9

Political Obstacles to Economic Reform

Political and ideological obstacles have been crucial in Brazil's—as in any other country's—ability to adopt sound, consistent economic reforms. Brazil's democratization in the 1980s was based on solid economic and social reality. Contrary to the conventional interpretation, it represented the victory of civil society rather than a concession of the military regime. But it failed to address some of the basic ideologies and political practices that are typical of middle-income, industrialized, yet underdeveloped countries—such as, on one hand, economic populism, developmentalism, anachronistic nationalism, political clientelism, and unrealistic worker demands and, on the other, conservatism, monetarist orthodoxy, neoliberalism, and the inability of a shortsighted business elite to recognize and defend the national interest.

In Chapter 8 I analyzed the political crisis in Latin America, particularly the crisis of the left, because the basic cause behind that crisis was the fiscal crisis of the state. In this chapter I examine the political obstacles to economic reforms, but I interpret them in a broader sense, relating them to the ideological debate between the left and the right. In the developed countries political obstacles are identified with nationalist and populist policies, which are usually identified with the left but are also germane to the opportunistic right. In addition to the nationalist and populist practices, it is also important to detect another type of political or ideological obstacle: the adoption of inefficient, if not ineffective, economic policies as a result of the adoption of dogmatic monetarism and neoliberalism.[1]

In the early 1980s the economic crisis was a major player in the downfall of the authoritarian regime. Later, stubbornly resisting a solution, the economic crisis became a threat to democratic regimes. Recession and high inflation are destabilizing factors for any political regime, whether authoritarian or democratic. In the 1990s, when most Latin American political regimes are democratic, it is democracy that is being jeopardized by the economic crisis, as we saw in Peru and Guatemala. Despite an economic crisis provoked by extreme orthodox measures, Venezuela was able to preserve democracy in the early 1990s, but the entire region suffered anxiety.

According to conventional wisdom, the causes of the economic crisis in

Brazil and, more broadly, in Latin America are political. The political obstacles I examine in this chapter clearly buttress this view. But there are also purely economic causes for the crisis. Economic reforms and stabilization policies are often inefficient and excessively costly, if not outright incompetent. And market failures—not only the classical ones, related to monopoly power and externalities, but also new ones, such as the inertial character of inflation that the market is unable to tackle—are not political problems but strictly economic ones.

In Brazil today capitalism and democracy have been consolidated. There is little doubt about the dominance of a modern, industrial, capitalist mode of production, as well as of the political and ideological hegemony of the business class. But from 1987 to 1994 new doubts arose—doubts that had not previously existed—about the country's prospects for economic growth. Capitalism rather than self-sustained growth seemed assured in Brazil.

At one time I believed that, when a country had completed its industrial and capitalist revolution, self-sustained growth would automatically follow as a consequence of the demands imposed by the accumulation of capital and the incorporation of technological progress. Following the Brazilian economic crisis, which kept income per capita stagnant for almost fifteen years, I am no longer so sure. One is forced to concede that Brazil's continued economic development depends on the adoption of a number of short- and long-run economic policies (adjustments and reforms), which involves making decisions and taking initiatives.

Democracy in Brazil is more solidly entrenched in the economic and social system than is usually acknowledged, however. First, modern industrial capitalism is able to appropriate an economic surplus through the market, thus dispensing with the direct force needed in precapitalist and mercantilist societies. Also, the bourgeoisie, or business class, does not feel threatened by the left. Further, the military and, more broadly, the authoritarians do not have alternative projects for Brazil (they are as perplexed as the bourgeoisie over how to solve the economic and political crises). Finally, the United States no longer resorts to "big stick" tactics (such as coups d'état, military interventions, and the like) as part of its strategy to consolidate capitalism in Latin America, and it is sincerely committed to consolidating democracy in the region.

But it is not possible to say that democracy has been consolidated. Guillermo O'Donnell (1988:85) emphasized that if a military coup is not likely, the "slow death" of democracy—that is, the continued loss of the effectiveness and credibility of political institutions as a result of the government's failure to meet or resolve socioeconomic problems—is another possibility.

