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Understanding Reform in Latin America

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**Global Development Network
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Synthesis of Country Studies from Latin America**

UNDERSTANDING REFORM IN LATIN AMERICA

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Resumen

Este artículo aporta un panorama general del proceso de reformas pro-mercado en ocho países de América Latina, basado en estudios de caso país llevados a cabo en el proyecto “Entendiendo las Reformas” de la Red de Desarrollo Global (Global Development Network, GDNNet). Después de una breve presentación de las reformas en América Latina y en los ocho países del proyecto, el artículo toma algunos temas clave en la economía política de la reforma. Revisamos las condiciones iniciales; el papel jugado por tecnócratas y grupos de interés; la participación política; el peculiar atajo a las reformas que representó el “cambio de políticas” (anunciar algo y hacer lo contrario); algunos temas tradicionales en la literatura de las reformas como la secuencia, el rol de los shocks y del aprendizaje; el rol aparentemente clave jugado por las características locales; los complejos procesos de retroalimentación entre las reformas pro-mercado y los procesos políticos; y el reciente vuelco contra las reformas en América Latina. El artículo termina con algunos comentarios sobre lecciones de carácter normativa que se extraen de esta experiencia.

Abstract

This paper provides an overview of the pro-market reform process in eight Latin American countries, based on country studies undertaken within the Understanding Reform project of the Global Development Network. After a brief presentation of the reform in Latin America and in the eight countries in the project, the paper addresses some key themes on the political economy of reform. We review the initial conditions of reform; the role played by technocrats and stakeholders; political participation; the peculiar shortcut to reform represented by “policy switches” (announcing something to do the opposite); some traditional topics in the literature on reform like sequencing, shocks and learning; the apparently key role played by local characteristics; the complex feedbacks between pro-market reforms and the political process; and the recent backlash against reform in Latin America. The paper ends with some remarks mostly on normative lessons from this experience.

JEL: O540, O570, P160

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1 Introduction

Most Latin American countries have undertaken sweeping “market-oriented” reforms over the last two decades. This paper provides an overview of the reform process in eight Latin American countries, based on country studies undertaken within the Understanding Reform project of the Global Development Network.⁴ This project had some ambitious questions with respect to the ability to undertake reform, the capacity to successfully implement reform, and the ability of the reforms to deliver the expected outcomes in different countries. We did find quite difficult to provide clear cut comparative answers to these questions from the information provided in the country studies. This was probably the case because the object of analysis is itself quite complex, because the (quite rich) country studies had somewhat different emphases, and because it is inherently difficult to answer any question with 8 data points, even if those data points were clearly measured. There is also the fact that all these countries, with the possible exception of Venezuela, did undertake a substantial amount of reforms, so that we do not have much variation on some of the dependent variables of this project.⁵

Nonetheless, it is an interesting exercise to take a look at these countries together, as there are several common contextual factors to most Latin American reform experiences (which we highlight in Section 2.1), and we attempt in this paper to provide some insights from these cases that might be of some help in the broader project. The rest of Section 2 provides a very brief description of the reforms in the region and an assessment of the outcomes of reform – we stress the difficulty in inferring the actual effects of reform. Section 3 provides a glimpse at the richness of the cases providing a sketch of some of the dynamics of the reform process in each of the 8 countries. Section 4 presents our discussion of several of the main themes on the political economy of reforms. Section 5 concludes.

⁴ The countries studied are Argentina, Brazil, Chile, México, Paraguay, Perú, Uruguay and Venezuela. The country studies on which this synthesis is based are listed in the References at the end.

⁵ According to some metrics, Uruguay would be another case of “less” reform. Yet, it is our sense that whatever degree of reform was achieved in Uruguay, is achieved in a way that makes it relatively stable

2 The Reform Process in Latin America

2.1 *The Latin American Context*

Before describing the reform process itself, we provide some brief characterization of the Latin American context. The region followed a common import substituting industrialization (ISI) model in the post-war period. This development strategy reshaped the Latin American economies, societies and institutions. While traditional interest groups linked to the primary sectors reduced their political influence, new social groups with interests in the local industries gained social and political strength. After a while however, this inward-oriented development strategy began to show clear signs of exhaustion. The performance of Latin American countries was not good enough compared with the South-East Asian countries that claimed to adopt an almost opposite economic model.⁶ The political support of the ISI model was gradually eroding in Latin America when the debt crisis unleashed in 1982 and the failure of early policies implemented by some countries to deal with it – the Austral Plan in Argentina, the Cruzado Plan in Brazil, and the APRA plan in Perú – played an important role in reshaping policy views in the region. It was a turning point in consolidating the view about the failure and unsustainability of the previous development model.

These views were connected to a climate of ideas which had a focal point in the so-called “Washington Consensus”, a list of policy prescriptions summarized by John Williamson circa 1990 capturing the conventional wisdom at institutions such as the U.S. Treasury Department, the World Bank, and the International Monetary Fund on policy reforms that would aid development in Latin America. Most of the Latin American countries also had local carriers of those ideas, oftentimes cosmopolitan US trained economists, linked across countries, especially within the region. (The form of articulation of these individuals into the policymaking process varies from country to country.)

Democratic rules were restored between the mid-eighties and the early nineties in the region –this is the case in all the country studies, with the exception of Mexico and Venezuela (in fact, there was a reversal in this last case). This means that, as in the case of transition countries in Europe, the region was struggling with both economic and political transformations simultaneously.

consensual and, probably, succesful, so that we would have a hard time classifying Uruguay as a “failure” to be explained in this regional comparative perspective.

⁶ In recent years, the “official” view that the East-Asian model actually rested almost exclusively on market forces and State retrenchment has been challenged (see Rodrik 2003 among others). Nevertheless, it is true that the “South-East-Asian model” was heavily advertised on these terms in Latin America in those years.

Latin America of course is not homogeneous, but there are some structural characteristics common to most countries in the region that had a bearing on the reform process. The region's competitive advantages are biased in favor of natural resources, and primary commodities explain a large share of exports, such as minerals and oil (Chile, Venezuela, Perú) and agriculture (Argentina, Paraguay, Uruguay). Even in more industrialized Brazil and Mexico primary products are still relevant. This feature impinges on the region's political economy via the so-called natural resource "curse".

The region was affected by common shocks that impinged on the reform path and outcomes (terms of trade, changes in the foreign exchange rate and in the market sentiment concerning the region, which may create contagion effects). Salient examples include the debt crisis, which was one of the factors starting the reform wave, the large capital inflows of the beginning of the nineties which facilitated the implementation of reforms, and the Russian shock in 1998. While the first two seem to have fostered reforms, the latter seems to have worked against the reforms, as the general public and politicians in many countries see the reform less favorably due to the macroeconomic crisis.

There have been important "contagion" effects across countries, that is, some learning from the interpretation of the (successful and unsuccessful) experiences of other countries in the region.

In several of the countries, the so-called structural reforms came hand in hand with efforts at macroeconomic stabilization, considered "deeper" than previous ones.

