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Los Angeles

The Determinants of Presidential Spending in Latin America (1970-2009)

A dissertation submitted in partial satisfaction of the

requirements for the degree Doctor of Philosophy

in Political Science

by

Maria Elena Guadamuz

2012

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ABSTRACT OF DISSERTATION

The Determinants of Presidential Spending in Latin America (1970-2009)

by

Maria Elena Guadamuz

Doctor of Philosophy in Political Science

University of California, Los Angeles, 2012

Professor Barbara Geddes, Chair

Balancing public sector budgets has long been considered an essential element for implementing effective economic strategies. Economic policy analysts across several schools of thought have thus focused on identifying the factors which increase the likelihood that politicians will reign in spending that grossly exceeds annual revenues. Some analysts assume that legislators have stronger incentives to spend than do presidents, because chief executives represent more encompassing interests. As a solution to this dilemma, they recommend the adoption of budgetary rules that increase presidential powers at the expense of legislators. Contrary to the predictions in this literature, I argue that, while executives are motivated to build strong economies, Latin American presidents' respond first to retaining power, which often implies amassing enough capital to preserve their political influence long after leaving office. This

dissertation uses a mixed method approach to support my contention. Through case studies, I analyze two countries with similar, centralized presidential controls over budgets: Argentina and Nicaragua, and show that empowering the president backfires when excess spending reinforces and supports narrow political interests. My research also shows that chief executives are often quite cunning in circumventing legal constraints and altering institutions that limit their powers. This is not to say that institutions are inconsequential. In fact, I show that term limits do, on average, increase presidents' incentives to increase spending. The empirical chapter of this project shows that Latin American presidents, contrary to conclusions drawn from earlier research, do not "buy" elections by increasing budgetary expenditures. Nor do left-wing presidents spend more, as most observers have assumed. Instead, over the last thirty years, excess spending has been the work of termed-out presidents, primarily right-wing chief executives. The differences among administrations throughout this project demonstrate that incentives vary and fiscal outcomes are ultimately dependent on the president's motives when politicial institutions grant great discretion to executives. Thus, the conditions questioned in this dissertation challenge numerous claims advanced in much of the accepted fiscal policy literature on Latin America.

The dissertation of Maria Elena Guadamuz is approved.

William Summerhill

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2012

Dedicated to,

My father and mother, Jose and María Elena,

for sharing their balanced take on history,

and for the love, support and guidance that has been essential to my success.

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Psalm 121:3: *He will not let you stumble; the one who watches over you will not slumber.*
To God's presence in my daily life and throughout this process.

***

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As is commonly known among the UCLA community, Barbara Geddes provides one of the best working relationships any graduate student could hope for. Her detailed feedback, from my first days to the last week of this dissertation, never failed to significantly improve my ideas and explain the complicated political realities of my region of focus. Most importantly, however, it was her patience with my progress that helped carry this project to completion. I truly believe one of the hardest aspects to the end of a doctorate degree is having to part from those individuals who have been an integral part to one's success and personal growth. Barbara has been at the center of this journey, and I will forever miss her guidance and presence on such a consistent basis.

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"The Paradox of Democracy: an Analysis of Nicaragua's 2006 Presidential Elections"
Latin American Studies Association Conference, Montreal, Canada, September 2007

"Unfinished Business: Testing the Partial Reform Model"
Latin American Studies Association Conference, Puerto Rico, March 2006

"Self-Placement in Latin America: Who Self-Places on the Left"
Rice Undergraduate Research Conference, Houston, Texas, January 2003

"Self-Placement in Latin America: Who Self-Places on the Left"
American Political Science Association Annual Meeting, Boston Massachusetts, August 2002

Introduction

In a relatively short period of Nicaragua's electoral democracy, right wing populist candidate, Arnoldo Alemán, successfully rebuilt the small PLC (Partido Liberal Constitucionalista) into a powerful political force. In 1996, he emerged to presidential power, with campaign promises to eradicate the Sandinista revolution from the national memory, integrate Nicaragua into the global economy and implement so-called "structural adjustments" to move the nation toward prosperity. Once in office, he wooed foreign investors, the pace of privatization resumed much faster than that seen under his predecessor, tariffs fell and inflation continued to drop. Moreover, Alemán in his demagogic speeches, boasted about "good governance initiatives":

"The New Nicaragua that we are building is also a society based on institutionalization and transparency, where there is a respect for the functions and attributions that the law gives to the different powers of the state. Where there is an application of laws and regulations clearly applied in a consistent and impartial form to every citizen."[1]

By 1998, USAID had approved Alemán's budget, which was alleged to contain more accountability, transparency and anti-corruption measures than prior years (Brown and Close, 2005). During the first few years of his administration, he was neoliberals' champion.

But Alemán's attempt to conceal reality behind a smoke screen of economic liberalization and rhetoric of good governance was soon unmasked. By the end of his term, it was clear that he had not only failed to carry out fiscal reforms - one of the *Washington Consensus'* most important policy measures - but had used the national treasury to build the PLC, nourish his governing coalition and multiply his personal wealth. He walked out of the

[1] President Arnoldo Alemán at the Consultative Group meeting for reconstruction and transformation, IDB headquarters, Washington D.C. May 23-24, 2000.

presidency with much more wealth than when he arrived and left Nicaragua with one of its largest budget deficits in its history, higher levels of poverty and less democratic governance.[2]

Nicaragua's economic and political realities under Alemán contradict much of the literature on what kinds of policies and institutions contribute to responsible fiscal policy. In this literature, it is assumed that presidents have incentives to balance budgets and that empowering presidents relative to legislature thus leads to reduced budget deficits. Clearly, in this case, the executive was not the primary force, or even a key force, in imposing fiscal discipline and limited spending. Hierarchical budgetary institutions and strong presidential powers, both of which characterize Nicaragua, did not lead to more responsible budgetary outcomes, as most scholars who have written on this subject would expect.

Instead, Aleman is an example of other features of Latin American reality when it comes to budgets: presidents with unusually strong budgetary powers can run up extraordinary deficits if their long-term political goals provide motivations for heavy spending; and formal deficit limits and donor conditionalities do not fully constrain presidents who can sometimes find other revenue sources and can often devise ways of keeping revenues off-budget. In short, although the literature has focused on the effects of formal political institutions, in the real world presidents can often find informal ways to circumvent formal institutional constraints.

In light of these realities, this study investigates the effects of both formal political institutions and informal work-arounds on budgetary politics in Latin America. Balancing budgets is one of the central elements in successful economic strategies, and scholars and policy analysts have devoted considerable attention to identifying the conditions that increase the likelihood that politicians will resist the temptation to spend more than they have revenues to pay

[2] In 1990 Aleman enters politics with a net worth of $26,118. By 1997, his estimated wealth was well over $999,000 (Brown and Close, 2005).

for. Some analysts have assumed that legislators have stronger incentives to spend than do presidents because presidents represent more encompassing interests; consequently they recommend the adoption of budgetary rules that increase presidential powers over the budget at the expense of legislators. Others advocate legal limits on deficits and donor conditionalities.

In this study, I show that that empowering presidents can backfire when excess spending can help them achieve important political goals and that presidents can often find ways to get around legal constraints or to change institutions that limit their powers. This is not to say that institutions never matter. In fact, I show that term limits do on average increase presidents' incentives to spend. I also show, however, some of the ways that presidents determined to spend have gotten around legal and institutional constraints, including term limits themselves.

I argue that presidents' re-election opportunities influence spending, but not in the ways suggested by the traditional political business cycle. Empirical evidence in Chapter 2 show that, Latin American presidents, contrary to conclusions drawn from earlier research, do not "buy" elections by increasing budgetary expenditures. Nor do left-wing presidents spend more, as most observers have assumed. Instead, over the last thirty years, most excess spending has been the work of termed-out presidents, primarily right- wing chief executives. These results support my claim that in the post 1980s democratic period, presidents standing for re-election were well aware of the political costs of inflationary spending. Apparently, citizens have become more sophisticated about the causes of inflation and reward politicians for responsible economic behavior except when severe economic crisis has induced a focus on very short term survival needs.

Another theoretical literature claims that hierarchical budgetary institutions and strong presidential power are factors necessary for executives' to decrease fiscal deficits. Contrary to

the predictions in this literature, I argue that, while executives are motivated to build strong economies, Latin American presidents' respond first to the goal of remaining in power, which often implies building political capital to stay active in politics well beyond their current terms. These goals directly conflict with the incentive to balance budgets, since controls on spending diminish the resources needed to build political support.

Presidents with the need to buy support or motivated to build their political parties are most likely to run up deficits when taking power in uncertain economic conditions that diminishes citizens' concern over deficit spending. Even in the new era of democracy, where voters punish parties for economic mismanagement (Reid, 2007), I contend that if citizens' sense of security is threatened by recurring economic crisis, the survival and success of presidents can depend heavily on what they can provide their people. Budget expenditures and populist policies assist presidents build their political capital when voters' welfare has deteriorated after an economic disaster and their time horizons have been shortened by concerns about how they will manage within the next weeks or months. Thus, presidents that campaign on promises to eradicate the everyday ills of society become an immediate appeal for citizens frightened by recurring economic crisis, high levels of poverty, joblessness and violence. As Vilas (1997) argues, the rise of mavericks in Latin America electoral politics has been the result of citizens' "insecurity, uncertainty, and the search for defensive mechanism, which always pave the road for the search, or acceptance, of political strongmen" (23).

To reinforce my contention and demonstrate that it is supported by Latin American realities, I analyze two countries with similar centralized presidential control over budgets: Argentina and Nicaragua. Executives in both countries have broad latitude to impose fiscal discipline. Moreover, in the last two decades, they have enjoyed relatively high levels of party

discipline and congressional majorities, which, combined with formal institutional powers, have given them substantial control over fiscal policy. Both countries have also experienced the most serious economic catastrophes in their histories during the period under study. Lastly, while these countries are similar in executive discretion over budgets, they also are very distinct. Argentina has a higher gross domestic product and entered its democratic period after a military dictatorship, while Nicaragua is one of the region's poorest nations and launched its democracy after a civil war. These distinctions present an opportunity to examine presidential decision making in contrasting, yet in some respects similar, sets of economic conditions and democratic progress.

The findings in these case studies arrive at the same conclusion: that, while political structures and rules allow executive branches to implement budget preferences, varying types of presidential goals result in diverse sets of fiscal outcomes. Clearly, while centralized power is at times used to create balanced budgets, these very same powers have led to less efficient outcomes than those predicted in the literature. Specifically, the centralization of power gives executives the tools to achieve whichever goals they value most highly. For some, the most important goal is to implement balance budgets and create stable economic conditions for their respective countries. For others, it is building political support bases, electoral victories and political machines. The differences among administrations in case studies demonstrate that incentives vary and fiscal outcomes are ultimately dependent on the president's motives when political institutions grant great discretion to executives. Thus, the reality uncovered in this dissertation debunks numerous claims advanced by the fiscal policy literature on Latin America.

PLAN OF STUDY

Chapter 2, The Effects of Institutions on Latin American Fiscal Outcomes: A Theoretical Perspective, reviews the various claims of how elections and hierarchical budgetary institutions impact presidential spending behavior. In this chapter, I argue that the predictions found in these literatures are not generally consistent with the contemporary real world in Latin America. I draw my insight by highlighting that previous conceptualizations of electoral periods have overestimated spending increases throughout election cycles.

Instead, I argue that pre-electoral spending will not occur across all electoral periods and maintain that presidents standing for re-election are motivated to control spending, but lack equivalent or similar discipline at the end of their terms. While it is difficult to conceive of executives' exercising fiscal discipline just before elections, new studies indicate that Latin American voters have rewarded incumbents who stabilized economies and refused to allow deficits to climb (Drazen and Eslava, 2005). However, I also contend that president who are insulated and with highly concentrated budgetary powers often spend more when their first goal is to build political capital and citizens' concerns with deficit spending is not a priority, especially after economic crises.

In Chapter 3, The Effect of Elections on Latin American Fiscal Outcomes: A Cross Country Time-Series Analysis (1970-2009), I investigate the relationship between elections, spending and deficits. This model is unique compared to previous studies, because it includes both the timing of presidential elections and a dummy for termed out presidents. Controls for economic and social factors are also included, as well as a set of control variables, presidential ideology and party fragmentation, which is traditionally associated with fiscal outcomes. I use a

time-series cross sectional (TSCS) data set that includes annual figures on government spending for 17 Latin American countries between 1970 and 2009.

The main finding is that election year spending increases identified in previous studies are driven primarily by termed out presidents. Specifically, from 1970 to 2000, spending increases originated with right-wing candidates, and, by 2000, all lame duck presidents initiated spending increases. I also use an alternative dependent variable, primary balance, as a percent of GDP, to determine if the variable of interest has the same effect on an alternative fiscal variable. There was clear deterioration in deficits when executives were leaving office. Outgoing Latin American presidents influence future levels of government consumption and the decline in fiscal balances, which can later tie their successors' hands.

In Chapter 4, The Politics of Budget Manipulation: Post-Crisis Argentina, I discuss what happens when presidents have extraordinary budget powers, particularly when the Congress relinquishes budgetary powers to them. These superpowers enable executive branch's to manipulate the composition of the budget and annual revenues. This chapter is based on field research conducted during the fall of 2008, which included interviews with policy makers and legislators as well as evaluation of congressional documents. In this case, the executive's superpowers over the budget, without congressional oversight, allowed the president to manipulate spending allocations according to her short-term preferences. Meanwhile, limited transparency and little congressional oversight had significant influence on final budget outcomes.

In Chapter 5, Nicaraguan Presidents' Quest for Power: the Unanticipated Consequences of *Neoliberalism's* Enhanced Budgetary Prerogatives, focuses on budgetary outcomes during the country's democratic period. Nicaraguan institutions have been given a great deal of executive

budgetary discretion. In this case, the internal procedures of political parties allowed presidents to secure legislative consent by using their control over legislators' career success.

The centralization of power enabled all Nicaraguan presidents to achieve their policy goals. If balancing budgets was central to presidents' policy goals, she had an array of tools to maintain budgetary discipline. Paradoxically, these same powers also helped presidents accelerate spending, which exacerbated fiscal imbalances. Finally, while executives' unilateral action is not unique to Nicaragua, unwarranted levels of presidential dominance is due to weak institutional checks on presidents. Thus, executive dominance over budgets is a result of astute acquisition of power to control all aspects of the political landscape.

In Chapter 6, Presidents and the Future of Latin American Budget-Making, the dissertation concludes by discussing how president's dominance over budgets becomes a bargaining tool to shore up political support. This dominance ensures that presidents can determine where, how and to whom "spending" is allocated. These findings point to the need to focus on institutional incentives and the informal political processes that shape spending to better understand budget politics and the impediments to fiscal restraint in Latin America.

Chapter 2

The Effects of Institutions on Fiscal Policy in Latin America: A Theoretical Perspective

Most scholars who weigh the political difficulties that impede economic liberalization have relied, sometimes implicitly, on several assumptions about voters and politicians. Central to the literature is the assumption that voters either do not understand the link between deficit spending and inflation, or have such short time horizons that they prefer spending now even if it will lead to inflation in a few months. As a result, voters tend to reward politicians who spend heavily on distributive benefits of one kind or another. Given voters preferences, politicians whose future careers depend on winning elections are likely to choose spending policies voters' desire, especially in the final months before elections. Equally, important, since presidents represent all citizens and deputies represent narrow geographical interest, executives are assumed to have stronger reasons to consider the full economic consequences of spending decisions than do legislators.

These assumptions about citizens and politicians lead to a set of expectations about the real world and to policy prescriptions about which kinds of political and budget institutions would lead to more responsible fiscal behavior. For one, given the assumption that voters prefer increased spending and that politicians focus mostly on re-election, the traditional political business cycle (PBC) informs us that elections alter presidents' spending habits, since incumbents are motivated to manipulate budgets in advance of winning essential votes. In the absence of a re-election opportunity, it also leads us to expect that term limited presidents will decrease spending as they no longer must appeal to voters who demand larger benefits.

Moreover, more prudent fiscal policy should materialize when executives are situated in hierarchical budgetary institutions whose rules increase presidential control over legislatures. This is based on the expectation that presidents insulated from pressures by other political interests are more likely to pursue responsible fiscal policy than chief executives forced to bargain with legislators or who are beholden to societal interest groups (Haggard & Kaufman, 1992).

In this dissertation, I show that none these expectations are generally seen in contemporary Latin America. First, I found that term limited presidents actually spend more than those up for reelection and that voters apparently reward them for responsible budgetary outcomes. These findings support recent research which indicates that a new type of politics has emerged throughout Latin America. According to Reid (2007), "in the new democratic era, voters have been merciless in punishing parties that have failed in their management of the economy" (288). Moreover, I challenge theoretical assumptions in the widely accepted literature on this subject: that enhanced presidential power leads to reductions in spending. Through two case studies, I show that presidents with highly concentrated budgetary powers often spend more than presidents who have to bargain with legislators. If economic or political crises proceed the executive, strong budgetary powers have led to opportunistic behaviors by self-oriented presidents focused on building political capital. My case studies also show that presidents often circumvent legal restrictions on spending and donor stipulations by creating off-budget funds and finding hidden sources of revenue not covered by existing laws and agreements.

This chapter's aim is to present existing assumptions on voters and politicians that comprise the accepted theories on fiscal policy and which are tested in subsequent chapters. The chapter is organized as follows: Section (1) discusses voters' preferences on spending as

described in the assumptions in the literature on electoral cycles. Section (2) is an examination of politicians' best re-election strategies given voters' preferences on these spending decisions. Section (3) reviews the alternative arguments presented by advocates of hierarchical budget institutions as a requirement for fiscal discipline. Section (4) questions how the literature conceptualizes elections and thus clouds the analysis of election cycles.

In particular, I argue that spending increases are not a phenomenon across all election cycles, but hinge, instead, on whether incumbents are permitted by electoral rules to stand for re-election. Furthermore, I discuss my argument's implications about voters. My argument takes into account the changes in the international economic context that have had a greater impact on Latin America than the OECD countries, as opposed to most of the literature on this subject. Section (5) concludes with a contribution to the literature on fiscal policy.

I. The Effects of Presidential Elections

One of the central themes in political economy is the study of politicians' responses to electoral cycles. One of them is the theoretical discussions that start with a set of assumptions on voters' spending preferences and incumbent strategies for responding to voter preferences--specifically the trade off between macroeconomic variables--to achieve electoral victory. The first strand of literature that made began to explain the impact of elections on the behavior of incumbents was the traditional political business cycle (Nordhaus, 1975).[1]

The political business cycle argues that elections alter the spending behavior of presidents since incumbents are motivated to manipulate spending before elections in hopes of attracting

[1] The relevant actor within this framework is not completely specified, but whether the relevant actor is the president or party, the prediction of the political business cycle (PBC) is a consumption binge during elections to maximize the likelihood of electoral victory.

essential votes. Early in their terms presidents spend less, but increase expenditures as elections draw near. By poring money into the economy, voters' purchasing power is increased and candidates thus increase voters' perceptions of good economic performance. In turn, voters reward them with a higher share of votes. Recent studies on fiscal policy and elections, however, challenge the notion that presidents are likely to increase spending in re-election years. The studies instead indicate that re-election possibilities create incentives to build positive reputations by controlling spending and deficits (Besley & Case, 1995a; Johnson & Crain, 2004). Thus, the term limits literature argues that spending is cut before elections if presidents have strong re-election possibilities and that increases in spending do not occur unless incumbents are termed out.

While the arguments in the literature on elections present contrasting assumptions about candidate motivation and voters' preferences on spending, the most interesting aspect of both theories is their claim that politicians' desire to manipulate economies to win votes. According to both theories, opportunitistic candidates are driven to effect upcoming elections, but the arguments diverge in their assumptions about voters' spending and taxation preferences. The political business cycle literature assumes spending is a way to improve chances of winning by introducing a temporary growth spurt, while the reputation building model posits that voters are, in fact, aware of the short-run effects of expansionary spending and punish politicians accordingly.

When applied to Latin American presidential behaviors, these assumptions illuminate important ways in which elections might impact fiscal policy. Given the assumptions about Latin American presidents--their desire to stay in power, finish their terms and win re-election if constitutionally able to do so--understanding the methods they utilize to maintain power is

imperative. The recent changes in presidential term limits and empirical work that challenged the basic idea that expansionary fiscal policy contributes to electoral victories (Remmer, 1993; Brender & Drazen, 2008; Gonzales, 2002). Chapter 3 marshals evidence accumulated over the last thirty years that sheds lights on several critical ways electoral politics play out in Latin America. The following analysis presents theories on fiscal policy and the various claims on how elections and hierarchical budgetary institutions impact presidential spending.

Voter Preferences over Spending

Voters are the foundation of studies on election cycles. For the most part, political scientists say politicians hunger to remain in office and thus carry out voter preferences. Voter preferences, however, depend on the assumptions these studies attribute to their interests; some authors highlight spending as a tool to win over voters who fail to understand its longer term consequences (Nordhaus, 1975), while others point to fiscal control as a way to signal competency and impress them (Johnson & Crain, 2004).

According to the political business cycle, voters are only concerned about recent economic performance. To give the illusion of good economic performance, incumbents have the incentive to enact immediate measures affecting unemployment, spending and tax cuts before elections. This framework assumes that since voters are fixed on short term gains, politicians are less constrained by long-term reputation incentives. It views voters as shortsighted, as well as incapable of fully understanding that spending in the present leads to future inflation and slow growth. It also underestimates their concerns over current, rather than future growth. Second, the political business cycle holds that voters focused on distribution prefer government spending that benefits them personally (e.g. increased unemployment and expanded infrastructure, etc.).

Lastly, spending increases are associated with voters' lack of information. With more complete information, voters would not systematically make the same choices over successive election periods, since they ultimately pay for pre-election spending with dangerous levels of inflation. However, the claims of voter myopia advanced by Nordhaus (1975), are often challenged by scholars who position voters as rational actors with the ability to judge candidates by what they expect to receive in the future (Rogoff & Sibert (1988), Rogoff (1990), Persson & Tabellini, 1990). This calculation is based on information voters have acquired about the incumbents' political behavior. Rogoff (1990), was among the first scholars to question backward looking voters. He instead presented an argument based on a forward looking (and rational) electorate that receives signals from incumbents that are indicative of their ability to govern. Rogoff (1990) argues that voters' use past performances to predict future performance and determine their preferences for candidate.

So while asymmetrical information between voters and incumbent governments does not provide voters with complete histories on politicians' competency, economic outcomes enable them to overcome this deficiency and judge incumbents on their competency. Several economic outcomes are easier to observe, such as deficits and inflation, versus changes in the composition of budget outcomes, which politicians might utilize to garner votes. Accordingly, the reputation building model of politics argues that voters are aware of spending and deficits and prefer sound fiscal performance. In sum, the rational voting model framework presents voters as aware and fully capable of judging incumbent competency, given the information with which they are presented. This scholarship do not discount political opportunism, but assumes that voters' level of information and ability to judge incumbent behavior is a major constraint. These competing theories present voters' preferences and abilities to judge politicians in various scenarios.

Section II presents how scholars pivot from these assumptions about voters and how they conceptualize the strategies incumbents employ to achieve electoral victory.

II. Re-Election Strategies

Political Business Cycle

Politician's best re-election strategies respond to voters' demands, given the various assumptions about their preferences on spending, and their understanding of how the economy works. According to the traditional political budget cycle, an opportunistic government chooses policies to maximize re-election chances by using various tools (e.g. monetary policy, increased welfare spending), but in particular, incumbents are motivated to increase spending before elections in hopes of spurring growth and attracting votes (Nordhaus, 1975).

According to conventional wisdom, Latin American officials display fiscal austerity when their terms begin, but increase spending as elections loom (Ames, 1987). Immediately after elections, incumbents rein in spending to combat inflation. Since fiscal manipulation is utilized to win votes, politicians have difficulty sacrificing short-term consumption, thus election cycles are believed to create budget deficits. This creates a cyclical effect around elections, prior spending and reductions forced by inflationary pressures when victory is achieved. The predictions in this model are based on the short-sighted behavior of voters, and, most importantly, their failure to understand that excess spending leads to future inflation or to remember lessons from past behavior. Consequently, Dornbusch and Edwards (1991) view frequent elections as barriers to fiscal discipline in Latin America because they lead to long cycles of over spending. Given that politicians do what voters prefer and typically concentrate

their efforts in the final year before upcoming elections, countries with more frequent elections have more difficulty in maintaining fiscal discipline. Recent research, however, has confirmed the degree to which budget cycles are dependent on the transparency of governments in determining the extent of the political business cycle. Countries with higher levels of transparency show evidence of fewer bust-and-go spending cycles, since voters will punish politicians who intentionally manipulate the economy. Accordingly, the deterioration in fiscal outcomes is greater in countries with less transparency and voters' ability to hold incumbents accountable is much more difficult. When voters have more information, incentives for politicians to reduce waste increase and competence also rises (Brender & Drazen, 2008).

Term Limits, Reputation Building and Rational Voters

On the other hand, the reputation building literature projects incumbents as motivated by voters' preferences to behave responsibly, depending on their re-election chances. Higher electoral ambitions are clear incentives for politicians hoping to build reputations among electorates who will judge them favorably after receiving these signals (Rogoff, 1990). Contrary to the spending increases predicted by the political business cycle, the reputation building model assumes that politicians' electoral strategy is based on controlling spending to signal competency to their electorates. Since electoral opportunism is easily observed by voters (Rogoff, 1990), incumbents are not inclined to exert their power to affect elections because voters are informed. In fact, as argued by (Alesina & Roubini, 1997), an overt, pre-electoral manipulation may be counterproductive, as voters can punish opportunistic policymakers.