The failure of governments to address these problems directly cannot be attributed solely to country-specific limitations or to the sheer size of economic obstacles. Real economic obstacles do exist. It is not by chance that Latin America has stagnated for ten years, ever since the foreign debt crisis manifested itself. However, the failure of Brazil's government to lead the country out of this crisis is clearly related to political practices and beliefs that are not conducive to the adoption of bold, coherent, and firm economic policies.

What are some of these political beliefs and practices? They are discussed below, where they are classified according to their political origin as obstacles originating from the opportunistic right, the moderate left, or the ideological right. One political practice is common to both the opportunistic right and the moderate left: economic populism, the distinguishing economic policy of opportunists and a basic political disease in Brazil.

Because *populism* has several meanings, the adjective *economic* is appended to distinguish it from other connotations. Populism usually carries a different meaning in Latin America than it has elsewhere, being tied to the practices of political leaders who are able to establish a direct relationship with the people without the intermediation of political parties. It is also related to the class coalitions or "populist pacts" that offered political support to import substitution industrialization. Such pacts were based on some kind of alliance among industrialists, workers, and the new, bureaucratic middle class.[2] In contrast, economic populism refers to a more general, although related, political practice: fiscal laxity, usually tied to naive distributivism.

The first economist to write on economic populism was probably Adolfo Canitrot (1975). Guillermo O'Donnell, although he is a political scientist, has also written admirably on the subject (1977). Carlos Díaz-Alejandro (1979) has addressed economic populism, specifically in connection with the "populist cycle."[3] Populist policies usually precede and are also the cause of economic crises, which then require painful orthodox stabilization programs.

There are two types of economic populism: (1) populism of the left, often characterized by naive redistribution of income and the "refusal-to-adjust" attitude; and (2) populism of the right, a phenomenon very close to developmentalism. In any case it is a kind of fiscal laxity, defined by a tendency to acquiesce to most of the demands of workers and businesspeople. This course is invariably embraced by opportunistic and clientelist politicians.

Populist economic policies lead to increases in the public deficit and to an imbalance in the current accounts (balance of payments). Some of the more common populist practices include wage increases for public-sector workers and officials; expenditure increases by the state; increased consumption and investment subsidies; overvaluation of the local currency, provoking increases in real wages and artificial prosperity; and credit subsidies offered by the official banks. These concessions offer something to everyone—public officials, businesspeople, and workers.

The outcome of these practices is the populist cycle. It begins with the government adopting a combination of the following policies: overvaluation of the exchange rate, which reduces inflation, increases wages and consumption, promotes imports, and restrains exports; direct increases in public-sector salaries; increased public expenditure, leading to a higher budget deficit; artificially low domestic interest rates; and artificially low prices and tariffs for state-owned enterprises. Thus the first phase of the cycle is characterized by a high rate of consumption and investment, an accelerated growth rate, and a decline in the rate of inflation as a result of the overvaluation of the exchange rate and the reduction of real public prices.

However, this stage proves to be a short-lived paradise because these practices generate distortions in the economy. Disequilibrium appears in the balance of payments as imports increase and exports decline. The budget deficit soars. Eventually, as the threat of a balance-of-payments crisis becomes evident, the currency is devalued. Domestic prices increase, setting in motion an often dramatic inflationary spiral. This stage of the cycle often leads to a severe crisis, sometimes accompanied by, at the minimum, a change of ministers if not a coup d'état, and it inevitably ends with a radical change in economic policy.

The expansionist policies of 1979–1980 (probably the worst mistake in the history of economic policy in Brazil) and of the Cruzado Plan (an excellent plan and an opportunity lost to incompetent management) are typical examples of recent populist episodes in Brazil. The 1979–1980 experience was conducted by conservative economists under the military regime; the Cruzado Plan was designed by competent economists soon after the democratic transition took place, but its implementation was populist.

It is important to distinguish the opportunistic right from the ideological right. Of course, opportunists exist all across the political spectrum, from right to left. An opportunist is, by definition, a politician who lacks firm ideological convictions. Opportunists command the right rather than the left only because capitalism is dominant in Brazil. In a capitalist country political opportunists, whatever their ostensible political persuasion (even if they purport to be left or center-left), will tend to be conservative because their fundamental interests require that all possible and imaginable concessions be made to the rich and the powerful.

To be developmentalist is to have economic growth as the major objective, subordinating stabilization and income distribution. This was a dominant ideology and political practice in Latin America from the 1930s to the 1980s.