Having referred to many common factors, it is also important to stress that Latin American countries are quite different in many dimensions. Country size is obviously one of the dimensions in which the region is not homogeneous; a dimension that became particularly relevant for the fate of the inward-oriented ISI model (think about the size of the domestic market in Brazil as compared for instance with Uruguay). Economic and social development show a significant variation across countries as well. Just to give an example, GDP per capita (in PPP terms) ranged in 2004 from 12468 in Argentina to 1625 in Haiti. The historical starting points in terms of social and economic structure, as well as in the details of past policies was also different in different countries when the pro-market reform began. Latin America is often mentioned as the most unequal region in the world in terms of the distribution of income and wealth, but there is a significant heterogeneity within the region in this matter. Social indicators as literacy ratios, life expectancy and the like also show much variation in the region. Even when most countries adopted a version of the ISI model in the postwar period, the progress they could make in that direction varies considerably in terms, for instance, of the degree of industrialization they reached. This was partly dictated by the size of the domestic market and partly by policy options and political conditions (for instance Paraguay had a relatively open economy even before the pro-market reform era).

In spite of some common institutional heritage from the colonial era, political and institutional history also shows significant variation across countries in Latin America. Most countries in the region experienced periods of dictatorship in the twentieth century, but while some spent most of the century under those conditions, others did it for relatively short periods. The quality of institutions and the incidence of corruption varies accordingly (Kaufmann et al 2003). As authors of the UR country studies often stress, these different starting points were key for the fate of the pro-market reform.

2.2 What Reforms Were Undertaken and How Far They Have Gone

In the words of the coordinators of this GDN project, “it is technically complicated to measure reform policies and outcome.” In order to get a general sense of what has happened in Latin America, we use one of the most comprehensive attempts at measuring reforms, by Eduardo Lora and collaborators at the Inter-American Development Bank. Lora (1997 and 2001) has built an index to measure reform advances; the index is composed by a set of sub-indexes which capture five reform areas throughout 19 Latin American countries for the 1985-1999 period (the areas covered are trade, tax, financial, privatizations and labor reform). Figure 1 shows the path of the Lora index of reform for our 8 Latin American cases in comparison to the regional average. It is evident that the average of the index for Latin American countries as a whole grows considerably throughout the period. Comparing across countries,⁷ we can see the persistent and always consistent march of Chile, the explosive trajectory followed by Argentina and Peru (see the big-bang behavior between 1990 and 1995 in both indexes), and the smoother path of the Mexican, Brazilian and Uruguayan cases throughout their series.

<Insert Figure 1>

Figure 2 presents “the margin of reform utilized” in the five reform areas studied by Lora, at different points in time. This plot allows seeing performances by area and their progressive advance combined. The “margin of reform” accomplished by 1989, 1995 and 1999 is measured from 1985 (that is to say, the margin of reform existing in 1985 that has been utilized by either one of those years). It is easy to observe that the reform on trade sector was the fastest and largest one. It was always on top of the motion to finally accumulate almost 76 percent of the original margin available. Financial liberalization was second: it progressed vastly, especially between 1995 and 1999, showing a final index of 0.70 while the 1985 mark had been 0.26. Tax reform and privatization conquered 22 and 26 percent of the original margin available (it is interesting to note that

⁷ This statement is partly based on a longer series by Morley, Machado and Pettinato (1999) for the 1970-1995 period. That series shows that for most countries except Chile and Uruguay, most of the action occurs after 1985.

privatization is the only area in which the Lora index starts from 0 everywhere). Finally, labor reform was practically null in accordance with these indicators (actually, the labor reform index exhibited some reversals as it concludes in 1999 in virtually the same position where it started fifteen years earlier).

<Insert Figure 2>

2.3 The Impact of the Reforms

Identifying the impact of pro-market reform is not an easy task. Reform involves a series of policy and institutional changes taking place over a number of years. What outcomes can be ascribed to what policy changes is usually controversial. To deal with that difficulty, and to anticipate some information that we will use in our later discussion, we follow the strategy of summarizing what other analysts as well as the authors of the URP country studies have said on these issues.

2.3.1 Economic Outcomes

Everybody agrees that one of the main achievements of the reform era has been the substantial reduction of inflation in the region. This connects to the fact that, in many if not all of the countries, structural reforms have been intertwined with stabilization efforts. In most countries, fiscal consolidation and price stabilization were key components of pro-market reform. Argentina was probably the most celebrated case, where the convertibility plan became the cornerstone of an ambitious reform program (Acuña et al 2005), but other countries in the region also managed to stabilize while implementing structural reforms. A noticeable exception was Venezuela, where president Pérez failed to get the fiscal reform that the country badly needed to achieve macroeconomic stability (Monaldi et al 2004).

However, in recent years and despite the pro-market reforms, financial and exchange rate crisis caused large macroeconomic fluctuations in several countries in the region. Reforms implemented in the eighties and nineties could not insulate Latin-American countries from macroeconomic shocks. Furthermore, it has been argued that macroeconomic imbalances undermined the effectiveness of reform in other sectors. Several analysts argue, for example, that capital account liberalization can be harmful in the presence of macroeconomic imbalances or poor bank supervision (Arteta et al 2001; IMF 2001). Castelar Pinheiro et al (2004) argue that reform could not significantly foster investment in Brazil partly because of weak regulatory institutions, but also because of macroeconomic instability.

We focus now on the stated main goals of pro-market reforms: to increase productivity and to foster economic growth (Lora, Panizza et al. 2003). Not long ago, most studies used to find that reforms

had had positive and substantial effects on economic growth in Latin America (Easterly et al 1997; Fernández-Arias and Montiel 2001; Lora and Barrera 1997). Lora and Barrera (1997), for example, reported that economic reform raised annual GDP growth in the region by almost 2 percentage points.

More recent assessments have been less favorable. In recent years, an increasing number of analysts agree on the fact that economic growth in the nineties in Latin America was “disappointing”: greater than during the eighties (the “lost decade”) but below the rates of the sixties and seventies and far below the rates of the East Asian countries. Recent research conducted in the IFIs conclude that the impact of reforms on growth is less than initially thought and probably temporary (Lora and Panizza, 2002; Loayza et al. 2005).⁸

The UR country studies do not report clear cut findings about the impact of reform on growth. If anything, they suggest that pro-market reform stimulated GDP growth, but only temporarily. Pinheiro et al (2004) observe that Brazil's economic growth was not particularly strong in the aftermath of the reform. Monaldi et al (2004) assert that the Pérez pro-market reform stimulated economic growth in Venezuela, but the effect was short-lived. Peru experienced high economic growth during most of the nineties, coinciding with the adoption of pro-market reforms, but the process was also temporary (Garibaldi and Molinet, 2004).

Reform does not seem to have raised productivity as much as expected either. According to Lora, Panizza et al. (2003), total factor productivity made a negligible contribution to growth in the nineties in Latin America. Castelar Pinheiro et al (2004) report significant productivity gains in some privatized firms in Brazil, but they also mention that these gains were mostly temporary. Besides, privatization and trade liberalization do not seem to have spurred investment in Brazil. Galiani et al. (2003) report productivity gains in privatized firms in Argentina. These gains were largely associated to reductions in employment, but there is also evidence that privatizations did contribute to increasing investment in Argentina.

2.3.2 Social Outcomes

Lora (2003) reports the following findings on the impact of reform on the labor market in Latin America. (i) There are no systematic effects on the sectorial allocation of employment. (ii) No systematic effects on unemployment. (iii) The reform contributed to widening the gap between the

⁸ Other analysts are even more critical. Rodrik (2003) has argued that comprehensive pro-market reform packages have not been necessary either to begin or to sustain economic growth. He argues that in several cases of economic success, particularly in Asia, the policy recommendations of the Washington consensus were not adopted. See also Ocampo (2005).

wages of low and high skilled workers. (iv) The new exporting sectors have labor conditions that are at least as good as the traditional sectors, and in several cases, they are better. (v) Labor conditions in the privatized enterprises are worse than in the former state-owned enterprises.

