

**BUSINESS ELITES AND DEMOCRACY IN LATIN AMERICA:  
Reflections on the May 1991 Kellogg Institute Conference**

**Juan J. López**

**Working Paper #185 - December 1992**

**Juan J. López** is a Ph.D. candidate in the Department of Political Science at the University of Chicago. His field of specialization is comparative politics (Latin America) and his dissertation is on political institutions and private investment in Argentina. He has been a Lecturer at the College of the University of Chicago and has an article on methodology and the philosophy of science, "Theory Choice in Comparative Social Inquiry," forthcoming in *Polity*.

## **ABSTRACT**

The discussion focuses on three themes. One is the divergence between positions of business associations and concerns of individual entrepreneurs regarding several determinants of investment. Another issue is under what conditions economic growth can be achieved under democracy; why market reforms have generated little private investment in many cases, and which government policies and political institutions can promote investment. The third topic is the relationship between democracy and capitalism in Latin America. The current acceptance of democracy by capitalists challenges assumptions about the conflictual relationship between democracy and capitalism and opens the question of what determines capitalists' preferences for political regimes.

## **RESUMEN**

La discusión se concentra en tres temas principales. Uno de ellos es la divergencia existente entre las posiciones que adoptan las asociaciones empresariales y las preocupaciones de empresarios individuales con respecto a varios determinantes de inversión. Otro tema es bajo qué condiciones se puede alcanzar el crecimiento económico en un régimen democrático; por qué las reformas de mercado han generado, en muchos casos, una respuesta pequeña de la inversión privada, y cuáles son las políticas gubernamentales y las instituciones políticas que pueden promover la inversión. El tercer tema es la relación existente entre democracia y capitalismo en América Latina. La aceptación actual de la democracia por parte de los capitalistas cuestiona los supuestos acerca de la relación antagónica entre democracia y capitalismo y formula la pregunta de qué es lo que determina las preferencias de los capitalistas con respecto a los regímenes políticos.

## 1. Introduction

This is an attempt to integrate the papers, presentations, and discussions for the conference “Business Elites and Democracy in Latin America,” held at the Kellogg Institute, May 3-5, 1991. Obviously, it is impossible to do justice to the richness of detail and to the many important ideas brought forth by the participants. I had to limit myself to the most common themes; in addition, I have included some comments of my own.<sup>1</sup> The conference addressed key issues that gained prominence in Latin America with transitions to democracy and to markets during the 1980s, in the context of a serious economic downturn.

A central topic was the problematic relationship between the positions that business associations adopt and the concerns of individual entrepreneurs, e.g., with respect to neoliberal economic policies. Unlike individual businessmen, business associations support market reforms. Businessmen seem to be in a prisoner’s dilemma situation with respect to economic reforms. Which, business associations or the state, can solve this dilemma and how can it be done under democracy?

Another main issue was why market-oriented restructuring has failed in many cases to generate significant increases in private investment. Under what conditions would capitalists invest? What can governments do to create such conditions under democracy? Fundamental in the political economy of growth under democracy is the question of how to implement policies that promote good economic performance but that are opposed by voters, organized groups, and/or government officials. In other words, how to ameliorate the discrepancy between collective rationality and particularistic rationalities as organized actors, voters, and incumbents influence government economic policies. Political institutions are central to this problematic. The exclusionary style of policy-making common in Latin America undermines economic performance and confidence in democratic institutions. How can a participatory style of policy formulation be created and yet prevent access to the state from being converted into rent-seeking, obstructing economic reforms.

A widespread belief among conference participants is that, contrary to previous periods in Latin America, entrepreneurs are now prepared to adapt to democracy and may even prefer democracy to authoritarian regimes. That capitalists want democracy contradicts theoretical conventions postulating aversion to democracy among business elites, raising the question as to what determines capitalists’ preferences for given political regimes. A major claim in the study of

---

<sup>1</sup> I only provide bibliographical references for material not presented at the conference.

development in LDCs is that there is a tradeoff between democracy and growth. If democracy used to be threatening to business interests, why not now? Have assumptions about the conflictual relationship between democracy and capitalism in Latin America been invalid all along? Or will the successful consolidation of neoliberal economic reforms increase the potential danger of democracy for capitalism?

## **2. Business Associations' and Capitalists' Particular Interests**

A main theme at the conference was the relationship between business associations and divergent interests among entrepreneurs. Two issues discussed were: (1) the difficulty that business associations have in aggregating the preferences of individual capitalists; and (2) the conflicts that informal channels of access to the state generate between elite firms and their business associations. Yet it was argued that situations of high economic uncertainty induce large capitalists to engage in collective action. In addition, conference participants offered explanations for the increase in organizational and political activities by businessmen in the 1980s.

Tavis and Valenzuela observe that conflicts of interests among individual capitalists arising from market competition hinder their ability to pursue collective action. According to Valenzuela, it is more difficult for businessmen to act collectively than for workers because entrepreneurs compete with each other more severely than workers do over jobs. In Spain, Wozniak argues, businessmen viewed social pacts concerning economic stabilization as means to overcome conflicts among themselves; entrepreneurs could unite by being forced to bargain with the government and with labor.

Durand, Jarvis, and Payne indicate that the heterogeneity of interests among capitalists makes it difficult for business associations to adopt policies that are generally supported by their members. Jarvis observes that disagreement among businessmen over economic policies is a problem for business associations in opposing government policies. Payne argues that business organizations are often fragmented and normally limit their policy advocacy to highly diluted compromise positions or to broad consensus principles, e.g., protection of the free enterprise system. According to her, in Brazil business elites proved most effective in defeating legislation (e.g., job security) that the business community as a whole strongly opposed. Durand states that the peak employers' association in Peru, the Confederación Nacional de Instituciones Privadas (CONFIEP) adopted the policy of not supporting an issue unless all its member trade associations agreed on it.

While reconciling sectoral interests is a major problem for peak business associations, as Kaufman remarks, the cohesion and political effectiveness of business associations varies with

the level of interest aggregation. Acuña mentions that the Sociedad Rural Argentina (SRA) is able to act with clearer economic and political objectives and implement much more consistent strategies, in comparison with the Unión Industrial Argentina (UIA), because the former aggregates interests that are more homogeneous than those in the UIA. Jarvis maintains that national associations of large agricultural producers, in Latin America as well as in economically advanced countries, have been successful in influencing government sectoral policies. Velasco e Cruz argues that the economic and political turmoil in Brazil during the 1980s resulted in the sharpening of internal tensions within established business associations and led to the creation of new, more homogeneous associations. Payne remarks that during the Sarney government, small industrialists felt marginalized by FIESP, and the discontent resulted in the formation of specialized trade associations that competed with FIESP.

A source of conflict between individual capitalists and their business associations is the opportunity that managers of large firms often have to influence government decisions through informal, personalized channels.<sup>2</sup> Kaufman mentions that peak business associations find it very hard to solve free rider problems among capitalists because particularized lobbying is very tempting.<sup>3</sup> He poses the questions of whether it may be idealistic to think that business associations can solve problems of investment by negotiating with governments. Tavis argues that when a firm can have preferential access there is no reason to join in collaborative activities. In apparent contradiction to Tavis's argument, Bartell states that in Brazil entrepreneurs perceived business associations as useful for lobbying and negotiating with government agents. Yet while in Brazil business associations may be useful channels of influence, especially for large companies,<sup>4</sup> these associations may not be the main avenues of access to the state for the top firms.

Heredia argues that in Mexico, although conglomerates dominated business organizations, it was in the interest of conglomerates to keep such associations secondary in importance to personalistic ties in influencing government policies.<sup>5</sup> According to Heredia, the most effective way for capitalists to influence policy-making has been through informal, personal connections. Moreover, in contrast to small- and mid-sized firms, conglomerates have tended to

---

<sup>2</sup> Valenzuela observes that informal social groups are important means of contact between capitalists and government officials.

<sup>3</sup> According to Kaufman, in the transition to economic liberalization in Korea and Mexico, informal particularized negotiations between big business and the state were very important.