Johnson and Crain (2004), argue that we should see more fiscal restraint when presidents are candidates for re-election, but not as much when they are stymied by term limits. The idea of

reducing spending in a re-election period is contrary to the assumptions of the traditional business cycle, but plausible, as the transformation in Latin American voters' awareness is influenced by the region's history of runaway inflation and concerns over government corruption, since they prefer spending for investment categories over higher state salaries (Gonzales, 2002). Moreover, it may seem counter-intuitive for presidents to control spending; while voters may not have the fullest information to reward or punish specific legislative initiatives, they can benefit from the results, such as reductions in inflation and stability in prices. This assumption is also based on the belief that if presidents increase spending during election periods, they will have more difficulty in combating inflation levels during their future terms in office.

The Effects of Term Limits

The desire to increase spending - given politicians motivations' to win office - is the key to the political business cycle theory. The political business cycle, however, does not make clear whether the relevant actor is the incumbent president or the incumbent party. If the relevant actor is the president, we should not expect spending increases during the last year before elections, unless presidents can be reelected, since termed out incumbents have no incentives to win future elections. But if the relevant actor is the incumbent party, term limits have no effect and any incumbent government will increase spending in its final year to increase the party's chances of winning. A majority of Latin American analysts would agree that the president is the most powerful actor, except in the case of Chile with its strong political parties. Moreover, (Streb, 2011), argues that unless presidents have the ability to influence the party's candidate, they have virtually no stake in that candidate's victory. This leads to the expectation that termed

out presidents have no incentives to spend and that the political budget cycle, anticipated by the political business cycle theory, should not be present unless an incumbent stands for re-election.

On the other hand, underlying the term limits argument is the implicit premise that incumbents are self-interested, with little concern for their party's future or reputation, since being termed out eliminates the desire to maintain positive reputations. Cohen and Spitzer (1996), illustrate how term limits could impede the incentives legislators need to be responsive to their constituents' interests and pass legislation that runs counter to their personal self interest. In their study, the authors treat the relationship between voters and legislators as a prisoner's dilemma. They show that legislators in the lame duck period will have fewer incentives to serve constituents, since their efforts will not be rewarded in the next term.

As Tien (2001) argues, legislators without the fear of voters' punishment act as "free agents" in their last terms. Accordingly, legislators without incentives to protect their constituents' interests "vote their own preferences, the preference of another group they desire to represent, or succumb to the temptation of voting to protect the interests of special interest groups who may promise lucrative lobbying jobs just around the corner" (Tien 2001: 127). Consequently, binding term limits are expected to create fewer incentives for reputation building and less concern for establishing reputations for lowering deficits.

The theoretical prediction of the reputation model of politics has informed recent studies on term limits' effects on fiscal performance. Besley and Case's (1995a), work was the first to test the reputation-building model on fiscal policy in the United States. In an effort to verify whether the reputation building model of political behavior works, they analyzed United States (U.S.) governors who faced term limits, compared to those who didn't. Taking into consideration the factors that could possibly weaken the relationship between term limits and

fiscal policy, they control for party loyalty, lack of gubernatorial discretion and life after governorship. Their results suggest that these other factors are not "strong enough to rein in governors whose days are numbered" (775). The authors found that among the 48 states, from 1950 to 1986, term limits have given rise to increases in both total government spending and tax rates. During a governor's lame duck period, total state spending and tax receipts increase, particularly when Democrats hold office. These findings support the reputation building model of political behavior if we assume that most citizens prefer lower spending and lower tax levels, which predicts that re-election possibilities act as powerful incentives for politicians to limit spending and maintain lower taxation levels.

Besley's and Case's (1995) findings may seem contradictory when compared to the conventional wisdom that assumes voters prefer high public spending in the form of the pork that legislators bring home. In his study on OECD countries, Alesina and Perotti (1996), challenges the assumption that voters prefer high spending and found that incumbents who spend more are not likely to receive greater support than fiscally conservative executives. He found that what matters more to voters is whether the fiscal adjustment initiated via conservative policies is successful in terms of economic growth. For instance, fiscal adjustments that contribute to national economic growth are rewarded, while those that are followed by deteriorations in macroeconomic performance are punished.

Alesina and Perotti (1996) further supports his findings through a survey of voters in OECD countries. He did not find that governments which implement strict economic policy are necessarily replaced or lose popularity. In fact, he found that fiscal adjustments are rewarded with an increased probability that incumbents will remain in office. Having established some empirical validity in the importance of term limits on fiscal spending, Besley and Case (1995a),

provide the groundwork for expanding the study of term limits to other institutional settings. Johnson and Crain (2004), utilize Besley and Case's model to analyze the effect of executive term limits on fiscal policy in 48 democracies. Johnson and Crain (2004), found increasing levels of fiscal spending and taxes in democracies with a one term limit rule. Under single-term rule, government spending grows systematically, in comparison to two term limits or no term limits at all.

On the other hand, countries operating under two-term limits suffer significantly from fiscal volatility, though they do not experience a significant increase in government spending over time. Furthermore, under two-term limits, executives spend more and increase taxes during the lame-duck period. Their evidence supports the reputation building model. These studies have confirmed that term limits are related to increases in spending, which is attributed to the executives' lack of incentives to adopt fiscally disciplined policies in their final terms, since their reputations are not tied to future economic performance. Therefore, the implications from the reputation building model of politics seem to demonstrate that re-election creates different incentives than binding term limits, causing executives to act much differently in these two institutional environments.

Why term limited spending?

The studies on term limits fail to mention the motivations driving spending increases when incumbents are termed out. However, there are several explanations as to why presidents might increase spending or deficits may rise during lame duck periods. Lame duck presidents may be motivated to fund a range of projects that reflect their preferences. For example, Argentinean presidents are known to increase spending in their home provinces. On the other

hand, as argued by Molinas, Perez-Linan and Hallerberg (2009) "[a]n unconstrained president could, for instance, compromise the budget balance in order to reassert his short-term priorities and then happily transfer this legacy to the next administration" (161).

However, not all presidents have the same, or even similar preferences, backgrounds or goals. One key factor to consider is whether ideology and/ or other external circumstances impact fiscal discipline. Termed out presidents may seek to tie the hands of new presidents if they're members of opposing parties. According to Alesina and Tabellini (1990), public debt is typically used by each government to influence choices by successors. If the incoming executive is already saddled with debt, it will be harder for him or her to find the resources to initiate new programs and projects. For this reason, the increase of public debt as presidents leave office is predicted to be greater in countries with higher degrees of polarization between altering governments (Alesina & Tabellini, 1990). In the context of the United States, Persson and Svensson (1989), found that conservatives run fiscal deficits to constrain the spending choices of the elected officials coming after them, especially if liberal candidates are their successors.

This practice is seen in Latin American cases, where candidates of the right and left possess strong preferences in the allocation of public funds. In Latin America, leftist presidents, for example, may promise supporters increased spending to reduce inequality, poverty and create employment, which leads higher levels of spending. Consequently, out-going presidents exhibit a redistribution of funds toward their preferred spending components. Meanwhile, lame duck presidents are also concerned with 'diminishing' legislative bargaining power in the final year of their terms, which may force them to increase spending to offset these effects.[2]

[2] What I mean by 'diminishing power' is that while President may still be powerful, legislators may not have the same incentive to bargain with the President when they know he/she will soon be out of office.

III. Hierarchical Budget Making

The literature on electoral cycles and presidential spending explains budget deficits as a result of voters' spending preferences and politicians' responses during electioneering. In contrast to these points of view, a third theory in the literature asserts that budget balances are best achieved by institutional settings that encourage politicians to ignore voters' spending preferences. Thus these arguments implicitly assume that paying attention to voters will lead to budget deficits since voters prefer having the benefits governments spend their resources on but also prefer lower taxes.

Scholars such as Alesina, Hausmann, Hommes, & Stein (1999), argue that a centralized budget making process, in which members of the executive branch can choose spending levels without consulting congress, improves fiscal outcomes. Consequently, Alesina et al. (1999), indicate that hierarchical budgetary institutions that include certain constraints on Congress--veto powers, line item vetoes and the budgetary implementation phase--are necessary for balancing budgets. As argued by Leachman, Guillermo, Lange, & Bester (2007), hierarchical institutions "contribute to better fiscal policy design by limiting opportunities for politically motivated budget making" (371). Others assert that complete control over budget drafting should reside in the executive branch, and, more specifically, that the process [should] be placed in the hands of finance ministers.

Their argument rests on the same assumptions about voters' preferences as does the political business cycle, but they also assume that the executive, because he represents a national constituency and is held responsible for overall economic performance, has stronger incentives to be fiscally responsible than do legislators who represent geographically circumscribed

districts. They see executive's potential re-election as dependent on growth, which can be slowed by deficits and the inflation they cause, whereas they expect legislators to be rewarded for providing benefits to their constituents, regardless of whether those benefits eventually contribute to inflation. Voters in this context do not understand the relationship between spending and future inflation, but they punish incumbent executives and parties for periods of slow growth.

The suggestions advanced by the budgetary literature, however, at are odds with the predictions found in the reputation building model, which implies an unnecessary need to insulate voters from the budget making process (or politics), since voters respond to unsound macroeconomic decisions by punishing politicians who are responsible for them. The following section introduces a new line of argument concerning presidential spending decisions and what voters reward at election time.

IV. Elections, Executives and Voters

The theoretical frameworks presented in this chapter provide various assumptions on voters--their preferences on spending, what they understood about economics and whether they are myopic or forward looking--and subsequently, contrasting strategies incumbents may employ to win elections. However, the literature on electoral cycles has limitations on how electoral periods are conceptualized, and consequently, I argue that previous electoral studies have overestimated spending increases throughout electoral periods.

First, the political business cycle does not differentiate between incumbents who are eligible for re-election and those who are termed out. In other words, given the assumption that

incumbents' desire to spend as a way to increase their chances of holding onto political power, incumbents who are termed out--unless constrained by strong party loyalties--lose the incentive to increase spending because the motivation to win office disappears. Thus, the spending increases predicted by the PBC should fade when incumbents are termed out.

Second, both sets of literature lump all re-election possibilities together in one category that includes incumbents who have immediate re-election possibilities and those who must wait during an interim before running again. While six Latin American countries allow one immediate re-election, the majority of incumbents are eligible only for re-election after waiting for one or more terms. Both theoretical frameworks - the political business cycle and studies on term limits - fail to analyze how these differences in re-election opportunities affect executive behavior. Moreover, the international economic context affects what economic strategies are feasible in developing countries. In the post-debt crisis era, executives are constrained by the costs of deficits and must strategically weigh the costs of unwarranted levels of inflation and/or losses to foreign investment. Therefore, I argue that spending increases should not be expected by either theory across all Latin American election cycles. Government spending, instead, is conditional on whether a president is termed out or up for re-election. I contend, and show below, that spending by incumbents up for re-election is diminished and utilized strategically, in comparison to termed out presidents. This argument is based on the observation that Latin American presidents are now constrained by economic factors that didn't exist prior to the debt crisis.

Due to Latin America's history of increased spending and run-away inflation, there has been a shift in voters' response to economic outcomes. Incumbent presidents understand there is a tradeoff between spending and inflation, whether voters do or not, and those who strike a

balance have been able to achieve electoral victories. This electoral strategy was evident throughout the 1990s reform era; among the many economic policies pursued by Latin American presidents, there was a marked effort to reduce inflation levels. As Remmer (1993), suggests, a return of democracy to the region has actually "enhanced, rather than undermined" the ability of political leaders to address economic management (393).

In fact, budget deficits have fallen over the past two decades, inflation has reached stable levels, with a couple of exceptions, executives are apparently trying to maneuver budgets that can assist them in remaining in power, but not at the expense of economic disasters. So while voters punish politicians who can't maintain spending to which they've become accustomed, they may not necessarily reward spending for new programs. Overall, in order to maintain spending programs, executives must build a solid base of growth and a healthy revenue stream. Lastly, executives are also constrained by, and aware of, the costs of deficits in terms of future inflation and loss of potential foreign investments. Investors abhor inflation and factor the relationship between deficits into every calculation about its economic effects, unlike the majority of citizens and weigh voters' demands against future economic conditions that will ultimately impact their profits. Consequently, given growing voter insistence on holding presidents accountable for run-way inflation, the lack of incentives for fiscal responsibility among termed out presidents implies they will increase spending on becoming lame ducks. Thus, spending increases will not necessarily come into view during every election cycle, unless termed out presidents gain incentives to maintain positive reputations and control spending to signal fiscal restraint to the electorate.

V. Conclusion

This chapter presents conflicting arguments about voters' spending preferences and the strategies presidential candidates utilize to appeal to them. Ultimately, the political business cycle position is built on the argument that electoral victories occur because candidates artificially stimulate economies and that voters are short-sighted and/or lack the ability to monitor the effects of short-term spending increases. A new line of research, however, informs us that presidents are fiscally conscious when having to build reputations for accountability and that they control spending when faced with re-election possibilities (Johnson & Crain, 2004).

I not only highlight the contrasting differences in the assumptions around voter and candidate strategy, but also shed light on how election periods are conceptualized. In addition, I point out the limitations of the theories on election cycles and argue that spending increases are not a given across all elections. Moreover, I argue that spending is strategically used by presidents seeking re-election in the post-debt crisis era but less so by termed out presidents. Since political actors are motivated primarily by their desire to remain in office, incumbent presidents running for re-election polish their images with sound fiscal policy. Presidents hoping for re-election are motivated to signal their capability in managing economies and utilizing public resources to satisfy constituent demands within the constraints imposed by balanced budgets. The next chapter is a test of how politicians' time horizons impact spending. Ultimately, an analysis of how institutional structures impact fiscal outcomes will shed light on incumbent responses to institutional differences. My results shine a spotlight on the distinctions between the various arguments discussed above.

Chapter 3

The Effect of Elections on Latin American Fiscal Outcomes: A Cross-Country Time Series Analysis (1970-2009)

The theoretical arguments presented in Chapter Two dissect the literature on fiscal outcomes. The aim of this chapter is to investigate the predictions of two theories connecting electoral cycles to fiscal outcomes in Latin America. The traditional political business cycle predicts that incumbents increase spending prior to an election period, while the literature on term limits position voters as being well-aware of presidents' policy choices. Hence, voters are well equipped with the ability to punish pre-electoral manipulations. In this chapter I investigate how theoretical expectations stand up to the real world. Given the recent evidence by Johnson and Crain (2004), on the effect of term limits on fiscal spending, I employ their model as a starting point to test the effects of presidential time horizons from 1970 to 2009.

A number of Latin American countries initiated significant constitutional changes in presidential term limits during that period, which makes it a good time to test the arguments because the effects of presidential reelection can be compared to one-term limits in the same countries. Beginning in the 1990s, several Latin American countries, such as Argentina, Brazil and Costa Rica and Venezuela, for example, adopted constitutional changes that enabled incumbents to seek two (or more in Venezuela) consecutive terms. Table (1) shows the various presidential term limits and changes from 1990 to 2009.

Table 1: Presidential Term Limit Changes

1990s			2000s		
1-Term	Re-Election Possible		1-Term	Re-Election Possible	
	Inter-Term	Immediate		Inter-Term	Immediate
Colombia (1991)	Bolivia	Argentina (1994)	El Salvador	Chile	Argentina
Costa Rica	Chile	Brazil (1997)	Guatemala	Costa Rica (2003)	Bolivia (2009)
Guatemala	Dominican Republic (1994)	Peru (1993)	Honduras	Peru (2000)	Brazil
Honduras	Ecuador (1998)		Mexico		Colombia (2005)
Mexico	El Salvador		Panama		Ecuador (2008)
Panama	Nicaragua		Paraguay		D.Republic (2002)
Paraguay (1992)					Venezuela (2009)
					Nicaragua (2010)

These institutional changes provide natural variation with which to test the arguments about the effects of term limits on fiscal outcomes. This chapter is organized as follow(s): Section One describes the model specification and research design. In order to test the effect of time horizons on fiscal variables, I add a dummy variable to capture the electoral cycle for presidential elections to Johnson and Crain's (2004) model. This is a difficult but necessary test since previous studies on time horizons analyzed the influence of electoral cycles on executives' incentives without considering whether they stood for re-election.

Most studies have analyzed the motivation of governments to increase spending ahead of elections. Given that the primary actor in Latin American budgetary politics is the president, this method provides a better understanding of how these distinct time horizons affect presidential incentive structures. I also expand the years of study beyond 1990 to 2009, and revise the

Johnson and Crain (2004) classification of democracies by utilizing Geddes (2012). Her coding provides a more accurate measure of political institutions in Latin American countries.

Section Two discusses my results. I find similar results to Johnson and Crain (2004) on term limits and government spending. However, the spending trend is slightly different for the South American region, compared to Central American countries, where the increase in government spending is less pronounced when executives are termed out. Section Three explores whether the effect of term limits is stable between 1990 and 2000. The results are consistent: termed out presidents spend more than executives poised for re-election. Section Four suggests future areas of research to disentangle the institutional differences across countries. The institution of term limits plays a fundamental role in how presidents respond to their policy choices, but equally important, is the economic reality in which presidents are forced to operate.

Model Specification and Research Design

To test the impact of time horizons on fiscal policy, I use a time-series cross sectional (TSCS) data set that includes annual figures on government spending for 18 Latin American countries between 1970 and 2009. In this study the number of observations varies by country, and only includes countries coded as democratic according to Geddes (2012). The countries and time periods covered are: Argentina (1984-2009), Bolivia (1983-2009), Brazil (1986-2009), Chile (1990-2009), Colombia (1970-2009), Costa Rica (1970-2009), Dominican Republic (1979-2009), Ecuador (1979-2009), El Salvador (1995-2009), Guatemala (1996-2009), Honduras (1982-2009), Mexico (2001-2009), Nicargua (1991-2009), Panama (1990-2009), Paraguay

(1994-2009), Peru (1981-1991) & Peru (2001-2009), Uruguay (1970-1972), Uruguay (1985-2009) and Venezuela (1970-2004).

When using a TSCS data set, Beck and Katz (1995) advise using OLS regression with panel corrected standard errors once the serial correlation is eliminated.

I utilize Johnson and Crain's (2004) empirical model that tests the effect of term limits on the behavior of executives:

$$Pct = \gamma\, Tct + \alpha Zct + \varepsilon ct,$$

Where P is government spending (percent of GDP), T a dichotomous variable measuring whether the executive can run for re-election, Z a set of control variables related to government expenditures, and c and t are country and time identifiers.

Variable of Interest

The main variable of interest is T, a dichotomous variable for whether the executive can run for re-election. T equals one (1) if the executive can stand for re-election, and zero otherwise. The main coefficient of interest is γ. If γ *equals* zero, then the data suggest that term limits have no effect on fiscal variables. While term limits is my main variable of interest, I also include a dummy for *presidential elections*, which identifies all years in which presidential elections are held, to capture any electoral opportunism, since the political business cycle predicts incumbents are motivated to increase spending to achieve electoral victory.

Dependent Variable(s)

My dependent variable measures of *government spending*, as a percentage of GDP from the Penn World Tables 7.1. I also run a series of robustness tests with an alternative fiscal variable: *primary balance,* which I retrieve from the Inter-American Development Bank database. The primary balance excludes debt-service payments and thus eliminates the effects of prior deficits on the current one (Neto and Borsani, 2004) and therefore measures fiscal policy in any given year net of the effects of debts incurred in the past.

Independent Variables

Z represents a vector of control variables, which include economic and demographic factors associated with traditional determinants of government spending. All these variables are logged throughout all tests. I include *real income per capita* in constant U.S. dollars. According to Wagner's law, the demand for government service is income elastic and is expected to rise with higher levels of income. I expect this variable to be positively associated with government spending. The second and third control variables are *population size* and *population density*. I also retrieve *income per capita and population size* from Penn World Tables 7.1. Following the model specification provided by Johnson and Crain (2004), these variables control for population, since larger constituencies create pressures on governments to spend.

The fourth control variable is *average rate of inflation* provided by the International Monetary Fund World Economic Database. Higher levels of inflation will prohibit an administration from increasing spending over time. As higher inflation levels increase, governments may be restricted from increasing their budgets to evade placing further pressure on rising prices. The fifth control variable is Sach's measure of *trade openness*. An increase in

trade openness will generate higher revenues for governments, which has the potential to increase a government's ability to spend or decrease deficits. The sixth control variable is *Gastil index* of political rights. I use the *Gastil Index* to control for the effect of democratic governments on fiscal spending. Democratic governments have a greater tendency to respond to popular pressures than do authoritarian countries, which should positively affect spending. The Gastil Index is a seven-point measure of political and economic rights. For the purpose of this project, I use the political rights variable. The seventh control variable is *Previous Decade Spending*, which is government spending as a percentage of GDP, lagged by one decade. It is included to control for unmeasured country characteristics that might affect spending.

Political Variables

The eighth control variable is *Majoritarian* (MAJ) -*Margin of Majority*, which is retrieved from the Database of Political Institutions. It represents the fraction of seats held by the government party of coalition. It is calculated by dividing the number of government seats by total seats (government plus opposition plus non-aligned). Presidents who need the support of a larger number of congressmen may need to spend more to keep their coalition together. On the other hand, presidents with single-party congressional majorities will utilize fewer resources and lower spending levels are expected.

The ninth control variable is *Ideology*, also retrieved from the Database of Political Institutions. This variable measures the president's ideology on a three point scale: Right (1), Center (2), and Left (3). This coding is based primarily on the party's orientation with respect to economic policy. I transform this variable into two dummy variables: *Right-Wing* and *Left-Wing* Presidents. Government spending preferences are often associated with the ideological makeup

of governments. It is often assumed that leftist parties prefer higher spending, while parties from the right will reduce spending in pursuit of fiscal austerity (Ames, 1987). The tenth variable is N*on-concurrent legislative Election.* The frequency of legislative elections also plays a role in executives' behaviors in office. If presidents want to influence the outcome of legislative elections, they may increase spending levels with the expectation of gaining support from legislators in the future, or electing more legislators from their party. Furthermore, when the cost of spending during mid-term elections is lower than the cost needed to build post-election coalitions, it may be in the best interest of the president to increase spending to sway results. In non-concurrent elections, presidents must work harder to ensure that they maintain majorities.

I utilize an interaction in my diagnostics checks: *Termed Out*Right-Wing* and *Termed Out*Left-Wing* presidents. This interaction helps to isolate if spending is a general phenomenon or driven by specific ideological leanings. Lastly, I include yearly dummy variables from 1984-2009. Given that the region experienced several economic shocks from the 1990s to 2002, (i.e. Debt Crisis, Tequila crisis in Mexico, 2001 Argentina debt default) these controls capture time specific effects.

RESULTS

Table 2 presents the regression results for the effect of term limits on government expenditures. The coefficient on T, the indicator variable for incumbents who cannot stand for re-election, is positive and statistically significant at the one-percent confidence level. The coefficient on this variable equals .1225, indicating that government spending (as a percent of GDP) increases from 7.46% to 8.43% (a spending increase of approximately 1 % of GDP) when an incumbent faces a final term. To obtain these measures of government spending (as a percent of GDP), I compute the predicted level of government spending when incumbents can and cannot run for reelection. To do so, I set all other variables equal to their mean, compute when

T=1 and T=0, and then anti-log the predicted spending level to return from logs to the original units.[1]

Table 2: Effects of Presidential Time Horizons on Government Expenditures % of GDP (1970-2009)

Dependent Variable	(1) Gov. Ex % of GDP	(2) Gov Ex % of GDP	(3) Gov Ex. % of GDP	(4) Gov Ex. % of GDP
Specification	OLS	OLS	OLS	OLS
Termed Out	.1225***		.1164***	
	(.016)		(.016)	
Termed Out (One-Term)		.1161***		.1105***
		(.0166)		(.0155)
Termed Out (Two-Term)		.1564***		.1477**
		(.0597)		(.0594)
Presidential Elections	-.0035	-.0039	.0005	.00028
	(.026)	(.0268)	(.0260)	(.0261)
Income per Capita	-.0700***	-.0706***	-.0748***	-.0753***
	(.021)	(.0217)	(.0205)	(.0206)
Population	-.0642***	-.0652***	-.0602***	-.0612***
	(.013)	(.0138)	(.0148)	(.0148)
Population Density	.0477***	.0502***	.05236***	.05435***
	(.006)	(.0074)	(.0081)	(.0088)
Inflation	.0068	.0088	.0087	.0105
	(.005)	(.0063)	(.0063)	(.0067)
Trade Openness	-.1392***	-.1330***	-.1249***	-.1195***
	(.024)	(.0265)	(.0280)	(.0296)
Political Rights	.0741***	.0740***	.0670***	.0669***
	(.008)	(.0088)	(.0099)	(.0099)
Previous Decade Spending Control	.7724***	.7698***	.7731***	.7709***
	(.011)	(.0116)	(.0138)	(.0140)
Congressional Majority			.1418	.1356
			(.0866)	(0845)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.88	0.88	0.88	0.88
No. Observations	397	397	394	394
Constant	1.84	1.83	1.70	1.69

*significant at the 0.05 level; *significant at the 0.01 level; *significant at the 0.001 level. Standard errors are in the parenthesis. Negative and significant year dummies: 1995-1997; 2000-2004 & 2006-2009. The Mexican tequila crisis negatively affected Latin American economies in 1995. In 2001 Argentina defaulted on its debt, which also negatively affected the economies in the region.