There are different views on the impact of reform on poverty and income distribution. One view is that reforms reduce poverty because they foster growth without affecting income distribution (Gallup et al 1998; Dollar and Kraay 2000a and b; World Bank, 2001). But other analysts have a less positive view. Foster and Székely (2001) show that the income of the poor grows less than average income with economic reform. Other authors mention that trade liberalization may have widened the wage gap. There is also some evidence of a temporary rise in unemployment due to reform. Morley (2000) could not find robust econometric results about the impact of structural reforms on income distribution. He finds that different pro-market reforms had different impacts on inequality in Latin America. Tax reform was regressive and capital account liberalization was progressive. He found non-robust effects for trade, privatization and financial reform.

The UR country studies do not report consistent patterns across countries in the social outcomes of reform. Castelar Pinheiro et al. (2004) assert that reform in Brazil had little impact on inequality and poverty alleviation. It could have contributed to significantly reduce poverty had it been more successful in fostering investment and growth, for inequality remained mostly unchanged. According to them, reform in Brazil was too partial, incomplete and inconsistent to speed up economic growth significantly. Aguilera et al. (2004) emphasize the absence of attempts to modify the highly unequal distribution of resources, particularly land, in the pro-market reform agenda in Paraguay. Acuña et al. (2005) report a significant rise in inequality and poverty during the reform in Argentina, but that was to some extent a continuation of previous trends in the country. Monaldi et al (2004) report that in Venezuela “income distribution has not significantly worsened in the last two decades”, but poverty reached the highest levels in Venezuelan history during the Perez’s reformist period. Income distribution did not change much and poverty reduced in Uruguay during the reform (Forteza et al. 2004), but the 2002 crisis had a significant negative impact on these two indicators.

2.3.3 Perceptions

Public opinion and political discourse have been turning against pro-market reform in Latin America in recent years, a trend that Lora et al. (2003) have baptized as “reform fatigue”. According to Latinobarometer, the percentage of the population that thought that privatization was good dropped from 50 to 25 percent between 1998 and 2003, and the percentage that supported market economy dropped from 77 to 18 percent in the same period.

The attitude of citizens about reform varies across the region. Satisfaction with the market economy is low on average, and has decreased in recent years, but there are significant differences across countries. According to Latinobarometer, the percentage of the population that was either very or pretty satisfied with the working of the market economy in 2004 ranged from 36 percent in Chile to only 5 percent in Perú. The percentage of the population who agreed on that private enterprises are necessary for development ranged from 76 en Dominican Republic to 48 in Bolivia. Most of the population (from 59 to 98 percent) seems to be against privatizations. Despite of this negative turn of public opinion regarding reform in Latin America, there has been little reversion so far. According to Lora and Panizza, only Argentina and Venezuela show some reversion. According to some of the country studies, the 'status quo bias' operates now in favor of maintaining reforms.

3 The Country Cases

As stated in the introduction, answering the questions formulated in the Understanding Reform project is a complex undertaking in general, and it is particularly difficult to reach any conclusive answers from a set of seven papers containing studies of eight countries. From our point of view, one of the messages of this project is the uniqueness of country cases. Reform processes are different experiences, embedded in peculiar political, economic, institutional and social dynamics in each country. In order to distill some of the flavor of these rich cases, in this section we provide a very succinct summary of country narratives from each case.⁹ In the next section we attempt to draw somewhat general messages from these cases.

3.1 Argentina

Argentina returned to democracy in 1983 after a much interrupted democratic history. The country had been immersed in a not always consistent State-centered inward-looking development strategy since the 40s. By the 80s there were many inefficiencies, severe external and internal imbalances, and very high inflation. After some partial opening attempts during the military dictatorship, the first democratic government (Alfonsín) did progress in democratization, and some timid trade liberalization, but left with the macroeconomy in disarray. The entering Peronist government (Menem) surprised everybody with its market-oriented turn. It implemented a broad and speedy market liberalization program. From the very beginning it was tied to macroeconomic stabilization attempts, and since 1991 it became connected to the peculiar macroeconomic mechanism of

⁹ This summaries are quite selective, but based on statements by the authors of country studies except when explicitly noted. For brevity we avoid citations throughout. We invite the reader to consult the rich underlying studies for more detailed arguments.

“Convertibility”. The overall political and economic dynamics of the reform process became intertwined with the Convertibility regime.

Menem and his entourage decided that the market oriented route was the risky bet to take in a context of great social and macroeconomic chaos. He conveyed several signals to convince skeptical domestic and international economic actors. He maneuvered the institutional and political resources at hand, sometimes stretching institutions. The support of powerful provincial governors of small overrepresented provinces was key to the passage of reforms, and it was purchased through (federal fiscal) favors. Even though the labor movement was debilitated, some unions and especially union leaders were favored with some privileges. A similar strategy was followed with the business sectors. There were some natural winners in the financial and other sectors. Crucial conglomerates received a “piece of the cake” through privileges in the privatization business. Some import substituting sectors were net losers because their collective action capacity was weakened.

The economy had a strong performance in the first years of the reform. In 1995 Menem was reelected (after maneuvering to change the Constitution and after sailing through the Mexican crisis). The second term was less reformist, and the more negative aspects of the administration became more salient. In 1999 a new coalition was elected, on the promise of maintaining convertibility and some broad aspects of the reforms, while improving in the social front and transparency. The new government was unable to steer through the difficult external and internal situation, and left in disgrace in December of 2001. The Convertibility regime fell, and the governments coming afterwards had an anti-reform discourse which seems still prevalent in public opinion.

3.2 Brazil

Brazil returned to democracy in 1985, after more than two decades of uninterrupted military governments. The first democratic government unsuccessfully tried to stabilize the economy and made little progress with reform, but since 1990, when Collor de Mello arrived to the presidency, the successive democratic governments carried on a series of market-oriented reforms.

Authors of the country study argue that democratization facilitated the introduction of market-oriented reforms in Brazil. While the military stayed in government, the protective mantle of “national security” and “key-sectors protection” became a standard speech, always blocking a deeper integration into the world economy and, especially, impeding the privatization of large SOEs. This ideological view was present not just at the top of the military regime but also inside the mid-level military officers who were commonly appointed to prominent positions in economic ministries and

state enterprises. In the nineties, under democratic rule, a new breed of internationally-minded top civil servants replaced these officers.

According to the country authors, reform in Brazil followed a “**pragmatic way**”, meaning that it was gradual, piecemeal, and loosely coordinated. Fragmentation of the political system prevented any group from gaining dominance and forced a negotiated style, leading to gradualism. So, most policies took time, were negotiated, and had to go through multiple veto points. The informal institution of rather fluid ties among state elites and between them and business facilitated consensus building around reform policies, but they had to be negotiated. In this manner, the policy outcomes were unlikely to be extreme.

The actual social and economic outcomes have not been too spectacular, and some discontent against “the reforms” has bred. Yet, the arrival to office in 2003 of a left-wing party, the PT, has not generated any reversal, suggesting that “pragmatism” is not likely to be displaced soon in Brazilian economic policy making.

