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PUBLIC POLICY MAKING IN ARGENTINA

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Abstract

Public policies in Argentina are deficient in several dimensions. However, the welfare effects of policies depend not only on their "content" (i.e., whether tariffs are high or low, whether there is redistribution towards some sectors or towards others), but also on several "properties" such as: 1) if they are stable and predictable, 2) whether they respond to changes in the underlying economic conditions, 3) whether there is a good coordination among several policymaking units, 4) whether appropriate investments in policymaking capabilities are undertaken or, 5) whether the State has the capacity to enforce its legislated policies, etc. We argue that those characteristics of public policies are the outcome of a non-cooperative behavior in the policymaking game. Such non-cooperative behavior, in turn, is the product of institutional instability and institutional rules that negatively affect the expectations and horizons of the actors involved in the policy process.

Congress is a relatively weak policymaking arena, populated by amateur legislators. Political power lies in the hand of provincial governors, who are more interested in obtaining some advantages in a perverse federal fiscal game than in the quality of national policies. Possible intertemporal enforcement technologies, such as delegation to a qualified civil service, or arbitration by an independent judiciary, are also absent. All of this leaves an under-institutionalized national policy making arena populated by transient political actors who tend to behave myopically, and who do not build long-term policy agreements.

1. Introduction

Argentina in the 1990's was involved in what was described in international circles as a wide and profound process of market-oriented economic reforms. With its ambitious program of macroeconomic stabilization, liberalization, privatization and deregulation, Argentina became the poster child of the Washington establishment. After decades of inward-looking policies, stagnation, and fiscal crises that lead to hyperinflation in 1989, Argentina seemed to have found its way. The measures undertaken during the 1990's followed pretty much the so-called Washington consensus, with one "twist", the Convertibility Plan, a currency-board system that tied the peso to the dollar.

After some spectacular macroeconomic performance for a good part of the 1990's (with GDP growth switching from negative in the 1980s to an increase of over 50% in the 1991-1997 period, and inflation coming down from 23104% in 1990 to around cero in 1997), the Argentine economy entered into a long recession in 1998, exploding into one of the deepest economic crises in modern history in December of 2001.

It seems clear now that many things went wrong in the Argentine "reform" experience of the 1990's. The causes of this, at least partial, failure are multiple. There were weaknesses in the economic recipes being implemented; there were idiosyncrasies in the trajectory of the Argentine economy and the dollarized contractual system around the Convertibility experiment; but also, there were some maintained weaknesses in the Argentine policymaking process that prevented the development of more robust mechanisms of intertemporal credibility. We have written more extensively on those issues, in the context of the international debate on market-oriented reforms (Tommasi, 2003), and on the Convertibility regime itself (Galiani, Heymann and Tommasi, 2002). This paper focuses on the third theme, attempting to characterize some "structural" aspects of policymaking and hence of policies in Argentina, and exploring its institutional determinants.

Policies, to be effective in achieving sustained changes in economic and social behavior, do require certain "properties" such as stability, credibility, flexibility, and coherence. These "properties" are to some extent independent of the specific substance of the policies in question -- such as whether protection for some economic sectors is high or low, whether the Value Added Tax is 15% or 21%, or whether the regulation of a particular utility sector is based on price cap or on rate of return.

The responses of economic agents to economic policies depend on their expectations about their future evolution. Policy stability as well as cross-policy coherence facilitate the development of positive policy expectations, thus promoting long-term risk-taking and investment. Reforms that are not politically consistent over time, may only promote short-term actions attempting to arbitrage away rents generated by those reforms, leading to open political conflict and the self-fulfilling reversal of the reform. This issue has been the focus of the substantial literature in economics on the "time consistency" or "credibility" of policies. Calvo (1989) provides an insightful rendering, particularly attuned to the issues emphasized here, in which the expectation of future reversals of a trade reform lead to an

economic dynamics opposite from the one expected from a credible trade liberalization. On the empirical end, Acuña (1991) discusses the reluctance of Argentine businessmen to respond to export-promotion policies, due to the uncertainty about their durability; and Hopenhayn and Neumeyer (2003) present evidence of the negative effects of trade-policy uncertainty on the macroeconomic performance of Argentina.

The privatization of utilities is another case in point. The long-term welfare effects of the "privatization" of a given utility sector will depend on many aspects of the regulatory framework put in place, and on the adequacy of that regulatory framework to the broader institutional capabilities of the country (Levy and Spiller, 1996). Similarly, the privatization of pensions will achieve desired objectives only if it can change the incentives and constraints of private actors and of the public sector in the right direction. (We devote the next section to elaborate this example.)

So, policies will be effective only if they have certain properties. We argue that whether policies have those properties or not, will depend on the process by which policies are decided and implemented. The functioning of this policymaking process, in turn, depends on the incentives and constraints that the rules of the political game ("political institutions") impose on key political actors.

We argue in the paper that policies in Argentina lack many desirable properties (sections 2 and 3); and that such is the case because the policymaking game leads to non-cooperative behavior (section 4). The roots of non-cooperative policymaking, in turn, are the product of institutional instability and of other structural incentives in the political system, which we explore in sections 5 to 9.

2. Privatization of the Pension System in Argentina

We begin with a brief example from one salient component of the reform epic in Argentina, the "privatization" of the pension system in 1993. Our choice of the example of pensions is not accidental. Pension policy is an issue with characteristics that make it particularly prone for political opportunism, an aspect that we will emphasize in the theoretical approach that we present below. Pension policy can be characterized, at its core, as supporting a "transaction" in which workers sacrifice current income in exchange for income to be received many years in the future. Using the language of "transaction cost economics," this is a transaction that is very likely to require fairly complex institutional support. (Imagine that an individual you don't know approaches you in the street and asks you to give to him 10% of your monthly income for the rest of your life, and promises to give you in return some monthly payment from the day you retire until you die. It is quite unlikely that you would enter into such an agreement without substantial safeguards).[1]

[1] Of course a pension system has other elements, such as intra-generational redistribution, insurance from the people who die early to the people who live longer, etc. But clearly, the intertemporal "investment" described in the text is at its core.