<sup>4</sup> Bartell and Payne point out that in Brazil, small- and medium-sized firms complained that business associations neglected their interests and favored those of large enterprises in dealing with the state.

<sup>5</sup> However, Heredia affirms that when the Echeverría government curtailed the individualized, informal channels of large capitalists to the state, new means to influence government policies became important for business elites; in 1975 big business decided to create a new umbrella association to confront the government as a united front.

monopolize the informal access to the state. In a similar vein, Durand says that in Peru large establishments have been more interested in direct discussions with the state, without the mediation of business associations. He indicates that the García government was willing to negotiate directly with conglomerates to promote investment; however, the García government tried to undermine the ability of CONFIEP to influence the policy-making process. Correspondingly, large capitalists wanted to have direct negotiations, keeping CONFIEP out.<sup>6</sup> Nevertheless, managers of conglomerates attended CONFIEP meetings and used the peak association as a shield in confrontations with the state.

As Acuña suggests, large capitalists have been able to influence government economic policies via informal, personalized access under both democratic and authoritarian regimes. The Alfonsín government coordinated strategies with union leaders and captains of industry via direct, informal contacts, despite opposition from the UIA to accords reached with large industrialists, e.g., regarding labor laws. Similarly, conglomerates benefited from a close relationship with the state during the Martínez de Hoz tenure as Minister of the Economy; yet the UIA was under military intervention.<sup>7</sup>

In Latin America in the 1980s, concomitant with the dire economic situations, there was a surge of collective action (e.g., formation of associations) among businessmen. Durand argues that despite the tendency of large capitalists to prefer informal, individualistic access to the state, economic “crises” induce them to engage in collective action. According to Durand, the Confederación Nacional de Instituciones Privadas (a peak business association), emerged in Peru from a perception among businessmen that they urgently needed organized action to face events generating a high degree of uncertainty, e.g., liberalization policies and the economic slump of the 1980s. In 1983-84, he asserts, the generalization of the economic crisis and the unpredictability of government policies facilitated the formation of CONFIEP by making common problems prevail over the individual or sectoral interests of businessmen. Similarly, Velasco e Cruz affirms, in Brazil in the 1980s there was a proliferation of ad hoc business organizations with the purpose of coordinating the public declarations of capitalists and struggling to influence government decisions.

In explaining the increase in political activity by national business elites in Bolivia and Peru in the 1980s, Conaghan emphasizes the crisis of legitimacy that, according to her, capitalism faces

---

<sup>6</sup> Durand contends that CONFIEP could not force the conglomerates to abandon their privileged relationship with the state because a fight with the powerful *grupos* could have meant a blow to the existence of the newly founded confederation.

<sup>7</sup> According to an executive of a conglomerate that I interviewed in Argentina (9/14/89), the most important lobbies function through informal channels. He claimed that under military governments it is especially easy to get benefits because deals are less transparent than under democratic regimes.

in those countries. She argues that large capitalists, both individuals and business associations, not only wanted to influence government economic policies but also infuse public opinion with probusiness values to mold the political culture in favor of capitalism. For Conaghan, capital flight and low levels of productive investment on the part of Bolivian and Peruvian capitalists resulted in poor economic performance; thus there is not a lot of support for capitalism in the society and culture of these countries. She interprets the businessmen's political campaigns of the 1980s as attempts to build legitimacy with public relations rather than productive investments. She concludes that despite the ideological shift toward economic neoliberalism in the 1980s, capitalists in Bolivia and Peru have a long way to go in resolving their perennial problem of legitimacy.

### **3. Economic Reforms**

Vernon concentrates on the tendency for greater foreign direct investment as a consequence of new technologies and lower costs in international communication and transportation. With such developments, large enterprises are becoming less afraid of getting involved in other countries, feeling more confident in their capacity to command and control. Vernon argues that with changes in international communication and transportation, government policies will be more influential than ever in determining whether the opportunities to attract productive investments in the next few decades are effectively exploited.

While transformations in communication and transportation can increase the flow of foreign investment into LDCs, such changes also facilitate the movement of capital out of developing countries; this is another point Vernon makes. He indicates that a number of large firms based in developing countries have developed international networks. Velasco e Cruz agrees with this observation, indicating that Brazilian firms are establishing productive investments abroad.

#### **3.1. Business Elites' Attitudes toward Neoliberal Reforms**

In an international context where the mobility of capital has increased, the importance of market reforms for the economic performance of Latin American countries is magnified. One of the main issues of the conference was the position of capitalists and their organizations regarding neoliberal economic changes in the region.

In the transition from economic stagnation to sustained economic growth, individual capitalists oppose economic reforms. Tavis comments that businessmen do not support neoliberal reforms because such changes reduce their ability to obtain protection and privileges from the state. According to Weffort, a lot of capitalists in Brazil want state protection for

themselves and markets for others. Bartell reports that in Brazil during 1988-89 there was little support for promoting exports or reducing protection of the domestic market.<sup>8</sup> Velasco e Cruz maintains that although in Brazil at the end of 1989 a broad conservative coalition, including practically all capitalists, advocated the virtues of economic liberalism, this ideological consensus is only superficial. Within the ideological discourse among capitalists, economic liberalism coexists with the need for protection of the national market. Heredia states that in Mexico, although businessmen publicly support market reforms, entrepreneurs extensively oppose implementation of liberalization policies when such policies hurt their particular interests.<sup>9</sup> According to Heredia, in Mexico governments implemented trade liberalization because they were willing and able to resist strong opposition from businessmen. Conaghan indicates that in Peru, liberals in Vargas Llosa's Movimiento Libertad feared that the conglomerates would press Vargas Llosa, once in office, to water down his radical stabilization and restructuring program.

On the other hand, when economic reforms achieve success, entrepreneurs support them. Weffort remarks that capitalists in Latin America have been followers of market reform initiatives taken by the state. In the interviews Bartell did in Chile during 1987-88, businessmen overwhelmingly supported an internationally open economy. They saw themselves as very capable of successfully competing in the domestic and international markets without special privileges from the government, expressing a sense of freedom from the paternalistic mentality of the past.

Certain sectors that benefit from the outset by reforms will be initial supporters. Jarvis declares that the agricultural sector in Latin America has usually favored economic liberalization since liberalization generally benefits farmers by redistributing income to agriculture. Bartell points to the high investment in agriculture in Chile (especially in export-oriented production), arguing that economic liberalization removed the penalties imposed on agriculture by ISI policies.

In contrast to individual businessmen, business associations support market reforms, thus taking the side of capitalism in the collective action dilemma of capitalists. By the mid 1980s in Mexico, Heredia contends, most business organizations accepted the idea that market reforms were necessary and that such reforms were the only way to limit the arbitrariness of executive intervention in the economy. According to Conaghan, leaders of the Confederación de Empresarios Privados Bolivianos (CEPB) realized that they had to convince many of the CEPB membership, accustomed to protection and subsidies provided by the state, that market reforms were desirable. Conaghan argues that employers' associations in Peru were also in favor of

---

<sup>8</sup> Yet among the businessmen Bartell reinterviewed in Brazil in 1991 there was more pessimism about the viability of the current economic model and more support for opening the economy.

<sup>9</sup> Concurring with Weffort's observation about businessmen in Brazil, Heredia indicates that in Mexico protected private firms advocated trade liberalization for everybody except themselves.

market reforms. However, Durand indicates that in Peru the depression of the 1980s increased the support among national capitalists for abandoning neoliberal policies and favoring state intervention to promote economic recovery. Thus, Durand argues, CONFIEP in 1987 strongly endorsed Alan García's move away from market-oriented policies and toward promotion of economic recovery via demand stimulation.

### **3.2. Market-Oriented Reforms and Economic Growth**

Another key issue considered in the conference was the poor record of economic reforms in generating private investment. Heredia indicates that private investment in Mexico has not been as great as expected. Conaghan gives the example of Bolivia, where no major increase in private, productive investment has materialized after the implementation of market reforms in 1985, despite stabilization, the sustainability of reforms, and the agreement among the three major parties to support the economic policies.

