Shrinking Space: International Constraints on Economic Policymaking

by J. Preston Whitt

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Susan Sell
Professor of Political Science and International Affairs

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Abstract

In 2013, I first proposed the concept of “forced equilibrism” (FE), which called for researchers in critical international political economy to study the shrinking policymaking space available to medium power country leaders. In that limited, initial work, I focused on a single Latin American government that was forced to navigate between the demands of increasingly powerful international capitalists and their allies on the one hand, and the increasing potency of domestic political constituents either to make their demands heard or to disrupt the national market on the other hand. In this work, I identify three interrelated international channels through which countries face and accept or overcome the constraints of FE: trade, finance, and extractives. I then illustrate these forces through narratives focused on specific policy decisions. The goal of this work is to test the analytical robustness of FE by considering the cases of two of the region's other middle powers, Colombia and Chile, as well as Latin America's burgeoning global power, Brazil. The findings suggest that FE is indeed useful as an analytical tool or conceptual framework for explaining certain aspects of modern Latin American political economy.

Table of Contents

I. INTRODUCTION

The 113^{th} Congress of the United States, serving from 2012 to 2014, infamously became the least effective Congress in U.S. history. After 76 years of state operation, Mexico approved in 2014 the opening of its oil monopoly PEMEX to limited privatization. Chile suffered three years of protests from 2011 to 2013, demanding radical changes to the constitutional status quo and facing staunch resistance from the government until Michelle Bachelet's return to power in 2014. Brazil's own state-run oil company, Petrobras, was at the time of writing embroiled in a campaign financing scandal that plummeted approval ratings and threatened even the upper political echelons with imprisonment. Despite a decade of good governance reforms in Colombia, severe challenges remain around impunity and the real effectiveness of nominal policy changes.

What do these stylized examples illustrate? They show that the Western Hemisphere is awash in sometimes successful, often unsuccessful, and always difficult policymaking with the potential for radical changes in citizens' lives. But more profoundly, they are examples that demonstrate that the region provides excellent test cases for understanding how a variety of factors change and affect policymaking *space*.

In a 2013 initial work that this thesis develops, Whitt proposed the concept of "forced equilibrism" (FE) and called for international political economists to study FE and its effects on policymaking. In the FE phenomenon, two conflicting policy demands clash: those of international economic actors on the 'right', and those of domestic constituents on the 'left'. As these demands diverge, possible compromise solutions dwindle, shrinking the policymaker's policy 'space' in the middle, and leaving them with fewer viable options from which to choose that would be acceptable to both sides. Taken to the extreme, no compromise solutions exist, the middle disappears altogether, and policymakers are forced to choose between the two sides. The non-chosen side will find the policies unbearable. The left will spill into the streets or otherwise exhibit a massive democratic swell against the policymakers' government. The right will withdraw its productive or financial support from, or even wield its capital against, the policymakers' government. Either way, the next election is lost.

The FE concept intended to respond to the clear need for "a model that incorporates a fuller representation of organized interests and lobbying at the domestic level, while also allowing for the ways in which incentives and constraints are generated at the international level," which "is an extremely complex and challenging task that still remains, to a very large extent, undone" (Hiscox, 2010: p. 79). In this study, I explore the forces on the 'right' side of this dynamic more deeply, to identify and understand the international capitalist forces that pull the policymaker to the narrow middle, and constrict the space available therein. To carry out this exploration, I use three country cases from Chile, Colombia, and Brazil. These three countries each face a distinct but comparable array of the following forces.

First, the global trading system, both in terms of its economic benefits and its governance, tends to be biased against smaller, developing countries. Countries that are more dependent on trade and open economies will be more restricted in the types of economic policies they can implement. What is more, they are less likely than more powerful partners in the current World Trade Organization (WTO) and free trade agreement (FTA) system to have the means to change the rules of the trading game.

Secondly, and often the most powerful, is the international financial system, and its connection to domestic economic policymaking. As in Whitt (2013), international sources of FDI and government financing often wield immense power over the decisions policymakers can take. They can even go so far as to essentially ban many policies as off limits. Kaplan (2013) named this effect the "political austerity cycle" and delineated four categories of constraint based on the country's financial portfolio and history with inflation.

Finally, extractives play a key role in determining policymaker space, especially in Latin America. In certain cases, extractives may strengthen policymaking space against the first two forces. Countries subject to the restrictions of the trading force may be treated more leniently if they have significant enough deposits of key resources. Similarly, windfalls from extracting and exporting natural resources can drastically empower a government to resist the international financial restraints. However, this strategy is subject to many dangers, including global commodities price shifts, supply exhaustion, or, most severely, risks of becoming a rentier political economy (Omeje, 2008).