Presidential Elections has an unexpected negative relationship with government spending but never reaches statistical significance. Previous studies on Latin American election cycles

[1] I take the anti-log of 2.01 and 2.13 and retrieve 7.46% and 8.43% of government spending (as a percent of GDP).

have found a positive effect on spending (Ames, 1987; Kraemer, 1997), but my results suggest that spending is likely to occur *only* when presidents are termed out. This implies that previous findings on political-economic cycles were caused by the inclusion of termed out executives. In other words, spending by presidents, whether they were termed out or up for re-election, were averaged - leading to the apparent effect of election year alone.

Income per capita has a negative effect on government spending and is highly significant. This finding is surprising, given that higher levels of income lead toward increases in a government's ability to tax and redistribute wealth and are associated with higher levels of government spending in developed countries. However, during the late 1980s and throughout the 1990s, Latin American governments implemented a set of neoliberal economic reforms, which meant a reduction in government spending in efforts to balance budgets. Since countries were becoming richer over time, the apparent effect of wealth on spending probably reflects the change in policy emphasis associated with economic liberal rather than wealth per se. The effect of *population density* is positive and statistically significant at the 1% confidence level, indicating that governments in more urbanized countries spend more. The coefficients on *Population* are not expected, as an increase in this variable leads to decreases in government expenditures per capita. This suggests there are economies of scale in government provision of social services and public goods as would be expected.

Trade openness is negative and significant. This result suggests that greater openness to trade leads to decreases in government spending. Unlike high trading countries in Western Europe who have large states and high levels of welfare spending, increased levels of trade openness in Latin America has not mobilized citizens to demand higher safety nets in anticipation that trade increases economic and income volatility. Or if it has, governments have

not responded with more spending. Trade openness is also associated with economic liberalization, and the negative coefficient reflects the tendency of governments pursuing liberal policies to emphasize balanced budgets as well as increased trade.

The variable *Political Rights* is positive and significant at the 1% confidence level. A single standard deviation rise in the political rights variables produces a 1.23% increase in government spending (as a percent of GDP). This result implies that, even in the era of neoliberal reforms of state cutbacks and reductions of national budgets, increasing levels of democracy allows Latin American citizens to pressure elected officials. This finding is consistent with previous studies on democracy and government spending, particularly that democratic countries are associated with higher levels of social spending in Latin America (Avelina, Brown, Hunter, 2005). *Previous decade spending* is positive and statistically significant at the 1% confidence level, as expected given the inertia in all budgets. *Inflation* shows no significant effect.

Model (2) is a comparison between *One-Term Limit Countries vs. Two-Term Limit Countries*. Both forms of term limits have a positive and statistically significant effect on government spending at the 1% confidence level. However, there is a slight spending difference between termed out presidents in two-term countries who increase government spending by .96% of GDP, while termed out presidents in one-term countries increase government expenditures by 1.32% of GDP. This difference is statistically significant. These results contrast with those of Johnson and Crain (2004) who find that one-term limit countries spend more than two-term limit countries.

In Model (3) and (4) I include *Congressional majority* to capture the fraction of seats held by the government and analyze if an increasing number of veto players forces presidents to

increase spending. *Congressional majority* comes up with the wrong sign, but never reaches statistical significance. The non-significance of *congressional majority* may reflect the centralized nature of budget making in many Latin American countries. Specifically, presidents and cabinets have enhanced budgetary power, and an increase in party system fragmentation may not necessarily lead towards deficit. The *Termed Out* variable stays positive and significant at the 1% confidence level.

Table 3 test if presidents' ideology affects government spending. In Model (5) and (6) I control for Presidential *Ideology* with the inclusion of two dummies: *Left-Wing* and R*ight-Wing* dummies. While R*ight-Wing* presidents fail to reach statistical significance, *Left-Wing* presidents have a negative relationship with government expenditures. Unlike the results found in Leblang (2002), where incumbents, especially from left-wing parties, face strong incentives to engage in unsustainable expansionary economic policies, my results suggest otherwise. This unexpected negative relationship may imply that leftist presidents were under more pressures from international financial institutions or nervous foreign investors to implement structural adjustments and balance budgets. Lastly, in Model (7) and (8) I control for non-concurrent *Legislative elections*, in order to explore if congressional elections motivate higher levels of spending as a way for presidents to influence the composition of the legislature. Ironically, while significant - the sign is negative and contrary to the predictions found in election cycle studies. However, while this finding seems counterintuitive for a region plagued by poverty, unemployment and politicians' eagerness to increase their chances of staying in office, through pre-electoral manipulation, recent evidence found that Brazilian voters reward parties that run surplus than those who increase the deficit prior to elections (Arvate, Avelina, and Taraves, 2009). So our standard image may be outdated.

Table 3: Effects of Presidential Time Horizons on Government Expenditures % of GDP (1970-2009)

Dependent Variable	(5) Gov. Ex *% of GDP*	(6) Gov Ex *% of GDP*	(7) Gov Ex. *% of GDP*	(8) Gov Ex. *% of GDP*
Specification	OLS	OLS	OLS	OLS
Termed Out	.1223***		.1243***	
	(.019)		(.0214)	
Termed Out (One-Term)		.1154***		.1193***
		(.0176)		(.0195)
Termed Out (Two-Term)		.1563***		.1492**
		(.0647)		(.0639)
Presidential Elections	.0033	.0030	-.0068	-.0069
	(.0255)	(.0255)	(.0255)	(.0255)
Income per Capita	-.0761***	-.0767***	-.0702***	-.0708***
	(.0246)	(.0246)	(.0251)	(.0249)
Population	-.0592***	-.0603***	-.0580***	-.0588***
	(.0175)	(.0174)	(.0175)	(.0174)
Population Density	.0500***	.0522***	.0536***	.0551***
	(.0093)	(.010)	(.0115)	(.0129)
Inflation	.0115**	.0134**	.0104	.0119
	(.0053)	(.0061)	(.0055)	(.0062)
Trade Openness	-.1327***	-.1270***	-.1412***	-.1369***
	(.0323)	(.0342)	(.0326)	(.0343)
Political Rights	.0645***	.0643***	.0655***	.0654***
	(.0092)	(.0093)	(.0096)	(.0096)
Previous Decade Spending Control	.7822***	.7797***	.7831***	.7813***
	(.0165)	(.0158)	(.0165)	(.0163)
Congressional Majority	.1186	.1108	.1050	.0995
	(.0942)	(.0902)	(.0931)	(.0889)
Left Presidents	-.0976**	-.0972**	-.0999**	-.0996**
	(.0444)	(.0445)	(.0471)	(.0469)
Right Presidents	-.0372	-.0352	-.0371	-.0357
	(.0402)	(.0383)	(.0414)	(.0394)
Non-Concurrent Legislative Elections			-.1271**	-.1253**
			(.0510)	(.0497)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.89	0.89	0.89	0.89
No. Observations	391	391	391	391
Constant	1.75	1.75	1.72	1.71

*significant at the 0.05 level; **significant at the 0.01 level; ***significant at the 0.001 level. Standard errors are in the parenthesis. Model (5) dummy 1996 significant and negative due to the negative effect from the 1995 Mexican Tequila Crisis on Latin American economies.

Overall, the term limits variable, *Termed Out* remains significant throughout all eight models, which illustrates the strong effect of this time constraint on presidential spending behavior. Moreover, the insignificance of the *presidential election year* variable implies that previous findings on political-economic cycles were caused by the inclusion of termed out executives. Hence, in order to accurately capture how presidential incentives transform over time, and subsequently influence government spending, previous studies on election cycles must revisit how to conceptualize time horizons. As my results suggest, termed out presidents behave differently around election times than presidents with re-election opportunities.

ROBUSTNESS CHECKS

In order to analyze how robust the effect of term limits, I run a series of additional tests. First, I split the data by two distinct periods: (1990-2009) and (2000), to check if my results are sensitive to time specific trends. In this analysis, I also use an interaction to further analyze my term limits with presidential ideology. Second, I include a *South American* dummy, as a way to capture any region specific effects. Lastly, I use an alternative fiscal variable: P*rimary Balance*. Since primary balance excludes debt-service payments and eliminates the effects of prior deficits on the current one, it provides a way to understand actual spending in any given year (Neto and Borsani, 2004). The years for which primary balance data are available range from 1990 until 2009.

Table 4 and 5 analyzes the effect of time horizons on government spending from 1990 to 2009, a period notably characterized by neo-liberal economic reforms. My variable of interest, *Term Limits*, remains positive and significant throughout all models, but its magnitude is reduced, as would be expected during a time when international economic pressures to keep

budgets balanced have been much stronger than they were historically in Latin America. The termed out variable in Model (1) has a coefficient of .0867. This implies government expenditures increase from 7.94 % to 8.6 % of GDP when an incumbent faces a final term. The spending increase, however, reduces in magnitude during this time period: 0.66% of GDP. *Presidential Elections* remains negative throughout these models but never reaches statistical significance. Model (2) captures the different effects of *One-Term Limit Countries vs. Two-Term Limit Countries*. Similar to previous results, termed out presidents in two-term countries spend more than lame ducks in one-term countries. The most important result of looking at the 1990 to 2009 period separately is to show that the effect of term limits is not just an artifact of the initiation of presidential reelection in a number of countries during periods when economic policies were more liberal than in the past.

In Model (3) I test for the influence of party fragmentation on government expenditures. *Congressional majority*, while highly significant, comes up with the wrong sign. A possible explanation for this unexpected finding may be rooted in the unconventional turn by many Latin American presidents to adopt structural adjustment economic reforms throughout the 1990s. The controversial policy switch may have forced many Latin American presidents to buy more support from their own party to carry out these measures. For example, during the 1990s Argentinean President Carlos Menem of the Peronist party found himself undermining fiscal reform efforts by transferring subsides to pay off Peronist governors of several backward states in return for legislative support of economic reform at the national level (Wibbels, 2000). All other control variables remain with their original sign and statistical significance, except *Trade Openness*, which loses its significance once the *Congressional majority* variable is included.

Table 4: Effects of Presidential Time Horizons on Government Expenditures as % of GDP (1990-2009)

Dependent Variable	(1) Gov. Ex *% of GDP*	(2) Gov Ex *% of GDP*	(3) Gov Ex. *% of GDP*	(4) Gov Ex. *% of GDP*
Specification	OLS	OLS	OLS	OLS
Termed Out	.0867***		.0631***	
	(.0196)		(.0212)	
Termed Out (One-Term)		.0686***		.0480**
		(.0191)		(.0228)
Termed Out (Two-Term)		.1549**		.1233*
		(.063)		(.0639)
Presidential Elections	-.0166	-.0173	-.0069	-.0075
	(.0286)	(.0290)	(.0291)	(.0292)
Income per Capita	-.1027***	-.1076***	-.1355***	-.1383***
	(.0239)	(.0240)	(.0209)	(.0219)
Population	-.0404***	-.0408***	-.0214	-.0225
	(.0150)	(.0147)	(.0180)	(.0182)
Population Density	.0719***	.0788***	.0877***	.0930***
	(.0070)	(.0065)	(.0115)	(.0113)
Inflation	.0057	.0107	.0075	.0117
	(.0082)	(.0096)	(.0090)	(.0104)
Trade Openness	-.1017***	-.0830***	-.0627	-.0477
	(.0300)	(.0296)	(.0366)	(.0372)
Political Rights	.0609***	.0593***	.0426***	.0416***
	(.0090)	(.0093)	(.0128)	(.0129)
Previous Decade Spending Control	.7294***	.7207***	.7133***	.7070***
	(.0180)	(.0161)	(.0208)	(.0204)
Congressional Majority			.2861***	.2711***
			(.1038)	(.1037)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.87	0.87	0.88	0.88
No. Observations	316	316	313	313
Constant	1.76***	1.76***	1.57***	1.54***

*significant at the 0.05 level; **significant at the 0.01 level; ***significant at the 0.001 level. Standard errors are in the parenthesis. Year dummies are negative but never reach significance throughout these models.

In Table 5, Model (5) and (6) is a test of whether *Presidential Ideology* has an effect on government spending in the 1990 to 2009 period. Neither *Left-Wing* nor *Right-Wing* presidential dummy variables reach statistical significance, a signal that presidents confronted rigid international pressures in the era of neoliberal reforms. This suggests that during the region's reform process, presidents - regardless of party affiliation - were often ignoring the demands of

their constituent base. Another possible explanation for why presidential ideology fails to reach significance is due to the limitations of testing the leaning of a single party (i.e. the presidents in power). According to Neto & Borsani, (2004), since Latin American presidents typically govern with a coalition, measuring presidential ideology does not capture the ideological influence of other parties and cabinet members.

In Model (7) and (8) I control for non-concurrent *Legislative elections*. While highly significant, non-concurrent legislative elections have an unexpected negative sign.

As argued above, this unexpected finding may be the result of voters' history with run away inflation or elected officials' ability to generate economic growth and yet constrain spending. Another possible explanation, however, is provided by Remmer (1993), who argues that pre-electoral spending does not always occur in Latin America, but instead, post-election when executives are in need of building and forming the legislative coalitions required to pass the policies they promised during the campaigns.

Table 5: Effects of Presidential Time Horizons on Government Expenditures % of GDP (1990-2009)

Dependent Variable	(5) Gov. Ex *% of GDP*	(6) Gov Ex *% of GDP*	(7) Gov Ex. *% of GDP*	(8) Gov Ex. *% of GDP*
Specification	OLS	OLS	OLS	OLS
Termed Out	.0679***		.0697***	
	(.0226)		(.0231)	
Termed Out (One-Term)		.0518**		.0564***
		(.0209)		(.0209)
Termed Out (Two-Term)		.1253*		.1166
		(.0652)		(.0643)
Presidential Elections	-.0056	-.0061	-.0200	-.0200
	(.0273)	(.0273)	(.0274)	(.0274)
Income per Capita	-.1278***	-.1315***	-.1225***	-.1256***
	(.0276)	(.0276)	(.0262)	(.0255)
Population	-.0238	-.0247	-.0220	-.0228
	(0188)	(.0189)	(.0185)	(.0187)
Population Density	.0807***	.0860***	.0872***	.0914***
	(.0104)	(.0101)	(.0106)	(.0114)
Inflation	.0114	.0154	.0094	.0127
	(.0077)	(.0092)	(.0083)	(.0096)
Trade Openness	-.0825*	-.0680	-.0902**	-.0781*
	(.0380)	(.0367)	(.0381)	(.0366)
Political Rights	.0464***	.0451***	.0461***	.0450***
	(.0107)	(.0108)	(.0106)	(.0106)
Previous Decade Spending Control	.7275***	.7204***	.7250***	.7193***
	(.0258)	(.0242)	(.0242)	(.0230)
Congressional Majority	.2471**	2307**	.2413**	.2281**
	(.1077)	(.1057)	(.1067)	(.1038)
Left-Wing President	-.0839	-.0797	-.0825	-.0791
	(.0528)	(.0519)	(.0551)	(.0537)
Right-Wing President	-.0241	-.0176	-.0237	-.0184
	(.0512)	(.0478)	(.0520)	(.0484)
Non-Concurrent Legislative Elections			-.1565***	-.1528***
			(.0584)	(.0569)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.88	0.88	0.88	0.88
No. Observations	311	311	311	311
Constant	1.63	1.61	1.62	1.60

*significant at the 0.05 level; **significant at the 0.01 level; ***significant at the 0.001 level. Standard errors are in the parenthesis. Year dummies are included. In this analysis, there are no year dummies that reach statistical significance in all 4 models.

Table 6 analyzes the effect of presidential time horizons from 2000 to 2009. My variable of interest, *Term Limits*, remains positive and significant at the 1% level. The effect of a termed out president implies that government spending increases from 7.41 % to 8.78 % of GDP. The spending increase by termed out presidents is at its highest during the 2000 to 2009 period: +1.37 % of GDP. *Presidential Elections* variable has a negative relationship with spending in this time period but never reaches statistical significance. *Income per capita* loses its significance in this time period, but all other control variables remain with their original sign and statistical significance. Model (2) captures the different effects of *One-Term Limit Countries vs. Two-Term Limit Countries*. The effect remains robust during this time period: presidents in two-term institutions spend slightly higher (1.31% of GDP) than termed out presidents in one-term countries (1.13% of GDP). In Model (3) I include *Congressional Majority*, but while the variable comes up with the wrong sign, it never reaches statistical significance. Model (4) controls for presidential ideology but both dummies never reach statistical significance.

Table 6: Effects of Presidential Time Horizons on Government Expenditures % of GDP (2000-2009)

Dependent Variable Specification	(1) Gov. Ex. *% of GDP*	(2) Gov. Ex. *% of GDP*	(3) Gov. Ex. *% of GDP*	(4) Gov. Ex. *% of GDP*
Termed Out	.1698*** (.0246)		.1444*** (.0297)	.1482*** (.0360)
Termed Out (One-Term)		.1267*** (.0228)		
Termed Out (Two-Term)		.2639*** (.0828)		
Presidential Elections	-.0097 (.0203)	-.0159 (.0191)	-.0065 (.0213)	-.0052 (.0202)
Income per Capita	-.0185 (.0346)	-.0178 (.0394)	-.0474 (.0334)	-.0320 (.0488)
Population	-.0581*** (.0132)	-.0564*** (.0132)	-.0519*** (.0121)	-.0496*** (.0125)
Population Density	.0344*** (.0062)	.0488*** (.0100)	.0470*** (.0097)	.0405*** (.0099)
Inflation	.0225 (.0139)	-.0201 (.0146)	-.0299** (.0127)	-.0228*** (.0164)
Trade Openness	.1220*** (.0271)	-.0718 (.0176)	-.1081*** (.0193)	-.1109*** (.0215)
Political Rights	0664*** (.0114)	.0716 (.0145)	.0629*** (.0129)	.0705*** (.0149)
Previous Decade (Spending Control)	.7839*** (.0200)	.7666 (.0155)	.7621*** (.0230)	.7763*** (.0317)
Congressional Majority			.2864 (.1584)	.2896 (.1734)
Left-Wing Presidents				-.0944 (.0908)
Right-Wing Presidents				-.0725 (.0787)
R-Squared	0.89	0.89	0.90	0.90
No. Observations	171	171	171	171

*significant at the 0.05 level; **significant at the 0.01 level; ***significant at the 0.001 level. Standard errors are in the parenthesis. Year Dummies: Model (1) 2007-2009 negative and significant; 2008 is negative and highly significant. Model (2) 2006-2009; 2001 & 2003; Model (3) 2001 & 2003-2004; 2006-2009. Model (4) 2001 & 2003 is negative and significant, and 2007-2008.

Term Limits & Presidential Ideology

Table 7 further investigates the effect of presidential ideology through an interaction I create with my term limits variable: *Termed Out*Right-Wing* and *Termed Out*Left-Wing*. I find

that spending associated with my *Term Out* variable in this study is actually driven by right wing presidents throughout the period of 1970 to 2000. Model (1) illustrates a positive relationship between my interaction, *Termed Out*Right-Wing,* and spending associated from 1970 to 2009. Specifically, a one unit change increases spending by 1.12% of GDP. I further break up the data by time period: 1980s, 1990 to 2000, and 2000s. Model (2) and Model (3) continue to support the relationship that right wing presidents increase spending before elections in the 1980s and 1990 to 2009 period. While this result is surprising - given that left wing presidents have traditionally been associated with increases in electoral year spending (Leblang, 2002) - in fact, it has been right wing parties that have strong reputations for patronage, delivering goods and pork before elections.

On the other hand, in countries with fewer parties, such as Argentina and Mexico, leftist parties are associated with clientelism but also expensive programmatic policies that benefit their constituents.[2] The *Termed Out*Left Wing* interaction never achieves statistical significance until 2000s, when the theoretical effect associated with increases by lame duck presidents takes place by both right wing and left wing actors. In fact, Model (4) illustrates that, during the 2000s, left wing presidents increase spending slightly higher at 1.21% of GDP compared to right wing presidents who increase spending by 1.15% of GDP. This result draws further attention to the complexities behind electoral year spending.

[2] I thank Barbara Geddes for this insight.

Table 7: Effects of Presidential Time Horizons on Government Expenditures % of GDP
Termed Out * Ideology Interaction

Dependent Variable Specification	(1) Gov. Ex. *% of GDP* (1970-2009)	(2) Gov. Ex. *% of GDP* (1980-1990)	(3) Gov. Ex. *% of GDP* (1990-2009)	(4) Gov. Ex. *% of GDP* (2000-2009)
Termed Out	.1188***	.1154***	.0782***	.1475***
Right-Wing	(.0168)	(.0510)	(.0172)	(.0232)
Termed Out	.0611	.0105	.0277	.1980***
Left-Wing	(.0361)	(.0505)	(.0522)	(.0420)
Presidential Elections	-.0030	.0154	-.0135	-.0019
	(.0267)	(.0461)	(.0285)	(.0196)
Income per Capita	-.0784***	-.1511	-.1134***	-.0289
	(.0194)	(.0847)	(.0216)	(.0301)
Population	-.0634***	-.1303***	-.0366***	-.0601***
	(.0146)	(.0253)	(.0171)	(.0137)
Population Density	.0514***	-.0168	.0758***	.0426***
	(.0054)	(.0378)	(.0067)	(.0061)
Inflation	.0071	-.0209	.0066	-.0253
	(.0059)	(.0214)	(.0081)	(.0143)
Trade Openness	-.1502***	-.3407***	-.1064***	-.1158***
	(.0254)	(.0700)	(.0295)	(.0249)
Political Rights	.0731***	.0350*	.0539***	.0679***
	(.0089)	(.0176)	(.0096)	(.0130)
Previous Decade	.7689***	.9393***	.7246***	.7684***
(Spending Control)	(.0123)	(.0270)	(.0193)	(.0165)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.88	0.95	0.87	0.89
No. Observations	394	93	314	170
Constant	1.96	3.95	1.84	1.38

*significant at the 0.05 level; **significant at the 0.01 level; ***significant at the 0.001 level. Standard errors are in the parenthesis. Model 1: 1995-96, 2001-05, 2007-08 are negative year dummies. The Mexican peso crisis negatively impacts the region in 1995 and remains until the end of the 1990s. 2001 and 2007 mark years of global economic slowdown.

South American Dummy

In Table 8 I include a South American dummy to test for whether regional differences affect my findings. The *South American* dummy is negative and significant at the 1% confidence level. This implies that the spending increase by termed out presidents in South America is from 6.86% to 7.76 % of GDP.

Table 8: Effects of Presidential Time Horizons on Government Expenditures % of GDP
South American Dummy

Dependent Variable	(1) Gov. Exp. % of GDP	(2) Gov. Exp. % of GDP	(3) Gov. Exp. % of GDP	(4) Gov. Exp. % of GDP
Specification	OLS	OLS	OLS	OLS
Termed Out	.1235***	.1180***	.1231***	.1251***
	(.0134)	(.0139)	(.0172)	(.0187)
Presidential Elections	-.0025	.0012	.0032	-.0066
	(.0238)	(.0235)	(.0234)	(.0239)
Income per Capita	-.0540***	-.0579***	-.0609***	-.0555**
	(.0198)	(.0192)	(.0231)	(.0237)
Population	-.0793***	-.0765***	-.0732***	-.0717***
	(.0137)	(.0147)	(.0163)	(.0162)
Population Density	-.0336***	-.0287**	-.0180	-.0133
	(.0080)	(.0111)	(.0125)	(.0130)
Inflation	.0068	.0077	.0097	.0087
	(.0051)	(.0053)	(.0050)	(.0051)
Trade Openness	-.2290***	-.2166**	-.2070***	-.2139***
	(.0231)	(.0274)	(.0300)	(.0295)
Political Rights	.0809***	.0751***	.0720***	.0729***
	(.0080)	(.0088)	(.0089)	(.0090)
Previous Decade Spending Control	.6956***	.7013***	.7186***	.7206***
	(.0196)	(.0197)	(.0210)	(.0207)
South American Dummy	-.2570***	-.2468***	-.2104***	-.2067***
	(.0371)	(.0372)	(.0366)	(.0360)
Congressional Majority		.0687	.0671	.0550
		(.0776)	(.0878)	(.0862)
Left-Wing Presidents			-.0723	-.0750
			(.0393)	(.0418)
Right-Wing Presidents			-.0346	-.0345
			(.0368)	(.0379)
Non-Concurrent Legislative Elections				-.1225**
				(.0489)
Year Dummies	Yes	Yes	Yes	Yes
R-Squared	0.89	0.89	0.89	0.89
No. Observations	397	394	391	391
Constant	2.773***	2.67***	2.53***	2.41

*significant at the 0.05 level; *significant at the 0.01 level; *significant at the 0.001 level. Standard errors are in the parenthesis. 1997 is negative and significant in Model 1 and 2. In these models, ideology does not reveal statistical significance.

This increase is approximately > 1% of GDP. In comparison, when *South America* equals zero in the regression equation, government spending rises from 8.87 % to 10.03 % of GDP when an incumbent is termed out - a spending increase of 1.16% of GDP. Overall, the inclusion of a South American dummy isolates a region specific effect. Not only is average government spending (as a percent of GDP) lower for South American countries, but also the spending increase associated with termed out presidents. Controlling for region does not affect the basic results, however.

Alternative Dependent Variable: Primary Balance (1990-2009)

In the following analysis, Table 9 presents the effect of my variable of interest against *primary balance* as an alternative fiscal outcome. I opt for primary balances because it excludes debt service payments, which eliminates the effects of previous deficits on the current one (Neto & Borsani, 2004). Similar to the previous analyses throughout this chapter, the following employs the empirical model provided by Johnson and Crain (2004), with the inclusion of a *Presidential Elections* year dummy to capture the spending predictions of electoral studies. I also include a control for lagged *% Growth Rate* because positive economic performance increases a government's ability to spend more, if desired.