The Argentine pension system inherited by the early 1990's was a public "pay as you go" (PAYG) one. The system had been chronically under funded for many decades, due to unrealistic parameters, low compliance, and the tendency of successive governments to manipulate those funds politically (Rofman, 2002, Demarco, 2003, Kay, 2003); and hence was failing to provide adequate coverage to the elderly.

The diagnostics of the early 1990's pointed to the weaknesses of PAYG systems as creating poor incentives and constraints for individuals and for the political system. In the words of the labor minister who oversaw Chile's privatization of the pension system (the leading model of the times), "[t]he PAYG social security system ...destroys, at the individual level, the essential link between effort and reward – in other words, between personal responsibilities and personal rights. Whenever that happens on a massive scale and for a long period of time, the result is disaster." (Piñera 1999, cited in Kay 2003). Also, it was expected, on the basis of the Chilean experience, that privatization of the pension system would prevent political manipulation of pension funds (see for instance Mesa-Lago's 1996 description of the position of international organizations on this issue.) It was believed that a structural reform of the system was necessary to overcome those "institutional weaknesses" leading to very low public confidence in the system (Demarco, 2003).

After intense debates, a reform was undertaken in late 1993, including some changes in the parameters (increasing employee contribution rates, increasing the minimum retirement age, etc), and, crucially, in the institutional arrangements of the system.[2] The system was organized in two "pillars." One would grant a flat benefit of around 28% of average wage to those satisfying some age and years-of-contribution requirements. The second pillar offered a choice between staying in the public PAYG system, or switching to a private system of funded individual accounts, where individuals accumulate personal contributions (net of some costs). These funds are administered by pension-fund managing companies ("AFJPs"). Most workers joined the private funded scheme, either by choice (2.3 million workers), or by default assignment (those not exercising an explicit choice, 2.8 million workers, were randomly assigned to one of the AFJPs).[3] With some minor caveats, we can summarize the reform, as most observers do, as a privatization of the pension system.

Yet, privatization of the pension system does not eliminate the role of the state. The state still has an important role to play in running the first pillar, in protecting citizens by regulating the private pension funds, in enforcing compliance with the contributions to the system, etc. The reform does not eliminate political risk either (Kay, 2003b). The Argentine reform case painfully illustrates that the performance of the system after privatization was no real improvement over the pre-existing situation, because the

[2] For details on the alternatives considered and the political debates, see Demarco (2003). For a detailed description of the new system, see Rofman (2000).

[3] Informal evidence (Ronconi and Tommasi, 2003) suggests that the decision to switch to the private system was in some cases not based on higher expected returns, but on the cajoling of male workers by the beautiful miniskirted ladies which constituted the majority of the AFJP's sale force. The sales effort developed by the new AFJPs was very large. In a few months they created a sale force of almost 30,000 (0.25% of the Argentine labor force), and spent more than half a billion dollars in marketing and sales commissions in the first few months (Rofman, 2002).

Argentine state failed to deliver in its positive regulatory role, and also failed to refrain its grabbing hand from tinkering with people's savings once again.

A good indicator of state capacity in this case is the extent to which the state is able to compel workers to contribute to mandatory social insurance programs (Kay, 2003). As stated above, it was expected that the shift from a system in which there was no relation between individual contributions and the pensions received, to a system of individual accounts, should very much sharpen the incentives to contribute, greatly increasing compliance with the system. It turns out that such an expectation was not fulfilled in the Argentine case. The number of people contributing to the system did actually go down from the inception of the system in 1994 to 2001 (and continued to fall in 2002).[4] Such a decline, and even the low level of compliance, do not necessarily mean that the reform itself did not improve compliance, since compliance depends on the level of formal employment, which declined throughout the period; and it is also true that most Latin American countries have difficulties enforcing compliance. Yet, there is wide variation in compliance rates among Latin American countries; as Figure 1 (from Kay, 2003) indicates, Argentina is the worst enforcer of the 7 countries considered there. Also, compliance has fallen even among those pension funds affiliates that stay in the system. Countries with similar rates of informality have had varying success in enforcing performance. Figure 2 shows that the percentage of formal employees contributing to the pension funds is far lower in Argentina than in Chile, Colombia, Mexico, and Uruguay.

<Figure 1>
<Figure 2>

Argentina also ranks poorly in a potential indicator of the quality of regulation of the private pension funds, commission fees as percentage of wages. Argentina, Peru and El Salvador have commission fees above 2% of wages, unlike Bolivia, Colombia, Chile, Mexico, and Uruguay (Kay, 2003).