Conaghan repudiates capitalists' explanations for the low level of private investment and dismisses their demands for building confidence to increase fixed investment. She argues that such explanations and demands seem to be excuses because capitalists have repeatedly expanded the list of what they want in order to invest. According to Conaghan, something that really matters in accounting for the investment behavior of domestic entrepreneurs is their mentality,<sup>10</sup> at least in the Andean countries.<sup>11</sup> An interesting question is why foreigners (who should have a different mentality) have not rushed to make productive investments in these countries.

Tavis mentions that managers make investment decisions based on their perception of future risks and returns. He maintains that uncertainty is probably the most important factor in explaining the low level of private investment in Latin America. Payne and Bartell contend that in Brazil the uncertainty generated by the high unpredictability of government economic policies is a key determinant of the low level of private, productive investment. Moreover, Bartell found that in Brazil many entrepreneurs believe that the fiscal deficit is a main cause of inflation and that private borrowers are crowded out from capital markets because the government finances its deficits through short-term borrowing at high interest rates.

Despite the radical nature of market reforms in Bolivia, there are factors that may explain the uncertainty regarding the stability of policies and consequently the investment response to the reforms. During 1987-89, the country had high fiscal deficits, mostly financed by foreign

---

<sup>10</sup> For example, status anxieties about utilizing investment capital from anyone outside one's immediate family and confidantes, e.g., selling stock to the public.

<sup>11</sup> Bartell indicates that although entrepreneurship in Brazil is inadequate, it is inaccurate to conclude that Brazil lacks the entrepreneurial capability of Chile.

borrowing and by reducing foreign exchange reserves, a fragile situation.<sup>12</sup> Conaghan reports that Bolivian capitalists demand a reduction of the fiscal deficit in order to increase fixed investment. Contributing to the uncertainty is the lack of institutional safeguards<sup>13</sup> against a reversal to inflationary money creation to finance fiscal deficits (Bernholz 1991: 50).<sup>14</sup> Moreover, the implementation of the tax measures, the most important being the establishment of a VAT of ten percent, has been slow and uneven; despite the formation of a new Ministry of Taxation, no major effort has been made at reforming the tax administration (Morales and Sachs 1989).<sup>15</sup>

It is commonly realized that stabilization and the implementation of economic reforms do not ensure sustained growth.<sup>16</sup> Przeworski (1991) cites three possible reasons why reforms may not improve economic performance: international events; reforms may involve a temporary deterioration of the economy; and some reforms measures may be badly designed. Another important factor accounting for low levels of growth after economic stabilization and enactment of market-oriented reforms is the dampening effect of policy uncertainty on private, fixed investment. Even a small degree of doubt that reforms might be reversed can deter private investment.<sup>17</sup> To understand capitalists' cautious behavior under policy uncertainty, one should keep in mind that entrepreneurs can incur heavy losses if they make fixed investments in response to reforms and then the policies are reversed.<sup>18</sup>

Rodrik (1989, 1991) lists a number of factors that can generate uncertainty about the stability of government policies: (1) inconsistency among concurrent policies; (2) time-

---

<sup>12</sup> This observation about the fiscal situation in Bolivia is taken from Morales (1991: 17 and 20).

<sup>13</sup> For example, an independent central bank or legal limitations on budget deficits or on the amount of credit the central bank can provide to the government.

<sup>14</sup> Morales (1991: 44) argues that a stronger judiciary is essential in Bolivia to avoid uncertainties about the violation of property rights, and thus build business confidence.

<sup>15</sup> In Bolivia after 1985, the two most important changes in tax administration, according to Bird (1992: 13-16), have been strengthening tax enforcement and turning over tax collection to commercial banks. Yet two of the three direct taxes that replaced the abolished personal and corporate income taxes rely on self-assessment. Tax revenues as a proportion of GDP has declined from 1986 (10.87%) to 1987 (9.92%) to 1988 (8.15%) (Cheibub 1991).

<sup>16</sup> Williamson (1990: 406) indicates a somewhat weak correlation between pursuit of reforms and growth. Remmer (1986) reports a moderate correlation between implementation of IMF prescriptions and the achievement of desired economic results. Dornbusch (1990: 312) points to failures of stabilization programs to restore growth.

<sup>17</sup> For an elaboration of this argument, see Rodrik (1991).

<sup>18</sup> To make productive investments in response to economic reforms, entrepreneurs have to pay the cost of reallocating capital from alternative businesses; moreover, fixed investments are partially irreversible. If reforms are abandoned, investments induced by reforms are likely to become unprofitable or less profitable than the ventures from which capitalists moved the resources in the first place.

inconsistency in governmental policy-making;<sup>19</sup> (3) doubts about the government's commitment to policies;<sup>20</sup> (5) perceptions that policies may be reversed due to strong political opposition; (6) the transient nature of policies that violate economic constraints (e.g., highly overvalued exchange rates) which lead, among other things, to unsustainable external imbalances; and (7) a scant investment response to economic reforms.<sup>21</sup> Fiscal deficits and high real interest rates are some indicators that policies will be changed.<sup>22</sup> Small fiscal deficits are particularly important in generating confidence in the private sector that reforms will be sustained (Rodrik 1990).

For economic reforms to succeed in generating an adequate level of self-sustained growth, a necessary condition is to increase tax revenues in order to control fiscal deficits as well as to create a surplus for public investment in infrastructure, provision of incentives for private investment, and amelioration of the social costs of reforms.<sup>23</sup> But tax collection performance is a widespread problem in Latin America. One reason is that, as Bresser Pereira (1992) puts it, wealthy people do not pay taxes in the region. In Latin America, income taxes (personal and corporate) as a proportion of GDP are on average the lowest in the world (3.7%).<sup>24</sup> Taxes on consumption are the main source of tax revenues in the region, indicating the regressive nature of the tax structure (Cheibub 1991: 12). Deficiency in the capacity for tax collection is another important factor in the performance of tax revenue in Latin America (Dornbusch 1990). A conclusive lesson from tax reforms in LDCs in the postwar period is the significance of improvements in tax administration and compliance (Gillis 1989). In Spain, as part of the post-1982 economic reforms, tax revenues increased from 25% of GDP in 1976 to 36.7% in 1988; the largest increase was due to reducing evasion of taxes on income and wealth (Bresser Pereira,

---

<sup>19</sup> That is, the current government or future governments may have the incentive to change policies (e.g., regarding exchange rates) after the private sector ties capital into physical assets in response to existing policies.

<sup>20</sup> It may be unclear, for example, whether a government pursues reforms just to get conditional loans from foreign sources and will abandon reforms after obtaining the desired funds.

<sup>21</sup> The likelihood that market reforms will be sustained is positively related to the level of aggregate private investment following the implementation of reforms (Rodrik 1991). It is assumed that causal feedback exists between private investment and uncertainty about policy reversals. A supporting argument is that greater investment increases political support for reforms from entrepreneurs who invested in productive ventures and from other actors, due to improved economic performance.

<sup>22</sup> See Rodrik (1990) for a longer list.

<sup>23</sup> For coinciding arguments see Bresser Pereira (1992). He argues that the inability of the state to finance itself with taxes is an essential feature of Latin American countries.

<sup>24</sup> See Cheibub (1991: 11-12). The data are for the period 1970-88. The average for the industrialized countries is 10.8% and for the developing countries 5.06%.