Clientelism is a political practice halfway between populism and sheer corruption. Populism, clientelism, and corruption imply the use of public funds: in the case of populism public funds are used impersonally to assure the goodwill of those groups and communities that benefit from public expenditure; in the case of corruption public funds are privately appropriated. Clientelism also involves the use of public funds, but indirectly. Politicians engaged in clientelist practices do not steal but use state resources to enhance their personal careers. The Brazilian term for this practice is *fisiológismo*.

The fisiológismo politician is, by definition, an opportunist, one who treats politics like a business in which political influence is the means of exchange. He is *fisiológico* because he puts his own personal and material interests above the ideas and moral principles he has pledged to serve and that are supposed to orient political action.

These opportunistic practices are deeply embedded in Brazil's political system and are both a symptom and a consequence of the country's low level of citizenship. Lack of information, a poor political education, and mistrust of popular candidates are characteristic of the average Brazilian voter. Thus, in the words of Wanderley Reis (1988:24), "given the characteristics of the Brazilian electorate, it is not realistic to expect that the stabilization of the democratic game takes place around parties that are defined in ideological terms; it is more likely that the process of formation of the political parties will continue to be based on traditional clientelism with an electoral appeal of populist tones."

Different, but producing similar results, are the ideologies and political practices of the left. The golden years of the left were the 1930s to the 1950s. Since the 1960s the left has faced increasing problems as the communist or statist model of society experienced hard times in the former Soviet Union, and the state-led import substitution strategy became disfunctional in Latin America. This strategy was appropriate for the 1950s, but by the early 1960s it became apparent—as I pointed out at the time—that domestic and international conditions had changed sufficiently to require a new analysis of the economy and a new strategy for economic growth.[4]

In the 1970s and early 1980s the moderate left severely criticized the orthodox economic policies put forward by the authoritarian regime. Sometimes this criticism was justified, but often it represented merely old-fashioned populist and nationalist slogans. When the transition to democracy was completed in 1985 the new democratic government (the Sarney-PMDB administration) proved to be the outcome of a populist and nationalist political coalition of the opportunistic right and the old left. The old left clung to its typical ideologies and policies, one of them being old-fashioned nationalism.

In the 1940s and 1950s the left espoused the proposition that "imperialists," or foreign interests (including multinational enterprises), had allied themselves with the interests of domestic agro-mercantilist capital to prevent or oppose industrialization. However, in the mid-1950s those same multinationals proceeded to make large investments in manufacturing, thus altering the situation and acting in contradiction to this proposition (Bresser Pereira 1963; Cardoso and Faletto 1969).[5] If this analysis had once been true, it was no longer so. Nevertheless, some old-fashioned nationalists still think in terms of the 1950s. As we will see in Chapter 16, these anachronistic nationalists fail to understand that to be nationalist today requires having a clear notion, in each case, of what the national interest really is rather than adopting a nondiscriminating attitude toward multinational corporations or, more broadly, imperialists.[6]

In the mid-1960s the authoritarian regime opted for an export-led strategy of development. This strategy benefited the country, although in the short run it produced the perverse effect of making sustained rates of internal demand compatible with a concentration of income. From the beginning, the moderate left opposed this strategy and adopted a domestic market orientation, failing to acknowledge that not only had the import substitution growth model exhausted its virtues by the early 1960s, but the alternative growth model—based on highly capital-intensive import substitution projects—was even more disposed to concentrate income over the long run than the model based on the export of labor-intensive manufactured goods.

During the 1970s it was common for spokespersons for the left to criticize Korea and Taiwan as mere "export platforms" for the multinationals, whereas Roberto Campos, one of Brazil's leading right-wing intellectuals, viewed these same countries as liberal societies. Today we know that both were wrong. The extraordinary development of these countries was based on an export-led strategy in which the state played a decisive, and the multinationals a minor, role. Korea and Taiwan were neither export platforms nor liberal economies. Furthermore, their development strategy proved consistent with a much more even distribution of income than that existing in Brazil. One cause of this better income distribution was the agrarian reform undertaken by these countries following World War II; another factor was the export-led growth strategy, which was necessarily based on labor-intensive industries.