3.3 Chile

A far reaching reform process was undertaken by the military dictatorship since 1973, being the pioneer market reformer in the region. During the deep crisis of the early eighties, there were some partial reversals, but the reform process resumed soon afterwards. One of the most notable aspects of the Chilean process is that after the return to democracy in 1990, the center-left coalition that has governed the country since, did not revert the market reform process.

There were several peculiar factors leading the military dictatorship to follow the suggestions of a group of foreign-trained economists towards market liberalization (against the nationalistic tendencies of part of the military). Some possible sources of opposition (such as unions or left leaning parties) were silenced by the dictatorship. Business sectors were relatively grateful since firms were devolved to private owners after nationalization by the previous socialist government of Allende, so that they did not oppose trade liberalization.

The way the transition to democracy was instrumented in the late eighties was key for the consolidation of pro-market reforms in Chile. Contributing factors were: (a) the good performance of the economy in 1985-1989; (b) the concurrent fall of socialist regimes in Europe; (c) the economic failure of democratic transition in Argentina (that contributed to convince several left-wing politicians of the risks of “heterodox” policies); (d) the intellectual renovation and internationalization of the circles around the Concertación, which led to a “reevaluation of continuity”; and (e) several institutional enclaves in the new constitution, increasing the veto power and political relevance of

“the right”, which forced democratic presidents to follow consensual strategies on economic matters.

3.4 Mexico¹⁰

Mexico followed inward looking policies since the great depression. The “*Desarrollo Estabilizador*” model delivered growth for many decades, but showed signs of exhaustion in the early seventies. Populist policies in 1970-1982 contributed to its failure, including the build up of a large public debt in spite of favorable oil prices.

The reform process was gradual through three administrations from 1982 to 2000. It got momentum around the signing of NAFTA in 1993, which meant an acceleration of trade liberalization (cum preferential access to the US market). Privatization was important, as was foreign direct investment, although some areas are still restricted. The government used privatization proceeds to push a social agenda that facilitated popular acceptance of the reforms.

The reform was led by technocrats within the dominant party PRI who had to convince PRI politicians that some democratic and economic liberalization was the path to maintaining power, while convincing the public at large of the benefits of the policies so that they kept voting for PRI in the now more open political environment.

Currency overvaluation and current account deficits led to the “Tequila” crises in 1994. The ensuing period was one of debilitation of PRI machinery and some loss of reputation for the technocrats. After further political liberalization under President Zedillo, a new era of divided government started, Congress as well as regional powers gained more importance. All of this has led to a strong deceleration and stalemate of reforms.

3.5 Paraguay

The Stroessner dictatorship was a handbook example of a “**predatory state**”, exercising power in the interests of a narrow group of actors in the military and Colorado Party. The rents behind that process became exhausted and this led to some political opening. Market oriented reforms came along in this context, and politicians paid lip service to them as legitimating their “modernity”. Some of the deep determinants did not change, and the predatory state was replaced by a “predatory party”. Transition politics were more about “state capture” than about building new state capacity.

¹⁰ This brief summary of the Mexican case draws from Lehoucq et al (2005) as well as from the UR project Garibaldi and Molinet (2004).

That lack of technical capacities characterizing the Paraguayan bureaucracy also limits possible benefits of the reform process.

Regarding economic reform themselves, the change was not as pronounced as in other countries because Paraguay was always characterized by a comparatively low density of regulation and a rather open economy. Some pro-market reforms were made on fiscal, financial and trade fronts, as well as some minor privatizations.

Very important obstacles to growth, such as a large sector of loss making state enterprises, a large informal sector and poor institutional conditions of the bureaucracy and judiciary, have not been removed. Neither the Colorado Party, nor any private sector lobby, have pushed for privatization. Public appointments and promotion are essentially dependent upon political loyalty and personal contacts.

3.6 *Perú*

Perú used to have a centralized oligarchic system based on export led policies until the late 70s and 80s, when an ISI structure with stronger role for the State was introduced. This period ended with the loud crash of Alan Garcia's government in 1989, with GDP falling 16%, 4-digit inflation and no international reserves. At the same time, there was a growing terrorist offensive of Shining Path guerilla, which led to an increase in power for the military.

In this context, A. Fujimori, an outsider to the party system, reached the presidency in 1990. He confronted a complex lack of political and institutional support: no economic team, no Congress majority, and a weak party behind him. His energetic strategy was to rely on the military (partly for the war on Shining Path), to use many emergency decrees, and to obtain legislative delegation to advance key policies. All of this was buttressed by a political architecture of backstage dealings with traditional political parties.

The reform package started with stabilization measures and included shock-therapy reforms in several areas at the same time. The reform path was strengthened since 1992 when Fujimori staged a self-coup closing Congress and the Judiciary for one year. After that, the Constitution was modified and Fujimori reelected.

Reform was a strategy to enhance the survival chances of an outsider president, and was implemented to prove to the opposition and the public that the President could deliver governability in the midst of a major crisis. The Fujimori era ended up in scandal, and that has tarnished the

image of the reform process. The current government has been ineffective. Current trends include the revival of popularity of Alan García (and even Fujimori!) and cast some doubts on the future of the reforms.

3.7 Uruguay

Uruguay has been gradually implementing pro-market reforms for several decades. There were several attempts at macroeconomic stabilization, but without a close tie to structural reforms. The triggers of reform have been idiosyncratic across areas. In general, the reform process has been very **gradual**, mostly due to the active participation of opposition groups, not out of a specific plan or strategy.

Gradualism in market reforms and political pluralism and inclusion are two faces of the same coin. Opponents of reform used referendums and plebiscites to slow down and limit the scope of the process. There has been progress in trade and financial liberalization, but very little advance in labor markets and almost no privatization. Public enterprises continue to operate key activities as electricity, telecommunications, oil, and water.

Influence (“learning”) from neighboring countries has been important. During the first half of the nineties, the examples of Chile and Argentina served the purposes of reformers in Uruguay. Events in Argentina in recent years have contributed to undermine the legitimacy of reforms in Uruguay. The resistance to market reforms has always been strong and the deep crisis Uruguay went through, as well as the collapse of Argentina after the IFIs insisted that was the model to follow, contributed to further discredit the pro-market reform agenda.

Some policies and institutions that badly need reform could not be changed sufficiently, leaving vulnerabilities in banking, the fiscal system, bankruptcy procedures, etc. Some achievements such as low inflation, a more open economy, and some improvement in state capabilities have been sustained. In 2005 a left-wing party that had systematically opposed reform came to power. It has so far shown a fairly market-friendly approach.

3.8 Venezuela

Venezuela had an oil-centered development model which seemed to work for many years, and that also sustained an oligopolistic and stable two-party system. That model started to crumble in the late seventies and eighties. In 1989, recently elected president C. A. Pérez adopted a

comprehensive reform package, known as “*el Gran Viraje*” (the Great Turnaround), a clear episode of “neoliberalism by surprise.” (Stokes, 2001).

Pérez initiated this ambitious program with little support from the (then weakened) apparatus of traditional parties. Having witnessed the failure of populism with Alan García in Perú, and the success of market-friendly policies of socialist Felipe González in Spain, he trusted in a group of well-trained technocrats. The population showed immediate discontent, including street riots in Caracas (the *Caracazo*). Opposition was unorganized and this allowed Pérez and the technocrats to get through for a while.