This study proceeds as follows. Section II more fully defines the concept of forced equilibrism specifically and the shrinking space phenomenon more generally. It reviews the literature surrounding this idea, and details the theoretical underpinnings of the three forces. Section III explains the original Peruvian case used to elaborate FE as a concept, and presents the case studies of Colombia, Chile, and Brazil. Section IV summarizes the case studies and then concludes.

II. THEORY, LITERATURE, and DEFINITIONS

This section more fully defines the concept of forced equilibrism specifically and the shrinking space phenomenon more generally. It reviews the literature surrounding this idea, and details the theoretical underpinnings of the three forces.

Theory behind the Concept of Forced Equilibrism (FE)

Whitt (2013)'s treatment of FE explored the concept from both angles, highlighting how domestic actors on the left and international constraints imposed from the right conflict, and reduce policymaking space. It is important to note, as do Wiesehomeier and Doyle (2012), that this left-right division is of course an ideological shortcut to group and predict policy preferences. While the exact content of this division will necessarily be country context specific, in general terms research has identified sufficient similarities that such a simplification does not lose very much analytical rigor. Thus, FE continues the ideological shorthand "predicated upon differing attitudes towards equality…the roots of, and responsibility for, inequality in society, together with the practical translation of these beliefs into economic policy" via "the responsibility of the state to level the playing field" (p. 25).

This previous exploration cited a wealth of information from critical international political economy, showing that FE should not be considered an entirely new concept, but rather an extension of several critical forays into the effects of international economic processes on policymaking agency. For example, the primary previous stream of theoretical inspiration began with Polanyi. Polanyi (1944) launched a groundbreaking analysis of how unchecked market forces can denigrate humanity to the point of inciting a social-led, reactionary backlash demanding that the state offer some degree of protection. From this basis, Kayser (2007) studied how through modern globalization the more powerful and pervasive internationality of the economy changes the *how* of the policymaking process, and does not only affect the *what* of policy outputs. Similarly, Moraña (2008) observed that "cultural institutions, economic structures, and political parties collapsed…under the shadow of debilitated states", such that the state is "the space of negotiation and management…the objective of new strategies of social recognition" (p. 32-38).

Cox founded a closely related branch of this first stream. Cox (1981) introduced the historical materialist conception of international affairs, which considers states as unique configurations of "state/society complexes" instead of "competing bureaucratic entities" (p. 127). It treats social conflicts as the smelter of old and new structural relationships between these complexes. Alongside Cox, Strange (1997) addressed the erosion of the traditional state, in terms of reduced importance of military might, less financial independence, and an ever-more vehement struggle to balance taxes and welfare spending. This "elite-driven process" of globalization as identified by Cox began to shape states' "preferences and outlooks… state apparatuses acted as mediators between the global restructuring of capitalism and the spheres of finance and production most closely linked to these exogenous changes. The interests of national social forces were therefore subordinated to the demands of the global economy…" (Macartney & Shields, 2011: p. 33).

If the first stream focused on the effects of the power dynamics of globalization on policymak*ing*, the second stream provides the basis for analyzing the effects of these dynamics on policymak*ers*. Holsti (1970) applied 'role theory' to international relations and political economy. Previously, role theory had emerged in other social sciences and focuses on the interaction between the free will and decision making of the agent with the expectations placed upon him or her by the principals. Holsti developed the idea of a "national role consensus", which consists of four key concepts: Role performance, "the attitudes, decisions, and actions" of the executive; national role conceptions held personally by the executive that interplay with the role prescriptions "emanating…from the [domestic principals] or external environment"; and finally the position itself, the institutional and legal powers of the executive (p. 239-240). Though Holsti originally held it as a constant, his national role consensus even included the 'international context' as a source of influence on role prescriptions. This influence was transmitted via a set of stimuli to which the executive responds such that different states would have different state-society complexes interacting with the system in distinct ways.

Holsti's work with role theory inspired Cantir and Kaarbo (2012) to hold a special conference specifically to address the promise of role theory in IPE. Cantir and Kaarbo promote consideration of "contested roles" between domestic elites and social movements who tend away from a national role consensus. That is, "the impact of international norm and role structures is not automatic, [but rather] shaped by the agents (and domestic structures) in the domestic political process" (p. 5). Santiso (2006) further analyzes these agents specifically in the Latin American context. For him, policymakers in Latin America adopt a "political economy of the possible" based on pragmatic combinations of social policies within neoclassical orthodoxy, often through "neoliberalism by surprise" (p. 184).