Maravall, and Przeworski 1992). Changes in tax administration and collection procedures were crucial in the successes of Chile's tax reform under Pinochet (Harberger 1989).<sup>25</sup>

A way to build confidence that economic policies will be sustained in the foreseeable future, and thus promote private investment in physical assets, is to create institutional constraints to make it more difficult for governments to change policies even when tempted to do so, e.g., because of time-inconsistency in policies or political pressures. Some relevant restraints are international free trade agreements, independent monetary authorities, legal protection of property rights, and an effective system of checks and balances among branches of government to limit arbitrariness in policy-making.<sup>26</sup> Heredia argues that a secure environment for investment appears to involve more than the implementation of market reforms. She mentions that the free trade agreement between Mexico and the United States has been important in creating confidence among Mexican and foreign capitalists. According to her, entrepreneurs believe that the agreement is a signal of solid commitment to economic reforms by the Mexican government. In Bolivia, Conaghan states that despite market reforms capitalists express the need for additional government measures to feel confident enough to invest, e.g., changes in laws to facilitate domestic and foreign investments.<sup>27</sup>

Ros questions the suitability of market-oriented reforms to get Latin American countries out of the economic slump they have been in during the past decade. In his critique of liberal policies, Ros implicitly makes an association between market-oriented restructuring and a laissez-faire economic role for the state. According to him, if any generalization can be made from the experiences in Latin America during the 1980s, it is that economic success is unrelated to neoliberal policies; such policies are neither necessary nor sufficient for economic recovery. He points to several countries as examples. In Mexico, the turning point leading to economic recovery after 1987 involved a heterodox plan with active state participation in negotiations with capital and labor. Moreover, the fastest growing export industries in Mexico were protected during the 1980s. In Chile, a large part of the increase in the rate of investment has been due to public investment in the modernization of infrastructure. Chile and Colombia are the only two countries in the region where public investment (as a proportion of GDP and of total investment) was higher in 1990 than in 1980. Colombia moved toward a more export-oriented economy

---

<sup>25</sup> In Korea before 1961, tax collection was poor. In subsequent tax reforms, administrative aspects were emphasized. The improvements under President Park led to tax collection increases of 18.6% in 1964, 44.5% in 1965, and 68.7% in 1966, with little change in tax structure or rates (Haggard et al. 1990).

<sup>26</sup> See Bernholz (1991) and Rodrik (1989) on the important role of institutions for business confidence in the policy environment. The Aylwin government supported a law granting independence to the central bank.

<sup>27</sup> Conaghan indicates that in Peru the Sociedad Nacional de Industrias actively lobbied to include an explicit commitment to market principles in the 1978 constitution.

utilizing export subsidies, protection of the domestic market, and foreign exchange controls. Yet all these countries have been among the best economic performers in the region during the last decade. By contrast, Bolivia which strictly followed a market-oriented package of structural reforms since 1985 has stabilized at a very low level of economic growth.<sup>28</sup>

Market-oriented reforms are not necessarily incompatible with state intervention in the economy. Kim mentions that in the movement toward liberalization in Korea during the 1960s, the state compensated businesses with incentive packages, e.g., export subsidies. Wozniak indicates that in Spain the state has played an important part in creating the existing economic dynamism. A central question is under what conditions state intervention in the economy is beneficial or detrimental for economic growth. Johnson (1987: 140-41) argues that state intervention in Japan, Korea, and Taiwan has been compatible with market forces. The institutional characteristics of a country are vital in explaining the impact of government involvement for economic performance.

#### **4. Democratic Political Institutions and Collective Rationality**

An essential question in Latin America is how to reconcile democracy with collective rationality in economic policies. In other words, under what conditions would participation by capitalists, and other social actors, in the policy-making process lead to economic growth? Kaufman notices that conference participants make two disparate hypotheses: (1) that businessmen lack confidence to invest partly because they do not have enough opportunities to participate in the policy process; and (2) that private investment has been hindered because states have been too vulnerable to rent-seeking pressures on the part of businessmen. He argues that the influence of capitalists on government policy-making is beneficial for economic performance if the state is able to pursue collective interests over the interests of individual capitalists.

##### **4.1. Institutional Autonomy**

For the state to act in the collective interests of capitalists, it must abate the influence of particularistic interests on policy formulation. One approach to this goal is to insulate policy-making from the pressures of social actors.<sup>29</sup> Singh endorses this strategy. He argues that,

---

<sup>28</sup> One important difference between Bolivia and Chile is that in the latter fiscal balances were turned into surpluses and many public businesses were privatized.

<sup>29</sup> It is claimed that autonomous economic policy-making agencies have been an important determinant in the economic successes of Far Eastern countries, e.g., the Economic Planning Board in South Korea and MITI in Japan (Evans 1989; Johnson 1987). According to Evans

given the political conflicts engendered by the distributional effects of economic policies, what is needed is some kind of mechanism that is somehow above politics. Heredia remarks that this strategy is problematic under democracy because of the difficulty of achieving an acceptable balance between the political accountability of insulated bureaucracies and their ability to make policies without being politicized, captured by rent-seekers. However, she maintains that the fundamental interests of capitalists would be well served, regardless of the orientations of the political group in power, by insulating economic decision-making agencies from particularistic interests.

Democracy is not incompatible with certain institutional autonomy in the economic policy process, e.g., independent central banks. Central banks vary in the degree to which political pressures prevent them from following collectively rational policies with a long-term perspective.<sup>30</sup> Bank autonomy can depend on: (1) legislation specifying that the central bank should pursue certain objectives; (2) the institutional relationship between the central bank and the executive; (3) the procedure to nominate and dismiss the head of the central bank; (4) the role of government officials on the bank board; and (5) the frequency of contacts between the executive and the bank (Woolley 1984; Alesina and Summers 1990). Autonomous central banks are justified as mechanisms to limit inflation by constraining elected officials from temptations to generate monetary expansion, seignorage, or exchange rate instability (Woolley 1977). Consistent with previous research, Alesina and Summers (1990) found a very high negative correlation between central bank independence and the level and variability of inflation.<sup>31</sup>

The fundamental danger of having autonomous state managers is that their actions may be contrary to the general interests of citizens. Yet there are arrangements to ameliorate principal-agent conflicts in autonomous institutions under democracy. When people want to establish some agent (e.g., a monetary authority) to force them to cooperate with one another, they face a conflict between controlling the agent and controlling themselves. O'Flaherty (1990) proposes a solution in terms of temporary tenure for the agent. At the outset, citizens give the agent instructions about what they want the agent to do; then, during the period of incumbency, people do not interfere with the authority. At a certain moment, citizens decide whether to reappoint the agent to another term in office, rehiring being contingent on whether the agent has performed in the long-term interests of the citizens. The agent must value being rehired; he must receive handsome compensation for his work. Moe (1990) argues that autonomous bureaucrats can be

---

(1989: 574) the ability of MITI to formulate its own goals and to implement them is what allows it to address the collective action problems of individual capitalists and help capitalism.

<sup>30</sup> "A central bank is independent if it can set policy instruments without the prior approval from other actors and if, for some minimal time period (e.g., a calendar quarter), the instrument settings clearly differ from those preferred by other actors" (Woolley 1984: 13).

<sup>31</sup> They used data from 17 OECD countries in the period 1955-1988.

constrained ex ante to act according to given goals by laws specifying in excruciating detail precisely what they have to do and how, leaving as little as possible to the discretionary judgement of bureaucrats.

#### **4.2. State Capacity**

Besides independent central banks, greater state capacity may enhance the ability of the state to resist the influence of particularistic interests on policy-making.<sup>32</sup> Przeworski (1990) argues that the greater the capacity of the state to implement policies the greater the motivation of social actors to control or influence the formulation of state policies. Yet while social actors may be more motivated, they may be less successful in influencing policy-making when state capacity is higher. In the case of the National Recovery Administration during the New Deal, for example, businessmen captured the administration because of weak state capacity (Skocpol and Finegold 1982). During the patronage system of recruitment into the bureaucracy prevailing in the U.S. during the late nineteenth century, the bureaucracy was incapable of exercising any control over large industrialists because of incapacity or vulnerability to pressures from capitalists (Skowronek 1982). Patronage-based bureaucracies with low-paid officials, characteristic of states with low capacity, are prone to corruption and clientelistic relations with social actors (Evans 1989; Mainwaring 1991). Geddes (1990: 220) indicates that the career success of bureaucrats in patronage networks depends on the fate of their political patrons; thus bureaucrats will make decisions that maximize support for their patrons, e.g., in granting subsidies, licenses, cheap credits.