In Model (1), the coefficient on T, the indicator variable for incumbents who cannot stand for re-election, is -1.59 and statistically significant at the 1% confidence level, which indicates that a standard deviation difference yields a -3.86% decrease in primary balance. A reduction in primary balance implies that termed out presidents spend higher than what they receive in

revenues. This result continues to support my claim that termed out presidents have a negative effect on fiscal outcomes.[3]

Table 9: Effects of Presidential Term Horizons on Primary Balance (1990-2009)

Dependent Variable	(1) Balance % of GDP	(2) Balance % of GDP	(3) Balance % of GDP	(4) Balance % of GDP
Specification	OLS	OLS	OLS	OLS
Termed Out	-1.59***	-1.71***	-1.67***	-1.63***
	(.292)	(.278)	(.275)	(.293)
Presidential Elections	-.6414	-.5933	-.5991	-.5915
	(.4174)	(.4277)	(.4318)	(.4094)
% Growth Rate	.0619	.0711	.0815*	.0874*
(Lagged)	(.0418)	(.0429)	(.0400)	(.0421)
Income per Capita	.6403***	.3866	.3532	.3701
	(.237)	(.326)	(.295)	(.3243)
Population	.5446	.5784***	.8879***	.8701***
	(.208)	(.199)	(.2292)	(.2296)
Population Density	.1171	.1944	.8640***	.8503***
	(.207)	(.1873)	(.200)	(.1649)
Inflation	.3792***	.3928***	.3293***	.2323**
	(.110)	(.1033)	(.0994)	(.1001)
Trade Openness	.3869	.4346	1.70***	1.794***
	(.353)	(.3515)	(.5142)	(.5381)
Political Rights	-.0783	-.1526	-.3056*	-.2701
	(.1421)	(.1493)	(.1474)	(.1640)
Primary Balance	.1713***	.2082***	.1030*	.1031*
(1990 Base)	(.0321)	(.0501)	(.0531)	(.0545)
Congressional		1.833	2.086	2.18*
Majority		(1.22)	(1.12)	(1.10)
South America			1.788***	1.68***
			(.350)	(.362)
Left-Wing President				.8518**
				(.3700)
Right-Wing President				.2259
				(.3078)
R-Squared	0.45	0.46	0.48	0.48
No. Observations	255	252	252	250

*significant at the 0.05 level; *significant at the 0.01 level; *significant at the 0.001 level. Standard errors are in the parenthesis. Model (1) negative and significant year dummies:2001; negative and significant: 2006-2007 positive and significance due to solid economic performance driven by a commodity boom. Model (2) positive and significant year dummies: 2006-2007. Model (3) negative and significant year dummies: 1998-1999 & 2001-2002. Model (4) negative and significant year dummies: 1998-1999 & 2001-2002. 1998-1999 are negative and significant because of the instability among many emerging economies during the late 1990s. The effect related to 2001-2003 is due to the 2001 Argentinean debt default, which negatively impacts Latin American economies.

[3] I also tested for differences between one two and two term countries. Only one-term regimes reveal significance, with a coefficient at -1.82.

Presidential Elections has the expected negative effect but never reaches statistical significance. *Income per capita*, unlike previous findings, has the expected positive and significant relationship with primary balance. Accordingly, as citizens' incomes increase in the Latin America region, governments are able to increase taxes. *Inflation* has a positive and highly significant effect on primary balance. The *Political Rights* variable loses its significance in this analysis.

In Model (3) I include a *South American* dummy. Similar to previous findings, this variable captures a region specific effect. The South American region continues to yield an improvement in fiscal outcomes, as primary balance improves by 1.75 %. *Trade Openness and lagged Economic Growth (%)* are positive and significance once the South American dummy is included. These results are expected, increases in trade allocate greater resources for governments, as solid economic growth allows government to increase spending without necessarily causing deficits. Model (4) controls for presidential ideology. Similar to previous results, *Left-Wing* presidents have a positive and significant affect on primary balance.

Concluding Remarks and Future Research

This study has four main findings. First, this study supports the claim that term limits have an effect on politicians' spending decisions. Between 1970 and 2009, I find a 1% increase in government expenditures (as a percent of GDP) by lame duck presidents compared to incumbents with re-election opportunities. In order to verify the validity of my results, I run a serious of robust tests, either by splitting the data by time periods or utilizing primary balance as an alternative fiscal outcome. Throughout all tests, the effect of *Term limits* has a positive and statistically significant effect on government spending (as a percent of GDP). The effect of term

limits on government expenditures decreases to .66% of GDP during the 1990 to 2009 period, but increases to an all time high of 1.34% of GDP from 2000 to 2009. Moreover, I find that primary balance deteriorates by -3.86% when presidents are termed out.

Second, unlike previous studies on Latin American electoral cycles, I test for the influence of term limits with the inclusion of a *Presidential Elections* year dummy. This test leads to an unexpected but important empirical finding for future research. Specifically, while I find that term limits are associated with an increase in government expenditures, the inclusion of an election year dummy fails to reach statistical significance across all models. The failure to distinguish executive type is a main flaw in electoral studies. Most regressions utilize a simple election year dummy, which takes a 1 for election year and a 0 otherwise (Neto & Borsani, 2004; Shi & Svensoon (2006); Brender & Drazen, 2005; Nieto-Parra & Santiso, 2009). This specification does not differentiate whether the type of presidential candidate up against the election: presidents with re-election opportunities or those who are termed out.

For example, Nieto & Borsani (2004) find a negative relationship between elections and primary balance. These findings are similar to the results found in Table 7 of this study, but my negative relationship is *only* associated with termed out presidents not with the electoral cycle per se. Thus, my control for termed out presidents captures a distinct electoral cycle finding: termed out presidents are related to the deterioration in primary balance. So while a deficit political cycle may be present in new democracies, the spending increase is not due to electoral manipulation of a naïve electorate but instead driven by executives not having the incentive to control spending. Overall, my findings question the assumption in the literature that politicians are often manipulating budgets to ensure their survival. Thus, Latin American elections have

been overestimated as causing fiscal disturbances, and the effects of presidential elections on fiscal outcomes are far more complex than the literature has theorized and empirically tested.

Third, I find an unexpected relationship when I control for *Presidential Ideology*. From 1970 to 2009, I find a negative relationship between *Left-Wing* presidents and government expenditures (as a percent of GDP). When the analysis starts in 1990s, however, both *Left-Wing* and *Right-Wing* variables never reach statistical significance. This implies that Latin American presidents faced stiff international pressures to implement a specific set of policy measures, and presidents were limited in their ability to implement the preferences of their constituent base.

I further investigate the effect of ideology. I use an interaction to understand if political leanings influence the spending habits of termed out presidents: *Termed Out*Right-Wing* and *Termed Out*Left-Wing*. I discover that the spending associated with my *Term Out* variable in Table 1 is actually driven by right wing presidents throughout the period of 1970 to 2000. Specifically, termed out right wing presidents are associated with an increase in spending by 1.12% of GDP. I further break up the data by time periods: the 1980s, 1990 to 2009s. I find the same pattern in the 1980s and 1990 to 2009: termed out right wing presidents are the driving force behind the associated electoral spending increase. Substantively, this result is not surprisingly. In countries with fragmented parties, such as in Brazil or Peru, right wing parties have traditionally used patronage before elections, and have done extremely well among the poor. It isn't until the 2000s when the general effect of term limits starts to generate among both right and left wing presidents. In fact, left wing presidents increase spending slightly higher during this period at 1.21% of GDP compared to right wing presidents at 1.15% of GDP.

Lastly, I isolate a regional *South American* effect. South American countries have lower government spending and increases in spending by termed out presidents are slightly lower than

Central American lame ducks. In sum, this chapter presents a nuance approach to test the effect of elections on fiscal outcomes. My central finding is that the spending associated with previous studies has been the result of a failure to differentiate between the types of presidents at election time. Specifically, I claim that one must differentiate between candidate types - termed out presidents or presidents with re-election opportunities. The inclusion of term limits with an election year dummy serves as an important vehicle for understanding time horizons and politicians' incentives. While the two-term rule limit is relatively new in Latin America, these preliminary results support the theory that term limit rules do affect fiscal outcomes in different ways. This finding creates new avenues of research to disentangle the potential impact that termed out presidents have on other standard macroeconomic policy variables such monetary and trade policy, as well as the trade-off between employment and inflation.

Summary of Variables					
Variable	Obs.	Mean.	St. Dev.	Min.	Mean.
Termed Out	442	0.44344	0.49735	0	1
Termed Out (One-Term)	442	0.38235	0.48651	0	1
Termed Out (Two Term)	442	0.06109	0.23976	0	1
Income Per Capita (Ln)	443	8.76557	0.49591	7.48202	9.81902
Population (Ln)	443	9.31847	1.10322	7.45906	12.1998
Population Density (Ln)	443	3.49281	0.88251	1.66307	5.69523
Inflation (Ln)	443	3.97596	0.54984	2.3359	5.36382
Trade Openness (Ln)	443	3.97596	0.54984	2.3359	5.36382
Political Rights	423	2.18203	0.93508	1	7
Initial Spending (Ln)	443	2.09803	0.56272	0.95308	3.31448
Growth Rate % of GDP	443	3.38759	3.94189	-11.8	18.3
Majority	421	0.51971	0.15763	0.09278	0.99497
Ideology of President	423	1.52246	1.00182	0	3
Executive Elections	425	0.20706	0.40568	0	1
Legislative Elections	425	0.24	0.42759	0	1
Presidential Power	443	15.4532	0.56272	0.95308	3.31448
Primary Balance	276	1.33424	2.46159	-6.74	9

Chapter 4

The Politics of Budget Manipulation: Post-Crisis Argentina

> "Evidence indicates that the structure of budgetary institutions is a key determinant of fiscal outcomes; hierarchical institutions contribute to better fiscal policy design by limiting opportunities for politically motivated budget making."
>
> *The Political Economy of Budget Deficits*
> (Leachman et al., 2007)

In the midst of a political and economic crisis, outsider Peronist candidate, Néstor Kirchner rose to the national scene. While his 2002 electoral victory represented a mere 22 percent of the popular vote, in many respects, Kirchner's presidency is accurately described as a period where the largest concentration of power occurred in Argentina's modern democratic history.[1] One of the first signs of his executive dominance was visible within months of his term, when strongly favorable public opinion influenced the Argentinean Congress to approve laws it had rejected in prior months (Cheresky, 2004). By 2005, with a solid congressional majority, Kirchner made a strong case for an extension of budgetary superpowers that allocated him prerogatives to recompose the budget as he saw fit; these powers were not only approved, but made permanent, centralizing further presidential power over the annual budget. Consequently, given Argentina's strong presidential powers, high popularity and the country's sudden economic spurt, Kirchner had all the tools to lead the country's policy making process.

The decade under Kirchner's rule presents an opportunity to investigate a third theory in the literature on fiscal policy that asserts if presidents (and their cabinets) control the budget

[1] The Economist Print Edition (2006). Argentina's Presidency, not so super power, Nestor Sidelines Congress and the courts. <www.economist.com/node/7281097>.

process it will increase fiscal responsibility by limiting opportunities for politically motivated budget making (Leachman, Guillermo, Lange& Bester (2007); Alesina, Hausmann, Hommes & Stein (1999); Baldez and Carey (1999)).[2] These claims are based on the assumption that executives have stronger incentives to control spending, than do legislators, in order to improve overall economic performance .

This chapter demonstrates that while an impressive commodity boom in the last decade presented presidents in Latin America with the opportunity to balance budgets, the arguments advanced by the hierarchical budgetary literature are not consistent with reality in Argentina – an extreme case of high executive control over the budget. In fact, full executive control of the budget has nourished politically motivated spending decisions in a post-crisis society. Indeed, budgetary institutions are stable over time, as advanced by Leachman et al. (2007); but the assumption in this literature, assuming legislators are the only actors with the desire to augment the budget, are devoid of evolving political realities that diminish even executives' incentive to initiate spending controls.

As this case study illustrates, amid the political vacuum after the 2002 financial crisis and Argentinean's mounting dissatisfaction with all its political leaders, Néstor Kirchner—armed with an *anti-neoliberal* discourse—emerges as the first candidate to revive its citizen's faith in the traditional political structures. Accordingly, in the face of an institutional crisis, Kirchner capitalizes on the opportunity to increase his political presence throughout the Argentinean landscape. While negating his predecessors policies, Kirchner, nevertheless, returned to

[2] Stein, et al (1998) and Alesina et al (1999) analyzed legal institutions that imposed limits on government spending and debt capacities at the sub-national level. These studies assert the important role of the president in controlling budget process in order to have the best deficit reducing/debt sustainability capacities. A case study of Chilean fiscal policy finds that budget institutions (i.e. rules and procedures created during the re-drafting of the Chilean constitution in 1980 were aimed at constraining civilian elected politicians to enact fiscal austerity. These authors assure that these institutions are the reason behind the fiscal restraint and stability during the ensuing years of 1985-1996 (Baldez and Carey, 1999).

Peronism's most effective political weaponry— *clientelism*— to co-opt segments of the population, and succeeded in using the strong presidential powers within Argentinean political institutions to manipulate government expenditures. The public purse became his primary tool to co-opt non-Peronist political forces, opposition legislators with public works projects, while also subsidizing his preferred private sector associates. According to Svampa (2008), the events that proceeded Néstor's rise "demonstrated once more Peronism's capacity to redefine the political landscape, forcing all other actors to reposition themselves in relation to the apparent ruptures it has enacted" (82).

It is worth to note that Argentina's economic crisis prior to Kirchner's rise left the country not only with a political vacuum, but reinforced a level of uncertainty among its citizens that had been present throughout the 1990s neoliberal era. Since the initiation of economic reforms, unemployment levels increased, particularly among state employees, while real industrial wages maintained a declining trend throughout the 1990s decade (Murillo, 1997). Not surprisingly, Kirchner's confrontational stance against the status-quo in line with neoliberal policies brought a sense of relief to a population that had recently confronted one of its worst economic crises ever. Moreover, with his main opponents disintegrated and discredited for their support for the economic policies that many viewed as the reason behind the 2002 crisis, high growth rate and presidential powers allocated Kirchner various resources to amass unusual levels of power.

In order to develop this thesis, this chapter proceeds as follows: Section (1) discusses the Argentinean budgetary procedures and the extent of Congressional influence on the final budget. It illustrates that while the budget process consists of various stages, the Executive Branch is the leading actor in the Argentinean budget process with capacity to control spending, if desired. To

specify the factors which facilitate Executives budgetary spending, I discuss three areas: (a) the executive's ability to modify the composition of the budget without congressional approval, (b) fiduciary funds, and (c) decree powers. Section (2) is an analysis of Argentina's spending levels in comparison to other South American countries, and point out the importance of not only analyzing government consumption levels but also domestic investment. Section (3) discusses the Kirchner administration throughout the 2000s. This section highlights Kirchner's spending preferences, use of decrees, and further illustrates how fiduciary funds raise incentives to find additional avenues to expand this type of discretionary spending. I focus on the federal government's unquestioned authority over export taxes by highlighting the Kirchner administration's proposed tax increase on farmers. Section (4) concludes with a brief discussion on Argentina's democracy. The findings of this chapter are based on field research during the fall of 2008. Throughout this chapter I rely on interviews with Argentinean government officials, legislators and watch-dog organizations to support my claims. [3] I grant anonymity to all my interviews.

I. The Argentinean Budget and Budgetary Superpowers

There are four stages in the Argentinean budget process: formation, congressional debate (and approval), implementation, and the final stage of evaluation and control (Abuelafia, Berensztein, Braun, and De Gresia, 2009). During the formation stage, a very limited number of actors participate: Ministry of Economy, Chief of Cabinet, and National Budget Office (ONP). The formation stage involves macroeconomic projections and expenditures ceilings, which are then proposed to Congress for the passage of the annual budget.

Contrasting opinions surround the role of the Argentinean Congress control over the

[3] I grant anonymity to all individuals I interview.

budget. Jones (2001) argues that Congress plays a central role in the formation of the annual budget due to the correlation between funds and provinces made up of the President's party, while Rodriguez and Bonvecchi (2004) claim that Congress exerts a weak influence over government expenditures. By analyzing three different time periods, these authors only find marginal additions to the executive's proposed budget. While Jones' (2001) argument rests on negotiations which occur outside of the legislative floor, interviews with various legislators support the conclusion that their role in the budget process is very minimal, whether on the floor or off.

As an opposition legislator noted:

> "I have virtually no say. The budgetary committee deals with formulating the budget. After the recent non-transparent local elections, I advised the committee to increase spending in order to bring greater transparency, but that was only a recommendation."[4]

While Congress is meant to estimate revenues and expenditures, it rarely challenges the executives' proposal or initiates their power to review the execution of the budget (Rose-Ackerman et al., 2010). Moreover, even if legislators are motivated to input in the budgetary process, the Executive Branch enjoys a number of prerogatives to bypass legislators, as explained further below. The centralization of the budget process, however, is supported by sentiments from Secretary of Treasury - who was in charge of formulating the budget from 1993 to 1997. He states:

"I wrote the budget. Once it passed through Congress, and politicians decide what to do, is another issue, but I was the person who formulated the annual budget. I was constantly depicted in newspaper caricatures as the man with the scissors, indicating I was always trying to cut government expenditures."[5]

Jones (2001) argues that executives' tailor the budget to appease legislative desires, and

[4] Interview with opposition member on September 2008.

[5] Interview with Secretary of Treasury on November 14, 2008.

consequently, gain their approval with the passage of the budget, and that these behind the scenes negotiations explain why budgets are passed without much amendment. However, party control over legislators' careers better explains the relative ease of the passage of the budget within the Argentinean context.[6] The norms within parties produce the high party discipline reflected in Argentinean parties. Moreover, strong Argentinean party loyalties stem not only from deputies' desire to run for office again, but also their concern for post-legislative careers. Since most legislators' careers start at the provincial level, where they return on completing their tenure at the state or congressional level, they need the support of party leaders to continue their careers. Hence, Argentinean legislators have good reasons to be party loyalists and almost never vote against party lines while in Congress (Siavelis & Morgenstern, 2008:3).[7]

Accordingly, when the president has a clear congressional majority in Congress, he or she has the ability to lead the policy making process with great ease. Budgetary powers and informal norms allows the Executive Branch to play a much more important role vis-a-via Congress than the formal rules indicate, and, while actors outside the formal process hold vital roles as well - such as provincial governors and international financial institutions - the implementation stage is where most changes occur, leaving the political bargaining done by the Congress almost always unenforceable (Abuelafia et al., 2009).

The lack of congressional input is one important dimension to consider when analyzing the budget process. In the post-2001 crisis era, however, the delegation of power to the Executive to combat the crisis has created various mediums that directed almost all spending power toward

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[6] Party discipline helped Argentinean presidents in the 1990s convince legislators from their own party to internalize the negative externality of fiscal imprudence and enact some level of fiscal reforms (Jones, Sanguinett, Tommasi, 2000).

[7] As a result, provincial party elites and governors are the actors who negotiate on the behalf of Congress, and thus, bring home resources. Due to legislators' concern of political survival and dependence on provincial party elites, the passage of the budget is relatively easy when presidents have solid majority. In recent years, however, provincial

the Executive Branch. While Congress delegated its budgetary prerogatives to the Executive Branch throughout the 1990s, it is evident that after Argentina's financial crisis of 2001, that legislative body relinquished even more power and its role has further diminished in the budget making process and overall fiscal policy.

4.2 Budgetary Superpowers

Budgetary superpowers were introduced by President Eduardo Duhalde during the 2001 financial crisis, which forced Argentina into the greatest loan default in its history, plunging the country into economic and political chaos. Finance Minister Domingo Cavallo called for these emergency superpowers to combat the country's instability, as a way to grant greater leverage for the executive branch to allocate resources as it saw fit. These superpowers were repealed shortly afterward, but under the Kirchner administration, these privileges were reinstated from 2002 to 2006. Later, in 2005, with a solid Congressional majority, President Kirchner made a strong case for an extension of budgetary superpowers for the Executive Branch. The powers were not only approved, but made permanent, centralizing further presidential power over the annual budget.

One of the most important superpowers is the Chief of Cabinet's power to alter budget allocations previously passed without congressional approval (Abuelafia et al., 2009: 35). This mandate is considered central to the Executive Branch's budgetary powers, not only because of the flexibility to reassign budget items at will - without congressional debate - but also because it eliminated a requirement for oversight by auditory agencies when budget items are reallocated.[8]

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governors have lose some of their bargaining power as former Kirchner initiated changes to the tax system that made governors' revenues more dependent on presidential discretion. (Abuelafia et al., 2009).

[8] For instance, whenever the president under-executives parts of the budget, the Chief of Cabinet is required to make reports to Congress, but the formalities of the reports are never checked, nor are there legal consequences of how the

In effect, the executive utilizes government resources as desired and has been a central instrument to build his political capital.

Moreover, the Argentinean budget is prone to manipulation because of its rigid structure. Given that almost half of the budget is predetermined and goes to social security, transfers to provincial governments and debt payments, the Executive has incentives to create fiduciary funds outside the budget process or the co- participation system tax sharing scheme (Abuelafia et al., 2009).[9] Even with a legislative majority, as in 2004 and 2005, the incentive to create funds outside the budget process is a way for the executive to bypass the rigid budget process or fiscal rules imposed by international agreements and are not subject among actors across the political spectrum, giving the Executive branch greater ability to implement its preferred policy and electoral goals (Abuelafia et al., 2009: 24).[10] The funds are established by three different methods: decrees, laws and resolutions (Abuelafia et al., 2009). Fiduciary funds range in their composition, from the state funding electricity initiates to subsidies for private sectors to provide public sector.

These funds, however, are a constant source of controversy and have increasingly become more so over the last decade because these resources are considered off-budget privileges since the president is allowed to distribute as desired without congressional input. While the Chief of Cabinet has been required to explain the use of fiduciary funds since 2003, the reports that were drafted from were mostly incomplete. Specifically, these reports are often missing adequate information on their disbursement, a violation of transparency and accountability laws.

Executive executes the budget. Many analysts contend that the lack of Congressional oversight in yearly budget alterations giving the Executive the ability to make expenditures particularistic versus representative.

[9] The formal budget process only accounts for 48% of total government spending (Abuelafia et al, 2009).

[10] For example, the former President Carlos Menem used an array of funds and trusts outside the budget to pass

Aside from presidential budgetary powers, three other mechanisms enhance Executive power over the annual budget. These include: a) necessary and urgent decrees, b) economic emergency laws and c) pre-existing delegated powers. The most important is the necessary and urgent decrees, which can be imposed without congressional approval and are easier to utilize than a delegated power. One decree, *Decretos de Necesidad y Urgencia* (DNU) is the simplest strategy to allocate spending, and represents a tool to shore up political support.

In sum, the Argentinean Presidency holds extensive power surrounding budgetary outcomes. But as is often the case, politics rather than policy recommendations drive economic outcomes. This is why studies that analyze institutional structures and budget rules often fall short of explaining why presidents, armed with so many tools influencing policy, cannot successfully complete effective fiscal reforms in their countries. My argument is that one needs to look first at the specific institutions that affect presidential motivation to balance the budget and how these institutions affect change during the course of a president's time in office.

II. Argentinean Spending Levels

The Argentinean economy experienced an impressive recovery after the 2001 economic crisis, particularly from high international commodity prices. In particular, the soybean industry has surged far ahead of meat and wheat combined, Argentina's traditional exports, providing the country with a solid revenue base (Richardson, 2009). In 2009, soy exports brought in $12.98bn, which represents 23% of total export earnings. Unlike previous decades, in which presidents were trapped between holding down domestic prices and letting the meat and wheat industries prosper, high soybean prices are no threat to domestic price consumption or price stability (Richardson, 2009).

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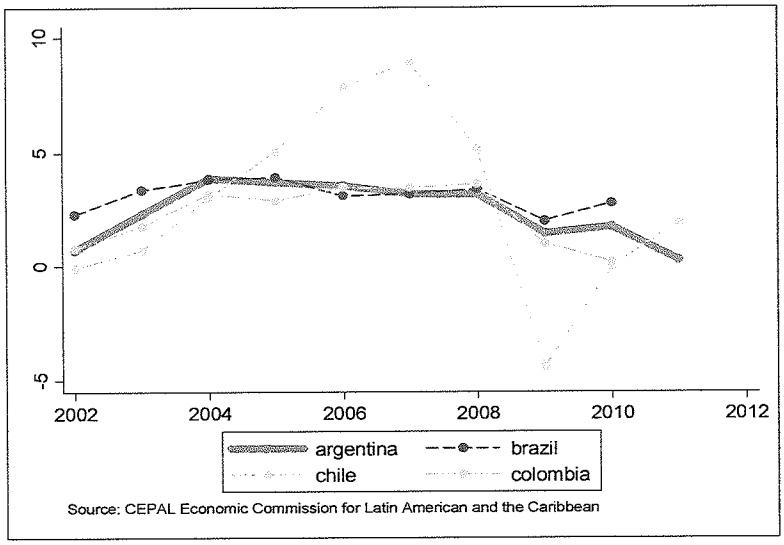
many economic reforms (Abuelafia et al, 2009).

Figure 1 shows the primary balance for four South American countries: Argentina, Brazil, Chile and Colombia. As illustrated throughout most of this decade Argentina is able to implement balanced budgets; however, it is important to reiterate that the administrations' fiscal surpluses have been the result of the country's economic growth and high commodity revenues versus any measures to control spending.