But eventually, political backlash triumphed, the reforms failed, and Pérez did not finish his term. He was never able to convince the public, perhaps because unlike Argentines before Menem or Peruvians before Fujimori, Venezuelans did not observe a full-blown crisis to justify these policies.

The fact of being an “oil economy” underlies the whole story. Oil wealth enters several ways: 1) influencing political ideology by shaping a historically successful rentist program; 2) shaping cultural myth of a rich country that only has to redistribute oil rents to develop; 3) inducing a clientelistic and corrupt state; 4) allowing to avoid full blown hyperinflationary crisis; 5) creating economic distortions; 6) making fiscal reform harder.

4 Themes on the Political Economy of Reform

4.1 The Initiation of the Reforms

The crisis of the ISI model in the sixties and seventies left Latin American leaders searching for new paradigms. In this context, the pro-market reform agenda began to gain strength, initially pushed by groups of professional economists trained in the US, and reinforced later in the eighties and nineties by the IFIs. In some countries, these new ideas got through to the ruling army forces. Chile was the leading case, after a short socialist experience that ended with a military coup. To a lesser extent, the military ruling Uruguay in those years began to follow a similar path.

Later on with democracy, several political leaders who gained elections proposing left-wing platforms ended up adopting the market-friendly package -- the leading examples are Menem in Argentina, Fujimori in Perú and Carlos Andrés Pérez in Venezuela. Some of these presidents were concerned by little more than their political survival in the midst of impending or ongoing macroeconomic crises, and were pretty much open to “anything” that might deliver some short-term

economic results that could lead to favorable political results for them. They were convinced by that the market-friendly package was the only sensible option they had. Mexico in the eighties also shows a fast change in the paradigms that were dominant in the formerly developmentalist PRI. In that case, the change was announced before elections.¹¹ The speech of the Paraguayan Colorado Party showed a considerable change as well in this period, but according to the UR case study, this change was more rhetoric than anything else. Uruguayan traditional political parties experienced a much longer and nuanced shift from developmentalism to economic liberalism.

4.2 Technocrats

Some country studies in the UR project emphasize the role played by teams of local “technocrats” (Chile, México, Perú and, to a lesser extent, Venezuela). Stokes (2001) also provides some interesting accounts of the role played by advisors in some policy switches (Miguel Rodríguez and Moisés Naím in Venezuela, Hernando De Soto in Perú, the Bunge staff and the Cavallo team in Argentina).¹² Other country studies do not stress this point, probably implying that “technocrats” played a less important role in those cases. Castelar Pinheiro et al (2004) say that: “Unlike many countries in Latin America, market reforms in Brazil were not associated primarily with any single president (as for example with Menem or Fujimori) and party coalition in democratic contexts, *or with the rise of a new dominant technocracy* in the executive branch in authoritarian settings (Chile and the ‘Chicago boys’ or the neoliberal technocracy in Mexico in the 1980s and 1990s.” (Emphasis added). Like in Brazil, there are no clear signs of a rising technocracy in Uruguay during the reform process. It is true that some politicians complained about the lack of political sensitivity of the “contadores” (meaning the accountants and economists that represented the technical face of the Uruguayan governments). These politicians would probably claim that “technocrats” played a key role in the case of Uruguay, as well. Yet, Uruguayan governments did not count with powerful teams of “technocrats” in the fashion of the “Chicago boys” in Chile, the IESA people in Venezuela, or the group that accompanied Salinas in México. This is not to say that the governments of Brazil or Uruguay lacked well trained professionals. We rather mean that we do not identify in Brazil or

¹¹ Also the “imbrication” of the technocrats into the political process is deeper in the Mexican case, where they emerged from within the PRI structure, while in Argentina the interaction looks more like political leaders picking teams of technocrats “from the shelf” of private think tanks. This has some implications for the continuity and quality of policies. (Spiller and Tommasi, forthcoming, and IADB 2005)

¹² The tales in Stokes suggest that the story of the Menem’s switch is slightly different from the other two in this respect. It seems as if Menem himself had a more clear idea of what he wanted in terms of economic policy than Fujimori or Pérez did. Nevertheless, it seems pretty clear that a group of economists trained in US universities played a key role in Menem’s reform, much alike in the other cases mentioned above.

Uruguay a group of professionals actively lobbying for their “own” pro-market reform project, at least not in so prominent government positions as it could be seen in other Latin American countries in the same period. The UR-study on Paraguay (Aguilera et al 2004) emphasizes the lack of technical expertise of the bureaucracy and the government teams, implying that no technocracy could be identified in this case.

4.3 Stakeholders

The initiation of reforms seems to have come mainly from the top of political leadership, with varying degrees of technocratic and foreign influence. This section looks into the “response” of key stakeholders.

The early literature on the political economy of reform devoted substantial effort to understand why entrenched economic interests didn’t oppose market-oriented reforms. That very question reflected a relatively low engagement of traditional “interests”. A somewhat surprising feeling that one gets from the country papers, consistent with the views in some recent literature (notably Schneider 2004), is that such “distributional coalitions” have been far less important than expected.¹³ Some of the UR country studies mention that some entrenched interests created during the ISI opposed reform in some specific episodes (Castelar Pinheiro et al for Brazil, Chumacero et al for Chile), but the general view is that they did not play as significant a role as it might have been expected.¹⁴ As Schneider argues, “the absence of anti-reform coalition in the case of trade liberalization is especially significant because trade reform affected the allocation of many more resources and the interests of many more economic agents than did the other more targeted market reforms such as privatization or the deregulation of particular sectors.” Looking into the micro-level, it seems to be the case that the interests of firms and of economic groups are much more multifaceted, dynamic, ambiguous and variable than expected in some interest-based accounts of the political economy of policy making. In some of the countries (notably Argentina) business interests were coopted into the reform agenda by clever maneuvering and, in some cases, compensation.

Even though labor market reform has not “progressed according to the plan” in most countries, neither the country papers nor the specialized literature on unions (Murillo 2001) give “the labor movement” much weight in their explanations of the broad aspects of the reform process. Here also there have been some accommodation, cooptation and transactions. Menem in Argentina

¹³ Moisés Naim (1993) referred to these surprisingly unimportant actors as “paper tigers.”

¹⁴ This interpretation may be somewhat biased by the fact that we are looking at a set of “reforming” countries as opposed to a random sample of countries in the world.

provides one example of an active policy oriented to divide and coopt unions, skillfully combining “sticks and carrots” (Acuña et al). The case of Mexico is also interesting because the ruling party, the PRI, like de Peronist party in Argentina, had traditionally been very close to the trade union movement. However, at the beginning of his term, Salinas de Gortari sent a clear message that the times were changing proceeding against one of the most powerful union leaders, the head of the PEMEX union, accusing him of corruption and criminal activities (Garibaldi and Molinet). In Venezuela, Carlos Andrés Pérez also belonged to a political party with close ties with the labor movement. But, according to Monaldi et al, by the time Pérez came to office and announced a pro-market reform program, the legitimacy and political strength of union leaders had already been considerably eroded. In other countries, the labor movement was more independent from the State and from the parties that ended up being reformist. In Brazil and Chile, trade unions would not favor pro-market reform, but they were forbidden in Chile when the reform began and relatively weak in Brazil (Castelar Pinheiro et al). The trade union movement in Uruguay has traditionally been strong and independent. Even though trade unionism weakened in the nineties, particularly in the private sector, the unions of the state-owned enterprises played a significant role in getting support for several referenda and plebiscites to vote down some of the reform norms (Forteza et al).