Knafo (2010) provides a conceptual way to unite these two streams, and it is her path that this study continues. Knafo shifts the analysis to "power struggles", in which agents are "social forces [attempting] to develop means to relate to a social reality [or structure] that partly escapes their control and which they seek to influence or change" (p. 510). Framing the problem in this way allows for the analysis of the effects of the dialectic between agents and their structure, the modern international political economy, which can also be conceptualized as forces that provide both constraints and opportunities.

The following subsections now detail these forces.

Force One: The System of Global Trade

Scholars have certainly not ignored power dynamics in the system of international institutions and global trade governance (Barnett and Duvall, 2005; Birkbeck, 2011). However, as Shadlen (2006) points out, there are two key ways in which the shape of global trade and its institutions and systems constrain policymakers that require further attention than they have hitherto received. These two channels comprise the constraining force of global trade as I define it in this manuscript.

The first mechanism involves *what is being negotiated*. First, both regional or bilateral free trade agreements (FTAs) as well as many of the modern negotiation topics in the WTO go far 'beyond the border', and are often actually instances of developing countries conceding policy space in exchange for market access from a more developed partner. That is, trade negotiations are increasingly moving towards "deep integration" and "regulatory harmonization", where "developing countries gain increased market access and opportunities for specialization in exchange for diminished space for use of industrial policy instruments to create new productive capacities" (Shadlen, 2005: p. 750-751). These sacrificed instruments cover a wide area of "policy autonomy" and possible "institutional innovations that depart from prevailing orthodoxies" (Rodrik, 2001: p. 45). They can include topics from the environment, energy, and mining, to intellectual property rights, innovation policies, and explicit legislative rationalization (Horn, Mavroidis & Sapir, 2010).

This constraining dynamic is much more powerful in FTAs than at the multilateral level (Shadlen, 2005), but this is not necessarily a positive design characteristic of the WTO. That organization, too, limits developing countries' "maneuvering space to implement their development policies… The only way they can gain enhanced market access is by restricting their own policy autonomy in exchange." (Rodrik, 2001: p. 4). Rather, the WTO being less intensely constraining may simply result from the same reason that FTAs are becoming more popular at the expense of multilateral trade liberalization; the WTO is less effective as a means to address these issues that the major global trading players wish to negotiate (Chauffour & Maur, 2011).

Secondly, and very closely related to the first mechanism, is *who is negotiating*. Power asymmetries between negotiating partners often constrain trade strategies "in the most basic and fundamental way…developing countries are not selecting from an unlimited menu of options" (Shadlen, 2006: p. 215). In many 'North-South' agreements, the developed country, by virtue of the potentially transformative effect of providing access to its relatively huge market, has far more bargaining chips than the developing negotiator. Of course, developing countries do not sign these agreements at gunpoint, and in fact there is evidence for developing country negotiating agency and skill (Singh, forthcoming). But the "very power of the US market and its negotiating body…constrains the set of 'rational' policies that [policymakers of] countries like those of LAC can choose from" (Gallagher, 2008: p. 51). That is, trade policymakers in a sense are forced by rational choice among trade strategies to sacrifice domestic economic and development policy space in order to gain market access; essentially, they are "trading away the ladder" of development (p. 37). Khan (2007) found empirical evidence for this "closing of development policy space" in low-income countries, although the only Latin American country to figure among their dataset was Nicaragua.

Nevertheless, not all academics agree that the trade imperatives of stronger trade partners can shrink a policymaker's economic policy space (Echandi, 2001). Indeed, some argue that "bilateral trade negotiations clearly provide national governments with a source of power that they can use to bring about domestic reform" (Crump, 2007: p. 195). But, as Shadlen (2006) explains, such an argument is incomplete:

> Unlike standard models of trade politics, which depict the "winners" as diffuse and weak and the losers as concentrated and strong, the politics of [FTAs] in the developing world generally feature well-organized winners who are acutely aware of how they stand to gain from proposed policy change and diffuse and disorganized losers. And it is not merely a question of interests but of influence. Those actors within a given developing country who stand to benefit from increased access to the U.S. market typically have more weight in policymaking than those who stand to lose from regulatory harmonization…Thus, *contra* standard models of political economy, it is the opponents to [FTAs] in developing countries that are likely to be politically impotent. (p. 217)

The argument that trade can empower policymakers defines policymakers as particular bureaucratic or political entities; they do not address the Coxian state-society complex conceptualization of policymaking space that I use in this paper. In other words, I do not argue that no one perceives benefits from their connections to international trade or their trade ideologies. Rather, I argue that on the whole the modern trading system is one force that reduces the types of policies that can be effectively chosen in the historical and dialectic process (Cox, 1981) of economic policymaking, such that there is sufficient consensus that the policy is successfully implemented.