A resistance to adjustment—which I am calling the refusal-to-adjust attitude—emerged as a consequence of an entrenched commitment to developmentalism (in this case also a form of economic populism) that characterized Latin American economists of the left, myself included, during the 1950s.[7] We severely criticized the adjustment of the 1960s. The fact that stabilization programs were usually based on reducing wages rather than on fiscal adjustment was indeed good reason for our criticism. However, the left predicated its criticism almost entirely on a "no to recession" slogan, and, in so doing, slopped over into economic populism. The left's only economic argument was a spurious adoption of Keynesian ideas favoring budget deficits and a demand-led development strategy.

In 1979, when some form of economic adjustment became absolutely necessary, the developmental, populist economic policy adopted by the right-wing military regime was—not surprisingly—supported by economists of the structuralist moderate left. When adjustment finally came in 1981, the left wrongly adopted the view that adjustment was unnecessary when, in fact, there was no other alternative. At the time it was impossible, as well as undesirable, to maintain large deficits in both trade and current accounts. The only serious innovative criticism of the orthodox adjustment policies to emanate from the moderate left came from those economists who developed the theory of inertial inflation.

A redistributive wage policy is typical of economic populism everywhere. Income concentration is recognizably a major problem in Brazil, which has one of the most uneven and unjust income patterns in the world. However, this fact alone does not legitimate unrealistic wage distributivism. A politically progressive economic policy in Brazil will necessarily have to fight this uneven distribution, which is uneven not only among wages and profits but also among wages and salaries. And when the policy proposes wage increases, it has to be careful not to increase real wages more than productivity.

Whenever such a plan was tried in the past, profits were threatened and the inflation rate accelerated. This is unavoidable. Wage policy should be limited to three objectives: (1) to protect real wages from inflation; (2) to assure that increases in productivity are transferred to the workers; and (3) to reduce wage and salary differences through a gradual increase in the minimum wage. Presumably it would be possible to increase wages more than productivity without affecting profits if either the difference were paid for by the rentiers or there were an increase in state efficiency that would allow for a tax reduction, which would be equivalent to the real wage increase. A third alternative is the prevalence of capital-saving technical progress, expressed in the increase of the output-capital relation. However, these alternatives are difficult to accomplish.

Efficient means of redistributing income include export-led industrialization, industrial policy oriented to the production of wage goods, agrarian reform, progressive tax reform, and orientation of public expenditures to the poor. Yet these ideas are rarely acceptable to the populist left. An oft-cited slogan is "wage increases are not a cause of inflation." This was true for a long period during the authoritarian regime because real wages either lagged behind productivity or were reduced in absolute terms. Nevertheless, a different picture began to emerge by the end of the 1970s. In 1984, following the defeat of the authoritarian regime, unrealistic demands from workers increased sharply. The salaried middle class, which was employed in the public sector, became particularly active in this area. As the distributive conflict deepened, the budget deficit increased, prompting the rate of inflation to accelerate. Real wage gains tended to be short-lived. Increased inflation soon wiped out any real gains, and the only lasting result was a higher rate of inflation.

In conclusion, some ideas and political practices of the moderate left, which are very much related to economic populism—old-fashioned nationalism, domestic market orientation, the refusal-to-adjust attitude, and wage distributivism—are not consistent with rational, coherent economic policies. Further, the political practices of the opportunistic right—developmentalism and clientelism—are not related to economic populism. They are political obstacles to stabilization and growth.

The ideological right is thus also an originator of irrational economic policy. This category includes the monetarist economists and neoliberal ideologues who adopt a militant theoretical view opposing virtually every kind of state intervention in the economy and who support only purely orthodox economic policies to stabilize the Brazilian economy. An increasing fraction of Brazil's business elite falls into this category. Its leaders may not be opportunists, but they are ideologically conservative. In developing countries conservatism means ideological subordination to the dominant value and belief system existing in the central countries, over and above typical conservative characteristics such as placing order above social justice and resisting change.

The ideological right is truly convinced that its views on economic policy are intrinsically rational, based as they are on both the logic of capitalism and their own logic. They rely on their own rationality to confront the irrationality of both the populist left and the opportunistic politicians. They control the means of communication, so they are usually able to convey their ideas to the general public, thus reinforcing their ideological hegemony.