Unfortunately, the Argentine state fails not only in its positive role, but also fails to restrain itself from expropriation. From the beginning of the system, through regulation, AFJPs had a heavy reliance on government-issued paper in their portfolio. In developed economies, pension funds are also required to hold government bonds, because they are considered safe assets. Government bonds are not safe assets in the Argentine case, though. Not only the fraction of pension funds invested in government bonds was high to begin with, but also through a series of negotiations and unilateral measures, the government forced AFJPs in the 2001 crisis to increase their exposure to government risk. The details are well depicted in the following quote from Kay (2003b):

"As discussed earlier, some analysts have suggested that privatization creates political insulation, which lessens the chances that social security will be subject to short-term budgetary considerations (Diamond and Valdés-Prieto 1994 p. 307). This was clearly not the case in Argentina, where the government intervened in pension funds in a series of actions prior to the default and devaluation of January 2002 in an attempt to reverse the

[4] See Colina et al (2002).

deteriorating economic and financial climate. The government first cut mandatory contributions to pension funds in an effort to raise salaries and stimulate the economy. It then cut pension benefits by 13 percent and halted court-ordered pension adjustments in an effort to improve deteriorating fiscal accounts. Next, the government pressured pension funds to accept a debt swap in an attempt to address its short and medium term financing needs. When these measures proved to be insufficient, and the market had no alternative sources of financing, the government expropriated pension funds by forcibly converting deposits to treasury notes.

After the default and devaluation in January 2002, the value of pension fund investments plummeted as government dollar-dominated debt was converted to pesos, and the government defaulted on its debt payments."

This episode indicates that the "privatization" of the pension system didn't do much to modify some key negative aspects of the operation of the system.[5] It highlights some more "permanent" characteristics of policies and of the policymaking process in Argentina, often present independently of the "content" (in this case "public PAYG" vs. "individual accounts administered by private pension funds") of the policy in question.[6]

3. Public Policies in Argentina

This brief rendering of the Argentine pension reform experience highlights some more general characteristics of policies and of policymaking. The Argentine polity seems particularly unable to enforce complex intertemporal policies, to regulate the private sector, or to fulfill its commitments. Also, often this inability transpires not (as emphasized in the "political economy of reform" literature) in difficulties in instrumenting policy changes, but in the lightness with which policies are changed. Figure 3 presents an indicator of policy volatility, the coefficient of variation over time, from 1970 to 1999, of the "index of economic freedom." This index, constructed by the Fraser Institute, measures how market-friendly are the policies of each country at each point in time. The coefficient of variation of that index over time could be thought of as a (rough) measure of the volatility of economic policy. Argentina ranks as the 7th most volatile case in a sample of 106 countries. Furthermore, the coefficient of variation cannot disentangle between cases where some important changes in one direction have taken place (Russia, Chile), and cases where the policy stance swings back and forth. As indicated in Figure 4, Argentina is a case of frequent shifts. Argentina has shifted from being one of the most market-friendly, to being the least after the then Soviet Union, and then back up during the reforms of the 1990's. Unfortunately, we do not have the data up to 2003, but it is certain that Argentina's index of market-orientation has started to swing back down.

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[5] There are several other important dimensions in which the reform did not improve the situation, and it might have worsened it – for instance on the fiscal side, and in terms of actual and expected future coverage of the elderly. These problems have put the system again on the table for further reforms. Given the current change in ideological winds, those reforms are likely to increase the role of public "pillars."

[6] The pension system in Argentina, before and after "The Reform" should be characterized as: "Pay-as-you-go, unless you can evade, and (most likely) you'll get little in return."

<Figure 3>
<Figure 4>

Argentina shows policy instability not only at this very aggregate level, but also in terms of more micro-level policy. For instance, Spiller and Tommasi (2003b) and CEDI (2000) document the volatility of anti-poverty programs in the 1990s, which show large changes without changes in congressional mandates. Each time a new Minister or Secretary takes office, a common event in Argentina, they feel compelled to discontinue pre-existing programs and to create their own, often with a substantial amount of tinkering with the geographical distribution of those funds.[7]

This volatility of policies, shortens the horizons of the economic and social actors that are supposed to respond to them, and hence reduces the effectiveness of policies. For instance, panel (a) of Figure 5 shows that the volatility of economic policies is perceived by international businessmen operating in Argentina as costly for the operation of their business.[8] The rest of Figure 3.3 presents other cross-national evidence from surveys of international businesses operating in the different countries (from Global Competitiveness Report, 2001); in each case, a higher bar indicates better policy characteristics. Panels (b) and (c) indicate that the Argentine state is a weak enforcer of its policies, not only in the domain of social security contributions, but also in other areas, such as minimum wages, or taxation. Panel (d) shows that Argentine public spending is not perceived as very useful in international comparison. Panel (e) shows that (in spite of the fact that Argentina still ranks well in indicators of literacy and school achievement) Argentine public schools rank relatively low in international comparison. Panel (f) shows that public officials are not perceived as being too competent, in comparison with the private sector. The one indicator where Argentina seemed to perform reasonably well was in terms of "expected exchange rate volatility," in panel (g). Unfortunately, that survey was taken in April of 2001, 8 month before the exchange rate blew off the ceiling, at the breakup of the (10 years long) convertibility regime. This suggests that in Argentina, policy credibility, stability, and predictability, can be built, if at all, on the basis of very rigid mechanisms, which may eventually become very costly under certain states of the world.[9] This attempt to curtail excessive volatility by imposing rigid mechanisms has manifestations in other policy areas. One salient example is the case of the federal fiscal arrangement, analyzed in Tommasi (2002) and in Eaton (this volume). The compromise assumed in 2000 by the national government to transfer fixed amounts of funds to the provinces, turned out to be too costly during the crisis of 2001, making it very difficult for Argentina to adjust its fiscal stance under very adverse economic circumstances, further driving the spiral of economic

[7] The average duration of department heads at the National Secretariat for Social Development is less than a year. Furthermore, the agency has been switching status back and forth from secretary, to undersecretary, to ministry. The position has been occupied alternatively by highly qualified technocrats, by high profile politicians, by the spouse of one President, and by the sister of another one.
[8] This is highly consistent with Acuña's (1991) account of the failure of export promotion policies in Argentina.
[9] See Galiani, Heymann and Tommasi (2003) for further analysis of the origins and dynamics of the convertibility regime.

hardship and credibility losses which ended in the social, economic, and political explosion of December 2001.[10]

In sum, Argentine public policies can be characterized as quite volatile, oftentimes rigid, not well coordinated among different policymakers (ministries, provinces), poorly enforced, and showing lack of investment in policymaking capacities.[11]

4. The Determinants of Policymaking Capabilities

The evidence of the previous section summarizes some characteristics of policies in Argentina that seem to be rather permanent, applying to the pre-reform times of more state intervention, as well as to the recent reform period. This suggests that perhaps, rather than focusing, as the "reform movement" in Latin America has, on the content of the policies, one needs to focus on the deeper determinants of these policy characteristics, the process of making policy. We attempt to do that in the rest of the paper.