Force Two: The International Financial System

The pressures of the international financial system create the second, and often most powerful, constricting force on policymaker space. Theorists from the more critical and non-traditional camps of international political economy have long signaled the dangers of the "mad money" of "casino capitalism" (Strange, 1998). Now, even some global development institutions, including the traditionally liberal stalwarts like the World Bank, have begun to recognize the restrictive effects of "macroeconomic asymmetries" in the international financial system: "Whereas the industrial countries have greater freedom to adopt countercyclical policies that help stabilize financial markets, the developing economies have virtually no breathing space…" (Ocampo & Martin, 2003: p. 118). At the same time that many of its past conditions on loans have contributed to the problem, the IMF, too, admits that developing country "fiscal space" is an issue, where developing countries suffer from ineffective tax systems and domestic financial markets and therefore have little "budget room" to provide welfare without damaging the government's financial position (IMF, 2001; Kaplan, 2013: p. 31).

Krugman (2009) named this force the phenomenon of 'depression economics', the global financial market's pressure for pro-cyclical economic policies especially observable in Latin America. Kaplan (2013) further refined and elaborated on this concept, developing the theory of globalized 'austerity politics' and the 'political austerity cycle'. I use Kaplan's robust and clear model to define the constraints of the international financial system. In the political austerity cycle, the makeup of a country's financial portfolio and its history of inflation largely circumscribe the policymaking space of that country's leaders.

In Kaplan's model, the first determinant in the financial force's effect on economic policymaking space is the way developing countries use the international financial system to expand their fiscal space. That is, since developing countries often cannot depend on domestic sources of funds, they turn to either traditional money supply expansion via the central bank or foreign financing in the form of bank loans or bond issuance. When a government depends on international bank loans for its debt financing, it can take advantage of the large stake each lender has in its fiscal position. Policymakers know that their creditors must treat them with a degree of leniency, perhaps even going so far as to accept discounted, postponed, or restructured repayment. This creates a bit of a moral hazard problem but allows these leaders to operate with more fiscal freedom.

However, when a government depends on global bond issuance, ownership dispersion and the risk of a sudden stop/reversal incentivize austerity and austerity signaling in policy choices. Policymakers know that their creditors could 'cut and run' at any time, and will therefore always make sure their policies do not cause any panic among lenders. This creates a strong constraint on policy space. Further, as Kaplan explained,

> a key structural shift in the global financial architecture…narrowed governments' policy space…the shift to decentralized bond market financing in the 1990s curtailed politicians' budgetary capacities to spend on their domestic agendas…what reduces policy autonomy is not the amount of financial integration, but rather the nature of creditor-debtor relations (p. 9).

But as Kaplan observed, focusing solely on financial means does not suffice to explain policymaking behavior in Latin America. Therefore, the second determinant of the financial force's effect on policymaking space involves the psychological power of historical experiences. In countries that have suffered the rages of inflation, a common occurrence in modern Latin American history, voters, technocrats, and politicians will all tend towards a consensus based on fearing inflation's return. Whether price stability's predominance is an ideology "chiseled into their political minds" or whether they are just aware that the electorate might panic if a political opponent raises the inflationary specter, policymakers in these societies will face a practically real constraint against expansionary economic policies (Kaplan, 2013: p. 32).

As a result of the combination of these two dynamics, Kaplan describes four different 'cycles' of policymaking. For the purposes of this study, I use these four cycles as four categories of policymaking freedom.

- Traditional Political Business Cycle: Policymakers inclined to stimulate the economy (because the historical fear or risk of inflation is low) do *not* face significant funding constraints, due to possible funding sources like windfall natural resource profits, international bank lending instead of bond issuance, and foreign aid. Therefore, they choose expansionary policies to generate electoral support.
- Market-Induced Political Austerity Cycle: Policymakers inclined to stimulate the economy (because the historical fear or risk of inflation is low) *do* face heavy funding constraints from global bond markets. As a result, "they do not use accommodative fiscal and monetary policies to boost the economy. Instead, they use a neutral mix…" (p. 48-9).
- Inflation-Averse Political Austerity Cycle: Regardless of funding constraints, "past inflation crises breed economic risk-aversion…Worried about crossing the threshold of price instability, risk-averse politicians choose cautious macroeconomic policies" (p. 67).
- Political Austerity Cycle: If inflation-averse politicians also face heavy funding limits from the international financial system, they will favor strongly contractual

economic policies. They will focus on signaling to voters and creditors that their policies are sound from a price stability standpoint, above any other consideration.