Unfortunately, not only are the ideas of the ideological right less rational than they purport to be, but they also raise a major obstacle to the adoption of a consistent economic policy in Brazil, especially when the time calls for bold, far-reaching economic decisions. What are these views and political practices of the ideological right?

Social conservatism is an obvious problem in a country where income levels are so sharply skewed, with so much going to so few. In Brazil the tax burden is relatively low, and the tax system very regressive. Thus progressive tax reform is an obvious tool for reducing the public deficit and distributing income more equitably. The ideological right systematically opposes tax reforms that increase the tax burden in any way or that make it more progressive. On the one hand, it refuses to recognize that the tax burden in Brazil is indeed low, whereas on the other hand it exhibits a sincere concern for the lack of incentives to savings and investment. In reality, tax renunciation and tax incentives to business enterprises are a major source of Brazil's budget deficits because they serve to reduce the effective tax burden. Most of these "tax breaks" or incentives lost their raisons d'être long ago. Still, the ideological right tends to ignore the problem, and it fights for lower taxes.

Although the ideological right professes its concern regarding income concentration in Brazil, it does nothing to help solve the problem. A social pact, which is essential to control wages and curb inflation, would involve concessions to the workers in terms of social reform. However, as a rule the ideological right opposes any effort at social reforms. This behavior serves its interests as a class and is also based on the firm conviction that social order takes priority over social justice: order must never be endangered in the name of justice.

Monetarism began as a conservative counteraction to Keynesianism. Monetarism originally developed in the Friedman version and subsequently evolved through the theory of rational expectations of the "new classics" (Sargent; Lucas). It is based on a fundamental contradiction: it is a macroeconomic theory, necessarily oriented toward economic policy, that professes radical abstinence of state intervention. However, this abstinence is not actually practiced. The stabilization policies monetarism recommends tend to be both active and aggressive. When and if the economy stabilizes, however, the stability achieved is always so precarious that continued intervention by the state is required to maintain it.

At the present time, monetarism, in its rational expectations variety, is the economic religion of the developed capitalist countries. As a result of the ideological subjection of the elites in the peripheral countries to those at the center, an almost unrestricted monetarism has been adopted by the ideological right in a peripheral country like Brazil. Two examples will suffice. Although in Brazil inflation has structural origins and an inertial character, making the money supply endogenous or passive, the right believes inflation can be controlled simply by the application of monetary and fiscal policies.[8] In an underdeveloped economy, such as that of Brazil, economic imbalances run very deep, but, based on monetarism, the ideological right believes market forces alone will be able to solve all problems.

The successive failures of this approach to solve the economic crises in Argentina, Brazil, and Chile contributed to a certain discrediting of monetarism in the early 1980s. However, after the failure of the heterodox Austral and Cruzado plans, monetarism recovered some of its lost prestige. Suddenly, as a result of a very interesting maneuver by the ideological right, conventional stabilization policies (based on fiscal and monetary policies, over which a relative consensus exists among good economists) were equated with orthodox monetarism and were opposed to Keynesian and structuralist theories, which were now thought to be heterodox. Through this rhetorical strategy, the ideological right was able to identify heterodoxy with economic populism. Whereas the theory of inertial inflation was being incorporated by mainstream economics in the developed countries,[9] and an increasing number of economists came to admit the advantage of combining conventional or orthodox (fiscal and monetary) with heterodox policies (policies that neutralize inertia), the monetarist neoliberal right in Brazil still insisted on shunning heterodox strategies and advocated only conventional policies to control inflation. When a stabilization program—the Real Plan—finally controlled inflation in 1994, monetarists refused to acknowledge its essentially heterodox character, although its authors were neostructuralist economists, and the URV was an ingenious strategy to neutralize the staggered contracts, that is, inertia.

In fact, economic policies that are specifically monetarist in nature are often inadequate or plainly irrational. It is obvious that a dogmatic rejection of state intervention, including macroeconomic regulation and an income policy, prevents a monetarist policy from dealing with the real problems of the Brazilian economy. Monetarism also tends to overlook certain characteristics specific to that economy. Inertial inflation may be a universal phenomenon, but the degree of formal and informal indexation in Brazil makes it specific to the Brazilian situation, creating a particularly Brazilian problem requiring measures especially tailored to its nature.

