of the mechanisms by which left-wing governments can resist convergence and implement their preferences. It examined how the different configuration of specific institutional structures impacted the control of partisan actors over decision-making and resulted in different path dependent effects. It has shown that the structure of institutions and their independent effects are crucial in either providing opportunities for left-wing governments to implement their preferences or constraining them from doing so.

This can be witnessed across the three cases. In Argentina, the high level of executive power, lack of policy delegation and the ability to manipulate the judiciary all combined to enable Kirchner to implement nationalisation, even when congress was hostile. In Brazil, Lula's strong powers were negated by the instability of his ideologically diffuse, unruly and undisciplined coalition. As he was hampered imposing his preferences upon congress, privatisation continued to trundle slowly

along because of the path dependent effects of Cardoso's policy design. Uruguay proved even more interesting. As the rest of Latin America converged around privatisation in the 1990s, Uruguay bucked this trend, mainly because of the specific institutional configuration that allowed for mechanisms of direct democracy. By the time Vázquez came to power, successive referendums had essentially removed privatisation from the political agenda. In fact, this institutional mechanism drove the nationalisations in Uruguay, even though initially, this was contrary to Vázquez's preferences.

However, it would be naïve to completely deny the effect of exogenous variables, in particular globalisation. In fact, during the election campaign, all three moderated their stance and all three announced the appointment of economic conservatives to their future cabinet, in order to prevent turmoil in the financial markets. When Lula arrived in power, the financial markets in Brazil had suffered serious fluctuations, and there was widespread concern regarding the economic direction Lula would follow. Following the devaluation of the *Real* in 1999, Brazil was desperately in need of foreign investment and Lula was desperate to soothe the nerves of potential investors. His conservative economic policy was awarded with an increase in Brazil's investment rating, precipitating a return of foreign capital to the Bovespa, and by the end of Lula's first term in office, there was widespread international demand for Brazilian IPOs and corporate bonds.

Amidst fears that Kirchner was instigating a widespread policy of nationalisation, *Gaz de France*, *France Telecom* and *Vivendi* all left the Argentine market. Furthermore, the decision of the World Bank's ICSID in May 2005, to award an American Gas company compensation for pesification, forced Kirchner to adopt a more conciliatory tone with privatised utilities. Also, Kirchner was only able to avoid IMF pressure by securing Venezuelan interest in Argentine sovereign bonds. Although the MerVal did rally during Kirchner's tenure, this is hardly surprising given the veritable meltdown it had suffered in 2001. Furthermore, although the Argentine economy continued to grow, the bond rating agencies refused to significantly upgrade Argentina's credit rating, further placing pressure on Kirchner to come to an agreement with privatised utility companies and secure an agreement from Venezuela for the purchase of Argentine bonds.

In fact, for Uruguay, the pressures of globalisation on such a small, trade-dependent economy can be clearly witnessed. In Uruguay, the letter of intent

Vázquez signed with the IMF in May 2005, committed the government to dismantling the state's monopolies in a number of sectors and also to the privatisation of the *Nueva Banco Comercial* (NCB). In order to attract much-needed investment, the government was keen to signal stability and continuity to private capital and immediately after the election, Vázquez announced that he would be abandoning his proposal to revise the public service concessions of the previous Batlle government, while also announcing that he would respect all previous contracts signed by private entities with the state, including a proposal to negate the retroactivity of the October referendum and respect the concessions of *Uragua* and *Aguas de al Costa*. Furthermore, the reliance of Uruguay on international trade is also clearly evident. Initially, Vázquez was highly supported of the Mercosur, but following an acrimonious dispute with Argentina, Vázquez, contrary to Mercosur rules and enormous domestic opposition, pursued a trade and investment framework deal with the US. Nonetheless, it was the political institutional structures that drove the state take-over of the two water companies, while the re-privatisation of PLUNA proved unnecessarily complicated due to constitutional limits on foreign ownership. Globalisation did undoubtedly have an impact upon policy outcomes, but this thesis has attempted to demonstrate that the institutional structure in each state also shaped these outcomes.⁶⁷⁶ Even in this current globalised era, it would appear that institutions still matter.

Thirdly, this research has extended this avenue of inquiry to a new policy area: privatisation. The focus of much of the empirical work in this literature has remained primarily on social welfare spending and taxation reform. However, according to the logic of the 'globalisation' or 'race to the bottom thesis,' the effects of convergence should be witnessed in other policy areas. Examining privatisation broadens the applicability of this debate and in doing so, it has provided, if anything, a more rigorous test of the argument presented above. While there is a case to be made that capital may be attracted to situations characterised by increased welfare spending, funded by progressive taxation, implemented by a left-wing government allied with an encompassing labour union, no such case could realistically be made

⁶⁷⁶ A recent study by Jensen & Schmith (2005) proves that Lula's election had no effect on stock prices in Brazil. Rather, plummeting stock prices at this time were a product of the slumping world economy. This may suggest, as others have done (see Campbell, 2004; Hay, 2000), that ideas about economic globalisation have an impact almost equal, if not greater to, the impact of economic globalisation itself.

for re-nationalisation. In the current era of globalisation, nationalisation should prove even more difficult to implement than progressive taxation or social welfare increases, but nonetheless, we have evidence of nationalisation in two of our three cases, albeit if in Uruguay, these nationalisations were related to one specific issue.