Figure 1: Primary Balance by % of GDP 2002-2011



For example, to draw attention to the country's economic prosperity apparent in this time period, one can point to Kirchner's ability to pay off the country's International Monetary Fund (IMF) debt three years early. The decision to pay off its debt is done to eliminate the conditions placed on by international financial institutions. Thus, so while balanced budgets are present, Figure 2 shows the general increase of spending throughout Kirchner's term in office. As a result, as illustrated in Figure 3, Argentina starts to experience a decline in primary balance, which implies that Kirchner's government, as of 2004, started to spend faster than it collected in revenues.

Figure 2: Gov't Spending % GDP

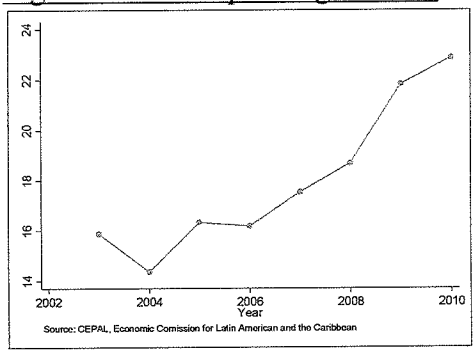
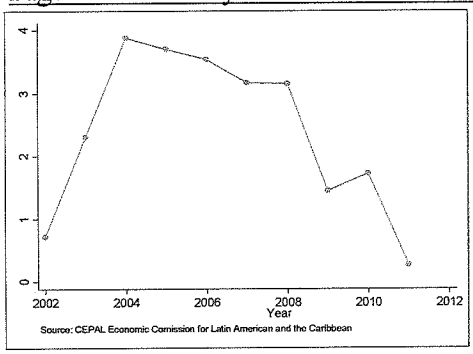


Figure 3: Primary Balance % of GDP



While increases to government spending are not undesired, if administrations can lead efficient budgetary outcomes without deficits, presidents' motivations to party build or buy support will conflict with balanced budgets since government resources are crucial to build their political capital. Thus, by the end of the decade when fiscal imbalances loom near, the Kirchners' fail to use their strong budgetary powers to control spending; instead, they use these very same powers to increase spend and create new avenues of revenues. Thus, strong budgetary powers have allocated Argentinean presidents with resources and prerogatives to acquire unusual amounts of presidential power. As argued by Wroclavshy (2007), throughout this period, Kirchner has successfully employed the Peronists' aggressive style of politics, capitalizing on windfall commodity revenues to increase spending in targeted programs as a way to trade rents to build its political hegemony. Kirchner's success is largely accomplished by distributing funds to his supporters, and the resultant increasing levels of government spending is central to this case study; however, the composition of the budget plays an equally important role, as Kirchner strategically recomposes the budget and re-directs spending towards his desired preferences.

III. *Néstor Kirchner (2002-2007):* Budgetary Superpowers and Spending Preferences

By drawing on an anti-status quo discourse, primarily against *neoliberal* economic policies implemented by his predecessors, Néstor Kirchner finds his immediate appeal among voters. Furthermore, Kirchner gains greater momentum by his initiatives removing impunities against military officers with violations of human rights abuses from the country's dictatorships years and by removing government officials connected to the corruption scandals from former president Carlos Menem's era. As Cheresky (2004) notes, Kirchner's actions, especially in his first months, gave the illusion that a president had finally arrived to address social justice issues.

While his most important policy measures were tied directly to government expenditures, he would employ spending decisions with strategic political reasons, and mostly through the country's present culture of *clientelism.* According to Brusco, Nazareno & Susan (2004), since the enactment of neoliberal reforms, Peronism may have had to relinquish their traditional labor based policies—but contrary to predictions of the downsizing of the state—c*lientelism* remains a powerful tactic as parties have adjusted to the types of goods they choose to deliver. Even with Menem's neoliberal reforms, and the reduction of the state, the *Partido Justicialista* (PJ) switched from labor based policies to material rewards, in order to sustain their electoral base. Understanding the political climate, Kirchner, equipped with budgetary superpowers, high growth and increases in commodity revenues—especially in 2003 and 2004—used his prerogatives to re-direct expenditures toward his preferred programs and provinces (Abuelafia et al., 2009).

His first targets were the *piqueteros*—the mass organizations of the unemployed—who had taken center stage in the country's political life. The claims of these social movements had

gained legitimacy, as Argentina's middle classes had started to question the benefits of neoliberal reforms in the aftermath of the 2002 economic crisis. While Kirchner failed to appease their demand with substantial policy measures to address structural unemployment or the country's income inequality rising, he did meet their immediate needs through various social policy initiates.

First, he expanded former President Dulhale's welfare rollout program, Unemployed Heads of Household Plan (PJJHD), from 700,000 to 2 million recipients (Svampa, 2008). Moreover, in his first budget, he initiated substantial increases in welfare programs with some increasing well over hundred percent. Kirchner's government also grew with increases to government employment; in fact, according to Svampa (2008), recipients of these programs were assigned forced employment, which ironically placed p*iquertors* within government posts working alongside the very same Menon aids they detested (Svampa, 2008).[11] Table 1 presents the growth on the non-financial public sector from 2002 to 2009.

Table 1: Non-Financial Public Sector Growth (2002-2010)
% of GDP

2002	2003	2004	2005	2006	2007	2008	2009
-	25%	25%	28%	28%	31%	33%	37%

Source: CEPAL, Economic Commission for Latin America and the Caribbean.

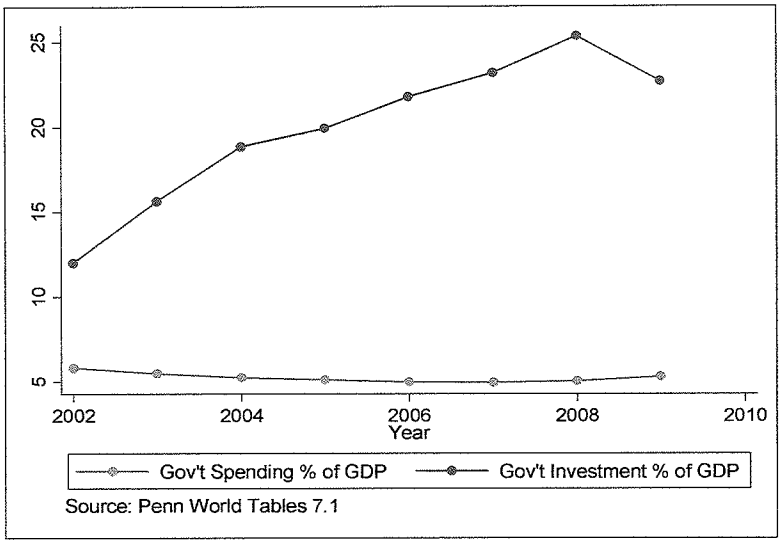
On the surface, the government expansion under administration is envisioned as a large increase in welfare programs, but as Fiorentini (2012) claims, the increases in social spending during Kirhcner's period are marginal and often used as policies tied with expectations of

[11] Svampa (2008) points out that Kirchner strategically identified parts of these social movements to co-opt, while marginalizing the most extreme segments.

political loyalty. In most cases, funds were distributed to the leadership of either political parties or *piquetero* organizations in return for political loyalty. In other words, spending measures were meant to control various players, while social policy to address the structural realities of the unemployed or rising levels of income inequality never materialized or played a part in Kirchner's policy agendas.

Nevertheless, the growth of government is part of Kirchner's economic platform but it's vital to analyze the various components of government expenditures and the size of each category. Figure 4 displays the discrepancy between different measures of government spending provided the *Penn World Tables 7.1.* One can see that expenditures as % of GDP (i.e. public goods) experience marginal increases throughout this decade, while domestic investment % of GDP substantially increases from 15% in 2003 to over 20% in 2006 when he leaves office. According to Wroclavshy (2007), the usage of public works projects (as well as government posts) has been central to Kirchner's strategy to buy the legislative support of smaller fractions in the opposition.

Figure 4: Government Spending % & Government Investment % of GDP



Furthermore, an Economist (2010) article, "*Socialism for foes, capitalism for friends,*"

further highlights the complexities behind Kirchner's presidency and his relationship with the private sector. While he continuously employs *anti-neoliberal* rhetoric, and some private sector entities are negatively affected by regulatory measures or complete take over of industries, businesses with political connections to the president do flourish. These private sector associations, known as *'Empresarios K,'* are Kirchner's closets allies, who successfully gain contracts and ultimately determines the difference between capitalist who win or lose in this era.[12]

For example, the owner of 'Austral Construcciones' began as a small construction enterprise in Santa Cruz (Kirchner's former province while governor) and today represents various industries in oil exploration and farming. In fact, most of his company's current day businesses are in public works projects for the region of Santa Cruz.[13] Additionally, Svampa (2008) points out that Kirchner's export-driven model is not unlike his predecessors, who emphasized economic activity on open-cast mining and mega-dam projects; he also provided large subsidies to the private sector, in specific to counter rising energy costs. His 2006 budget experienced a 4 percent increase[14] with 40 percent set aside for energy subsidies.[15] Moreover, while subsidizes arise from the annual budgets, fiduciary funds, as previously discussed, are also used to finance private companies that provide services for the state. Off-budget funds amount to $20 billion or 4 percent of the budget (Una et al., 2004). The growth of off-budget funds are a source of controversy during this decade and will be discussed further below.

It is also important to highlight that during the Kirchner Era, economic advisors are able

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[12] The Economist Print Edition (2010). Argentina under the Kirchners. Socialism for foes, capitalism for friends. <www.economist.com/node/15580245>.

[13] Kirchner has also allocated the firm oil exploration rights in Santa Cruz.

[14] El Clarin (2005, September 13). La Economia que viene y los superpoderes. Kirchner firmo el Presupesto 2006. <http://old.clarin.com>

[15] El Clarin (2006, September 7). Superpoderes: el oficialismo saca cuentes en el Senado y canta victoria. El

to increase his share of discretionary spending through two measures. 1) the underestimation of revenues, and 2) increase usage of emergency decrees. While previous governments' overestimated claims of solid economic progress, the tactic used during the Kirchner Era underestimated economic growth, inflation, and revenues to enhance the president's discretion over spending. Revenues not included in the original estimates can be used at the discretion of the Execution branch and without congressional approval. Given that Argentina experienced rising community prices, and subsequently, a surge in revenues from 2004 to 2007, governments intentionally underestimated revenues to exercise greater control over discretionary funds—a strategy to escape the rigidities of the Congressional budget process.[16]

For example, in 2004 the government received an excess of revenues, but without the incentive to ask Congress to approve any changes to the budget, the executive declared a series of decrees (DNU) and increased government expenditures by almost 15% of the original approved budget (Abuelafia et al., 2005). The growth of fiduciary funds through the use of decrees accounted for 9% of the federal budget in 2005, and by 2007, the budget assigned "5.6 billion pesos to fiduciary funds—an increase of 281 percent since 2002" (Abuelafia et al., 2009:47). According to Rose-Ackerman et al. (2011), emergency and non-emergency decrees are used for political and policy preferences, but mostly to further party goals.

According to Santiso (2008), the addiction to decrees in public budgeting has outlived Menem and become engrained in budgetary practices under Néstor Kirchner as his political hegemony expanded. The number of decrees under one term was 249 (an average of 55 per year), an increase from 37 per year under the Carlos Menem administration (Iñurrieta, 2007). In an interview with a PRO opposition legislator—who writes exclusively on transparency and

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"bloque K" suma 41 bancas sobre 72. Necesitan solo la mitad de los presentes. <http://old.clarin.com>

[16] Recent evidence reveals that a one percent increase in revenues leads to a 2.5 percent increase in discretionary

abuses of the budget by the executive branch—he discusses the budgetary process amid Congressional approval of its 2008 decision:

> "If you understand the constitution, article 76 states that Congress can only delegate its powers to the Executive under emergency situations. The 2001 crisis was 7 years ago and we just saw Congress pass the continual delegation of power. There is no need to do this, given that Argentina has experienced solid economic growth for several years now. The passage by the Kirchner administration to have these superpowers allows for the laws of the land to be violated."[17]

As many believe, the usage of the budget has been used strategically by the Kirchner administration with charges that this concentration of power was built "by trading rents to some pressure groups in exchange for political support (Global Integrity Report, 2007), while weakening formal institutional constraints through either gross disrespect or biased enforcement" (Santiso, 2008).

In the course of a few years, Néstor Kirchner emerged to the national scene and enhanced his presidential power through various measures. For one, he implemented several tax increases on the export sector, which not only generated higher revenues for the federal government but also greater bargaining power with regional key political actors. This is largely due to Kirchner's substantial reforms to the tax system, making provincial governments even more dependent on 'executives' good will.[18] As a result, provinces' share of tax revenues decreased since 2001, from a high of 39% to 34% in 2005.

Most importantly, in 2005, with the dominance of the *Frente por la Victoria/Partido Juristido (PJ)* in Congress and—a weak opposition—Kirchner successfully reinstated budgetary superpowers initially anticipated as temporary so presidents could counter the 2001 economic

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spending (Abuelafia, et al., 2009:33).

[17] Interview on September 14, 2008.

[18] The Economist. (2010). Argentina after Kirchner. The End of an Era. The President is widowed, politically as well as personally. <www.economist.com>.

crisis. These prerogatives further enhanced the Executive's budgetary powers, specifically its ability to recompose budgetary categories and target segments of the population. While economic growth and high commodity revenues afford Kirchner the ability to run budget surplus, substantial control over the budget has not led to more greater efficient outcomes; on the contrary, heightened power has resulted in giving the president discretion with spending decisions, and mostly for political purposes.

By as early as 2004, he had successfully co-opted large parts of the *piqueteros,* as is evident when *Corriente K* forces started to initiates rallies in support of the administration's policies. Moreover, given the increased level of revenues based on the reforms to the tax system, it is not a surprise that opposition governors from the Radical Party joined his governing coalition. They became known as *Radical K's.* In a short presidential term, Kirchner had successfully built his political influence and control with various segments of the Argentinean society. This was largely due to the political disorder left from the Argentinean 2002 crisis that disintegrated and discredited his opponents. Equally playing a part are the large amounts of government resources to aid pursuing his policy preferences.

Ironically, even with high popular support, by the end of his first term Kirchner steps down with the desire to unite the PJ. However, most observers view his departure as a way to return to power after waiting a term as well as a way to evade being termed out after a second presidency. The continuation of his influence in everyday politics remains, nevertheless, as he passes the thrown to his wife, Christina Kirchner. Her presidency is continuity of Néstor's legacy—of emergency decrees, unilateral decision making and bypassing institutions meant to check executive power—with aims to continue building their hegemonic power. As this dual presidency illustrates, Latin American executives find ways to circumvent institutional barriers

to heighted power, leading to their graduate increase in power.

Christina Kirchner (2007-present): Kichnerismo continued

Unlike the prosperity during Néstor's first years in power, Christina entered the presidency with an economic slowdown and pressures of external debt payments. It is important to point out that while Néstor paid off Argentina's IMF debt, it represented only 9 percent of country's total external debt (Svampa, 2008). Accordingly, the country's continual high debt figures placed a strain on the government's ability to generate a primary surplus, especially alongside the administration's growing spending levels. From a strictly theoretical perspective, strong presidential powers are expected to assist presidents' initiated controls to spending when fiscal imbalances are on the horizon. However, even with the economic slowdown and payments due on the external debt, Kirchner continued to enlarge the annual budget or find ways to increase revenue streams.

In 2008, the budget was increased by $11.6 billion with the claim that the administration had to confront an economic emergency (Rose-Ackerman et al., 2010). Moreover, analysts consider her 2008 export tax on farmers as a maneuver to steer resources to the federal government and increase her spending capacity. In her first year, using a presidential decree, Kirchner introduced Resolution 125, which imposed a sliding scale tax on agricultural exports, particularly soy and sunflower products from 35 percent to 44 percent. The tax increase would have generated $3 to $4 million in revenue (Barrionuevo, 2008).

While the administration claimed to initiate a tax on the most lucrative sector of the economy as a way to redistribute wealth and fight inflation, there are various angles to understand the tax increase. Since the agricultural sector is the most lucrative one and export

taxes are not included in tax revenues shared by the provinces through the co-participation system, many viewed the tax increase as a way for Kirchner to increase her discretionary spending power. An alternative explanation contends that Kirchner's political coalition was an alliance formed without the support of the farming sector. According to Dowd (2009), the 2007 congressional victories were not carried by the farmers' bloc, but the industrial sector. In the region of Santa Fe, which produces 33 percent of soybean production, the coalition received only 15 percent of the vote. Instead, their victory came from the industrial sector, and to placate their voting bloc, a tax on farmers became a tool to redistribute wealth to their supporters.

Yet, despite the claim to redistribute wealth, Argentineans citizens flooded the streets and formed an unlikely alliance with the Argentinean farmers. The previous tax increases on soybeans, from 10 percent to 35 percent after the 2001 economic crisis, were strongly supported by the general society to increase social spending and alleviate the conditions created by the financial crisis. But another hike, to 41 percent, failed to convince voters that they were needed, given the country's strong economic performance over the last decade. The tax resolution almost gained approval, as it passed the House of Representatives and reached a tie on the Senate Floor. But an unexpected tie-breaking vote by Vice President Julio Cobos rejected the measure a surprising and detrimental blow to Kirchner's leadership in 2008 (Barrionuevo, 2008). Many observers viewed this defeat as important to holding the president from further nourishing Kirchner's unilateral governing style.

As an opposition legislator noted:

"The latest vote by the Senate against the farm tax shows a sign of relief from executive abuses. That is what vertical accountability is all about. It is a sign that there still is life in the Argentinean society. Something has been received from their decisions, those men who are situated in both chambers of the legislature have maintained vertical democracy. We saw this in the last vote relating to the budget, the taxes for the agricultural."[19]

[19] Interview on September 14, 2008.

By 2009, deficits begin to appear after several years of strong economic growth and fiscal surpluses. Accordingly, limited in resources Kirchner continued to issue decrees to finance the country's various obligations. In 2010 she issued a decree to use central bank reserves to pay the external debt. While the Central Bank Director refused to accept her decision without congressional initiates to approve this measure, Kirchner issued another decree to force him from his position. Rose-Ackerman et al, (2010) points out that despite the Central Bank Director's fight—and victory—against this decree, the funds had already left the country without any measure to retrieve them.

The ongoing nature of emergency declarations by the Kirchner's has caused controversy and members of other institutional bodies to question these policy measures. In fact, many members of Congress, Central Bank, and the courts have denied that an emergency ever existed (Rose-Ackerman et al., 2010). The Argentinean courts especially have been inclined to check the Executive when they find it engaging in quasi-legislative behavior. Specifically, the courts have tried to use their discretion to question the "emergencies" declared by the Executive Branch to impose its decrees.

However, these attempts to limit Executive power have often failed, since Presidents have systematically opposed the court's efforts to check its authority by using the rhetoric of separation of powers (Rose-Ackerman et al., 2010). The Kirchner's have strongly disagreed and argued that the courts lack expertise on how to judge the state of the economy. This invocation constitutionally inherent of 'separation of powers—especially after the 2001 economic crisis,—has been the administration's clever manner to defend itself from attacks by the courts, regulatory agencies and the legislature.

While the use of decrees and the delegation of powers is not new to the Argentinean political landscape, as the 1990 era of reform and privatization were implemented with declarations of emergencies under the administration of Carlos Menem. However, the recent developments that have persisted into the 2000s, as the government has managed to increase the number of fiduciary funds, and utilize a great portion of revenues outside the budget process - in spite of controversy - are seen as becoming engrained into the future of budget making.

As PRO legislator states:

> "In 2006 the use of powers delegated from Congress to the president used 82 delegations provided by Congress (consisting of: ten decrees, fifty-four administrative decisions, fifteen resolutions, and three dispositions). In 2007, the Executive branch utilized these powers 78 times, while in 2008, there were 24 (before the actual implementation). We saw Carlos Menem doing the same thing, but it has increased during these last few years. Now the administration uses the excuse of the 2001 crisis, stating that the executive needs these powers for emergency reason."[20]

Although it is true Kirchner represented a current against the previous administrations of the 1990s era, Svamp (2008) argues that politics of the "old order" have "clung to life, in altered guise" (80). The rise of the presidents' usage of all possible prerogatives has jeopardized the outcomes of the budget process. Accordingly, the accumulated power by the Executive, over the budget process brought about by these superpowers and the lack of congressional oversight, has produced a very significant decline in the quality of budget making for a functioning democracy. Ultimately, the budgetary power is one of the most important components of the superpowers which many experts say devalues the budget making process.

The return to democracy in Argentina—and to a greater extent in Latin America—has provided countries with constitutional texts to restrain unilateral assertions of power; however, political actors will always search for ways to work around constitutional texts, as presidents will test the limits of their power.

As a Watchdog Representative noted:

> "Due to the control of the PJ, it is difficult for any opposition member to voice opinion, ask for transparency, or accountability. It is what president desires and very few of the party challenge the status quo. However, the recent increase of taxes on farmers did alienate some and there is now division within the PJ. But the division does not imply that we will see more democratic representation."[21]

According to Rose-Ackerman (2011), strategic presidents in Argentina are able to undermine constitutional amendments to control unilateral executive action "because of design flaws in the institutions established to control the presidency; the inability of other actors, such as weak opposition parties, to constrain the President; and the support of political allies" (2). The various outcomes presented in this case study illustrate how the delegation of power to presidents can jeopardize governance with regard to the budget, especially in environments where political actors lack accountability.[22] Specifically, institutional weaknesses create incentives for presidents to enhance their spending power, illustrating how the country has moved away from improvements in fiscal outcomes, whether defined by solid fiscal performance, transparency or representativeness. As a result, this chapter not only questions the idea of a strong executive for better fiscal outcomes, but raises issues of fiscal transparency, efficiency and democratic consolidation.

IV. Concluding Remarks

This case study challenges the common theme in the fiscal policy literature, arguing for the centralization of power in the executive branch as a way to improve fiscal performance. The

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[20] Interview September 14, 2008.

[21] Interview on September 12, 2008.

[22] The delegation of power has also manifested at the provincial level. In 2007, eighteen of the twenty-four provincial jurisdiction entitled their governors to redistributed provincial budget revenues without considering their respective legislative bodies.

legal delegation of budgetary superpowers in Argentina has created incentives for the Executive Branch to manipulate the composition of the budget, economic forecasts and create various avenues for discretionary spending, in order to escape the rigidities of the Argentinean budget process. While the budget process in Argentina has evolved into a more routine process since the 1980s, the 2001 economic crisis and its subsequent political outcome, has jeopardized the governance of the budget. Specifically, the delegation of budgetary powers to the Executive Branch are subject of being used to accumulate political power in the absence of strong checks and balances. Moreover, the elimination of multiple actors enables executives to implement their preferred policy decisions, influence election outcomes, and create environments where government spending becomes particularistic versus representative.

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My principal conclusion is that, to understand powerful presidents as a means to achieve fiscal discipline, it is necessary to consider how other equally important political goals affect presidents' motivations over time. Controls to spending when deficits are on the horizons are less likely when presidents have other equally important goals. In times of institutional crisis or economic uncertainty, presidents with aim to build their party or support base will use these strong budgetary powers to redirect resources toward their allies.

In countries without a tradition of strong democratic institutions, the combination of economic crisis—along with weak checks and balances—produces a power vacuum for political leaders. Santiso (2008) argues that emerging economies have various regulatory agencies to fight corruption and improve fiscal governance, but several remaining obstacles fail to uphold the goals of Argentina's audit agencies. Moreover, Santiso (2008) argues that agencies are not effective because they face political constraints, mostly from legislatures lacking the incentive or

the capacity to utilize audit reports and hold the executive branch accountable.

As a result, the centralized character of executive dominance over the budget as carrying fiscal solutions must be weighed against the institutional weaknesses of Latin American societies. While some observers identified President Néstor Kirchner's efforts to improve and democratize the Supreme Court, the country remains very low in judicial independence. According to the Freedom House measure of Judicial Independence, during the economic crisis, judicial independence decreased from 3.2 to 1.0 (on a 10+ scale) and has climbed back to 2.3 (on a 10+ scale). Moreover, as Richardson (2009) states, while President Kirchner made some efforts to improve judicial independence through a simple decree, he was capable of reducing the courts' influence if horizontal accountability became too demanding. This chapter speaks to issues of governance, transparency, but most importantly, it questions the assumption that Latin American countries ultimately need powerful executives as a necessity for fiscal reform.

Toward the end of my conversation with former the Secretary of Treasury, I asked if the caricatures depicting his reductions of government expenditures were accurate. He agreed:

> "Yes, of course. We know how countries get into trouble. Balanced budgets are necessary."

I followed up his remark by asking him if centralized budgetary procedures were in fact necessary to evade imbalances and recurring crises, as the predictions of the budgetary literature suggest. Unexpectedly, his last thoughts were:

> "I don't believe in a powerful executive. Of course not. We need more Congressional involvement. During the time I was Secretary of Treasury, I encouraged members of Congress to get involved: I wrote a book on how to inform the public. I wanted everyone informed. No one is responsible unless they are held up to the challenge."