From the country cases we were asked to consider, one gets the sense (consistent with the view of Schneider 2004), that reform (and even reversals) is (are) engineered more at the top of the political game, in interactions with partisan considerations, public opinion, and compensation or bribing of key political actors (such as governors in Argentina) which are not strongly tied to any particularly relevant socioeconomic interest.

4.4 *Inclusiveness of the Political Process behind the Reforms*

Schneider (2004) and others argue that countries that reformed by decree without much participation often managed to quickly pass reform packages, but at the expense of greater uncertainty about the ultimate fate of the reform. If reformers have to pass through several veto gates, the argument goes, the policy becomes more predictable and the likelihood of reversal is reduced. Venezuela and Brazil provide two contrasting cases. In Venezuela, few days after taking office, President Carlos Andrés Pérez surprised with a reform that was neither announced during the campaign nor negotiated with the opposition, but it took no longer to reverse it almost completely (Monaldi et al, 2004). In Brazil, President Fernando Henrique Cardoso negotiated the pro-market reform along several years, and there was no reversal, even after the opposition took office. Argentina with Menem and Perú with Fujimori provide two other examples of pro-market

reform implemented through political exclusion. Even if the effective occurrence of significant reform reversion is controversial in Perú, the change in the orientation of economic policy in recent years is obvious. Uruguay is another case in which reform was very gradual and partial, mostly due to the effective inclusion of opposition parties and social groups in the negotiation of reform. This participation slowed down reform, but it can be argued that it also contributed to render the economic policy more predictable (Forteza et al 2004).

Political participation might not only contribute to reform because it reduces resistance, but also because it promotes a more open society in which special interests find themselves more constrained. Paraguay could be a good (negative) example of this. Aguilera et al (2004) argue that political participation has been very limited in Paraguay during the reform period, and that this lack of participation was functional to the “predatory state” that in the end blocked the pro-market reform process and any serious development project. An active civil society could contribute to the economic and social development of the country, undermining the “predatory state”.

Referendums were not common in Latin America in the pro-market reform era, with the exception of Uruguay. In this case, the opposition made intensive use of referendum and plebiscites to fight reform. Forteza et al (2004) argue that these instruments of direct democracy allowed opponents to effectively slow down or definitely block reform, but without threatening democratic institutions. Furthermore, they argue that referendums contributed to the consolidation of democracy, because they gave the opposition effective weapons to resist reform within the rules of the system.

4.5 *Neoliberalism by Surprise*

Some political leaders in Latin America decided to take a shortcut to reform. Aware that public opinion was not favorable to pro-market reform, they campaigned for left-wing or even populist electoral platforms to get the votes, just to do the opposite when they took office. Among the best known cases are those of Fujimori in Perú, Menem in Argentina and Pérez in Venezuela, but Stokes (2001) counted twelve episodes of “policy switches” between 1982 and 1995.

Public opinion in Latin America has been pretty volatile. The uncertainty people have about the mapping of policies onto outcomes seems to be a key determinant of the volatility of public opinion. Voters who are uncertain about policy outcomes must be more willing to change their opinion about a specific policy when they see unexpected results than more ideological voters who, right or wrong, have stronger opinions. But the uncertainty of voters about policy outcomes may also contribute to the volatility of public opinion when “opportunistic” politicians decide to surprise voters announcing a policy and then switching to a completely different one when they are in office.

In the policy switches, there is a gap between policies desired by public opinion as expressed in elections and policies implemented by elected governments. Hence, when reform took place through policy switches there was an abnormally large distance between desired and implemented policies. Then, when the reform was successful (at least initially so, as in Fujimori or Menem), public opinion changed fast. *Neoliberalism by surprise may have induced high volatility of public opinion.* Policy switchers expected to change voters' minds about pro-market reforms not by convincing them before elections but by implementing the reform by surprise and showing them the good outcomes. They made a big bet expecting a significant change in people's minds. Politicians would not risk a policy switch if they thought that public opinion would not change even if the performance after the reform was very good. Hence some sort of "propensity" of public opinion to change seems necessary for policy switches to take place: there must be a sizeable uncertainty of voters about the mapping of policies onto outcomes for policy switchers to play this game. Otherwise, voters would not change their view about pro-market reform, ascribing good performance to good luck, and the policy switcher would not find the policy switch appealing.¹⁵ *Neoliberalism by surprise would not take place if politicians did not foresee a high potential for significant switches in public opinion, which in turn requires a significant uncertainty of voters about the mapping of policies onto outcomes.*

The three leading examples of neoliberalism by surprise eventually led to a failure of some sort. In Venezuela, Pérez could not complete his program and the reform was later reversed. Menem in Argentina and Fujimori in Perú enjoyed some initial success, but this was only temporary. Their governments finished with serious accusations of corruption, and public opinion turned against these presidents and against the reforms in both countries. These results suggest that neoliberalism by surprise is a risky shortcut to reform. It is worth noting that these "surprises" do not occur at random, but are more likely in countries which have some problems in their polity that prevent a more rational and informed construction of economic policy agendas.¹⁶

4.6 Speed, Sequencing, Shocks and Learning

A large part of the literature on economic reforms and on the political economy of reforms has been concerned with the issues of the sequencing and speed of introduction of market oriented reforms

¹⁵ Stokes (2001, pp 61-63) provides a sketchy model with these features, based on Harrington (1993). See also Tommasi and Velasco (1996) and Cukierman and Tommasi (1998a and 1998b).

¹⁶ See the next footnote.

(see for instance Tommasi and Velasco, 1996, Liew et al, 2005). From the 8 countries analyzed for this paper, we do not obtain a totally clear picture regarding sequencing issues. The main reading that we make of the speed issue is that the countries that went fastest, in general also in a surprising manner, seem to have the least consolidated reform processes. Countries that go more slowly (such as Brazil or Uruguay) seem to go more steadily. Those that “overshoot” via neoliberalism by surprise (Argentina, Perú) seem to fare worst in the medium to long term. But then, there is an obvious endogeneity problem, in that countries that are “forced” by the political equilibrium to act in such a spasmodic manner, are themselves those with weaker state capabilities in the first place.¹⁷

A related issue is that of the “bundling” of structural reforms with macroeconomic stabilization in general, and with peculiar stabilization attempts in particular. As discussed later, in such cases, the fate of reforms in terms of popular acceptance and political viability becomes too tied to later macroeconomic events, even to events to some extent beyond the control of the domestic polity.

Particular sequences of events have shaped perceptions and political strategies about the reforms. There have been peculiar “learning” dynamics within and across country experiences. Many countries in the region have been influenced at some point by the successes of the reform experience in Chile. In turn, within Chile, the relatively good economic situation at the transition to democracy facilitated the decision in favor of reform continuity. (The story might have been different, had the transition taken place around the 1982-83 banking crisis). Also, the left-leaning new democratic government in Chile, “learned” from the economic failures of the first new democratic government in Argentina to steer away from “heterodox” economic policies. Uruguayan reformers were boosted by the relative success of both Argentina and Chile during the early 1990s. After the Argentine crisis of 2001-2002, Argentina moved from the “poster child” of the Washington consensus to a “basket case” (Pastor and Wise, 2001), and was used as the case that demonstrated how wrong neoliberal policy recipes were. These experiences reflect how contingent on macroeconomic (and often outside) events and political and economic processes, and how “fragile” political and public opinion and learning are. (Even more fragile and volatile than professional opinion trends, which are themselves fairly flimsy and subject to fashions and fads.)