Force Three: The Effect of Extractives

The ability of a government to draw upon natural resource rents can actually be a counterforce against the first two constraining forces. In trade, a government may have more negotiating power if it has a particularly rich or unique deposit of a resource another country finds valuable. In finance, a government may have more policy flexibility if it has a sufficiently valuable resource endowment from which to draw funds. Commodities may therefore offer a degree of freedom from the "prison" or "straightjacket" of the market (Kaplan, 2013: p. 11). In this way, extractives could actually increase policymaking space.

However, this ideal situation has not yet become the norm, due to the role of institutions within the extractive force. Many developing countries, including those of Latin America, lack the necessary strong institutions to exploit natural resources without falling victim to the resource curse (Mehlum, Moene, & Torvik, 2006). "Resource extraction shapes the societies in which it takes place", so for extractives to contribute to net welfare in a sustainable way, they cannot be simply "administered" (Haarstad, 2012: p. 10). Instead, the governance of extracting natural resources must be designed and institutionalized in a specific, often difficult way that takes into account some form of 'social justice'.

But this is easier theorized than actually put into practice, as Haarstad (2012) explained. "The same [policymakers who] are responsible for, and have significant interests in, the expansion of the extractive sectors" make policies around social justice in extractives based on the "pressures on and incentives for state actors, in other words, on political spaces" (p. 12). Put another way, "natural resource governance [is] one of the main areas where competing notions and claims for justice clash, and different proposals and counterproposals for a "just" governance of natural resources have been put forward by a wide range of actors at different scales" (p. 10). Thus, extractives can be surrounded by a conflicted space that prevents their productive and welfare-enhancing exploitation and an expansion of the larger policymaking space.

This is the theory of "rentier politics" (Omeje, 2008), and forms the mechanism by which extractives often limit economic policymaking space. Rentier politics occur around and within the "rentier space", which Omeje defined:

> The 'rentier space' discursively subsumes and upholds activities related to the acquisition and control of rentier resources in a state, including the disposition, appropriation and utilization of any accruable funds, perquisites, dividends and opportunities. At the epicentre of the coveted space is the rentier state controlled by the rentier elites. The ruling and governing elites are a core part of the latter and broadly represent their interests. In addition to the rentier elites who dominate the rentier space, there are counter-hegemonic forces drawn from (un)civil and political societies who contest and compete for accumulation within the rentier space. (p. 10)

Thus, in the rentier space, appropriating the immense wealth represented by the natural resource deposit becomes the primary motivation of political activity. Rentier elites, those who prioritize private wealth accumulation, on the one side and "society", those who prioritize policies like "welfare, development, resource distribution, land rights, [and] environmentalism" on the other, battle politically in the rentier space to try to capture the rentier state (p. 11). Because the rent-based stakes are so high, it is this battle that reduces the possibilities of compromise solutions, and therefore constricts policymaking space.

Buxton (2008) defined the Latin American perspective of the rentier space. As she explained, the Latin American rentier space has been relatively free of the violent struggle that can often characterize it, for example in many African nations. Instead, the two competing forces, the poor on the 'left' and the minority elite backed by and connected to transnational foreign capital on the 'right', have tended to channel their competitions through politics. Historically, 'populist' redistributions of resource wealth allowed Latin American governments to keep the majority satisfied, and the high dependence on international capital to efficiently extract natural resources further reduced the vehemence of conflicts in the rentier space. However, with the predominance of neoliberal ideologies beginning in the 1980s, widespread privatizations began to deregulate natural resource sectors and contract out resource rents. In the wake of decades of such policies, "which, along with the negative impacts of neoliberalism on the poorest sectors, served to deepen previously muted class-based cleavages…a wider, more complex and polarizing debate on the distribution of resource wealth" has emerged (p. 200). It is a competition:

> very much conceived as a zero-sum game, in which the wealthiest in society (and transnational private interests) should forego resource control and the opportunities for profit in order to enhance the prospects for equitable development. In this political schema, renationalization is seen as a fundamental for social and national development… In those countries… that lack viable and legitimate institutions capable of mediating grievances around issues such as ownership, the environment and workers rights, resource wealth is emerging as a catalyst or deepener of increasingly violent conflict (p. 200).

Thus, as the Latin American rentier space becomes increasingly contested, it can become the third force that constricts policymaking space more generally.

This section has illustrated the theoretical underpinnings of the three international-linked forces that restrict policymaking space: trade, finance, and extractives. The following section explains the three case studies I will analyze in order to see these three forces in action, and in so doing, test the utility of FE.

III. CASE STUDIES

This section begins with a brief overview of the Peruvian case study that Whitt (2013) used to offer the FE thesis as an explanation. It then moves to each of the three case studies I use in this work to illustrate the three forces in action and demonstrate this concept's applicability for explaining Latin American IPE phenomena.