In building state capacity, essential elements are institutionalization of meritocratic recruitment and promotion in the bureaucracy and careers in the state that have predictable paths and are competitive with careers in the private sector (Evans 1989).<sup>33</sup> These characteristics of careers in the government bureaucracy reduce arbitrariness, corruption, and personnel turnover. Moreover, consistent career ladders allow bureaucrats to acquire the expertise necessary to

---

<sup>32</sup> I take state autonomy to mean independence from particularistic social interests in policy formulation and state capacity the ability to implement whatever policies are chosen despite opposition from social actors. State autonomy and capacity should be conceived as continuous dimensions rather than as dichotomous variables, and they may vary across policy areas. Government economic teams in developing countries may have the autonomy to set the values of some macroeconomic variables (e.g., exchange rates) but be unable to significantly open their economies or control government expenditures. The concept of autonomy is analytically useful only when some specific groups, organizations, or coalitions could control the state, when autonomy is one among possible outcomes (Przeworski 1990).

<sup>33</sup> Material resources for task performance are also important. Politicians can leave agencies with inadequate resources by using funds in their quest for political support; thus capacity also depends on insulating from politicians the process of funding the bureaucracy (Geddes 1990: 219-220). Another crucial factor in effective state intervention is strategic selectivity, i.e., limitation in the scope of state activities in line with its capacity for effective task performance (Evans 1989).

perform effectively and make them perceive that it is in their best interest to act in conformity with bureaucratic rules and goals (Evans 1989).

Some states (e.g., Brazil) while having mostly a patronage-based bureaucracy possess “pockets of efficiency,” organizations with meritocratic recruitment and clear career paths (Evans 1989; Mainwaring 1991). But the approach of increasing state capacity by addition rather than transformation has problems. One is that, as long as clientelism predominates in the bureaucracy, pockets of efficiency depend on the personal protection of individual presidents (Evans 1989). Another problem is a decrease in the organizational coherence of the state; the state becomes “segmented” and policy coordination becomes more difficult (Evans 1989).

Adequate state capacity to execute policies is necessary for economic reforms to succeed. Improvements in the ability to collect taxes, for example, is part of building state capacity.<sup>34</sup> The importance of state capacity for effective implementation of policies may explain Conaghan’s observation of the fear among Bolivian entrepreneurs that the state does not have the capacity to manage reform policies over the long run; businessmen demand that politicians demonstrate their managerial capacity as a condition to increase investments in physical assets.<sup>35</sup>

#### **4.3. Checks and Balances**

The dominance of the executive, common in Latin America, undermines collective rationality in policy formulation and leads to an authoritarian style of policy-making.<sup>36</sup> Heredia states that an executive with a lot of discretionary power, unchecked by the legislature and/or the judiciary, is a source of uncertainty for investments.<sup>37</sup> Moreover, according to her, only an executive with a lot of discretionary power can give rents to capitalists and enable large firms to obtain special treatment vis-à-vis one another.

---

<sup>34</sup> Geddes (1991) argues that in Latin America, patronage-based hiring into the state bureaucracy and outright corruption prevent governments from effectively carrying out economic programs.

<sup>35</sup> Low state capacity may partially explain the frequent failure of stabilization programs to improve economic performance and the weak association between the pursuit of economic reforms and economic growth in Latin America (Dornbusch 1990; Remmer 1986; Williamson 1990).

<sup>36</sup> Yet an exclusionary style is not universal in the region. According to Bartell, the Aylwin government has an excellent reputation for consultation and negotiation with the private sector.

<sup>37</sup> In Brazil, for example, Payne points out that the Sarney government made assurances to the private sector and then ignored the pledges when they proved inconvenient. Jarvis argues that in Argentina landowners could have cut a deal with the state, consumers, and industrialists about exchange rates and taxes that would have provided incentives to greater agricultural production and resulted in a non-zero sum game among social actors. According to Acuña, the landowners did not work out a deal with the state because they had no guarantee that the state would keep its side of the agreement.

The exclusionary style of economic policy-making under strong executives in Latin America is a phenomenon that occurs irrespective of political regime type. Durand states that in the new Peruvian constitution of 1979, the powers of the executive were increased, allowing it to issue decree laws through several legal means. So, it is not surprising that the executive has a tendency to decree policies. According to Durand, Alan García and technocrats in his government did not want to consult or negotiate policies with business organizations, nor were decisions on macroeconomic policies debated in congress. Acuña mentions that the economic team of Martínez de Hoz made economic policies excluding business associations, and the Alfonsín government, with decision-making concentrated in the executive, barred capitalists and workers from the policy-making process during 1983-85. After 1985 when the government asked industrialists and workers to enter into a tripartite concertation, the intention of the government was to seek support for its already-made policies, arousing joint protests from unions and business associations. Bartell and Payne point out that in Brazil the Sarney and Collor governments had an authoritarian style of policy-making, imposing economic measures without previous consultation or negotiation with affected social actors.

The exclusionary style of policy formulation subverts democracy and economic performance. Forcing economic policies against opposition undermines confidence in democratic institutions. Moreover, without consultation and compromise with organized social actors (e.g., about compensatory agreements), governments may fail to obtain sufficient acceptance or support to implement economic reforms. In addition, an authoritarian mode of policy-making fosters uncertainty among businessmen. Payne maintains that capitalists in Brazil are uncertain about future government policies because they have no permanent role in the economic policy process. Bartell reports that in his 1987-88 interviews with entrepreneurs in Brazil, they expressed a willingness to suffer fiscal austerity in order to control inflation if they could participate in government decision-making about the economy.

A more even distribution of power between the executive and the legislature would induce not only a more participatory style of policy-making but also would enhance the collective rationality of policy decisions. Przeworski (1992) maintains that the leverage of immediate, particularistic interests on government policies would be reduced by constitutional provisions forcing the executive to seek formal approval for policies before they are launched and requiring participation of representative institutions in the formulation of policies. According to Mainwaring (1991), in Brazil in the 1980s the ability of the executive to use clientelism was reinforced by the factual exclusion of the legislature from the budgetary process; the executive could use patronage without countervailing pressures or oversight from congress.

The establishment of institutions to promote collective rationality in economic policies under democracy should follow the general logic of institutional development. Although

institutions may be collectively beneficial, their development is best explained as the result of conflicts among actors over the distributive effects of institutions (Knight 1989).<sup>38</sup> Since actors choose among institutions based on their known or presumed effects, a theory capable of explaining institutions presupposes a theory of institutional effects (Moe 1990). Yet institutions are usually imposed by someone and at most accepted by others (Przeworski 1987b; Moe 1990).

## **5. Business Elites and Political Regimes**

Bartell, Payne, and Acuña maintain that capitalists in Chile, Brazil, and Argentina currently support democracy and do not want to return to authoritarian regimes. Yet it is questionable whether capitalists are now democrats. Weffort argues that while business elites in Latin America have abandoned support for authoritarianism and accepted democracy, entrepreneurs do not take the initiative to promote the consolidation of democracy. Payne and Durand assert that business elites are not inherently democratic. Bartell affirms that Chilean capitalists like democracy because it seems to be in their own interests. Heredia claims that pragmatism has been the golden rule of most Mexican capitalists. For Valenzuela, capitalists can become prodemocracy, whether they have democratic values or not, because they feel excluded from decision-making under authoritarian regimes.

### **5.1. Democracy and Capitalism: Limitations of Received Theory**

That capitalists support democracy at all contradicts theoretical convention. A central claim in the study of development in LDCs is that there is a tradeoff between democracy and growth. The arguments for the importance of political regimes in explaining economic performance hinge on the distinct abilities of regimes to restrain popular consumption and income redistribution through expropriation, taxation, and/or wage increases. Under authoritarian regimes, governments supposedly pursue politically unpopular but growth-promoting economic policies because dictatorships have more autonomy from the demands of citizens and interest groups (Haggard and Moon 1990). Democratic governments have to make politically expedient but economically growth-hindering concessions because citizens and workers have power and want to increase their present consumption. They can organize, pressure, vote, and strike, demanding from employers and governments increases in wages, services, and welfare. Under democracy, profits are squeezed and property may be seized (Przeworski 1991). In a democratic

---

<sup>38</sup> Institutions can be outcomes of bargaining among actors in prisoner's dilemma situations (Knight 1989). Institutions can provide political forces with reasonable security that their interests would not be affected in a highly adverse manner in the course of democratic competition. It is this capacity of institutions that makes institutional compromises possible (Przeworski 1987a).

regime, at least some unions succeed in increasing wages at the cost of investment and employment. Democratic governments are more responsive to welfare demands from citizens and therefore tend to spend and tax at higher rates. Higher taxes on corporate and personal income reduce savings and investment. Governments face a tradeoff between distribution and growth; policies that transfer income away from capitalists, whether via higher wages or higher taxes, reduce the rate of investment (Przeworski 1990).