In order to study the policy making process and its determinants, we follow an approach that draws from transaction cost economics, and its applications to politics, as well as from some perspectives in positive political theory attempting to explain the effects of political institutions on policymaking processes and on the characteristics of policies.[12] We view public policies as the outcome of multiple actions (taking place across time) by several actors in the policy process. In our language, policies are the outcome of intertemporal political transactions. Good public policies require cooperation of several actors over time; that is, they require political environments that foster cooperation and that facilitate the enforcement of political bargains. Political institutions, broadly defined, constitute the rules of the policymaking game. A particular country, given its political institutions and its historical trajectory, could be in a more or less cooperative environment.

Non-cooperative policymaking environments will foster political opportunism, in which temporarily powerful actors will implement policies that benefit them in the sort run. In an attempt to curtail opportunistic policymaking behavior, rigid mechanisms can be utilized; such mechanisms might also impede an easy adaptation to changes in underlying economic or social conditions states. Non-cooperative policymaking environments also lead to poor coordination across policymaking units (subnational governments, ministries, etc); and to under-investment in policymaking capabilities –as those actors undertaking investments

[10] Tommasi (2002) provides more details about the dynamic build up of the very rigid and very inefficient federal fiscal system in Argentina.

[11] See Spiller and Tommasi (2003) and Spiller, Stein and Tommasi (2003) for a game theoretic model that can account for both excess policy volatility (in response to political shocks) and excess policy rigidity (in responding to economic shocks). Spiller and Tommasi (2003b) show more evidence, based on policy case studies, on the properties described in the text.

[12] The approach is developed in more detail in Spiller and Tommasi (2003, and 2003b), and in Spiller, Stein, and Tommasi (2003). The pioneers in applying transaction cost reasoning to public policymaking are North (1990), Dixit (1996), Weingast and Marshall (1988), Moe (1990) and (1990b), and Epstein and O'Halloran (1999). Tsebelis (2002) and the collection in Haggard and McCubbins (2001) present complementary approaches on the effects of political institutions on policy. See also the collection in Sabatier (1999) for additional lenses on the policy process.

fear opportunistic expropriation of the returns to that investment. Multiple examples of the latter could be found in the federal fiscal game in Argentina, where provincial governments under-invest in their tax collection capabilities, since better local tax collection is likely to be penalized at the next round of intergovernmental redistribution (Tommasi, 2002).

Even beyond the example of provincial taxation, the reader will recognize that the characterization of policies in non-cooperative policymaking environments resembles closely the description of Argentine policies in the previous section. Hence, the next step is to understand why the workings of political institutions in Argentina are such that they lead to non-cooperative policy making. To do that, we take a very brief "theoretical" detour before we come back to the Argentine case.

We can use the theory of repeated games as a heuristic device to think about the determinants of (in this case) political cooperation. Political cooperation leading to effective public policies is more likely if the number of players is small; if those actors have strong intertemporal linkages, leading to long horizons; if policy and political moves are widely observable; if there are good enforcement technologies (such as an independent judiciary), and good delegation technologies (such as a strong and independent bureaucracy); if the short-term payoffs from deviating from cooperation are not too large; and if the key political exchanges take place in arenas where the previous properties hold.

To explain the characteristics of public policies in specific political systems, then, we need to look for the observable counterparts of the listing above. These observable counterparts are the workings of political institutions and their determinants in specific countries / time periods. Identifying these variables is a difficult task. It requires immersion in the "micro-detail" of politics (and policies) in each case. The type of variables to analyze include: key political actors, determinants of their payoffs, institutional veto points, variables determining who holds those institutional veto points at each point in time (related to parameters of stochastic description of the political process), horizons of key political actors and their determinants, institutional features (constitution, budget procedures, informal practices) that facilitate unchecked moves by some actors, independence and strength of Supreme Court or equivalent, characteristics of the bureaucracy. Beyond the more formal institutional characteristics just mentioned, there will be historical factors as well as cultural, social or economic configurations that foster or hinder cooperative political behavior and its intertemporal enforcement.

We are now in a position to come back to the case of Argentina and to sketch how several features of the configuration and workings of political institutions in Argentina are not conducive to effective political compromise and cooperation.

First, the constitutional structure (Presidential, Bicameral and Federal) implies that there are a relatively large number of institutional players in the policymaking game, placing strong demands in terms of the capacity to make agreements. Second, the intertemporal linkages among political actors, including those derived from electoral rules, as well as the history of political instability, lead to myopic behavior, not conducive to self-enforcement of cooperative agreements either. Third, alternative enforcement mechanisms, whether by judicial means or bureaucratic delegation, are weak. Fourth, the executive has substantial

leeway for undertaking unilateral actions that can undo legislative or other agreements. Fifth, key political exchanges do not take place in the Legislature, but in other less institutionalized arenas. Finally, the payoffs from non-cooperative spot actions are quite high (for instance, in the federal fiscal game).