III.0: Humala's Challenges to Peruvian Policymaking

The focus in Whitt (2013) differed slightly from that of this work, but nevertheless it was the original case used to propose FE as an important concept to be studied by international political economists. Therefore, it deserves a brief summary here. Whitt identified three 'critical points' for analysis, which were the three most significant policy decisions or dilemmas that the new Peruvian president, Ollanta Humala, faced in his first two years in office. These critical points were increased taxes on mining to boost social spending, neoliberal U-turns on campaign promises against FTAs and coca eradication, and a wavering management of widespread social protests.

The first critical point displayed, at least at first glance, a successful consensus policy that satisfied both the 'left', the broad swathes of Peruvian society demanding higher taxes on mining for greater welfare spending, and the 'right', the alliance of wealthy Peruvian elites and international mining companies who naturally wished to pay as few taxes as possible. Humala's policy space for this first decision was apparently not very constrained; he managed to negotiate with the mining companies to raise taxes enough to hopefully appease his base but not so far as to damage the companies' profits.

Shortly after this critical point, Humala faced the second, which took the form of two choices between his pro-indigenous, revolutionary campaign promises and the pressures of neoliberalism. The first choice related to FTAs; as an early candidate, Humala frequently denounced FTAs, using fiery rhetoric like calling such agreements treasonous to Peru's patrimony. However, by the time of the elections Humala had moderated significantly, and once in office he continued negotiating existing FTAs and even proposed new agreements. The second choice involved coca eradication, which Humala had previously pledged to end in order to attract support from pro-coca indigenous and peasant voters. But once in office, Humala accepted military aid from the U.S. to continue eradicating coca as part of anti-insurgent campaigns in areas of Peru still outside of state control.

Finally, the third and most powerful critical point was comprised of the ongoing social protests, largely around natural resource issues like mining projects. Humala shifted strategies multiple times within just a few years, alternatively appointing military hardliners, Catholic mediators, and justice-minded constitutionalists to attempt to resolve the crises. None of these strategies succeeded in appeasing the protestors, who were disappointed with Humala's performance against his promises, and demanded protection from the environmental degradation caused by mining projects, pay raises, and general welfare improvements.

Using these three observations, Whitt concluded that Humala suffered the effects of forced equilibrism. Although seemingly successful at increasing tax rates on extractive industries, the increase agreed with extractive companies was ultimately insufficient to satisfy the demands of society. Further, once in office Humala could not eschew the FTA strategy of his predecessors, but had to continue and expand it due to the belief that Peru's economy depended on international trade. In the terms of this paper, then, trade and resources were the two most important category of constraints. On trade, market access took precedence over policy freedom; Humala could not abandon the U.S.-Peru

FTA, could not walk away from negotiations for a FTA with the E.U., and saw the need to propose new FTAs with powerhouses in East Asia. On natural resources, the rentier space in Peru became so heavily and violently contested that Humala was unable to find a solution that both sides could swallow. Observing these forces limiting Humala's policy space resulted in the birth of the FE idea.

With the origin of FE reviewed, I now turn to the three in-depth cases of Chile, Colombia, and Brazil, to demonstrate how the three constraining forces previously identified function.

III.1: Chile

Chile was the last of the Southern Cone countries to fall to a military coup in 1973, and was also the last of those dictatorships to return to democracy in 1990. Since then, despite a series of leftist presidencies with one center-right exception, Chile has emerged as a poster-child for liberal economic development, growing on average more than 5% annually between the return to democracy and the global financial crisis in 2007. What is more, Chile used that growth to prioritize, at least rhetorically, policies for more balanced growth; the first democratic president elected after the dictatorship, Patricio Aylwin, even named his platform "growth with equity". President George H. W. Bush, in signing the US-Chile free trade agreement in 2003, noted that "For decades, Chile has proven the power of open trade and sound policies. It has become one of the strongest economies in the developing world" (Bush, 2003).

However, Chile's success was not without its challenges. Despite its achievements in reducing poverty, Chile's GINI coefficient has remained extremely high; at 0.51 in 2013, Chile had the highest level of income inequality in the OECD, although not in Latin America. Partly as a result of this pervasive inequality, Chilean society has begun to demonstrate "social disgust" with the status quo (Serra, 2011: p. 79). As mentioned in the first paragraph of this study, that social disgust most recently erupted as the massive student protests that cost tens of millions of dollars in public and private damages.

How can the three channels of FE shed light on Chile's paradox?

III.1.a: Trade

Trade has been a key driver of Chile's growth. Exports as a percentage of GDP grew from around 27% from 1986-1997 to almost 36% from 1997 to 2007 (Solimano, 2009). Though that percentage had fallen back to just under 28% in 2014, it still illustrates the significance trade plays in the Chilean economy.