In accounting for the relationship between democracy and the business associations of elite firms in Argentina, Acuña follows to some extent standard assumptions concerning the threats that democracy pose for capitalists. He argues that from the 1940s to 1983 democracy meant the electoral victory of the Peronist Party. Consequently, business associations connected with large capitalists (e.g, the UIA and the SRA) perceived democracy<sup>39</sup> as threatening for three reasons: (1) the profit rates of big businesses were jeopardized; there were increases in wages and in pro-labor legislation; (2) the functioning of market forces was endangered—there was greater state intervention in the economy, resulting in a lesser role for market forces; (3) for some business associations like the UIA, a Peronist victory meant their dissolution; and (4) the influence of unions on government policies increased while the influence of business elites decreased.

Acuña indicates that in Argentina after 1983 there was a transformation in the regime preferences of business associations linked with large capitalists; now these associations prefer democratic rather than authoritarian regimes. He argues that the governments after 1983 did not pursue the policies that had threatened entrepreneurs under previous democracies. The Alfonsín and Menem governments: (1) had a conflictual relationship with unions—Alfonsín sought to weaken the power of unions and attempted to control the level of wages and Menem wanted to displace the CGT leadership considered too defiant of government policies; (2) recognized the hegemony of the UIA as representative of the industrial sector—there was no risk of repression of business associations; (3) capitalists and their organizations were allowed to influence economic policy-making; and (4) the Alfonsín government advocated economic policies historically supported by the associations of big business—opening the economy, reducing the state's role in the economy (e.g., privatization of public enterprises), and decreasing the fiscal deficit by cutting back expenditures—and Menem vigorously pursued neoliberal economic policies.

Conference participants' arguments raise doubts about the coincidence between individual elite firms and their associations in perceiving state intervention in the economy, wage

---

<sup>39</sup> When Peronism was proscribed civilian governments were also considered menacing because such governments tended to strengthen state intervention in the economy and/or attempted to legalize pro-Peronist organizations (the CGT and the CGE).

increases, and prolabor legislation as threats. As previously discussed, there is a troublesome relationship between the policies advocated by business associations and the interests of individual capitalists; business associations tend to be internally fragmented and find it difficult to reach consensus on policies.<sup>40</sup> Particularly problematic is the position on government intervention in the economy. While business associations may claim to prefer free-market principles, it was widely acknowledged by conference participants that each large capitalist wants rents for himself and markets for everyone else. Business elites may want to present a public image of support for economic liberalism, but they have been one of the main opponents of market reforms.<sup>41</sup>

It is also doubtful whether, in countries whose domestic markets are highly protected from international competition, large capitalists fear that wage increases will deteriorate their profit rates. Big firms are likely to have monopolistic or oligopolistic positions in the internal market and, with protection from foreign competitors, are quite able to transfer (sooner or later)<sup>42</sup> wage increases (as well as other costs) to prices. Closed economies serve as protection to capitalists from increases in labor costs; thus businessmen become less concerned with unions than they would be in open economies.

One can pose the question of why when authoritarian regimes come into power they repress labor unions. The standard assumption is that authoritarian regimes suppress unions to lower real wages in order to increase private investment. It is often overlooked that unions play two roles: one economic and another political. Authoritarian regimes may be more interested in subduing unions for political reasons than for economic ones.<sup>43</sup>

In Argentina, as Acuña indicates, there has been an inflationary inertia propelled by the practice among firms of avoiding labor conflicts by granting wage increases and transferring the costs to prices.<sup>44</sup> In Brazil, Bartell and Payne maintain that entrepreneurs were not concerned with wage levels. According to Payne, businessmen even wanted wages to increase in order to

---

<sup>40</sup> Acuña recognizes that there have been conflicting interests inside the UIA, about opening the economy, between industrialists focused on the domestic market and those oriented toward exports. He indicates that during the transition to democracy in Argentina in 1973, a tension arose inside the UIA between large industrial groups linked to the internal market (who benefited from trade protection) and sectors related to manufactured exports.

<sup>41</sup> According to Adolfo Canitrot, most entrepreneurs in Argentina are mortal enemies of free markets (interview on 10/5/89).

<sup>42</sup> In conjectural situations, e.g., price freezes, capitalists may have to postpone price increases.

<sup>43</sup> In Korea, for example, the ability of the Chun Doo-Hwan government to control wages was severely limited by the openness of the economy, and the government role in containing wage growth may have been minor. Yet the government significantly limited strikes and union activity and weakened the structural centralization of industrial unions (Haggard and Moon 1990).

<sup>44</sup> The top industrial firms in Argentina view wages as unimportant in determining investments and have been able to transfer wage increases to prices (López 1991).

stimulate demand. Industrialists believed that low wages reduced consumer demand and therefore industrial sales and profits. Eighty-one percent of the industrialists Payne interviewed in 1987-1988 thought that the minimum wage in Brazil was too low.

Price freezes have not increased the overall importance of wages for profits. Freezes have been rather ephemeral and capitalists have found ways of protecting themselves from the short-term effects of price controls. Acuña states that the experience of wage and price controls in Argentina indicates that such controls work only for short periods at most. He also argues that the price freeze at the outset of the Austral Plan caught capitalists with a level of prices high enough to protect their profit rates. Bartell contends that Brazilian capitalists learned, from the experiences of price freezes during 1987-88, the value of advance preparation to minimize the costs of unannounced freezes, e.g., by increasing published prices enough to ride out a freeze period. In Brazil in 1991, Bartell found that entrepreneurs were much less concerned than they had been during 1987-88 about the effects of price freezes on their profits; moreover, most businessmen considered freezes to be temporary. Payne points to other strategies used by Brazilian capitalists to protect their profits from price controls: decrease in the contents of packages without reducing the price, noncompliance with controls by selling at black market prices, and withdrawal of products from the market until the government allowed price increases.

In contrast to Argentina and Brazil, in Chile, with a domestic market much less protected, capitalists are concerned about the level of wages. Bartell states that in his interviews during 1987-88, Chilean businessmen argued that to be competitive it was necessary to keep wages at levels consistent with productivity and that wage increases could be sustained only by gains in labor productivity; capitalists were worried that workers might ask for more than their share of productivity growth. Valenzuela remarks that when economies become more open to international trade and rely to a greater extent on exports, as in Chile, organized labor becomes more important in determining economic performance because unions are able to disrupt export production. In a similar vein, Acuña indicates that trade liberalization limits the ability of firms to transfer wage increases to prices, and thus leads firms to pressure workers to moderate wage increases; workers, in turn, are likely to restrain their wage demands fearing unemployment in case firms fail to compete with international prices.

Valenzuela affirms that an essential issue for the future of the Chilean economy is whether capitalists incorporate sufficient technology in the production of exports. To sustain concertation with labor, businessmen have to rely on productivity gains and specialization of products. Otherwise, capital-labor cooperation breaks down. Valenzuela presents an ideal scenario of capital-labor relations, arguing that these relations are important for the consolidation of democracy. For him, the more labor relations deviate from this ideal the more detrimental they are for the consolidation of democracy, e.g., because of economic dislocations. The ideal model

of capital-labor relations has the following characteristics: (1) mutually agreeable, relatively stable procedures that labor and business can follow to settle their differences with technical assistance from the state; (2) these mutually agreed procedures function with a minimum degree of politization; and (3) there is a transmission belt (e.g., political parties) between unions and business associations on one hand and the state on the other to create a consensus among politicians in support of capital-labor agreements. Valenzuela maintains that these ideal conditions are unlikely to exist after transitions to democracy, and the short-term strategies of political and social actors may not be directed at constructing these set of institutions.