Unless countries have strong checks and balances, functional democracies cannot

realistically be predicted. The institutionalization of the budget is vital for democracy and can be the first step toward consolidating democratic backbone. As they search for democratic consolidation, countries must find a balance to allocate power between the executive and other branches of government. The appropriate balance will be different for each country, and will depend on past histories, institutional context and its democratic process. In terms of the annual budget, a lack of congressional involvement can lead to issues of transparency, representation, and efficiency. The Argentinean case highlights how a lack of fiscal discipline and accountability is the result of political failure, political will, and a culture lacking a commitment to implementing formal rules allowing informal mechanisms to advance political power to unwarranted levels.

Chapter 5

Nicaraguan Presidents' Quest for Power: The Unanticipated Consequences of *Neoliberalism's* Enhanced Budgetary Prerogatives

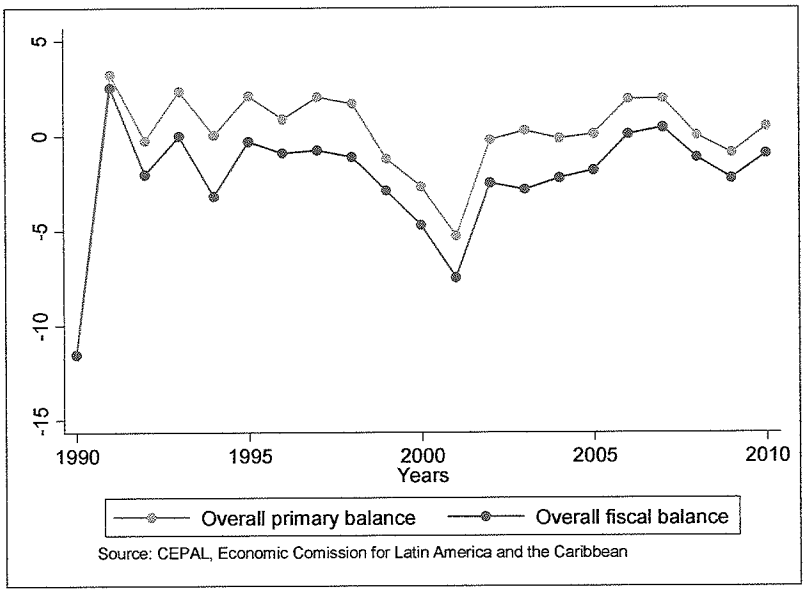
If *hyper-presidentialism* accurately describes Latin American societies, Nicaragua represents the classic case.[1] Notably famous for its history of strong *caudillos*, the Somoza family's 45-year dictatorship and its stunted undertaking of democracy in the 1990s, many elements of its authoritarian past remain intact.[2] This chapter seeks to explore how Nicaraguan political institutions and strong presidential powers interact with executives' motivations with regard to their spending habits.

Since democratization in 1990, four different administrations have captured the Nicaraguan presidency. While all varied in their governing styles, they faced one similar circumstance: assuming presidential power in an era of rigid neoliberal constraints. In this period, presidents, not only in Nicaragua, but throughout Latin America, became well aware of the costs associated with government policies disliked by investors, as capital flight became the common weapon used by investors (Roberts, 1997: 316). This awareness resulted in executives' strict obedience to the demands of the global economy, most notably the weight of the International Monetary Fund (IMF) and its recommendations to tighten budgets, reduce

[1] *Hyper-presidentialism* is defined as an executive's quest for unilateral power, often violating constitutional laws, bypassing checks from the Courts or congress (Corrales & Altschuler, 2009).
[2] The most recent violation is the Supreme Court's removal of article 147 of the constitution. This ban prohibited presidents from immediate re-election or serving more than two terms. However, the nature of the constitution change is controversial and current Daniel Ortega's presidency is not recognized by opposition members, human rights organizations and most international observers. Freedom House removed the country from its list of 117 democracies as of 2012.

spending, collect taxes and reform the public sector. Paradoxically, while Nicaraguan presidents were mostly 'consistent' in adhering to IMF requirements - specifically privatization - in practice, the budget remained the most important component of presidential resources to further political purposes. By the end of the 1990s, Nicaragua not only faced a substantial deficit, but one of its most corrupted presidencies in its history.

Figure 1: Overall Primary and Fiscal Balance % of GDP, 1990-2010[3]



Similar to Chapter 3 on Argentinean budget outcomes, this case study illustrates that strong presidential powers, hierarchical budgetary institutions and party discipline affect budgetary outcomes in more complicated ways than the literature leads us to expect. While these institutions have empowered executives to enforce budget discipline, these very same conditions have also provided presidents with unilateral power to increase fiscal deficits. Figure 1 show Nicaraguan fiscal outcomes from 1990 to 2010, which will be discussed in detail below.

[3] Primary balance excludes debt-service payments, which is a measure of fiscal policy in any given year net of the effects of debts incurred in the past. Fiscal balance represents the different between spending and revenues including services to the debt.

At the end of the 1990s, the Nicaraguan case, as well as other uneven reform efforts throughout the region, motivated the investigations of the factors behind their failures. Scholars pointed to the relationship between weak institutions, governance and corruption in an effort to understand countries' limited progress with economic restructuring. However, as argued in *"Washington Consensus or Washington Confusion,"* Naim (2000) stated that "once the economic reform establishment discovered institutions," or the need to strengthen them, few scholars provided "useful ideas on how to implement institutional reforms" (93).[4] I identify the difficulty in discussing institutional reform, primarily because of the assumptions inherent in predictions about economic restructuring, in general, and budgetary outcomes in particular. Over time, researchers have paid insufficient attention to the president because it is assumed that he/she is always motivated to reduce deficits and balance the budget.[5] Analyses that simply stress the importance of budget institutions that favor the executives in bargaining with legislatures, fail to note that such strong powers can have different effects on outcomes, depending on how a different set of institutions affect the president's motivation over time. Essentially, as Brown and Cloke (2005) argue, recommendations from international financial institutions have a narrow focus on procedural processes and offer a series of "technical solutions to what are essentially political challenges" (606).

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[4] Brown and Cloke (2005) note that despite the large sums of money entering Central American nations, to bring greater transparency, accountability and institutional strengthening, not much has resulted for citizens, alluding to good governance initiatives as nothing more than big business.

[5] At the onset of neoliberal reforms in Latin America, much of the literature on budgets focused on: 1) number of parties presidents must bargain with, and 2) the lack of hierarchical budgetary institutions, as the challenges to fiscal solvency. Haggard and Kaufman (1995) argue that fragmentation within a party system leads to collective action problems, in which legislators disagree on budget policy. This difficulty forces the executive to use resources, patronage and pork to buy the support of some members of congress to sign off his proposed policies. Hence during times of minority governments, when presidents lack the power of legislative majorities, it is assumed that executives have difficulty achieving political support for their preferred budgets. Subsequently, as a way to deal with party fragmentation scholars argued for hierarchical budgetary institutions as a way to assist presidents' bypass the legislature and impose his will.

To understand when reforms might occur, one must consider the political institutions in which executives operate and how they shape incentives to choose particular policies (Geddes, 1994). Indeed, efficient budgetary outcomes lead to lower inflation, a solid economy and thus a collective good that only presidents can initiate. However, the assumed incentive within the literature that presidents are motivated to balance the budget more than other actors fails to consider how other equally important long term political goals conflict with controls to spending. These include presidential incentives to build political machines for re-election, whether immediately or after they sit out a term, as well as to maintain their political influence well beyond their tenure (Geddes, 1994). How these motivations are prioritized directly affects fiscal outcomes and explains why presidents may choose not to initiative efficient budgetary outcomes - much less - the institutionalization of the budget, which, in Nicaragua, is costly to those who benefit from the clientelistic distribution of goods.[6]

While some administrations have utilized their prerogatives to balance budgets, I contend that the centralization of the budget process has enabled presidents' accumulation of political power -- if that is an intended goal of the president. Thus, while Nicaraguan political institutions allocate executives an array of tools to initiate their budget preference, varying types of presidential motivations have resulted in a diverse set of fiscal outcomes. Accordingly, I argue that enhanced presidential powers are potentially detrimental to how presidents utilize public accounts when executives lack both incentives to implement efficient budgetary outcomes and also institutions to keep them accountable.

To develop this thesis, Chapter Four proceeds as follows: *Section 1* introduces Nicaragua's recent history and political institutions. This section focuses on Nicaragua's

[6] Not surprisingly, President Bolanos' 2002 fight against corruption encountered incredible resistance from PLC legislators and effectively divided the party.

political parties and their internal rules to demonstrate how parties' procedures for selecting legislative candidates functions as a medium to control legislative behavior. Party control over legislative nomination, re-election and post-legislative careers play fundamental roles in the formation of executive dominance in Nicaragua. This is especially apparent within the FSLN (Frente Sandinista de Liberacion Nacional).

Section 2 discusses the Nicaraguan budgetary process to illustrate its hierarchical procedures. This section also highlights the limited number of actors in the formation of the budget, the National Assembly's marginal modifications - especially during the Chamorro and Alemán administrations and legislators' theoretically unexpected compliance with IMF requirements. Accordingly, Nicaraguan presidents have the ability to keep spending in check if it's their intended goal.

Section 3 is an analysis of Nicaragua's four presidential administrations and their budgetary outcomes. I stress that during the last 20 years several administrations have made efforts to initiate fiscal solvency while others have used the national treasury as a tool to accumulate greater political power. I identify these outcomes rooted in the inability of Nicaraguan institutions to constrain presidents' unilateral assertion of power. Subsequently, this chapter calls into question the economic utility of uncontested power of executive budgetary power, which may reinforce rent-seeking behavior from those in the president's coalition.

Section 4 concludes with a summary of the types of budgetary outcomes seen over the last 20 years. This discussion highlights how Nicaragua's political institutions and enhanced presidential powers create environments where presidents test the limits of their power. While assertions of power are not unique to this small Central American country, they are manifested in unwarranted levels of presidential power due to inherent weakness in institutions to check

executives' decision making. This case study contributes to the study of the second wave of reforms, which suggests a more country-specific approach to analyzing fiscal outcomes depending on the internal incentives created by varying types of political institutions.

I. Nicaraguan cleavages, revolution and electoral democracy

Nicaragua entered its democratic period with a weight of challenges. The historical cleavages between liberal and conservative political factions dominated the power struggles for most of its history, but by 1979—with the downfall of the country's 45 year dictatorship—an introduction of a new political force emerged in Nicaraguan society. The FSLN (Frente Sandinista de Liberacion Nacional), a leftist revolutionary movement held power throughout the 1980s. During their ten year rule, the Sandinistas built their party machine, making in-roads with some of Nicaragua's segments but also created anti-Sandinista cleavages. Thus, the Contras, a Nicaraguan counter-revolutionary group formed in the early 1980s with the financial assistance of the United States, which led to a decade of a devastating civil war. The strains of sustaining a military to maintain the war efforts against the Contras placed great pressure on the FSLN, alongside their bloated state apparatus, which by 1987 had led to the country's worst inflations levels in its history. These conditions forced the FSLN to open up to free and fair elections by the end of the decade. The first election represented an array of anti-Sandinista forces organized under an umbrella coalition, UNO (Unión Nacional Opositora); they comprised of Nicaragua's liberal parties, conservative segments and anti-Sandinista left-wing factions. UNO's landslide victory officially represented the end of a decade of Sandinistas rule, for the following fifteen years, but not their presence or control of governing bodies throughout Nicaragua's democratic period.

Democracy: 1990-present

In 1990, after many years of strife, Nicaragua entered its first period of electoral democracy. Even with an electoral victory for UNO, however, the demands of the coalition government presented a daunting task for President Violeta Chamorro to govern in a very polarized and economically unstable country. Specifically, central to her coalition's demands were immediate reductions of spending for the FLSN control military and to recover confiscated property during the revolutionary era. But her desire to bargain with all the major societal interests caused the immediate split of her governing coalition halfway through her presidency. The forces that emerged from the split mostly conservative factions who brought their 1996 presidential run under the banner of National Conservative Party. However, among all the break-off parties, none were of equal weight to populist leader Arnoldo Alemán and the PLC (Partido Liberal Constitucionalista), which became Nicaragua's strongest force by the mid 1990s. In particular, he created a multi-class following due to his poverty measures—which were unlike those found within the FSLN—but successfully made in-roads with various class segments and created a multi-class alliance. The FSLN's unexpected defeat in 1990 was a devastating blow to the party; however, throughout the last two decades they have successfully taken measures to restore their hold on Nicaraguan society.

Moreover, in the last twenty years Nicaragua has undergone both periods of harsh structural adjustments reforms and spurts of economic growth. The economic instability, alongside the dire reality of poverty, underdevelopment and lack of social mobility for the majority of citizens has often served to benefit populist candidates who have capitalized on citizens' insecurity to distribute material goods but not without political loyalties - even if presidents' search political survival relies on anti-democratic practices. Thus, political

developments over the last twenty years has returned Nicaragua to inescapable repetition of its authoritarian past. These political challenges are central to this case study and are partly rooted in the undemocratic nature of Nicaragua's political parties. The following section continues with in-depth analysis of Nicaraguan political institutions, but mostly political parties' candidate selection and nomination processes and the impact on executive-legislative relations.

Nicaraguan Political Institutions

The Nicaraguan president is elected to a five year term and may be re-elected after a term out of office. The president and members of the single chamber National Assembly, which consists of 90 deputies, are elected to concurrent five year terms.[7] In 1995, constitutional reforms were put in place to counteract executive power, giving the National Assembly power to override president's veto with a simple majority and eliminated pocket veto.[8] However, the president remains powerful against the National Assembly and other branches of government.[9]

Nicaragua's party system was considered one of the most institutionalized in Latin America ten years ago (Jones and Mainwaring, 2003). However, while the FSLN, remains an institutionalized party, its main opposition, the PLC has dissolved due to factional strife within the conservative liberal alliance. In fact, the PLC, once the strongest political force in the 1990s, suffered a telling electoral legislative defeat in 2011, leaving the party with only two deputies in the National Assembly. As a result, the PLI (Partido Liberal Independiente) has emerged as the second largest party in the National Assembly.

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[7] The electoral system is multi-member PR.

[8] http://www.state.gov/r/pa/ei/bgn/1850.htm Last accessed on April 11, 2012.

[9] The President has decree power over fiscal and administrative laws, nominates all ministers of his cabinet and proposes the National Budget. In times of national emergencies, the executive branch also has the power to propose and approve the national budget.

Nicaraguan Political Parties

The internal dynamics in political parties is an important component of Nicaraguan executives' ever-present power because of the discipline found among them, hence the president's extensive ability to control the policy making process. One of the defining factors of how political parties shape executive-legislative is their influence over their legislative careers, impacting the dynamics of executive-legislative relations, policy making and the executives' ability to lead the policy making process.

There are several elements which factor into party elites' control over the nomination process. Without primaries, party leaders complete control over nomination processes.[10] "*El dedazo,*" (i.e. unilaterally choosing of candidates by the party leader), is the strategy used to nominate legislative candidates. Nominations are usually based on identifying the most loyal candidates, those that are expected to be in the best interest of the party. Moreover, while candidate selection induces party discipline once legislatures reach the National Assembly, it also stems from parties' ability to expel members and force them to resign from their posts (Geddes, 1994). Expulsions from government posts (or the party) was utilized during the presidency of Arnoldo Alemán and reinforced significantly under the leadership of Daniel Ortega.

Given the history of divisions among rank-and-file liberals and rival leaders, internal cohesion was problematic during the UNO administration in the early 1990s and among the PLC in the 2000s. Party bosses influence ultimately control legislative behavior, but at times, there is conflict over leadership within the Liberal bloc. Thus, while internal rules and procedures for candidate selection are centralized and controlled by elites, these rules have not presented the

[10] While in 2004 there were efforts to introduce primaries and democratize legislative nominations, the process is still best characterized by the traditional method of party elites hand choosing candidates - for either municipal, mayoral or the National Assembly.

formation of factions around rival leaders, especially among Liberals, eventually leading to party splits. Consequently, the FSLN enjoys higher party discipline than any opposition party. One exception is the control President Arnoldo Alemán came to develop over PLC legislators during his 1990s presidency and after its conclusion, which is discussed below.

Liberal Alliance: UNO, PLC and PLI

In 1990, UNO - a coalition of anti-Sandinista groups, challenged Sandinista control of government. Its choice or presidential and legislative candidates - was done, amid much public criticism, behind closed doors and by a few party insiders. Violeta Chamorro, the widow of Pedro Joaquín Chamorro - Nicaragua's most renowned journalist - received the presidential nomination in a polarized period in Nicaragua's history. Her coalition splintered early in her presidential term, and was not unified, due to Chamorro's governing style which included reconciliation and negotiation with the FSLN. Given the divisions, Chamorro continued with her style of governance, allowing massive social protests against neoliberal reforms, the military stayed under FSLN control, and most importantly, she failed to address the appropriated property issue stemming from *La Pinata* - when high government FSLN officials pillaged government resources before relinquishing power in 1990.[11] The UNO coalition dissolved half way through her presidential term.

In contrast to Chamorro's faction-ridden government, Alemán's presidency in 1996 was a high point of presidential control and party discipline for the Liberals because Alemán hand picked PLC candidates and used government resources to build loyalties among legislators. The payoffs, both in government positions or patronage, gave him complete control over legislators' behavior and nourished his dominant style of governing. When supporters questioned his rule,

[11] Estimates range at $700 million dollars worth of stolen government resources.

he was notorious for immediately removing them from their posts.[12] Alemán's control over the PLC was apparent, even on the eve of the 2004 legislative elections, when he nominated legislatives candidates who were behind prison bars. The reasoning behind his extreme control over legislative behavior is due to various reasons. For one, he was the sole reason for many of his legislators' advancement in their political careers and increases in personal wealth. Thus, his members of his governing coalition were limited in abandoning Alemán's control because of their involvement in the rampant corruption during his administration, which consisted of embezzling state funds or benefitting from the privatization contrasts during the structural adjustment reforms.

Thus, when his successor Enrique Bolaños charges him with corruption, the party divided, and Bolaños was left with few PLC legislators in the National Assembly. In recent years, the Nicaraguan Liberal Alliance has continued to be divided as an array of break-off parties has emerged. In the 2006 presidential election, the ALN (Alianza Liberal Nicaragüense) challenged the PLC and this division effectively gave the presidential victory to the FSLN. Divisions continued throughout the 2000s, giving the FLSN incentive to capitalize on the Liberals' lack of cohesion. After the 2006 elections, the FSLN controlled Supreme Electoral Council removed the second place candidate, Edurado Montealegre, as the leader of the ALN. After losing the control of the ALN, Monetalegre was recruited by the PLI. PLI - a relatively small party in Nicaragua's history- has emerged as the country's second largest force in the National Assembly. However, even among these break-away parties, the procedures for choosing candidates are centralized, rigid and controlled by party elites.

[12] Revista Envío 1996. First Moves, First Signs. Envío <http:www.Envío.org.ni/articulo/3001>

FSLN (Frente Sandinista de Liberacion Nacional)

On the other hand, the FSLN, Nicaragua's left-wing party, is defined by its disciplined rank-and-file, organizational structure and strong loyalties. FSLN legislators display the clearest examples of *party loyalists*, as defined by Siavelis and Morgenstern (2008). Legislators who fall under this categorization behave according to party guidelines, because of punishment while standing for re-election. Accordingly, party discipline is rooted in the internal structure of the party's hold on candidate nominations, rewards and punishments. The internal procedures for the FSLN candidates are strict, and party members understand that betraying party decisions implies immediate expulsion from the party.

In 1994, the FSLN set a precedent by purging the democratic segment of the party and left only the rigid hardliners, those strongly tied to its revolutionary past and most loyal to party leader, Daniel Ortega (Rosenburg, 2009). Expulsion from the party continued throughout the late 1990s, as sexual abuse charges were brought against Ortega and segments of the FSLN spoke out in support of investigations. In 2006 Oscar-René Vargas ambassador to France, made several declarations to La Preñsa considered critical of the party. He was removed from his post before arriving in Europe. In 2012, Central Bank Chief Antenor Rosales (former coronel of the Sandinista military) was forced to resign for refusing to accept Ortega's decision to use one-percent of Nicaragua's international reserves to finance BALBA, a start-up bank proposed by Venezuela. FSLN's internal dynamics, of reward and punishment, influence legislators' behavior, not only in the National Assembly, but their ability to criticize party policies.

Over the last 20 years, there were only a handful of moments when FSLN legislators joined Liberals in the passage of legislation, such as when all 39 FSLN legislators voted in favor of President Chamorro's 1992 budget. This was a strategic vote, however, as Chamorro

alienated her coalition members with a gradual rather than rapid decrease in military spending for the Sandinista controlled national army (Close, 2004). In most cases, however, FSLN legislators vote along party lines, with Liberal presidents often unable to buy FSLN legislators to join *bancadas (platforms)* within the National Assembly. The FLSN is successful in forming alliances with smaller political parties (i.e. Resistance Party and the Social Christian Party), by using not only posts but programmatic compromises. [13] The 1990, electoral defeat took a toll on the party, but, by 1996, the FSLN had developed into one of the strongest and most organized leftist parties in Latin America (Hoyt, 2004). The FSLN leadership facilitates legislative consent by taking advantage of its control over legislators' future success through influence over nominations and fear of political isolation.[14] FSLN's rigid structure and centralized control often refer its leadership to 'Danielismo,' in recognition of autocratic rule of its leader, Daniel Ortega.

El Pacto

Other than formal institutions and party politics, Nicaraguan political outcomes are influenced by the power-sharing agreement between former President Arnoldo Alemán's and FSLN leader Daniel Ortega, known as *El Pacto* (The Pact). Conventional wisdom holds that Alemán brokered a pact with Ortega to share institutional power and centralize it between the PLC and FSLN, but most importantly, to set laws to protect them against their own future prosecutions for corruptions. Specifically, divisions within the PLC motivated Alemán to protect

[13] During Chamorro's administration, the FSLN capitalized on UNO's divisions and successfully bought the legislative support from UNO coalition members.

[14] Under Ortega's presidency, the FSLN also uses militant tactics to buy legislative support. Opposition members have denounced the administrations tactics known as, *"hapago-amenza"* (i.e. offer a favor with a threat), where legislators are asked for their legislative support, offered a variety of favors, and expected to agree. If opposition legislators decline the offer, FSLN legislators follow up with a series of blackmails. Blackmails take the form of threats to prosecute for any legal matter the administration finds in personal records (i.e. tax invasion, etc.)

himself from his own party and place barriers from future investigations by the faction that was alienated due to his governing style. Thus, central to the pact is a requirement of a two-third legislative vote to strip an ex-president of their immunity, as well as a lifetime seat in the National Assembly for an out-going president (Hoyt, 2004).

El Pacto also introduced a series of changes to the Constitution and electoral reforms in a cynical move to concentrate power in PLC and FSLN. Specifically, electoral laws reduced the percentage needed to win a first-round victory in presidential elections from 45 percent to 40 percent; furthermore, presidential candidates could win office with as little as 35 percent if the second candidate had 5 percent less than that (Hoyt, 2004). This law assured increased electoral victories for both top parties, but especially Ortega's since his base remained very narrow throughout the 1990s.[15] These constitutional changes continue to directly influence presidential and municipal elections, as well as all public offices, even though Alemán's's party, the PLC, has lost its position and primary representative of anti-Sandinista interest.

There are various explanations for the PLC's decline in national politics even if the power-sharing arrangement meant to assure the PLC's and Aleman's hold on political power. First, even if Aleman nourished strong legislative behavior, several top PLC members including his vice-president were at odds with his governance. Thus, immediately after his term, Aleman's vice president charged him with various counts of corruption. But these corruption efforts were only successful if Bolaños gained the legislative support of the largest opposition in the National Assembly, the FSLN, and gained the necessary two-thirds vote to strip Aleman from his impunity. Second, and equally important to Aleman's downfall, is the fact that *El Pacto* did not contain an enforceable mechanism to restrain the FSLN from capitalizing on efforts to break up

[15] The Aleman-Ortega pact also contained measures to eliminate smaller political parties and exclude societal groups (Hoyt, 2004).

the PLC. Bolaños' corruption campaign presented the FSLN with the opportunity to break up the PLC in a calculated step toward the most powerful political seat in the country—the presidency.

However, several elements of this power-sharing agreement are still firmly in present contemporary Nicaraguan politics. Specifically, *El Pacto* expanded other public offices with partisan appointments, such as the Office of the Comptroller General of the Republic. In addition, it increased Supreme Court justices, as well as the number of magistrates on the Supreme Electoral Council. The dealings of the *Alemán-Ortega* power-sharing agreement continue to influence Nicaraguan political institutions and the outcomes of current day politics. Moreover, the partisan appointments made during The Pact have influenced the behavior of institutional bodies and checks of the executive branch.

II. The Budget Process.

There are five stages in the formal budget process: The first stage consists of macroeconomic projections by the government of Nicaragua, International Monetary Fund (IMF), Central Bank and finance minster. According to Vogl & Kublbock (2010), the IMFs role is highly influential in the Nicaraguan budget process. The authors believe IMF's recommendations on budgetary procedures, restrictions on spending ceilings, debt and government payroll constitute *supraconstitutional* power. After projections are finalized, the finance minster sets the limits for government expenditures and investment projects. Next, government entities determine the direct budgetary allocations they need and present them to the finance minister before proposals are sent to the National Assembly. The final stage takes place at the National Assembly, when the budget arrives for approval (Vogl & Kublbock, 2010).

According to economist Adolfo Acevedo Vogl, political parties incentives to abide by IMF recommendations to ensure loan assistance. In fact, the National Assembly has often approved laws and restrictions on its own constitutional capacity, arguing it does not want to 'jeopardize' the program with the IMF (Vogl & Kublbock, 2010).