More uniquely, Chile's policymakers have made trade an intentionally integral part of their growth strategies. In the first stage, part of General Augusto Pinochet's drastic reforms when he took power in the early 1970s involved severe unilateral trade liberalization. As a result, "in a period of five years…all non-tariff trade barriers were eliminated and the average nominal tariff rate was reduced from 105%…to a single tariff structure of 10%, which was maintained until 1982" (Laban & Meller, 1996: p. 164). After a brief resurgence following a balance of payments crisis in 1982, Pinochet carried out another, albeit slower, unilateral liberalization. At the end of his rule, the flat tariff rate had returned to 11%.

The next stage of strategic trade promotion began with the democratic government of Patricio Aylwin, who focused on more proactively reinserting Chile into the international economy through "open regionalism" (Fuentes Julio and Fuentes Saavedra, 2006). This open regionalism focused on multilateral trade agreements throughout Latin America, although not exclusively, and "consisted in the consolidation and expansion of [Chile's] export markets, to strengthen its international presence in the commercial and external investment planes" (p. 235). Subsequently, in the early 2000s

Chile turned towards the global 'megamarkets' by focusing on FTAs with North America, the European Union, and Asia Pacific. These most recent agreements involve a wide range of both economic and political topics.

The declared reasoning behind this sustained focus on trade promotion across regimes and time is simple: trade has driven Chile's growth. But this simplistic explanation is insufficient in understanding the relationship between Chile's trade and economic policy choices. Instead, there are four characteristics that merit analysis in order to clarify how FE is at play in Chile's trade focus and dependence.

First, it is important to underscore that Chile's exports have been almost entirely based on natural resources or their first-order derived products. These products formed nearly 85% of Chile's export basket at the end of the 1990s (Ffrench-Davis, 2002), and despite a brief move towards diversification in the early 2000s, "the path to diversification came to a halt after 2003" such that "Chile has maintained its export basket that is mostly composed of products associated with a lower income, such as raw materials, forestry and agriculture" (Varas, 2012: p. 20). Section III.1.c below will discuss the implications of this concentration in terms of the resource curse, but one result, as Serra (2011) points out, is that:

> The highly productive sectors involve a very reduced proportion of labor, while at the other extreme we have those sectors with low productivity but that employ the majority of Chilean workers. This has direct repercussions on the salaries that workers receive…This is the base of the social and economic inequality that the country presents, since the excess of non-skilled labor [inundates] the least productive sectors in which the remuneration is also the least (p. 90).

Second, although Chile's leaders recognized the risks of export promotion to over-concentrating their economy, their efforts to use economic policy to mitigate these effects have been largely ineffective and, in some cases, counterproductive. For example, although the government explicitly adopted a 'horizontal' trade promotion orientation as opposed to more targeted or sector-specific policies, its early stages may have favored infant industries like fisheries and forestry (Silva, 2004). Later efforts to diversify, as shown by the data cited above, have met with limited success.

Third, Chile's high dependence on trade has caused it to actively pursue and promote multilateral trade rules for stability, non-discrimination, and to prevent protectionism (Rosales, 2004). These very same rules then applied to Chile, and limited its own policy space. For example, those established through the Uruguay Round of the WTO imposed "disciplines in areas such as subsidies, FDI and intellectual property rights [that] impinged on the government capacity to define and implement policies to upgrade the domestic export structure" (Silva, 2004: p. 35).

Finally, the Chilean government's efforts to involve the private sector must be mentioned. As Silva (2004) delineated, several institutionalized channels exist for business associations to participate in and influence trade negotiations through the various government departments responsible for carrying them out. Although some sector-specific divisions have arisen, in general Chilean businesspeople support the continued integration of Chile into the global economy, and continue to make this support known. However, there are some notable absences and unresolved challenges regarding participation in trade policy. Unions play little to no proactive part in negotiations. Environmental civil society organizations (CSOs) and consumer associations are similarly situated. Thus, open questions remain around how "to improve the quality of international integration in socially-inclusive terms", from higher real wages, environmental sustainability, and human capital development (p. 44).

The government has made strides in the face of these challenges, even though trade's constraint on policymaking is still strong in Chile. But more salient for the Chilean case are the compounding financial and natural resource effects. The next sections demonstrate this interplay.

III.1.b: Finance-Linked Economic Policymaking

Chile's elections and economic policymaking since the return of democracy have epitomized Kaplan's (2013) 'Inflation-Averse Political Austerity Cycle', where regardless of funding constraints, the scars of severe inflation crises in the past cause all major parties to converge around cautious macroeconomic policymaking. In 1973, a profound economic crisis involving soaring inflation and intense scarcity of basic goods helped propel the military dictatorship of Augusto Pinochet into control of the country. Kaplan traces how the memory of this painful period affected agenda-setting and policymaking in each of the four election cycles between 1989 and 2006.