With respect to labor legislation, Payne's account of the Brazilian case suggests that active opposition to labor laws by business associations does not imply that individual entrepreneurs perceive the prolabor legislation as threatening. According to Payne, FIESP complained that changes in labor legislation under the Sarney government (e.g., reduction in the maximum number of weekly work hours) raised employers's costs by thirty percent.<sup>45</sup> Yet only twenty-one percent of the industrialists Payne interviewed felt threatened by labor during the Sarney government; sixty-four percent expressed satisfaction with labor relations in their firms.<sup>46</sup>

## **5.2. Access to the State and Economic Performance as Determinants of Capitalists' Regime Preferences**

It is unlikely that in Latin America state intervention in the economy, wages, and labor legislation have been decisive in the preferences of business elites about political regimes. The question of what determines capitalists' attraction toward a particular political regime remains open. Two possible explanatory factors are the economic performance record of different regimes and the ability of capitalists to influence government policies.

Bartell and Payne declare that in Brazil, despite the unhappiness of businessmen with the economic performance under the Sarney and Collor governments, entrepreneurs do not want authoritarianism and believe that the economic situation would not have been better had the military remained in control of the government. Capitalists blame the previous military governments for economic mismanagement. Payne maintains that most of her respondents realize that Brazil is now paying the price of the military regime's growth-with-debt strategy. According to Bartell, capitalists criticize past authoritarian governments for failing to pursue economic restructuring, as Pinochet did.

---

<sup>45</sup> According to Payne, in the 1988 Brazilian constitution, the labor movement proposed changes in labor relations that had been already won in individual collective bargaining sessions by the most powerful trade unions, thus demonstrating moderation in their demands.

<sup>46</sup> In Argentina, the largest industrial firms consider labor legislation of little importance for their investment decisions (López 1991).

Bartell argues that capitalists' perception of stability in government economic policies is not inherently connected to a given type of political regime. He points to the lack of confidence of Brazilian capitalists under both the last authoritarian regime and the current democratic one. By contrast, in Chile, after the transition to democracy, government economic policies have been consistent and business confidence has been high. Capitalists feel quite convinced that the liberal economic model is too entrenched for a radical change in the model to occur.<sup>47</sup>

Acuña and Heredia contend that the ability of capitalists to influence government policies is decisive in their regime preferences. According to Acuña, prior to 1983, the UIA had an aversion to democracy because a Peronist electoral victory meant the dissolution of the association. He maintains that part of the explanation for the UIA's change in regime preference is that during the last authoritarian regime the UIA was suppressed, while in the current democratic regime it obtained governmental recognition as the main representative of the industrial sector and was allowed to influence the formulation of government economic policies.<sup>48</sup> Heredia argues that in Mexico large capitalists, in contrast to smaller entrepreneurs, have been politically subordinated to the regime in exchange for informal, individualized access to the economic policy-making bureaucracy. Big business have profited from rents in exchange for abstention from political involvement beyond concerns with economic policies.<sup>49</sup> By contrast, small and mid-sized firms, which were mostly excluded from the informal, personalized networks of influence, have been the most politically active among capitalists.<sup>50</sup> Small and mid-sized businesses have demanded political democracy, seeking to develop open and wide political participation, thus fostering a transition to democracy.

---

<sup>47</sup> In 1991, Bartell reinterviewed those who in 1987-88 had expressed the biggest doubts about the prospects for economic policy after the transition to democracy. Respondents enthusiastically considered long-term investment opportunities in Chile. However, capitalists expressed concern that economic policies could change for the worse after the Aylwin government because politicians might cater to sectarian wishes or because of uncompromising positions among political coalitions over economic policies.

<sup>48</sup> Although Acuña indicates that at times, under the Alfonsín government, business associations were excluded from the process of policy-making.

<sup>49</sup> Heredia mentions that only when the Echeverría government curtailed the privileged, personalistic access of large capitalists to the economic policy-making apparatus did big business engage in political activities that transcended the economic policy realm, e.g., sought closer ties with the opposition party PAN.

<sup>50</sup> With the exception of mid-sized capitalists in Mexico City, Heredia points out. The dependence of these businessmen on state resources have made them, as a rule, behave like large capitalists, i.e., their political involvement is quite limited.

## 6. Conclusions

Political institutions are fundamental in understanding the main themes of the conference. The nature of the state is of paramount importance. A key issue in Latin America is how to reconcile democracy with policies that promote economic growth. Institutional conditions must allow participation by businessmen and other social actors in the policy process and yet prevent special interests and arbitrariness on the part of politicians from subverting the collective rationality of economic policies.

A central cause for low levels of private, fixed investment, even after economic stabilization and the implementation of market-oriented reforms, is policy uncertainty (e.g., doubts that reforms will be sustained). Institutional constraints make it more difficult for governments to change policies even when tempted to do so, e.g., because of time-inconsistency in policies or political pressures. Certain insulated policy-making agencies, e.g., independent central banks, promote policy stability and general interests without being incompatible with democracy; there are arrangements to ameliorate principal-agent conflicts. Also, a more even distribution of power between the executive and the legislature can reduce the leverage of particularistic interests on government policies and limit arbitrariness in policy-making. A third institutional characteristic that strengthens confidence in the policy environment is the capacity of the state to implement policies. Adequate state capacity (e.g., in significantly reducing tax evasion) is necessary for economic reforms to succeed. In addition, greater state capacity reduces corruption and clientelistic relations.

To the extent that the above institutional changes are established the state would move toward solving the prisoner's dilemma situation among capitalists regarding economic restructuring. Opportunities for business elites to obtain privileges from the state and avoid taxes undermine cooperation among entrepreneurs. Each capitalist is tempted to defect due to uncertainty in the success of reforms. This dilemma can explain the observations that individual capitalists oppose market reforms during the transition from stagnation to self-sustained growth and support them once the economic reconstruction succeeds. Businessmen can benefit by the economic growth from successful restructuring and are willing to pay their share of the costs of neoliberal reforms, if they feel confident that the risks of playing the sucker are not too high.

Consolidation of market-oriented reforms and states able to raise and collect taxes on income increase the potentially conflictive relationship between democracy and capitalism in Latin America. Labor costs and taxes would have a greater effect on profits. Yet under democracy, the very possibility of success of economic reforms seems to depend on the establishment of

institutional safeguards (e.g., limits on the arbitrariness of governments) that protect the interests of capitalists.

Conventional propositions about threats to business interests under democracy fail to hold under prereform conditions in Latin America, thus raising doubts about the validity of the tradeoff between democracy and growth. The postulated threat for profits of increases in labor costs does not seem applicable to monopolies in economies highly protected from international competition. Nor is taxation as a mechanism of income redistribution likely to worry capitalists if tax revenues from personal and corporate incomes are low and tax evasion is rampant.

Given the difficulty of business organizations in reaching consensus among their members, expressions of alarm by business associations concerning wage increases, for example, should not be taken as a clear indication that higher wages are menacing for business elites. Associations may adopt policy positions that businessmen find hard to oppose in principle, without necessarily constituting burning issues for their membership.<sup>51</sup> The position on government intervention in the economy is particularly controversial. While business associations advocate free-market principles, individually their members want preferential treatment from the state.

If labor costs, taxes, and state economic intervention have not been critical factors in determining capitalists' preferences about political regimes, then how to explain such choices? One possible explanatory factor posed by conference participants is the economic performance record of regimes. The question that arises is whether there is a generalizable association between economic performance and regime type or whether the regime variable is not very important in explaining economic growth. The views expressed at the conference leaned toward the latter possibility. As Bartell argues, capitalists' perception of stability in government economic policies does not appear to be inherently connected with a given type of political regime.

---

<sup>51</sup> Payne found among the industrialists she interviewed that thirty-one percent believed FIESP played an important role in defending the industrialists' interests, another thirty-one percent considered it somewhat important, and thirty-seven percent thought that it was unimportant.