Once the budget arrives on the legislative floor, the ceilings are set and there is often limited maneuvering for legislatures to perform. Legislators are not allowed to increase the budget. However, while legislators are prohibited from increasing the budget's ceiling, legislators have the ability to re-arrange the composition (although very minimal) of the executive's budget. Moreover, the National Assembly is allowed to create and establish funds to increase spending - if desired (Vogl & Kublbock, 2010). In the last 20 years, the National Assembly has initiated very modest modifications to the executive's budget.

Overall, the budget process is highly centralized with the finance minister having the last word in budgetary decisions (Lora, 2007). In other words, if changes to the budget by legislators are not desired by the executive branch, the finance minister adjusts as desired. Hierarchical procedures and rules, according to much of the budgetary literature should, facilitate fiscal control. But while rules and policy recommendations are widespread, political incentives are the driving force behind final budget outcomes.

III. Budgetary Outcomes, Fragile democracy & Hyper-Presidentialism in Nicaragua

There are various reasons why the predictions in the hierarchal budgetary predictions fail to hold in practice. First, the national budget remains the most important resources for Nicaraguan presidents. And while IMF recommendations weigh heavily on the budget making process, presidents (and their finance ministers) still have leverage over spending levels and the budget composition. This leaves presidents with a line of discretion to channel government

expenditures in *clientelistic* methods and run deficits. Accordingly, presidents' budgetary decisions are often left unchallenged, as Nicaragua's institutions lack the ability to audit government expenditures. This is stems from the country's lack of accountability, where politicians are not forced to answer for their actions.

The lack of accountability within the Nicaraguan political system is due to several reasons. First, given the country's executive dominance culture, unless the sitting president nourishes horizontal accountability, investigations for the abuses of power from state agencies or other branches of government are subdued. What has transpired over the last twenty years has been executives either engaging in two strategies: 1) appointing partisan allies in institutional bodies to limit checks on abuses of power or 2) presidents buying the support of public officials within agencies or other branches of government to implicitly support their actions. Thus, separations of power are present but often without the checks and balances expected from a functioning democracy. Second due to the undemocratic nature of parties, citizens have limited options with the types of candidates they can vote in and out of office. So, while Nicaraguan citizens have used social protest to stop economic reforms, for example, their actions have rarely affected the behavior of public officials or influenced governments to punish abuses of power. Thus, Nicaraguan political institutions have several weaknesses in holding public official accountable for abuses of power. In sum, if the executive wants to nourish horizontal accountability, public officials are subject to respond to their actions. But, if sitting presidents take steps to weaken other branches of government with the responsibility to investigate the improper use of state positions, then accountability is absent from the political culture.

Lastly, Nicaragua suffers from a culture of *clientelism,* patronage and nepotism. This tradition directly affects presidential governance and often nourishes rent-seeking behaviors in

governing coalitions. All things considered, the centralization of power has virtually enabled all Nicaraguan presidents achieve their policy goals. If balancing budgets is central to a president's policy goals, they have an array of tools to maintain budget discipline. Paradoxically, these same powers have helped presidents accelerate spending and exacerbate the country's fiscal imbalances when they have cared about other goals more than budget balances.

Violeta Chamorro (1990-1996): Stabilization without the Rewards

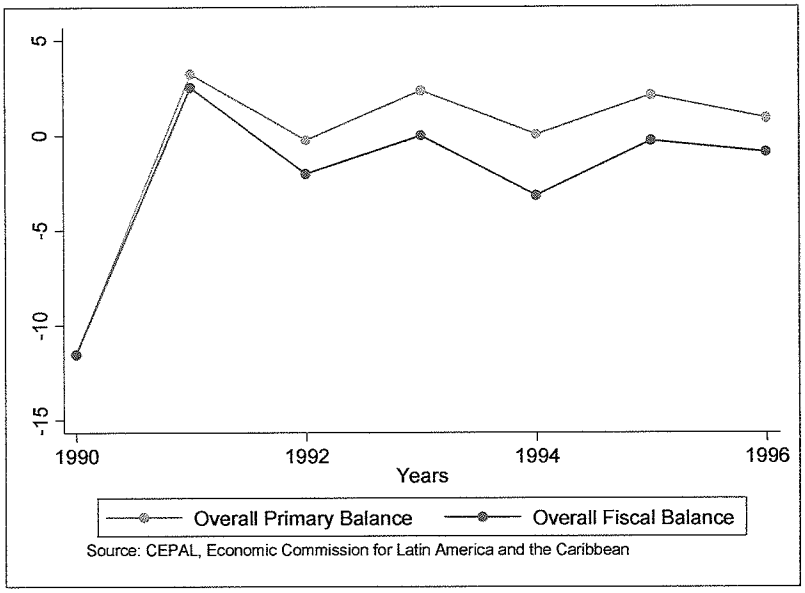
Nicaragua's first democratically elected president, Violeta Chamorro ran under a rainbow coalition UNO (Nicaraguan Opposition Union), representing a diversity of anti-Sandinista interests. Chamorro understood the challenges faced as the nation entered a decade of economic restructuring. Coming out of a civil war, the country was highly polarized with various segments of the population to appease. While international pressures left the small Central American nation with few economic options and UNO's center-right ideological leanings pressured for reforms, her structural adjustments were also done to correct for the various economic imbalances.

Her most important policy measure, however, was to reduce inflation. Since Nicaragua had undergone one of its worst periods of hyperinflation from 1987 to 1990, it had eliminated the purchasing power for most Nicaraguans. Moreover, the country did not only suffer from high inflation levels, a budget deficit and a default position on its debt, but her predecessors were known for their participation in *La Pinata - the* stealing of all possible government resources before their departure - left Nicaragua with virtually no resources with which to govern.

Chamorro implemented a set of austerity measures, including cuts to social spending and reductions to the state. In the first two years of her administration, she decreased the deficit, the

economy grew, foreign investments increased and negotiations to bring peace were successful in a very polarized period for Nicaragua.[16] Chamorro used her presidential powers to implement structural adjustments reforms and often governed by decree, with a third of the decrees used for fiscal policy.[17] Figure 2 illustrates Nicaragua's overall fiscal balance and primary balance during her administration. It shows the severe deficit left by the Sandinistas when they stepped down in 1990 and the subsequent improvements under Chamorro. The 1994 gap between the overall primary balance and fiscal balance is due to growing interest payments on the external debt. However, Chamorro's overall primary balance averaged positive surplus throughout her administration because of her effort to meet structural adjustment reform goals from the International Monetary Fund (IMF).

Figure 2: Overall Primary and Fiscal Balance % of GDP, 1990-1996
Violeta Chamorro Administration



[16] While Chamorro's stabilization efforts brought macroeconomic stability and a rise in gross domestic product, they were often criticized for their direct cause of a rise in unemployment and poverty levels.
[17] Revista Envío. 1996. Promises Coming and Going. Envío (181). <http://www.Envío.org.ni/articulo/1962>

More than just utilizing the centralization of powers, Chamorro implemented an array of strategies that boosted the passage of reform efforts in the early 1990s. In contrast to conventional wisdom that assumes presidents must use their budgetary resources to appease legislators, Nicaraguan presidents can utilize an array of other measures to buy the support of *bancadas* (i.e., smaller parties or coalitions), in the National Assembly. The buying of voters described in the Nicaraguan political landscape as *Canonazos* (i.e. bombing) - consists of government posts, cabinet positions and compromise on other policy measures. Chamorro was notorious for using bureaucratic positions to buy legislative support for her annual budgets.[18] Most importantly, however, Chamorro was able to implement many of her structural reforms with the condition that FSLN leadership remain in ownership of the property appropriated during "La Piñata" and in control of a number of other top governmental positions.[19] In a period when the country was implementing some of the most drastic measures, she found support for her preferred budgets with marginal modifications by the National Assembly. This strategy is often employed by executives,[20] but is either not considered or is underestimated within the arguments on budgetary outcomes.

The Chamorro presidency was defined by a substantial effort to reduce fiscal deficits and debt levels. Despite the -8 percent of GDP deficit and large external debt Chamorro inherited in her first year in office, she improved Nicaragua's fiscal imbalances. However, while achieving macroeconomic success, her cuts were often criticized for increasing poverty and causing a sharp

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[18] Revista Envío. 1991. Uno's Court Packing Plan. Envío (116). <http://www.Envío.org.no/articulo/2940.
[19] Revista Envío.1995. The Chamorro Administration: A Race to the Starting Line Envío (166). <http://www.Envío.org.ni/articulo/1859>
[20] Cheibub, Przeworski and Saiegh (2004) found that between 1946 and 1999, coalition governments formed in more than half democracies when presidents lacked a legislative majority. They explain this empirical regularity by showing that presidents have incentives to make coalition offers and parties accept them because parties are assumed to care about offices and policies in addition to government funds. In the Latin American context, Geddes (1994) systematically tests forty-four presidential terms via the development of Appointment and Survival Strategy Indices, and concludes that executives activity take steps to increase state capacity for patronage as well as appointment strategies and the assistance of the bureaucracy to gain the support of elite party organizers.

rise in unemployment. Moreover, her administration was not devoid of corruption scandals. Indeed, the Comptroller's Office discovered that a misuse of $500 million was tied to her finance minster Antonio Lacyao. Ultimately, her governing style, of peace and reconciliation lead to the early split among her UNO coalition. This first period of negotiations with the FSLN, fueled PLC Arnoldo Alemán's presidential candidacy, giving him political capital that he embraced and abused with great fervor.

Arnoldo Alemán (1996-2001): Building Political Power with the National Treasury

In the same fashion that neo-populist candidates materialized throughout Latin America in the 1990s, most notably Carlos Menem in Argentina and Alberto Fujimori in Peru, Arnoldo Alemán emerged as Nicaragua's version. At a time when the central government was undergoing structural adjustment programs, reducing social spending and public employment, Alemán distinguished himself as Managua's Mayor. He implemented an array of public works projects, successfully revitalized the local tax base, addressed education reforms and rebuilt the capital.[21] Alemán delivered as mayor and was expected to do the same as president.

At first glance, Arnoldo Alemán's presidency seems complex. While Chamorro's UNO coalition represented Nicaragua's anti-Sandinista elements, Alemán represented traditional Nicaraguan conservatism. He enjoyed the backing of liberals, who viewed his candidacy as an opportunity to return Nicaragua to its Somositsa days. His strong conservative leanings, ties to the business community and anti-Sandinista rhetoric symbolized the hardliner Nicaraguan conservatives awaited. Thus, he enjoyed higher political capital than Chamorro and was viewed as the candidate to de-Sandinisize Nicaragua, proceed with market based policies and re-visit the

[21] Alemán also received financial backing from his Miami's allies and those situated in city government (Caster, 1996).

property issue. Although many of Alemán's policies did align with the 1990s neoliberal era of economic restructuring, his presidency is best defined by protecting his personal interest than by adhering to any particular ideology.

Alemán won the presidency with a solid margin in 1996. His congress was made up of 46 PLC members and 36.5 FSLN members, with fifteen other legislators representing an array of smaller parties (Gonzales, 2011). While the relatively small PLC had emerged as Nicaragua's most institutionalized party - rooted in the momentum Alemán's generated from nation-wide campaigning while Mayor of Managua - the PLC was far from consolidated internally.[22] According to Hoyt (2004), top PLC legislators wrote a confidential memo to Alemán, stressing the need for cohesion within the Liberal Alliance.[23]

"The Liberal Alliance is fragile. Our first goal must be Liberal reunification under a single banner taking the PLC as the center...This unification will be realized sooner and more effectively if....the Liberal family comes together as in 1855, 1883, and 1946, around an authentic caudillo of quality, [who] in this case is Dr. Arnoldo Alemán Lacayo."

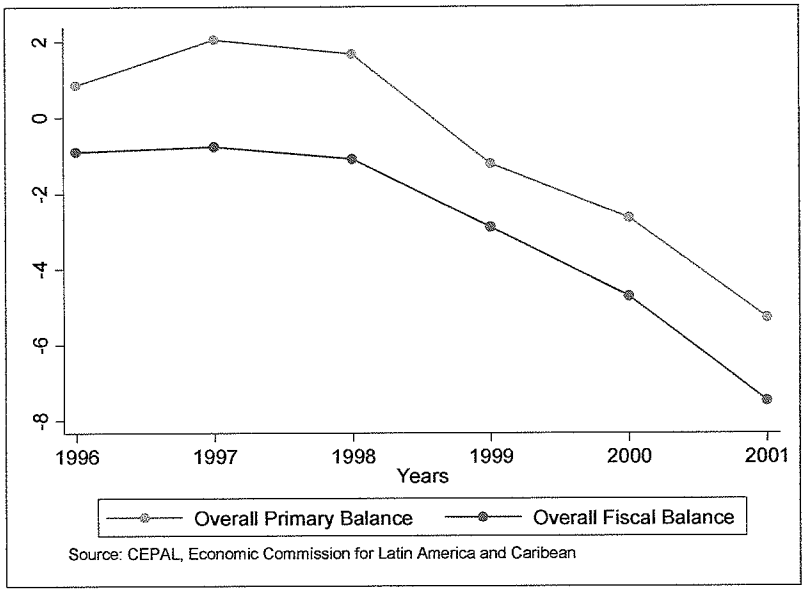
Hence, Alemán would continue to build his political machine and use the centralization of power ingrained in Nicaragua's political institutions to accomplish his goal. As Gonzales (2011), argues "in direct contrast to Chamorro," Alemán's governing style involved "direct instrumental power and central government resources to wage a permanent political campaign aimed at maintaining his support base in forthcoming elections, including the presidential campaign at the end of his term" (168). Immediately following his rise to the presidential office, Alemán - and his governing coalition - started looting the national treasury (Kinzer, 2003). State resources were important for Alemán, as he would not only use government expenditures, but

[22] The first sign of Alemán's PLC electoral success came in 1994 during the Atlantic Coast autonomous elections (Hoyt, 1994). The PLC gains 37 seats in the regional councils to FSLN's 33 seats.
[23] By the late 1990s the Liberal Alliance represented the collection of Nicaragua's liberal groups that aligned under the PLC.

was well known to utilize "juicy payoffs," consisting of government positions, all the way down to local levels, to buy the support of legislators and other important actors (Gonzales, 2011).

The usage of government resources allowed Alemán to build the PLC and nourished legislators' discipline with substantial success. According to Ferrey (2000), during Alemán's presidency, the liberal legislative majority did not initiate one law of their own and left all legislative activities to the president (as cited in Anderson 2006, p. 156). From his very first days in office, it was clear he would legislate from the executive branch. Most bills passed during his time were from the President, and at times he marked them urgent to avoid deliberation or modifications.[24] This power translated to his annual budgets, which were hardly modified during his presidency. Figure 3 shows Alemán's' declining fiscal balance over the course of his term. By the middle of his term, fiscal imbalances are apparent and increase steadily.

Figure 3: Overall Primary and Fiscal Balance % of GDP, 1996-2001
Arnoldo Alemán Administration



[24] Revista Envío. 1998. Time for Pact or Time for Reflection. Envío (204). <http://www.Envío.org.ni/articulo/1378.>

His 1998 budget, which included vetoes to include a slash fund amounting to a third of the budget, was approved without much congressional debate. This particular slash fund amounted to an equivalent of $190 million.[25]

Moreover, by the time Nicaraguan politics was under the influence of the *Alemán - Ortega* pact, the National Assembly was virtually under his complete control. Immediately following Hurricane Mitch, PLC and FSLN legislators joined and delegated a set of emergency powers used to initiate a general budget. In the 1999 budget, the National Assembly raised salaries for government officials: legislative salaries by $1,000, ministers' salaries and the president's base $10,000 salary, by $3000.[26] Effectively, Alemán's 1999 budget set off great conflict and suspicion on how government expenditures are utilized. Meanwhile, the Comptroller General's Office questioned the expansion of the budget for spending related to Hurricane Mitch, largely targeted toward areas of the country that suffered minimal - if any -damages.[27] Nevertheless, the National Assembly approved the executive's budget with very few changes.[28]

However, by the end of 1999, the start of investigations against the presidents and top government officials, took center stage. The Comptroller General's Office, under the leadership of General Agustin Jarquin, brought up countless corruption charges against the President.[29] Jarquin initiated investigations and audits against Alemán, not only over government

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[25] Revista Envío, Nipatelo Team. 1998. Nicarguan Briefs: Alemán's Budget Vetoes Okayed Envío (1998) <http://www.Envío.org.ni/articulo/1326>

[26] Revista Envío. 1999. Nicaraguan Briefs: Who needs a budget without salaries? Envío (210). <http://www.Envío.org.ni/articulo/2218>.

[27] Alemán also initiated a set of other measures against non-governmental organizations (NGO) to tax their funding sources during Hurricane Mitch's relief efforts. This measure is the first instance when NGO's are required to pay taxes on their funding (Leslie, 2006).

[28] Revista Envío. 1999. Nicaraguan Briefs: Budget Approved with Glitches. Envío (213). <http://www.Envío.org.ni/articulo/2234>

[29] In 1999, the Swedish government retrieves its developmental funds toward the budget when it suspects Alemán is using aid for partisan ends to build the PLC (Hoyt, 2004).

expenditures, but the privatization scheme during the 1990s.[30] However, due to Nicaragua's weak checks and balances, Alemán ended investigations by bringing his own charges against the Comptroller and imprisoned him (Hoyt, 2004).

Loud domestic and international outcries pressured Alemán to release Agustin Jarquínm but by the time of his release, the Comptroller's office had expanded with new appointees from *El Pacto* and prior investigations were eliminated (Hoyt, 2004). *El Pacto* effectively consolidated political power between the FSLN and PLC, filling all government bodies with partisan appointments, allowing Alemán to continue his presidency and expand the national budget. While major suspicions were expressed daily throughout Nicaraguan society, the institutions to check his abuses were virtually non-existent.

Alemán's last budget was substantially larger than his 2000 proposal, with increases to government expenditures by 35 percent. It contained a number of discretionary spending items, while reducing municipal transfers from 2 percent to virtually zero. He left Nicaragua with a substantial deficit, much larger than recommended by financial institutions.[31] The presidency that rose to power during this period was defined by corruption levels unmatched by any other in Nicaragua's history. Alemán was suspected of high levels of corruption, with charges that his administration appropriated up to $100 million of the nation's funds (Kizner, 2003).

The Alemán presidency is interesting for several reasons. First, most analysts on Latin American politics, allege that ideologically conservative presidents are better equipped to carry out controls to spending. In his early years, Alemán's presidency symbolized just that: the continuation of neoliberal reforms and the reduction of the state. In fact, to many from

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[30] One of Alemán's biggest misuses of government funds was the helicopter base built at his personal home. When asked to explain these dealings, he simply used security forces' recommendations as a protective measure. He financed this expenditure with the president's discretionary funds (Hoyt, 2004).

[31] Revista Envío. 2000. Nicaragua Briefs: Budget Games 2001. Envío (232) <http://www.Envío.org.ni/articulo/1460>

international financial institutions, his fiscal policies aligned with the recommendations sent from Washington. According to Brown and Cloke (2005) international financial institutions working with Nicaragua obsessed over structural reforms, primarily privatization, which often fueled the corruption under his administration. As long as Alemán kept up with the privatization plans, his other dealing were often ignored.

Second, according to the predictions of theories about party politics, if presidents are armed with party discipline, they are better equipped to initiate more efficient outcomes (Mainwaring and Shugart, 1997). This prediction, however, depends on the usual assumption that presidents desire, above all other goals, to implement controls on spending. Instead, as Geddes (1994), argues, party discipline works either way in regard to reforms. If presidents want to initiate reforms, they will do so, while those who do not, can stall it. Thus, while Alemán enjoyed the benefits of high party discipline, he did not use it to initiate balanced budgets; instead, he capitalized on his hold of the PLC to increase spending, strengthen his political machine and his personal riches. This style of governance effectively creates rent-seeking behaviors from those in his governing coalition. Many of the privatized state owned enterprises were done to strategically benefit the PLC and their members (Brown and Cloke, 2005). Through privatization, government contracts, foreign investment and donations, Alemán re-directed funds for his own personal benefit and embezzled large sums of the state's resources (Kinzer, 2003).

Lastly, this presidency illustrates how Nicaragua's weak institutional constraints on the executive branch place it at risk to *hyper-presidentialism*. In this environment, when presidents are motivation to solidify their political power or personal riches, public accounts are left unchecked. This not only impacted fiscal balances, but democratic consolidation as governmental resources allowed Alemán to solidify his power and gain the implicit support of

his governing coalition to attack all political institutions. During this period, Nicaragua experienced changes to the constitution and electoral laws that reduce electoral competition, as well as increased government overhaul over non-governmental organizations (NGOs). The *Alemán-Ortega* caudillo pact initiated during the 1990s set Nicaragua on a fragile democratic path.

Enrique Bolaños (2001-2006): Governing without a Party

Nicaragua's third presidency was not only defined by institutional weakness, but also ironically, by relative success in the passage of annual budgets. The weak presidency in this period was caused by Enrique Bolaños' first days devoted to the fight against corruption. As argued previously in this chapter, if presidents are motivated to nourish accountability, political actors are held for their misuse of public office. However, Bolaños' corruption campaign caused the split of his party due to his first target being former president Arnoldo Alemán as divisions within the PLC erupted. Bolaños' anti-corruption campaign divided the PLC into two camps, one supporting Bolaños and the other Alemán, although Alemán continued to hold great leverage over the majority of PLC legislators in the National Assembly.

Nunez (2005) explains the surprising loyalty among PLC legislators, even after Alemán's 20 year sentence for corruption, by using the "smear theory" advanced by Jorge Castañeda.[32] This theory evolved from the analysis of how PRI Mexican presidents nominated their successors—which was based on identifying candidates who had also engaged in corruption—to guarantee their own impunity. PLC legislators, all of whom were part of Alemán's governing coalition, benefitted and pillaged state resources, some with their involvement since his Mayoral

[32] Revista Envío. 2005. Aleman still controls the PLC and Will Hand Ortega the Victory. Envío (292). <http://www.Envío.org.ni/articulo/3111>

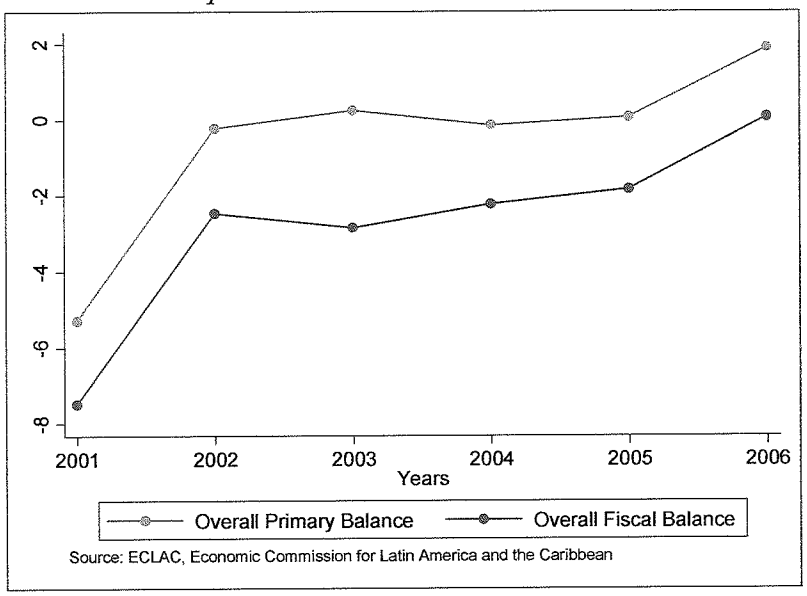
term. Hence, opposing the party boss would threaten their own political survival. And with his imprisonment, he could easily turn over hard evidence to threaten their freedom.

Consequently, by 2005 President Bolaños was left with only 9 of 92 legislators within the National Assembly (Brinkley, 2005). This type of executive-legislative environment is predicted to cause collective action problems, making it difficult for presidents and legislators to reach a consensus on fiscal balance (Haggard and Kaufman, 1995; Mainwaring 1999). But while Bolaños was unsuccessful in passing most of the laws he initiated in the National Assembly, he leveraged the HIPC (Heavily Indebted Poor Countries) initiative, which reduced the country's external debt, as a way to convince legislators to approve his annual budgets.[33] The incentive for the National Assembly to meet guidelines to enter this initiative is due to the ability of governments to re-direct resources toward education, health, and other services to address the needs of the vast majority of citizens which are also electorally useful. By the end of Bolaños' presidency, Nicaragua experienced an impressive fiscal recovery, as shown in Figure 4. In short, even a weak president lacking Assembly majority was able to use presidential powers to balance the budget if he set a high priority to do so.

[33] Aleman initiated efforts to meet HIPC requirements, but his administration's democratic progress jeopardized Nicaragua's entrance into the initiative. The country missed the opportunity by a few cutoff points.

Figure 4: Primary and Overall Fiscal Balance % of GDP, 2002-2006

Enrique Bolaños Administration



Enrique Bolaños entered the presidency in 2002, hampered by an economic slowdown. The growth Alemán enjoyed in the late 1990s waned, and by 2001, the boom in Nicaraguan export commodities had also slowed. Bolaños also confronted the legacy of Alemán's spending habits with a large deficit and high debt levels. [34] Consequently, Bolaños' budgets contained significant cuts, with a high priority to decrease the external debt, utilizing up to a fourth of the annual budget. He cut government salaries, discretionary funds, and compensation for top government ministers. In addition, he used a series of vetoes to block legislative input on government expenditures (Muhr, 2009). By 2003, as rising interest rates placed pressure on the country's ability to pay down the external debt, Bolaños took further measures with his proposed budget.[35]

[34] In the early 2000s, it's estimated that for Nicaragua to pay off its debt, it would have to use 30 years of its export earnings.