Fourthly, the three case study countries chosen for this research were all from the developing world. The vast majority of previous empirical studies in this literature have focused on the advanced industrial democracies, but the mechanisms by which left-wing governments resist convergence in the developing world remain by and large, unexplored. The constraining impact of economic globalisation is assumed to be magnified in the developing world and some recent empirical studies (see Wibbels & Arce, 2003; Kaufman & Segura-Ubiergo, 2001, Rudra, 2002) appear to confirm this. These studies have all suggested the importance of partisanship, but how partisanship matters remains unexplored. This research suggests that not only do left-wing governments matter in the developing world, but institutions matter also.

This has implications for the literature. Ironically, it was in situations where the political institutions were weakest or where power was concentrated in the hands of the government, as in Argentina, that left-wing politics appeared to matter most. In Argentina, the government's room for manoeuvre seemed to be largely rooted in institutional weakness. This means the political rules of the game are easily violated or changed. Brazil's institutions are stronger and so policy does not shift so radically. So, institutional weakness provides left-wing governments with more space for far-reaching policy change. This is not a new claim, especially in relation to Latin America (see O'Donnell, 1994; Levitsky & Murillo, 2005). In fact, a whole body of literature argued that the ability of Latin American governments to implement neoliberal reforms in the first place back in the early 1990s, was a product of executive power, executive dominance over the legislature, judicial independence etc (see Haggard & Kaufman, 1992; Shugart & Carey, 1992; Ames, 2001). Is it any surprise then, that the ability to reverse these reforms with partisan changes in government should be a product of the same institutional weaknesses?

So, what does all this mean? There are two important points to draw from this discussion. First, it may actually be in the developing world where we will still see distinctive left-government policies despite their increased exposure to economic globalisation. If the ability of a left-wing government to implement policies congruent with their preferences and resist convergence is a product of institutional

weakness, then in countries where the political institutions are stronger and better developed, such as the advanced industrial democracies, then, as in Brazil, it should prove more difficult to alter existing policy. This leads to the second point. If convergence is predicated upon partisanship combined with institutional strength or weakness, then this brings us, in rather a round-about-way, back to the original point. Policy outcome then, is also a product of institutional structures and partisanship, rather than a single exogenous economic imperative. Left-wing politics matter. Institutions matter.

Finally, the findings of this research also have important implications for Latin America at this particular juncture in its history. The ability of left-wing governments to pursue distinctive supply-side partisan policies in the region suggests that the recent repeated victory of left-wing political parties at the polls, the so-called ‘shift to the left,’ is an important political phenomenon, and may lead, at least in some countries, to a roll-back of the market-friendly reforms of the 1990s. What is more, it also appears as if many of the leaders of this ‘new left’ are well aware of the potential of political oppositions to prevent them from implementing their preferences. Witness the efforts of Hugo Chávez, Evo Morales and Rafael Correa to hold constituent assemblies in order to re-cast the political institutions in their respective states. If institutions did not matter, then why would they bother?

Future Research

As stated above, while generalisations from three case studies are difficult, the findings of this research could serve as a starting point for further work. This type of study could be replicated in other small-n comparative case studies in Latin America or, with minor changes, in other parts of the world. It could also be applied in many different policy areas thought to be impacted by the pressures of economic globalisation. More in-depth comparative case studies of this sort in other policy areas, in other countries, will further elucidate the role of political institutions in mediating or nullifying the effects of economic globalisation.

While qualitative studies allow us to trace the effect of institutions across specific policies, large-n, cross-country econometric studies are needed to generalise the argument presented here. A number of scholars have included institutional variables in their econometric studies in this literature, but perhaps other large n-studies could benefit from utilising some of the datasets that already have developed

excellent measures of political institutional variables (see for example Beck *et al.* 2001; Henisz, 2000).

Econometric studies that employ political institutional variables of the type presented here, or in the datasets above, could test the role of partisanship and political institutions in the face of increasing globalisation, firstly in the presidential regimes of Latin America in the policy areas of social welfare spending, taxation shifting and privatisation, and then depending upon the results, this model could be extended to the rest of the world. Large global samples could also attempt to decipher the effect of partisanship in resisting convergence across different institutional structures. So, for example, is a left-wing government more likely to resist convergence in a Presidential regime, than one say, in a parliamentary regime or semi-Presidential regime?

Finally, the findings presented could also act as a building block for scholars specifically interested in Latin America. Much has been made of the bifurcation of the 'new left' in Latin America,⁶⁷⁷ but as yet, we have no real understanding of this phenomenon. Part of the answer may lie in the varying levels of institutional weakness across the continent. Where members of this 'new left' have fewer institutional constraints, as in Argentina, it is likely that their policies may be more radical. Those that are institutionally constrained, as in Brazil, will be more moderate. Obviously the bifurcation of the left cannot simply be explained by institutional differences, but future research, either qualitative or quantitative need to incorporate the varying levels of institutional strength (or weakness) as a possible explanatory variable.

⁶⁷⁷ That is, the radical populist left and the formerly radical, reformist left (see Panizza 2005; Castañeda 2006).

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