Neoliberalism is the complement of monetarism. The Washington consensus was one of its manifestations in Latin America. The theme has been well discussed in this book. The ideological right knows (or should know) that the state played a pivotal role in Brazil's industrialization, although it persists in ignoring that fact. In the 1980s, after becoming heavily indebted to foreign interests, the Brazilian state suffered a severe fiscal crisis that stymied economic growth. For those who subscribe to unvarnished neoliberalism, this indicates that the state should totally abstain from playing any economic role and be reduced to the condition of a minimum state. Although this may indeed be a sensible alternative, the primary task is to solve the fiscal crisis: the goal is not to expel the state from the economy but to enable it to assume new roles in promoting welfare and technological progress.

A natural aspiration of Brazil's business community is to further integrate Brazil into the international economy. If this were achieved, Brazilian capitalism would be less vulnerable, both economically and ideologically. I will not argue about these objectives because they are fairly consistent. If a clear economic and ideological hegemony of the bourgeoisie exists (as I believe it does), and if Brazilian capitalism is well established, this desire for greater integration with the developed world is rather natural. The problem is how to accomplish this integration. Brazilian conservatives frequently believe this can be achieved by "being international." However, right-wing internationalism often takes the form of an uncritical subordination to the interests of the developed countries. This attitude—which I am calling subordinate internationalism—is a phenomenon of everyday life in Brazil. It is a consequence of the economic and cultural domination the developed world exerts over the periphery. In the case of the ideological right, this subordination takes on a militancy as inconsistent with the national interests as is the old nationalism of the left.

Another name for subordinate internationalism is the confidence-building strategy, which business elites in Latin America often advocate. The idea is to follow all recommendations or suggestions made by Washington (the administration) and New York (the financial system) in an attempt to build confidence. Mexico has consistently followed this strategy since August 1989, when it irresponsibly signed the term sheet of a debt agreement with commercial banks just six months after the Brady Plan was announced. Debt reduction was insignificant, but, as it was then argued, it "built confidence." From that time until the December 1994 crash, the Salinas administration was engaged in building confidence at the expense of the national interest and of macroeconomic fundamentals.

Today Latin American conservatives see the Chilean experience as an example of sound, successful economic policy. They are basically correct. Chile was the exception to the rule. After making major mistakes and being immersed in a severe crisis in 1982, Chile's authoritarian administration was able to overcome fiscal crisis and resume growth. Since democratization in 1990 the new democratic government has kept the macroeconomic fundamentals under control while giving stronger emphasis to social policies. Neither the authoritarian administration nor the democratic one privatized the copper mines, the source of a large proportion of the strongly positive public savings that prevail in Chile.

Chile's per capita income at the end of 1988, however, was still below that of 1980; 1987 wages were 6 percent below the 1980 level (Piedra 1988). Additionally, both poverty and concentration of income had increased. The mixed (positive and negative) results achieved by the Chilean economy were the product of orthodox policies and an authoritarian regime. John Sheahan (1986:161) noted that economic policies typical of the authoritarian regimes in Latin America include reduced price controls, lower protection, serious efforts to limit budget deficits, strict control of wages, and conditions highly favorable to foreign investors. Sheahan mixes regime rhetoric with the actions taken. In actual fact, Latin American authoritarian regimes do not necessarily adopt orthodox or neoliberal economic policies. Their rhetoric is invariably opposed to state intervention and protectionism. Although they may preach fiscal austerity, they hardly practice what they preach. The excessive external indebtedness and the corresponding public deficits of the 1970s were all incurred by authoritarian regimes in Brazil, Argentina, Chile, and Peru. Sheahan is on firmer ground, however, when he worries about the ability of Latin America's nonauthoritarian governments to survive the increase in populist policies, a trend that has only intensified since redemocratization: wage increases above the growth of per capita income; increases in public expenditures; and a trend toward excessive protectionism.

In summary, the combination of populist, developmental, and orthodox political practices and ideologies constitutes a major obstacle to the adoption of consistent, rational economic policies in Brazil and, more broadly, in Latin America. These practices led to fiscal crises, balance-of-payments problems, and inflation; the ideologies resulted in incompetent macroeconomic management, recurrent recession, and concentration of income.