A crucial component for self-enforcement of intertemporal political and policy deals is missing in Argentina. On the one hand, the polity has systematically witnessed transgressions by key political actors of the basic norms of democratic process. Between 1930 and 1983 twelve presidents, both *de jure* and *de facto*, were taken out of office by force. Furthermore, from 1930 until December of 1999 there was not a single orderly transfer of government from one president to another.[13] This history of disregard for basic norms of democratic life, in turn, left an imprint in the logic of operation of political and institutional actors. For instance, it is not surprising that the history of playing the federal fiscal game (provincial and national governments) has been marked by extremely myopic behavior (Iaryczower, Saiegh and Tommasi, 1999). Similarly, the tendency of military governments and civilian regimes to remove (or attempt to remove) Supreme Court Justices, has weakened the judiciary over the last half of the twentieth century, affecting its current functioning and reputation,[14] and in turn transforming the Court into an institution that has had limited ability to restrain the excesses of the presidents of the day. Also, the high rotation of the presidency translated itself into even higher levels of rotation in the upper echelons of the bureaucracy, also impeding the development of norms of cooperation across agencies, and impeding the development of a strong civil service, a problem that still haunts the Argentine polity.[15]

But the myopia of key political actors, and the weakening of the arenas for intertemporal political compromise, has also a more stable institutional component. This component is the result of electoral mechanisms that work against having a Congress populated by long-term legislators, weakening what could otherwise be a crucial arena for the discussion and enforcement of political bargains. Electoral rules in Argentina transfer power away from national legislators and national parties towards provincial party bosses, which leads to transient and "amateur" legislators, given the incentive of the party bosses (and of the legislators) to rotate them. The lack of legislators' incentives to undertake legislative activities, including supervising the bureaucracy or budgetary implementation, has granted the executive ample discretion concerning budgetary design and implementation.[16] This discretion, given the heavy financial dependence of the provinces on the center, counterbalances the power given by electoral rules to provincial Governors. Thus, the national government depends on the provincial political elites for its legislative agenda, while these depend on the center for financial viability. As we discuss in Section 6, a

[13] And that transfer of power from Menem to De La Rúa has been the only one since, in spite of the fact that Argentina has had 6 presidents so far from 2000 to 2003.
[14] See Iaryczower et al (2002), Miller (1997), and section 8 here.
[15] There are several other instances (all the way to the present) of manipulation of basic institutions and norms for short-term political benefit. They include tinkering with electoral processes to satisfy current partisan needs, the strategic use of social violence, etc.
[16] The capacity for unilateral executive action can also be understood as the result of proactive legislative powers of the President, weak judicial review, and the history of democratic instability. See below.

perverse criss-crossing of national and provincial policies and politics further limits the ability to reach cooperative policy outcomes.

Alternative institutional mechanisms for the enforcement of political agreements are also defective. A professional bureaucracy, well supervised by Congress, could be a channel for enforcement of intertemporal political agreements. Argentina does not have such a bureaucracy. This is the result, in part, of past political instability, but also of the current incentives of the key political players. A shortsighted Congress has left the bureaucracy without a long-term principal, and hence hard to motivate. Political appointees, the so-called "parallel bureaucracy," have then been used to fill the gap. These appointees, in turn, rotate very frequently and do not develop norms of cooperation across departments, contributing to the fragmentation and lack of coordination of public policies. The Supreme Court has not been a good enforcer either, as it has tended to be "too aligned" with the executive.[17]

The interaction of the capacity for unilateral moves, history, and the (endogenous) lack of institutionalization of Congress and of legislators' careers has moved the center of the political scene away from the national legislature and into other arenas. Political bargains take place in executive quarters, in meetings of the president with governors, or occasionally in meetings of national political party leaders. These informal arenas have not been structured for the institutional enforcement of bargains.

In what follows we bring into focus some of the components of the general picture we just sketched.

5. Congress is Not Too Important in Policymaking

Legislators in Argentina have high rotation and low tenure rates. Part of that high rotation has come from the high political instability of Argentina in the second half of the twentieth century. High rotation, however, is not all the result of political instability. Twenty years after the return to democratic rule in 1983, high rotation still characterizes the Argentine Congress. Since 1983, turnover rates have always exceeded 40%, with very low reelection rates -- only 20% of incumbents return to their seats. Of all the deputies elected from 1983 to 2001, 85% served only one term, 11% two terms, and only 4% three or more terms.[18] These figures are similar to those of countries (like Costa Rica) with term limits (Jones et al, 2001).

Looking at the determinants of high rotation one discovers that it is not the result of voters' rejection. Most legislators simply do not show up in the provincial party list for the next election. Those that do, have a two-thirds probability of being reelected. That conditional reelection rate is lower than the 94% of the U.S. but comparable to that of many other countries that have, nonetheless, much higher unconditional reelection rates. See Table 1

[17] See Section 8.
[18] Furthermore, Jones et al (2001) show that the probability of reelection, *declines* with tenure.

<Table 1>

The short tenure of Argentine legislators stems from the fact that those in charge of compiling the list of candidates (the "selectorate") do not reappoint them. Given that electoral districts coincide with provinces, and given the mechanisms of internal candidate selection, this *selectorate* is constituted by provincial party elites.

The members of the Argentine Chamber of Deputies (currently 257) are elected from 24 multi-member districts, the 23 provinces and the federal capital, for four-year terms. One-half of the chamber is renewed every two years, with every district renewing one-half of its legislators. Deputies are elected from closed party lists. A major difference with the U.S. is that (intra-party and general) electoral rules have made provincial party leaders powerful actors in national politics.