[35] El Nuevo Diaro. 2002. Un presupuesto que da ganar de llorar. <www.elnuevodiario.com> Last accessed April, 15, 2012.

The passages of his proposed budgets were ironically successful because Bolaños had a 'congressional majority at the beginning of this term,' with 49 PLC legislators, while divisions within the party reduced his legislative support. However, in this period, Nicaragua was eligible to meet requirements for the HIPC initiative and reduce its debt burden. Among the various macroeconomic austerity measures, to be eligible Bolaños' budgets must have also initiated cuts and reduced the deficit. Given Nicaragua's high debt, political parties have strong incentives to receive debt relief and lessen future budgetary expenses dedicated toward paying down the burden of the debt. Strategically, the National Assembly approved most of Bolaños' budgets allowing Nicaragua to enter the HIPC initiative. Consequently, the country experienced a substantial reduction in its foreign debt obligations (Close, 2005).[36]

Figure 5: External Debt as % of GDP, 2002-2007
Enrique Bolaños Administration

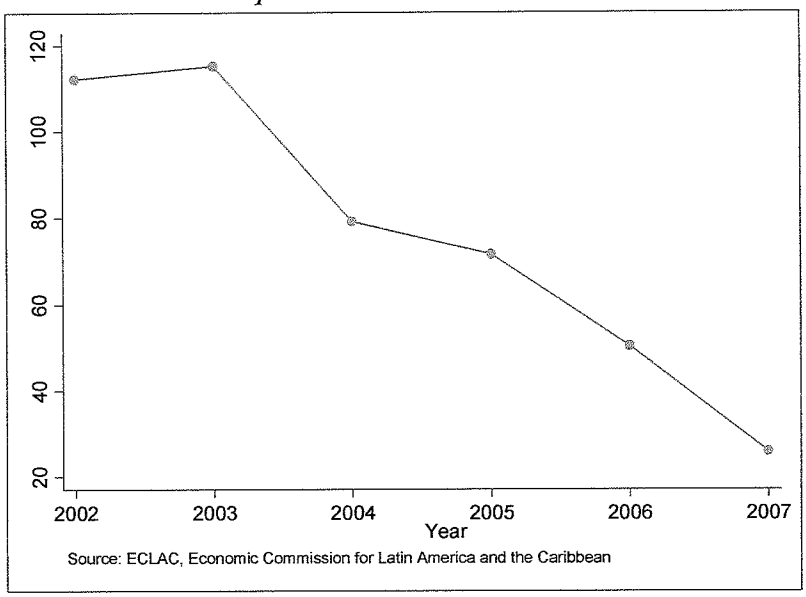


Figure 5 shows Nicaragua's debt reduction during Bolaños' term in office. Bolaños' last budget left Nicaragua with a surplus of 0.2 percent of GDP and a substantial reduction in

[36] One exception is the National Assembly's reactive role to Bolaños' 2005 budget. His desire to use 30 percent of the budget to pay down the debt causes legislators to initiate a set of changes to the budget. This caused a rather conflicted budget process and the IMF to temporary retrieve and stop loan assistance.

external debt. By 2004, Nicaragua secured $4.5 billion in foreign debt reduction under the HIPC, and by 2007 the IMF approved a Poverty Reduction Growth Facility replacing the nation's structural adjustment program.[37] He successfully increased grants and loans disbursed to Nicaragua from international financial institutions, while at the same time he also increased assistance toward health and education. Moreover, international reserves tripled by the time he left office.

The improved budgetary outcomes of this presidency are driven by strong economic incentives by political parties, since it is in the best interest of ruling parties to qualify for the HIPC initiative and reduce the proportion of the country's resources going toward the debt in order to increase a politicians' ability to direct resources toward electorally useful domestic programs. Nicaragua's annual debt obligations dropped from $200 million to $90 million. His anti-corruption efforts, however, were complicated by Alemán's hold over the PLC and left Bolaños with a coalition of fewer than ten legislators. Traditionally, it is assumed that if presidents hold state resources they can buy the support of deputies. However, Alemán's legislators are loyal to him because of his role in their accumulation of wealth through state positions, as well as the stark class division between Bolaños' closest allies, and circle, with Alemán's legislators. This presidency effectively splits the PLC and caused the decline of its presence in the national scene.

Daniel Ortega (2006-present): Finding New Methods to Keep Spending: Budgetary Politics Under Neoliberalism's Constraints

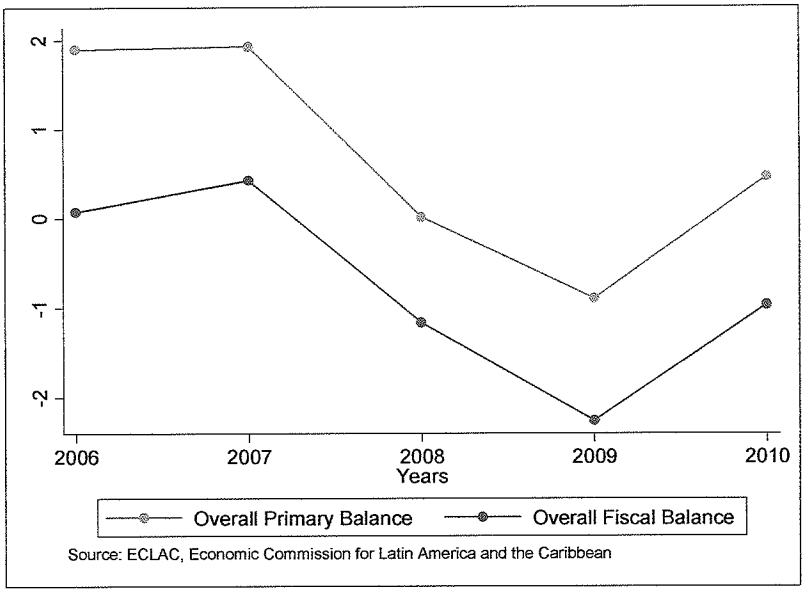
While Bolaños' corruption campaign and the arrest of former president Alemán was surprising and a first in Latin American history, equally startling is former revolutionary FSLN leader Daniel Ortega's response to the demands of the global economy. As with many leftist

[37] HIPC Wikipedia <http://en.wikipedia.org/wiki/HIPC>

leaders in the region, he accepted the role of markets but with social policies (Roberts, 1997: 316). Ortega has initiated market friendly policies for Nicaragua's private sector and fully embraced Central American's free trade agreement (DR-CAFTA). Exports have increased yearly and foreign investments has grown fivefold (Luxar, 2011). Moreover, Ortega has kept strong diplomatic relationships with international financial institutions, and according to Rosales (2011), Ortega has become the poster child of the IMF. In sum, Ortega has proven to toe the liberal line as a governing leftist president within a globalized world.

Yet Ortega's embrace of market forces was not accompanied by an acceptance of electoral democracy. His 2012 presidential campaign slogan, *"Vamos por mas victorias,"* (We are going for more victories), describes his most important priority: to remain in power. Since 2006, Ortega has taken calculated steps to accomplish his primary goal, successfully increasing his relatively weak electoral base with macroeconomic stability and targeted expenditures. As a result, his governing style has directly impacted budgets, but this administration's fiscal outcomes are more complex than mere increases in spending.

Figure 6: Overall Primary and Fiscal Balance % of GDP, 2006-2010
Daniel Ortega Administration

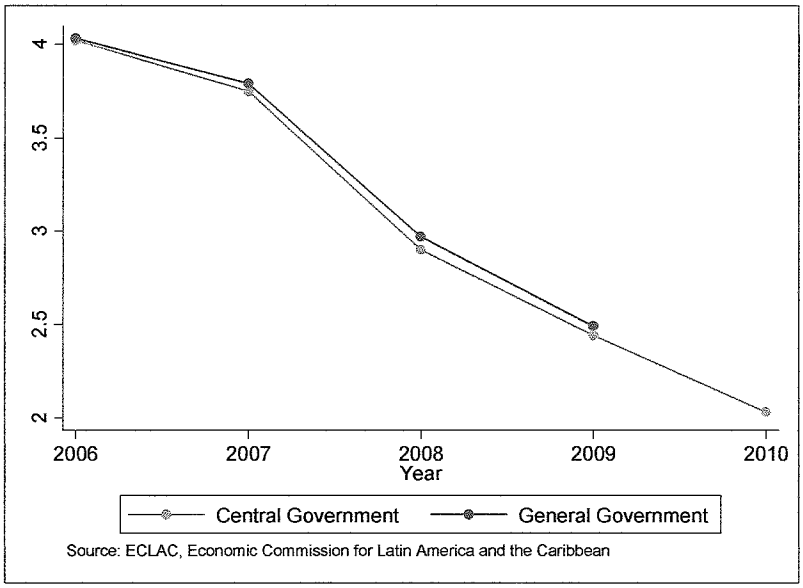


Ortega's electoral victory in 2006 was a direct result of the rule changes agreed to under *El Pacto's*. Without the reduction of minimal threshold for first-round victory in presidential elections to 35 percent, Ortega would have had to face a run-off, which he might well have lost. He won the presidency with 36 percent of the popular vote, a rather weak support base. Consequently, Ortega took immediate measures to increase his support through various measures. His first budget, however, was not a break from the previous presidency. In fact, his first budget mirrors those implemented during the Bolaños administration, with modest changes and efforts to pay down the external debt. This strategy was needed to meet IMF requirements, and, by 2007, Nicaragua was granted further privileges from the HIPC initiative. Nicaragua's external debt levels continued to drop - from approximately 50 percent in of GDP in 2006 to 25 percent of GDP in 2007.

However, by 2008, Nicaragua started to experience fiscal imbalances. While the global economic crisis directly affects Nicaragua's economy, deficits are also the result of the country's decline in its democratic progress. Specifically, the 2008 municipal elections are full of irregularities, lack of transparency, arbitrary elimination of power parties and refusal to allow independent electoral observers to enter the country. These political outcomes set a precedent for Ortega's governing style and causes alarm with international donors; subsequently governments begin to retrieve their funding. This causes fiscal imbalances because donations are historically an important component of Nicaraguan revenues, usually in the form of budget support for health, education and anti-other poverty measures. Furthermore, in terms of public service projects and infrastructure, the Nicaraguan government has not implemented privatization efforts (Lora, 2007). Thus, the national government continues to finance these

areas of spending, but annual budget calculations for public investment are heavily dependent on donor aid (Vogl & Kublbock, 2010).[38]

Figure 7: Grants % of GDP, 2006-2010
Daniel Ortega Administration



In 2008, Sweden, after 30 years of budget support, cancelled its aid. Thus, after 2008, Nicaragua starts to experience fiscal imbalances. By 2009, the European Union only disbursed $14.5 million of its $100 million pledge, due to further concerns about the country's political developments following a ruling allowing Ortega to run for presidential office a third time.[39] While executive term limits have changed markedly in Latin American nations, these constitutional amendments have been the result of Congressional approval. Ortega, however, does not receive enough legislative support to pass his re-election proposal with the National Assembly. Instead, he used his political control over the Supreme Court to declare the ban on reelection as unconstitutional. Today, most donors have withdrawn their aid (Vogl & Kublbock, 2010).

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[38] Ortega has issued emergency decrees to re-allocate budgetary expenditures toward infrastructure after heavy rains in 2011 destroy roads throughout the northern area of the country.
39 Revista Envío. 2009. Riding the Wind With The Sails Full. Envío (340).
<http://www.Envío.org.ni/articulo/4094.> Last accessed April 15, 2012.

Although it is true that Ortega displays an indifference to donors' request for greater transparency and democratic progress, in the neoliberal era, he is inclined to adhere to the demands of international financial institutions. International actors have an ease to influence Nicaragua's economic progress, through freezes on loans or signals to investors. Consequently, by 2010, Ortega initiates cuts to his 2010-2012 annual budgets, especially in health and education, to address fiscal imbalances caused by the economic slowdown and retrieval of donor aid.[40]

Ortega's conformity with the demands of the global economy raises a series of questions of how he is able to maintain voter support. Traditionally, decreases to government expenditures conflict with presidents' immediate ability to distribute goods and sway voting behavior. In this period, though, the emergence of Venezuela as a substantial donor allows Ortega to sidestep the rigidities of budgets in a neoliberal era and get along without first world donors. Since his first year in office, Venezuelan aid has been estimated to amount to seven percent of Nicaraguan GDP every year, approximately $500 million. While these funds are controversial because - unlike previous donor aid - they are not included in the annual budget, opposition legislators also argue spending is allocated strictly to Ortega's supporters and members of the FSLN.[41] According to Baez (2009), the usage of a parallel budget is the first time the country has experienced this strategy.[42]

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[40] In comparison to Bolaños' budgets, which dedicated 42 percent to health and education, Ortega's budgets allocate 35 percent to these spending areas.

[41] Funds are administrated by a private company ALBANISA (ALBA de Nicaragua, S.A.), which is under FSLN management control. Ortega asserts these funds are used for ALBA (Alianza Bolivariana para los Pueblos de Nuestra América), social programs, his anti-poverty initiatives.

[42] Ortega's share of discretionary spending is also supplemented with any increase in government revenues. In 2011 Nicaragua received an unexpected increase in revenues, and the government used it to pay off debt owed to a Nicaraguan energy company (Sáenz, 2012). It is speculated that this debt was owned from an FSLN private company.

Specifically, Venezuelan aid funds Ortega's Citizen's Power Councils (C.P.C).[43] C.P.C. provides assistance in the form of food subsidies, small business loans, public infrastructures and farmers' assistance. Targeted spending is Ortega's strategy to gain new voters but most importantly recover alienated Sandinista supporters (Rogers, 2011). As argued by Brown and Cloke (2005), voter dissatisfaction, in countries like Nicaragua and El Salvador, results from the lost ideological fervor found in the revolutionary struggles, and absorbed by "previously existing *clientelistic* power structures of the region, with the spoils of the state resources going to the winner" (606). Combining macroeconomic stability and Venezuelan aid to fund his social programs, Ortega has successfully increased his support, regardless of his anti-democratic practices. According to Rogers (2011), voters' hardships outweigh any concern with democratic practices, and it is the reason why the distribution of goods has satisfied segments of the Nicaraguan population. By the 2011 presidential elections, Ortega engineered an electoral victory with over 50 percent of the vote. He gained the support of not only alienated Sandinista voters, young and new voters but satisfied Nicaragua's independents that traditionally represented an anti-Sandinista vote (Rogers, 2011).

The Ortega presidency is defined by his transformed response to the demands of the global economy. He has met IMF obligations, signaled the country's friendly investment climate and appeased Nicaragua's private sector. However, despite the fact that Ortega has met expectations in a neoliberal era, he continues with his usual iron fist hold on Nicaragua's political institutions. With electoral fraud remaining an option for the regime, his politics have contributed to donor community's flight. But the costs associated with retrieving foreign aid has not motivated Ortega to comply with donor demands for democracy, transparency and

[43] The 2006 National Assembly voted against C.P.C's. However, Ortega initiated these local councils with the argument that citizens are best assisted through governing bodies on the ground (McKinley, 2008).

accountability. His indifference to vital international donors is due to two very important economic factors.

First, he has kept strong ties with the IMF and World Bank, and has supplemented the loss of aid with loans (Vogl & Kublbock, 2010). Accordingly, from 2008 to 2010 external debt grew from 24 percent of GDP to 30 percent of GDP.[44] But most importantly, his political strength is defined by the emergence of a large financial alley: Venezuela. This aid provides him with discretionary spending, due to the elimination of congressional involvement in the use of off-budget revenues, to solidify his political power. I shall maintain the general thesis of this chapter that, while Venezuelan aid has assisted Ortega's ability to address fiscal imbalances, and yet channel goods to supporters in order to preserve and increase his voter base, the centralization of power within the executive branch has been strengthened by a major source of revenue that the president can use without even the minimal congressional oversight experienced by earlier Nicaraguan presidents. Given the unpredictability of the world economy and Chavez's health, the dependence on Venezuelan aid is not a sustainable way to govern and Ortega may soon find himself confined within the limitations of Nicaragua's annual budgets. Controls to spending, however, will conflict with his most important political aim to retain absolute power.

As his presidency has illustrated, Ortega represents a continuation and revival of Nicaragua's past, of unilateral decision making by presidents and violations of constitutional practices. The most recent example of unilateral decision making is Ortega's decision to join the start up bank initiative, BANCO, a Latin American regional bank, and provide one-percent of Nicaragua's Central Bank reserves.

However, this decision is a violation of Central Bank Independence Law *(i.e. Ley Orgánica del BCN),* passed in 2010, to eliminate the Executive's Role from Central Bank

[44] ECLAC: Economic Commission of Latin America and the Caribbean

operations. Days after Ortega's announcement, Central Bank Director, Rosales, a FSLN party member, known to toe the party line very strategically (Rogers, 2012), did not remain silent about the president's decision. Having gained a solid reputation for five years of strong economic measures, he took an immediate stance against Nicaragua's role in BANCO, utilizing Central Bank independence Law to support it.

Rosales stated:

> "I don't sincerely see how this could take place because for the funds to leave the country, I must sign their release, and I'm declaring now, there's no possibility that a single amount will leave, not one *córdoba*, not one dollar, not one-hundred or two-hundred."[45]

Within a week, Ortega announced Rosales resignation. However, Nicaraguan institutional bodies that should be independent are solely driven by partisan politics and without the support of the party in power, the president can force the resignation of any official who disagrees with him. Ortega's violations of constitutional laws and unilateral decision making, offers an example of continuity in - rather than rupture with - his past authoritarian practices.

IV. Conclusion

The Nicaraguan case illustrates that presidents are often positioned to control spending by utilizing powers outside the budget process. These powers can include party discipline that prevents other members of the president's party from influencing policy and the capacity of international financial institution to share incentives facing politicians. However, executives have not consistently used these powers to balance budget. Instead, these very conditions have enabled some presidents to achieve the long-term goal of enhancing their political power through buying support with public money. Consequently, this case study raises the importance of taking

[45] Chamorro, P. (2012, February 15). La Salida del "Capi" del BCN. *La Presnsa.* Retrieved from www.lapresnsa.com.

into consideration other equally important presidential goals that conflict with controls on spending.

The four administrations analyzed throughout this chapter illustrate the various factors that play into fiscal outcomes. The Violeta Chamorro and Enrique Bolaños presidencies made strong efforts to solve the nation's recurring fiscal imbalances. Chamorro's administration initiated cuts to spending, decreased the size of the public sector and reduced the deficit. There are various factors that influence her motivation to implement fiscal reforms, such as her coalition's ideology and external economic forces, but equally important was the incentive to address the country's devastating economic conditions left from the 1980s civil war, economic mismanagement and hyperinflation. The Bolaños presidency, while defined by a weak presidency - due to the divisions among the PLC, convinced the National Assembly to meet budgetary conditions as a way to quality for the HIPC initiative and reduce the country's debt. By the end of his presidential term, the budget is balanced and the reduction of the external debt allows the possibility to redirect government resources toward social spending and human development.

On the other hand, Arnoldo Alemán exploited the national treasury to build his political machine. And while Nicaragua's Comptroller's Office initiated efforts to audit budgetary expenditures, Alemán used his allies to undermine these checks to control his over reach. Moreover, oopposition party, FSLN, did not exert its influence over the judicial branch to neutralize Alemán's violations of checks and balances, further leaving his actions unchallenged. Their lack of incentive to block the use of state funds to build an opponent's political machine was due to their negotiation with the FSLN to form *El Pacto*, but, most importantly, to use their reluctance to set a precedent and empower the Comptroller's Office to investigate future

irregularities and illegalities by Nicaraguan presidents at a time when they expected to control the presidency in the near future. This lack of involvement was a direct calculation to protect their interests, which have been successfully carried out. Ortega's second presidency is a direct result of the *Alemán's-Ortega* Pact, which left intact partisan appointments throughout institutional bodies.

This paved the way for Ortega's continual violation of constitutional and electoral laws in his current administration. Since fraud remains an option for his government, it has alienated international donors, causing fiscal imbalances in 2008 and 2009. But, Nicaragua's entrance into the HIPC initiative has profoundly influenced what presidents can do, which has motivated Ortega to meet IMF obligations, and initiate cuts to annual official budgets, especially in areas of education and health, while continuing off budget-spending to aid his political objectives. Venezuelan aid has offset the loss of aid from northern donors, allocating Ortega capital to finance his political campaigns. Moreover, since this aid is managed outside the budget, it represents an extraordinary spending tool to target expenditures toward FSLN supporters or non-governmental organizations aligned with his political project without input from Congress. Effectively, Venezuelan aid builds his political strength and enables him to sidestep all accountability. Furthermore, while Chamorro and Bolaños had factionalized or unconsolidated governing coalitions, Alemán and Ortega were largely successful because they had unified parties to pave for their unilateral mandates and their unusual amounts of formal as well as informal presidential power.

The rise of unilateral presidential action, however, is not unique to Nicaragua - as my case of Argentina illustrates - or other Latin American countries. As Rose-Ackerman et al., (2010) argues, presidents will always seek to enhance their power "by creating institutions that

give them freedom to act and by undermining institutions designed to check their influence" (2). However, the extent of president's success in increasing their power *is* dependent on each country's political institutions and ability to constrain executives. In a fragile and unconsolidated democracy such as Nicaragua's, the centralization of budget power can prove detrimental to the allocation of scare resources throughout the entire society. The strong executive found promoted in the neo-liberal era has contributed to the erosion of democratic consolidation; presidents have used their prerogatives to direct resources and buy the support of other political actors to bypass institutions designed to check their power.

This chapter contributes to the literature formerly known as the second wave of reform, which recommends the consideration of how political institutions shape incentives within each country. As this study illustrates, the search for power is not constrained by particular ideologies. Rather the quest is rooted in individual presidential behavior, influenced by various motivations where actors respond to political institutions. Without understanding how political institutions create incentives for actors, many of the predictions inherent in theoretical processes will remain disconnected from the reality on the ground.

Conclusion

This dissertation begins with an anecdote describing Nicaragua's second presidency in its short democratic period. According to several verifiable accounts, the priorities Arnoldo Aleman's articulated during his campaign for the chief executive's position changed dramatically the moment he first sat at his presidential desk. Suddenly, serving the nation and its interests were far removed from his campaign platform. Instead, Aleman used the presidency to exploit government resources to further his party building goals and enrich himself, his family, friends and loyal supporters. His presidency contradicts the notion in most institutional analyses that executives have more incentives to initiative controls and thus should be allocated greater budgetary powers to offset potential actors with the incentive to augment annual budgets. This project's aim is to draw attention to executives' evolving motivations and the spending behaviors which result from those motivations. The chapters in this dissertation analyze the formal and informal work-arounds on budgetary politics in Latin America and indicate that presidents' incentive to balance budgets are not static.

My first finding contradicts the claim that Latin American presidents engage in pre-electoral fiscal manipulation because they assume voters are unable to punish wasteful spending and that the electorate's information about them and their policies is limited and that lack the ability to process what they receive. Instead, I show that excess spending has, in fact, been the result of termed out presidents lacking any motivation to enact responsible fiscal policies and win voters' support. These findings complement recent research indicating that, while clientelist methods of swapping votes for political favors is likely to continue throughout Latin America in the foreseeable future, a gradual shift in their behaviors has been observed, as "voters have developed the habit of using the ballot box to punish mayors or governors who devoted a

disprorportionate share of their revenue to public employment, rather than services or investment" (Reid, 2007: 288).

Moreover, I challenge theoretical assumptions in the widely accepted literature on this subject: that enhanced presidential power leads to reductions in spending. While theory predicts that legislators are inherently driven to escalate fiscal problems, the case studies in this project point primarily to presidents as the primary driving force of excessive spending. In fact, I found no clear relationship between hierarchical budgetary institutions and presidential controls on spending. I found Instead that these very same powers, in the hands of self-motivated political figures, have led to opportunistic behaviors in the executive branch.

The Argentina case study is an excellent illustration and points to the danger of congressional bodies delegating further budgetary powers toward the executive branch. In the face of an institutional crisis, Néstor Kichner capitalized on the opportunity to manipulate spending decisions toward his political allies and acquire unusual amounts of informal power. This is turn left the country's main opposition further marginalized and limited in its ability to check unilateral acts of power throughout the 2000s. In similar fashion, strong presidential powers in Nicaragua have backfired when presidents believed they could serve their political interests by more spending. In an unconsolidated democracy such as Nicaragua, these powers also demonstrate that actors can buy enough support to bypass or alter institutions expected to check their political power. Both case studies further illuminate executives' nuanced ways to go off-budget to pay for expenditures previously included in annual budgets. This strategy becomes a medium to spend without congressional input or control, and is primarily used as a tool to buy the support of allies and eliminate checks on their power.

In short, this dissertation reveals that while procedures, rules and spending ceilings are constantly written into constitutional texts, laws are often bent to suit politically motivated decisions. The findings in this dissertation will hopefully play a role in illuminating future research on fiscal policy, as previous assumptions have led to inaccurate predictions about presidential incentive structures and spending habits. Most important, the case studies point to occasions in which formal institutions are often circumvented when presidents have equally important political interests and find unusual amounts of informal presidential power to reach their political aspirations. Without fully understanding the kinds of methods presidents use to circumvent formal institutions, the prevailing literature on political difficulties that impact economic liberalization will continue to fall short in predictive value--unless the most important factor in Latin American politics, the executive branch, is placed at the center of analysis.

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