¹⁷ See Stein and Tommasi (2005) and IADB (2005) for a comparative study of State capabilities across Latin American countries. See also our remarks in Section 5. Countries with better state capabilities seem to be those that take a more “nuanced” approach to reform, and are better able to adjust the “Washington package” to local context.

4.7 Local Idiosyncrasies Conditioning the Reform Package

Some of the UR country-case studies emphasize the role of local characteristics to condition the specific contents of the reform. Castelar Pinheiro et al (2004) emphasize the Brazilian “pragmatism” and “piecemeal approach” to reform as a response to the many contradicting influences on the policy-making process in the country. In their view, while being pragmatic, Brazilian policy makers were effective in exploiting the opportunities for reform in specific areas, but at the cost of some erosion of the efficacy of the reform process. Aguilera et al. (2004) mention that politicians in Paraguay have also been pragmatic and even opportunistic. But pragmatism has not been sufficient in this case to foster reform. According to Aguilera et al., weak institutions and the “predatory state” impeded the progress of the reform in Paraguay. Forteza et al (2004) say that reform in Uruguay was a home-grown process, which departed considerably from the blueprint of the Washington Consensus. Garibaldi and Molinet (2004) argue that reformers in Perú and México used informal networks to push the policy changes. These “informal institutions” helped the reformist players to overcome resistance to reform. Menem in Argentina managed to put some very disparate actors together - including the traditional clientelistic Peronist networks - to push reform. (That affected the characteristics and the sequence of some reforms – Acuña et al 2005). According to Monaldi et al (2004), this was not the case of the Venezuelan experience during the Pérez administration: “the Pérez team followed a textbook version of the paradigm of the times, the ubiquitous “Washington Consensus” espoused by the International Financial Institutions.”

Some local idiosyncrasies of the reform process were dictated by recent macroeconomic history. In no country as in Argentina the macroeconomic stabilization program and the structural reform were so tightly linked. After years of inflation running out of control, the convertibility plan adopted as a shock therapy to defeat inflation became the cornerstone and the landmark of the whole government program in Argentina in the nineties. The case of Venezuela shows the key role that natural resources can play in the reform process.

4.8 Feedbacks Between the Reforms and the Countries’ Political Processes

Market-oriented reforms occurred in the context of each countries’ policymaking process. According to some authors (Acuña and Tommasi, 2000, Tommasi, 2004) market-oriented reforms where medium-level institutional reforms and not changes in “deep institutions”, and the workings of those deep institutions still heavily condition the performance of economies and societies. Yet, there could be potentially important interactive effects, in which market-oriented measures could lead to changes in fundamental political games. We have already mentioned the fact that the

success of market oriented reforms in Chile and some details of the transition to democracy might have created some sort of virtuous connection between political and economic dynamics. A theme in the literature is whether market reforms and fiscal retrenchment reduce the scope of clientelism, and hence transform fundamental political games. The country studies seem to give mixed answers to this question.

Some country studies (México, Uruguay, Venezuela¹⁸) mention the possibility that the reform reduced the scope for clientelism and patronage, which were typical devices used by the political parties to get support. The paradox is that the same parties that implemented or at least attempted the reform had extensively used clientelistic networks in the past to build their political power. While pushing reform, these parties might have eroded their own basis of political support.

In Argentina, Acuña et al (2005) emphasize the ability of Menem to manage the clientelistic political machineries of Peronism to advance reform. In their view, the pro-market reform does not seem to have significantly eroded clientelism in Argentina, and this might be one of the main flaws of Argentine reform: “The power of “governors” (more generally, territorially based clientelistic networks in Provinces over-represented in national Congress) has increased.” (...) “The quality of democracy is severely deficient in many Argentine provinces, and part of the overall logic of national politics and policymaking seems “linked” to those feudal networks. Voters tend to vote majoritarily for those political “elites” since at the margin they are the ones that “deliver” in the current political environment.”¹⁹

A common issue behind these different experiences is the tension between pro-market reform and traditional forms of policymaking in Latin America. Pro-market reform may reduce the scope for clientelism and patronage (apparently not the case in Argentina), potentially raising resistance among traditional parties. The paradox is that many of the parties that were ideologically closer to the pro-market reform agenda were also the ones with stronger clientelistic networks. They could

¹⁸ Monaldi et al 2004: “...in 1989 Pérez decided, against the polity and the patronage network built around it (most importantly perhaps, against his own party, see below), to embark on a radical solution to Venezuela’s economic problems. Doing so, he unveiled the long-hidden ills of the Venezuelan economy, thereby destroying the popular support for the two-party system and for his party in particular.”

¹⁹ Acuña et al (2005) follow Spiller and Tommasi (2003) in arguing that the policy making process in Argentina lacks intertemporal credibility, something that the reform could not substantially modify. Political instability reduces the horizon of political actors, undermining the ability to do self-enforcing intertemporal political deals. They also argue that the electoral rules “transfer power away from national legislators and national parties towards provincial party bosses, mostly provincial governors,” who are not too interested in the quality or the content of national policies. The comparatively strong powers of the Executive vis-à-vis the Parliament could have also contributed to policy instability, because of lack of effective checks and balances. The judiciary and an independent bureaucracy that could have helped to do intertemporal deals also failed in Argentina.

not openly resist reform, but embraced them with less enthusiasm than what they could have done if reforms had not represented a threaten to their political machines (Paraguay could be a leading case, with its extended reform rhetoric and little actual implementation. See Aguilera et al. 2004). The other side of this paradox is that some political parties that opposed reform on ideological grounds benefited politically from the erosion of the well established political machines of the parties that implemented or attempted reform. The UR studies for México, Uruguay and Venezuela mention this effect.

4.9 The Backlash Against Market-Oriented Reforms in Public Opinion and Political Discourse

Market oriented reforms are far less popular today than they were a decade ago. In very few recent Latin American elections are political candidates explicitly pushing a market-oriented agenda.²⁰ This phenomenon, dubbed by some observers as “reform fatigue” (Lora and Panizza, 2003), is addressed in several of the country studies.

As stated earlier in this paper, evaluating the effects of “reforms” is a very difficult task even for professional analysts. It is certainly also very difficult for the general public. Current perceptions probably mix some genuine disappointments, perceptual biases, and political gaming.

As described in section 2.3 economic and social outcomes “after the reforms” have been mixed. Yet, it is very hard to disentangle the effects of reforms because of lack of precise counterfactuals. Some micro-level studies seem to indicate that perceptions (for instance on the benefits of privatization) are more negative than justified by actual results.

This may be due to several factors. An important one seems to be the bundling of structural reform measures with macroeconomic stabilizations, and the subsequent fragility to macroeconomic crisis. The country studies provide highly suggestive accounts of the negative impact of recent economic crisis on the popularity of pro-market policies. Another reason might have been the political overselling of the benefits to be expected from the reform process. Also, in several countries reform was implemented “by surprise” against the will of large segments of the population. This also

²⁰ Satisfaction with the market economy is low on average and has tended to decrease over time, but there are significant differences across countries. According to Latinobarometro, the satisfaction with the market economy in 2004 ranged from 36 percent in Chile to 5 percent in Perú.

seems to have undermined the legitimacy of the pro-market agenda. In some of those cases, the reformist government was tarnished by an image of corruption, which spread to the reforms themselves. Also the reforms are associated in the public's mind with a deterioration of income distribution and with the weakening of labor actors.