De Luca et al (2002) explore in detail the mechanisms of candidate selection, and show that the provincial-level party leaders are the key players in the nomination process, with the national party leadership and rank-and-file members playing a decidedly secondary role. Jones et al (2001) analyze the incentives of local party leaders and of legislators, and show that, in equilibrium, nobody has the incentives to build a long-term career in Congress.[19]

All of this limits the incentives of legislators to invest in policymaking capacities. Legislators have little incentive to specialize, to acquire policy expertise, and to develop strong congressional institutions. As a consequence, they do not provide strong supervision of the executive or the bureaucracy. Jones et al (2002) provide evidence on the patterns of legislative committee organization and membership: legislators tend to belong to a large number of committees, and they last less than a legislative period in each committee, even in important ones. This is a sharp contrast with the picture depicted in the gargantuan literature on the U.S. Congress, where legislators are selected by constituencies, have long careers, specialize in powerful committees, and acquire substantial policy expertise.[20]

We already discussed the fact that national legislators owe allegiance to provincial party leaders. This dependence is strengthened when the leadership in question coincides with provincial government. This is so because provincial executives have both more currencies with which to reward and punish their representatives in the national congress, and more need to occasionally pull those legislative strings to obtain benefits for the province (see next section). The strength of provincial governors was reinforced by electoral outcomes. During 1983-2001, the legislative contingent of the President's party has oscillated between 45.1% and 51.6% (Molinelli, Palanza and Sin 1999, Table 2.121, and Calvo and Murillo, this volume, Table 1), automatically granting any block of unified votes from a few provinces veto power over the President's agenda.

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[19] These *amateur* legislators are nonetheless *professional* politicians who after serving a term in Congress are moved to other political activities in the party, the province, or in the federal government. Jones et al (2001) show that of the 108 deputies in the 1991-95 cohort, 83% were as of mid-1998 in other positions strongly influenced by party ties. Congress is just a temporary stop in their political career.

[20] Jones et al (2002) provide references on each of these points. Diermeier et al (2002) provide an extremely rich characterization of the career paths and characteristics of U.S. legislators.

Governors, then, are extremely important players even for *national* politics and policies. A crucial question is, then, what do governors care about? The next section considers the arena in which the main concern of provincial governors, the distribution of tax revenues, is determined.

6. The Federal Game

In Argentina, national and subnational politics and policies are intertwined to a much larger (and convoluted) extent than in other federal polities. The main "linkages" are: (1) from subnational to national political arena through the electoral mechanisms described in the previous section; and (2) from "central" decision-making to provincial politics and policies through the channel of federal fiscal arrangements.

Provinces undertake a large fraction of total spending, yet a small fraction of taxation. Provincial spending amounts to 50% of total consolidated public sector spending. This figure goes up to close to 70% if we take out the pension system and focus on "more discretionary" spending. Furthermore, the type of spending in the hands of provincial governments tends to be the most politically sexy, such as public employment and social programs, much closer to territorially-based constituencies. Yet, provinces finance, on average, only 35% of that spending with own revenues. The rest of their spending is financed out of a common pool of resources, the "sharing of federal taxes" (*Coparticipación Federal de Impuestos*). In a large number of small provinces the amount coming from this common pool constitutes more than 80% of their funding. Local politicians get, then, a large share of the political benefit of spending, and a small fraction of the political cost of taxation.[21]

This is one of the reasons why many professional politicians are more interested in making a career through appointments in the government (or even in the party) at the provincial level than in the national Congress. On the other side, the powerful provincial brokers, the governors, depend heavily on the allocation of "central" monies to their provinces to run both their political, as well as their policy, businesses. That is, they need central money to deliver political goodies, as well as to provide general public goods in the province. There are several channels for the funneling of central funds to the provinces, the main ones being the geographical allocation of the national budget, and the Tax Sharing Agreement *Coparticipación*.

The game in which these allocations are determined is the source of many political and policy distortions, both at the national and provincial level. It even affects the quality of democracy at the local level. The Argentine voter at the provincial level, tends to reward those politicians that are more effective at extracting resources from the center, not

[21] The details of these mechanisms, their geography, and the comparative advantages of different parties in reaching different constituencies are addressed in Calvo and Murillo (in this volume.)

necessarily the most competent or honest administrators.[22] Given the political mechanisms by which funds are allocated, it also adds uncertainty into provincial public finances, because it is not easy to project future allocations.

The history and evolution of the Tax Sharing Agreement (narrated in detail in Tommasi, 2002) is fraught with examples of opportunistic manipulation, occasionally curtailed by fairly rigid and inefficient mechanisms. Unilateral, bilateral and coalitional opportunism (by the national government, by a province or set of provinces that turns out to be pivotal for an important vote in Congress, etc) has been common in the allocation of central monies to the provinces. The national executive has had substantial discretion in the geographical allocation of the federal budget. In an attempt to prevent adverse changes in the future, political actors have tended to increase the rigidity of the FTSA, reducing the capacity to adjust fiscal policy to changed economic circumstances. An example of such rigidities has been the earmarking of taxes for specific programs with clear regional distributional effects. This led to a rigid and convoluted federal tax collection and tax distribution, which has been christened the "Argentine Fiscal Labyrinth."

Recent attempts at simplifying that labyrinth, also reflecting the inability to strike efficient intertemporal agreements, led to the 1999 and 2000 "Fiscal Pacts" between the National and provincial governments. As explained in Eaton (in this volume) and Tommasi (2002), the rigid commitment to minimum revenue guarantees from the center to the provinces agreed at that point turned out to be a very costly straightjacket for the De La Rúa government during the build up of the crisis in 2001, and the lack of cooperation from the provinces has been credited as the proximate cause of the country's move to default (Eaton, p. xx).[23]

The last episode of the Argentine federal fiscal soap opera, leading to the largest default in modern world economic history, was a clear manifestation of one of the central points in our argument. Provincial governors, whom we have established are crucial players in national politics and policymaking, have only secondary interest in national public goods (such as macroeconomic stability), in the quality of national policies, and in investing in those institutions (a professional Congress, a stronger civil service) which might improve that quality.