## References

- Alesina, Alberto and Lawrence H. Summers. 1990. "Central Bank Independence and Macroeconomic Performance: Some Comparative Evidence," manuscript.
- Bernholz, Peter. 1991. "Comments" in *Lessons of Economic Stabilization and Its Aftermath*, Michael Bruno, Stanley Fischer, Elhanan Helpman, Nissan Liviatan, and Leora Meridor, eds. Cambridge, MA: MIT Press.
- Bird, Richard M. 1992. "Tax Reform in Latin America: A Review of Some Recent Experiences," *Latin American Research Review* 27 (1): 7-36.
- Bresser Pereira, Luiz Carlos. 1992. "Crisis and Reforms in Latin America: Washington Consensus or Fiscal Crisis Approach?" in *Economic Reforms in New Democracies*, Luiz Carlos Bresser Pereira, José María Maravall, and Adam Przeworski, eds.
- Bresser Pereira, Luiz Carlos, José María Maravall, and Adam Przeworski. 1992. *Economic Reforms in New Democracies*. New York: Cambridge University Press, forthcoming.
- Cheibub, José Antonio. 1991. "The Determinants of Taxation in Latin America: A Preliminary Analysis," manuscript, University of Chicago.
- Dornbusch, Rudiger. 1990. "Panel Discussion on Latin American Adjustment: The Record and Next Steps" in *Latin American Adjustment: How Much Has Happened?* John Williamson, ed. Washington, D.C.: Institute for International Economics.
- Evans, Peter. 1989. "Predatory, Developmental, and Other Apparatuses: A Comparative Political Economy Perspective on the Third World State," *Sociological Forum* 4 (4): 561-587.
- Geddes, Barbara. 1990. "Building 'State' Autonomy in Brazil, 1930-1964," *Comparative Politics* 22 (2): 217-235.
- \_\_\_\_\_. 1991. "A Game Theoretic Model of Reform in Latin American Democracies," *American Political Science Review* 85 (2): 371-392.
- Gillis, Malcolm. 1989. "Tax Reform: Lessons from Postwar Experience in Developing Nations" in *Tax Reform in Developing Countries*, Malcolm Gillis, ed. Durham, N.C.: Duke University Press.
- Haggard, Stephan and Chung-in Moon. 1990. "Institutions and Economic Policy: Theory and a Korean Case Study," *World Politics* 42 (2): 210-237.
- Haggard, Stephan, Byung-Kook Kim, and Chung-in Moon. 1990. "The Transition to Export-Led Growth in South Korea, 1954-66," World Bank, Policy Research and External Affairs Working Paper No. 546 (November).
- Harberger, Arnold C. 1989. "Lessons of Tax Reform from the Experiences of Uruguay, Indonesia, and Chile" in *Tax Reform In Developing Countries*, Malcolm Gillis, ed. Durham, N.C.: Duke University Press.
- Johnson, Chalmers. 1987. "Political Institutions and Economic Performance: The Government-Business Relationship in Japan, South Korea, and Taiwan" in *The Political Economy of the New Asian Industrialism*, Frederic C. Deyo, ed. Ithaca, N.Y.: Cornell University Press.

- Knight, Jack. 1989. "Institutions and Distribution: A Reconceptualization of the 'New Institutionalism'," manuscript, Washington University.
- López, Juan J. 1991. "Determinants of Private Investment in Argentina," paper presented at the Latin American Studies Association meeting, Washington, D.C.
- Mainwaring, Scott. 1991. "Clientelism, Patrimonialism, and Economic Crisis: Brazil since 1979," paper presented at the Latin American Studies Association meeting, Washington, D.C.
- Moe, Terry M. 1990. "Political Institutions: The Neglected Side of the Story," *Journal of Law, Economics, and Organization* 6: 213-253.
- Morales, Juan Antonio. 1991. "The Transition from Stabilization to Sustained Growth in Bolivia" in *Lessons of Economic Stabilization and Its Aftermath*, Michael Bruno, Stanley Fischer, Elhanan Helpman, Nissan Liviatan, and Leora Meridor, eds. Cambridge, MA: MIT Press.
- Morales, Juan Antonio and Jeffrey D. Sachs. 1989. "Bolivia's Economic Crisis" in *Developing Country Debt and the World Economy*, Jeffrey D. Sachs, ed. Chicago: University of Chicago Press.
- O'Flaherty, Brendan. 1990. "The Care and Handling of Monetary Authorities," *Economics and Politics* 2 (1): 25-44.
- Przeworski, Adam. 1987a. "Democracy as a Contingent Outcome of Conflicts" in *Constitutionalism and Democracy*, Jon Elster and Rune Slagstad, eds. Cambridge: Cambridge University Press.
- \_\_\_\_\_. 1987b. "Capitalism, Democracy, Pacts," manuscript, University of Chicago.
- \_\_\_\_\_. 1990. *The State and the Economy under Capitalism*. Chur, Switzerland: Harwood Academic Publishers.
- \_\_\_\_\_. 1991. "Political Dynamics of Economic Reforms," chapter in *Democracy and the Market*. Cambridge: Cambridge University Press.
- \_\_\_\_\_. 1992. "Economic Reforms in New Democracies: Poland in the Eastern European Perspective" in *Economic Reforms in New Democracies*, Luiz Carlos Bresser Pereira, José María Maravall, and Adam Przeworski, eds. New York: Cambridge University Press, forthcoming.
- Remmer, Karen L. 1986. "The Politics of Economic Stabilization: IMF Standby Programs in Latin America, 1954-1984," *Comparative Politics* 19 (1): 1-24.
- Rodrik, Dani. 1989. "Credibility of Trade Reforms: A Policy Maker's Guide," *The World Economy* 12 (1): 1-16.
- \_\_\_\_\_. 1990. "How Should Structural Adjustment Programs be Designed?" *World Development* 18 (7): 933-947.
- \_\_\_\_\_. 1991. "Policy Uncertainty and Private Investment in Developing Countries," *Journal of Development Economics* 36: 229-242.
- Skocpol, Theda and Kenneth Finegold. 1982. "State Capacity and Economic Intervention in the Early New Deal," *Political Science Quarterly* 97 (2): 255-278.
- Skowronek, Stephen. 1982. *Building a New American State: The Expansion of National Administrative Capacities, 1877-1920*. Cambridge: Cambridge University Press.

Williamson, John. 1990. "The Progress of Policy Reform in Latin America" in *Latin American Adjustment: How Much Has Happened?* John Williamson, ed. Washington, D.C.: Institute for International Economics.

Woolley, John T. 1977. "Monetary Policy Instrumentation and the Relationship of Central Banks and Governments," *The Annals of The American Academy of Political and Social Science* 434 (November): 151-173.

\_\_\_\_\_. 1984. *Monetary Politics: The Federal Reserve and the Politics of Monetary Policy*. Cambridge: Cambridge University Press.

## Speakers

*Raymond Vernon*, Harvard University  
*Jaime Ros*, Kellogg Institute  
*Lee Tavis*, Kellogg Institute  
*Lynne Wozniak*, Kellogg Institute

## Presenters

### **The International Environment of the 1990s: Implications for Latin America**

Paper by *Raymond Vernon*, Harvard

### **Intereses Empresarios, Dictadura y Democracia en la Argentina Actual**

Paper by *Carlos Acuña*, University of Chicago and CEDES, Argentina

### **Brazilian Business Elites and the Transition to Democracy**

Paper by *Leigh A. Payne*, Yale University

### **Fragmentos do Novo? Brasil: Empresariado e Crise no Limiar dos 90**

Paper by *Sebastião Velasco e Cruz*, CEBRAP, Brazil

### **Business Perceptions and the Transition to Democracy in Chile**

Paper by *Ernest Bartell, c.s.c.*, Kellogg Institute

### **Hot Money and Hegemony: Andean Capitalists in the 1980s**

Paper by *Catherine M. Conaghan*, Queen's University at Kingston, Canada

### **Businessmen and Democracy in Mexico**

Paper by *Blanca Heredia*, Columbia University and ITAM, Mexico

### **Business Peak Associations in Latin America: The Case of Peru**

Paper by *Francisco Durand*, Kellogg Institute and P. Universidad Católica, Peru

## Discussants

*Lovell Jarvis*, University of California—Davis  
*Robert Kaufman*, Rutgers University  
*Samuel Valenzuela*, Kellogg Institute  
*Francisco Weffort*, Kellogg Institute and CEDEC, Brazil

## Rapporteur

Juan López, University of Chicago