One of the finest empirical analyses of this phenomenon, by Carrera, Checchi and Florio (2004), studies the ingredients of discontent with privatizations in 17 Latin-American countries. They find that disagreement with privatization is more likely when the respondent is poor, privatization was large and quick, involved a high proportion of public services, and the country suffered adverse macroeconomic shocks in a condition of high inequality of incomes.²¹

One could conjecture that as countries are recovering from macroeconomic crises or recessions, support for market reforms might recover. Yet, that statement would need to be qualified, depending on whether the recovery is interpreted as associated with the reforms or with reform reversals. The strong anti-reform discourse of the current Argentine government "construes" the recovery as due to the abandonment of the Washington Consensus.²²

Despite the negative turn of public opinion there has been little reform reversal so far. According to Lora and Panizza, only Argentina and Venezuela show some reversion. They argue that "status quo bias" operates now in favor of maintaining reforms. The Brazil and Uruguay country studies emphasize the point that incoming left-wing governments have not reversed the reform course. Both governments have gone through special efforts to reduce the uncertainty naturally associated to such changes in political sign.

5 Concluding Remarks (Some Lessons that "Washington" Seems to Be Learning)

Pro-market reform has been taking place in Latin America for several years. In several cases it has achieved some valuable outcomes, yet it has underperformed in various fronts. The reading of the reform experience is today unfriendly in several countries.

²¹ Interestingly, they also find that more educated respondents are more adverse to privatization.

²² In fact the recovery seems more likely to be a standard re-bounce after a very deep fall, in the context of very favorable external circumstances, with a more aligned exchange rate after the fall of convertibility, exploiting unused capacity built with investments during the reform decade. In relation to this topic, see Tommasi (2004).

Broad sectors of the Latin American public, including important social and political actors never felt included in the pro-market reform agenda. There is a view in the region that the agenda was imposed from abroad, a view that seems confirmed by the term “Washington Consensus”. The efforts of the IFIs to push this agenda²³ disregarding strong local anti-reform feelings might have led to not very successful reform processes and to the reinforcement of these anti-reform feelings. The attempts to impose reforms during dictatorships and “by surprise” in some democracies contributed to the discredit of the agenda.

Recent studies at the IFIs have starting to acknowledge that domestic political conditions and institutions seem more important than conditionality for the success of reforms. This seems to be forcing the IFIs in the direction of more humble and less universal recipes. There is also a lesson learnt from this experience in terms of the importance of details and local idiosyncrasies. The same formula that worked in one country may not work in another, due to differences in history, local institutions and even opinions. If policy ownership is key for reform, the view of local social and political actors about the reform agenda is a “hard fact” that cannot be disregarded. Besides, the experience shows that there are not only many ways of doing things wrong, but also more than one way of doing things right. Hence, there is no one-size-fits-all reform.

In recent years, there seems to be a growing consensus about the key role of domestic policy ownership, participation and the need for home-grown reforms. There is no consensus about the kind of reforms that the Latin American countries need, but the notion that the way the policies are designed and implemented and that participation matters is gaining more adepts. The IFIs in particular have explicitly acknowledged the importance of these things in several recent reports. (See in particular IADB 2005).

²³ There was a tendency in the 80s to introduce these measures as part of conditionality when funding countries facing financial difficulties.

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Figure 1

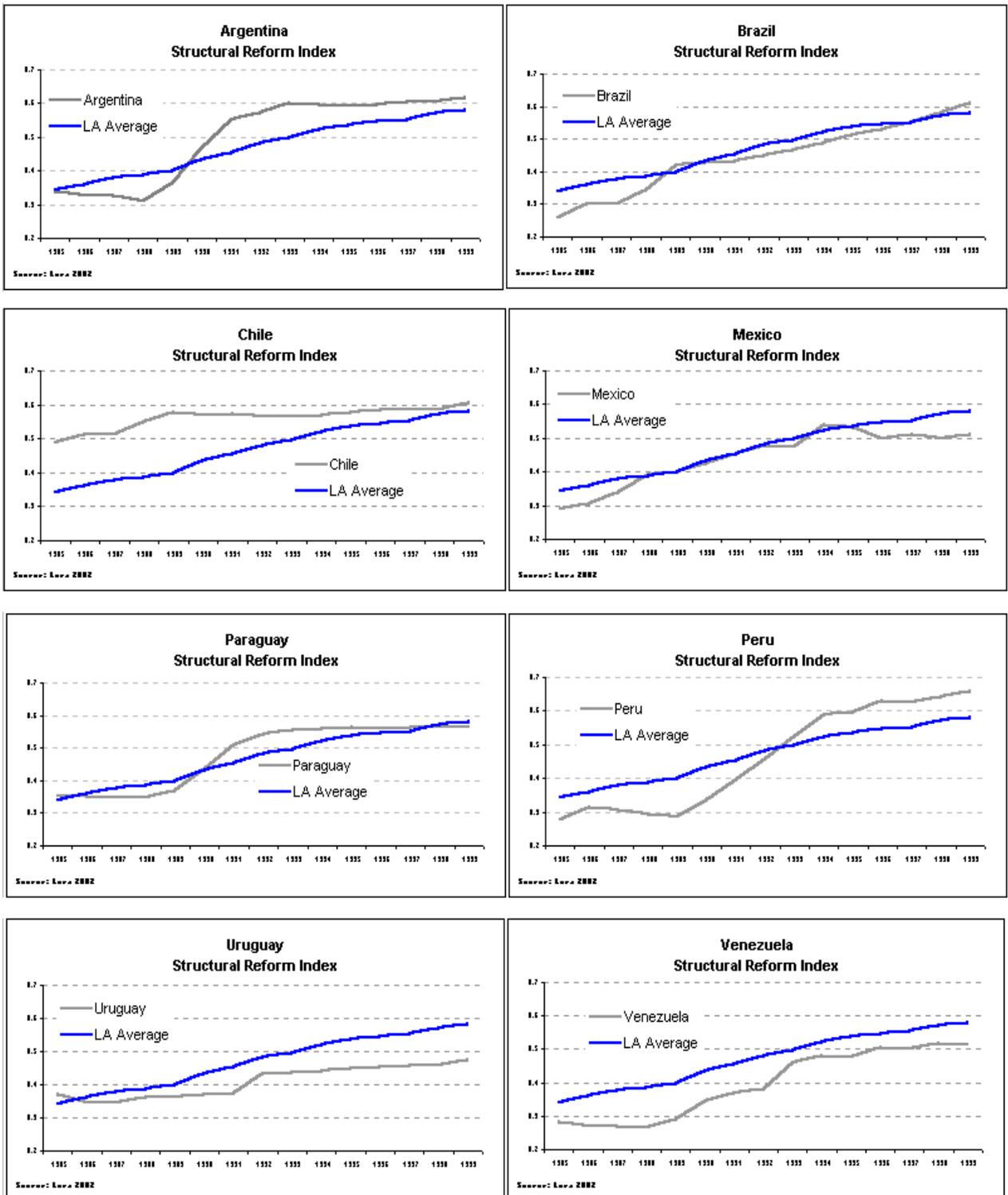


Figure 2