7. A Bureaucracy Without a Long-Term Principal

One possible mechanism for enforcement of intertemporal political agreements is delegation to a relatively independent, yet accountable, bureaucracy. Argentina, however, has not developed such a bureaucracy. Rauch and Evans (1999) rank Argentina in the bottom five among 35 developing countries in terms of bureaucratic quality. The lack of

[22] Jones, Sanguinetti and Tommasi (2002) show that voters in Argentina, unlike those in the U.S., reward provincial spending at gubernatorial elections. They term that effect "voters as fiscal liberals," by contrast to the expression "voters as fiscal conservatives," used by Peltzman (1992) to describe the U.S. case.
[23] Tommasi (2002) also describes how the build up of a very dangerous aggregate fiscal position in the late 1990's was related to national-provincial political gaming.

any long-term principal, can be seen, following Spiller and Urbiztondo (1994), as a key factor behind the lack of a professional bureaucracy. Executives, in almost all Presidential systems are transient; in Argentina Congress is not a long-term principal either, as legislators rotate rapidly and are not particularly motivated to control the Administration.[24]

The bureaucracy, as a consequence, faces weak long-term incentives, facilitating shirking and requiring intrusive administrative controls to avoid corruption, further reducing its ability to generate timely and effective policies. Each new executive, unable to motivate (or to fire) the permanent bureaucracy, has nominated large numbers of political appointees, often under much more flexible labor agreements, creating a parallel, transient, bureaucracy. The parallel bureaucracy undertakes the same actions as the normal bureaucracy is designed to, but unable (or unwilling) to, undertake. The rotation at the ministerial and secretarial levels implies rotation at the "parallel bureaucracy" as well, limiting the extent of institutional knowledge, and the development of cooperation across ministries and secretariats, deepening the heterogeneity in policy quality, and the lack of policy coherence.

The parallel bureaucracy is widespread, but difficult to measure. Bambaci, Spiller and Tommasi (2001) report information for one agency. In that case, the parallel bureaucracy represents well above 50% of total employment, and a larger fraction of the wage bill, as those tend to be better-paid (but shorter-lived) employees than permanent civil servants at similar levels.[25]

8. Weak Judicial Enforcement

The workings of judicial institutions have direct implications for the feasibility of private contracting, of contracting among private and public actors, and of arrangements among political agents. We focus here on the latter, emphasizing the role of the Supreme Court as potential enforcer of constitutional and legislative contracts. The Argentine Supreme Court has not been a very strong and impartial enforcer of political agreements in the last several decades. Weak judicial enforcement has been more the result of politics than lack of doctrine. Indeed, Iaryczower et al (2002) show that a strategic behavioral model similar to the one used to explain the U.S. Court can explain quite well the behavior of Argentina's Supreme Court Justices. Furthermore, the fragmentation of the Argentine polity would suggest that the Argentine Court should be a rather strong and independent Court. History, however, has implied that some key explanatory variables of the behavior of Argentine Supreme Court Justices took very different values than in the U.S. case, leading to a substantially diminished role (Iaryczower et al, 2002).

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[24] As Krehbiel (1991) argues, legislators tend to undersupply that kind of public good, an effect that is magnified in Argentina since legislators only attend to provincial party leaders' interests who, in turn, are not particularly interested in the quality of national policymaking.

[25] Although in principle, national parties could develop a cadre of potential bureaucrats, the fragmented nature of national parties into provincial parties makes such cadre development ineffective as compared to the practice of a parallel bureaucracy composed of individuals highly aligned to the secretary or minister of the moment. A current example of this fragmentation is the composition of the top echelons of the administration of President Kirchner, crowded with people from his province of origin.

<Table 2>

In particular, since the mid-1940s, Argentina's Supreme Court Justices have had very short tenures. Indeed, it has been one of the Supreme Courts with the shortest average tenure in the world. As Table 2 indicates, from 1960 until the mid 1990s, the average Argentine justice lasted around four years in his post. This low average tenure of Argentine justices puts the country in the bottom league, alongside countries not associated with long-term stability and the predominance of the rule of law. Iaryczower et al (2002) show that this is a feature of the last 50 years. After WWI, the Argentine Court was on its way to become not too distinct from its US counterpart. Since its creation in 1863 until the mid 1920s, the average tenure of the Argentine Court systematically increased, reaching the same level as that in the US. The subsequent political instability drastically reduced the tenure of justices on the bench. The impeachment brought during the first Perón administration against the sitting Court members had a lasting impact. Since then, the norm of not manipulating Court membership was lost. Several military and civilian Presidents who alternated in power got to appoint their own Courts. In 1991, the first time since 1946 in which a President might have faced an opposition Court, President Menem expanded the court from five to nine members granting him a "working" judicial majority. Indeed, the control over the court was such that since the mid-forties' until the administration of de la Rúa inaugurated in 1999, no President faced a Court with a majority appointed by a political adversary.

Courts whose tenure is very short will naturally tend to be aligned with the sitting government, and hence will not be too strong in their role of judicial review. During a large part of the twentieth Century -- due mostly to *de facto* governments, but also to the political alignment during the interim democratic spells – executives had often a high level of political alignment in the legislature. This alignment is also a variable leading to a diminished tendency for the Court to challenge the government (Iaryczower et al, 2002).[26]

The dynamics of a Court without much clout and regard are fairly perverse and self-reinforcing, to the point that several recent presidential candidates have promised to remove (some or all of) the sitting Justices, and current president, Nestor Kirchner is succeeding at doing that.

9. The Executive in a Non-Cooperative Policymaking Equilibrium

The previous sections have characterized a policy-making environment in which institutions (such as Congress) especially designed to facilitate political debate, bargaining, and the intertemporal enforcement of those agreements, are quite weak; in which key political players (the Governors) do not care much about the qualities of national policies;

[26] Helmke (this volume) make the perceptive point that Justices start tilting their rulings *against* the executive as the sitting executive become less likely to stay much longer, what she calls "strategic defection." But both, strategic accommodation and strategic defection reflect some deviation from impartial rulings only on the merits of the case, something that we conjecture will be more likely if the Supreme Court was stronger. See also Miller (1997.)

in which complementary enforcement mechanisms such as a strong Judiciary or a strong Bureaucracy are not available either. These factors are reinforced by, and in turn reinforce, the capacity and tendency of the Executive to act unilaterally.

The sources behind the executive's ability to make unchecked moves and undo previous (say, legislative) agreements are various, including the fact that the Supreme Court has tended to be politically aligned to the President, the lack of a strong and independent bureaucracy, and the "general equilibrium" result that Congress has not built strong technical capacities. The budget process is a manifestation of this feature. Congress' inability to monitor and control the budget has given the administration substantial budgetary discretion. Since the beginning of the twentieth century, Congress has often not approved in time the budget sent by the executive, which in practice meant that the administration functioned independently of Congress. In the high inflation years the executive did often not bother to submit a budget. Even in the low inflation period of the 1990s, while ex ante budgets started being approved in time, ex post control has not been exercised – the ex post budget verification process ("*Cuenta de Inversión*") has not been dealt with promptly enough to be an operational instrument for Congress to verify the fulfillment of the budget "contract" by the executive.[27] Current budget practice has tended to overestimate revenues, and the (non-legislative) ex post adjustment mechanism has given substantial leeway to the Secretary of the Treasury to allocate the scarce funds. Secretaries of the Treasury have exercised this prerogative according to a mix of their own whims and pressure from line Ministries, occasionally arbitrated by the president.[28]

The unilateral power of the executive has also been based on some constitutional capacities and practices amounting to proactive legislative powers of the president. These practices have evolved partly out of the political instability that has tended to focus in the executive processes that in a more stable environment would have drifted towards the legislature. They are also the result of some explicit constitutional capacities and constitutional lacunae (and their interpretation by a weak Supreme Court), including the fact that the President is endowed with the capacity to "regulate" the laws from Congress, and the practice of issuing Decrees of Urgency and Necessity (Carey and Shugart, 1998, Molinelli et al, 1999).

Some authors, such as Magar (2001) and Jones (2001), have argued against the oversimplified "hyperpresidential" views of Argentine politics, indicating that policies in Argentina are not the outcome of an all powerful executive interacting with a totally irrelevant Congress. We have no quarrel with that assertion. As is clear in the account of the budget process provided by Jones (2001) the distribution of seats in Congress does matter (for instance for the geographical distribution of the budget), but it is remarkable that these "deals" are not cut in Congress, but in Executive chambers. Further evidence of

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[27] Jones (2001) indicates that almost all of the substantial budget activity happens in executive quarters and not in Congress: "…relatively little modification of the budget proposed by the executive branch occurs at any time during the treatment of the budget bill in Congress." (p. 161). Furthermore, Jones indicates that while ministries and other entities submit detailed disaggregated budget plans to the (executive) National Budget Office, the draft finally sent to Congress contains expenditure only at a very macro level (p. 160).

[28] Based on a personal interview in 1999 with the then Secretary of the Treasury, Pablo Guidotti, as well as on a recent presentation by Jorge Baldrich (2003), who was Secretary of the Treasury in 2001.

extra-legislative exchanges with the executive is presented in Murillo (2001), with regards to many of the market-oriented measures of the 1990's.[29]

10. Quo vadimus?

We come back now to some of the issues raised at the beginning of this paper. In the 1990's Argentina undertook a rather surprising sharp turn towards market-oriented policies. According to the logic of policymaking in Argentina described in this paper, that turn was not the outcome of a reasoned public debate in which most relevant political actors debated whether such was the most desirable course of action. It was a decision of the executive of the day, approved in Congress through "votes" mostly purchased through the federal fiscal system and related mechanisms.[30]

The implementation of these reforms carried the imprint of the non-cooperative policymaking process described in this paper. This was reflected in several peculiar characteristics of the policies of the 1990s, such as the rigidity of the Convertibility regime, the inefficiencies of federal fiscal arrangements, the lack of enforcement of some policies, and the incoherence of privatization and regulatory policies across sectors. The overall experiment, inclusive of the Convertibility Regime, did not end up well, at least as evaluated by the Argentine public at the time of this writing. The current administration of president Kirchner is fairly vocal against several aspects of the reform process of the 1990s. It seems clear that unless some fundamental changes in the rules of the political game take place, we will continue to observe low quality policies, independently of the political inclination they respond to.

[29] Pion-Berlin (1997) also provides an excellent example, that of defense budgeting, of the different locus for lobbying activities in the U.S. (Congress-centered) and in Argentina (Executive-centered).

[30] There is by now a large literature on the political economy of reform in Argentina. See for instance, Palermo and Novaro (1996), Torre (1998), Gibson and Calvo (2000), Bambaci et al (2002) , Eaton (2002), Murillo (2001), and Tommasi (2002), as well as several chapters in this book (especially the one by Etchemendy).