In 1989, an alliance of leftist parties in opposition to the dictatorship formed the *Concertación de Partidos por la Democracia*, or more simply the Concertación. These former leftists, including socialists and Christian democrats, spent the run-up to the 1989 election pledging continuity with Pinochet's conservative macroeconomic management, and publicly recognizing the achievements of his policies. Many of the front-line campaign efforts focused on "gaining credibility that [they] would have good economic governance", even going so far as to promise to "reduce government expenditures to show the private sector that [they] were serious…not populists, that [they] could control inflation, that the government would do its part" (p. 206). In 1993, 1999, and 2005, the government possessed the means, via access to cheap credit and natural resource income, to generate pre-election bubbles. But in every administration, the government focused on conservative economic management and, often, directly contractionary policies. Although the Aylwin government did carry out some tax reforms in 1989 and 1990, for the most part, privatizations and austerity policies, such as institutionalizing a required 1% of GDP budget surplus, dominated.

This mindset persisted, even when policymakers found themselves faced with economic crises. In responding to the 1998 recessionary effects of the Asian crisis, the government still prioritized keeping inflation at a minimum, opting for an intentionally limited stimulus that did not prevent a net contraction for the year (Kaplan, 2013). When short-term investment fleeing that crisis threatened to overwhelm Chile's exchange rate, growth concerns were secondary to the priority of reestablishing "macrostability" (Ffrench-Davis, 2002: p. 221).

Of course, democratic presidents are only elected if their constituencies support their represented ideas and platforms. That is, Kaplan's thesis rests on the social consensus around fiscal conservatism being a necessary fundament of the economy. While "a clear majority of Chileans [had] endorsed the government's cautious socioeconomic policies in both opinion polls and elections" from 1990 to 2000, by the end of the second Concertación administration Weyland (1999) could already identify that "continued social inequality…and the slow trickle-down of the fruits of growth compared to people's high expectations [had] fueled slowly rising discontent" (p. 69). This social discontent with a sacrosanct growth model came violently to a head in Michelle Bachelet's first term from 2006 to 2010, as two different large-scale protests shook the status quo.

In 2006, the 'Penguin Revolution' of high-school students, so called because of the design of their uniforms, mobilized hundreds of thousands of protestors. Though education was their primary focus, the protests more broadly "provided an outlet for the accumulated discontent with regard to limited political representation, the reach of state social policies, and the frustration of broad middle-class sectors over the barriers to social ascent" (Ruiz, 2012: p. 75). Partly inspired by the Penguin Revolution, in 2007 a more violent movement erupted from workers in precarious waged positions without contracts or social protections. These workers represented close to 15% of the workforce, and were paid as low as one third the wage of contracted workers. In terms of narrowing Bachelet's policy space,

> this movement involved the most representative group to emerge out of the neoliberal reforms, and therefore it produced alarm across the business world… They were rebelling against an employment status that had become fundamental to the prevailing economic system: flexible labor that led to precariousness of employment and sustained the high profit rates of the Chilean economy's most dynamic areas (p. 77).

In other words, many of Chile's social classes were dissatisfied and disenchanted, and therefore began to threaten to rupture the centrist model. The governing coalition was at a loss for a new compromise solution.

Despite these troubles, Bachelet recovered to end her administration with a high approval rating. However, this personal support did not translate to support for her coalition. As a result, in the 2010 elections, the Concertación lost to a wealthy businessman from the moderate right, Sebastián Piñera. Piñera triumphed in part because of the Concertación's inability to find a candidate, and a platform, that could satisfy its center left and far left wings. They eventually settled on previous president Eduardo Frei, who had left office with the lowest approval rating of any of the Concertación presidents. Piñera was thus able to market his campaign to constituencies previously solidly in favor of the Concertación, presenting himself as fresh and new and promising to both retain Bachelet's successes while improving jobs and growth (Toro and Luna, 2011; Quiroga, 2012). Put differently, Bachelet's administration should be seen "as a figure of continuity than of change and, in that sense, as embodying the limits of the Concertación's political and economic model", and "to comprehend the Bachelet period and its aftermath it is crucial to understand the narrowness of the civic space created by Chile's two dominant political coalitions" (Fernandez and Vera, 2012: p. 5-6).

Piñera's promises, however, were not fulfilled, and his administration found itself hamstrung by even more vehement student protests than Bachelet experienced in 2006. In large part, these protests were rooted in continued dissatisfaction with the education system as a path to social mobility. But this satisfaction was nested within a larger sense of unresponsiveness from the political system to citizens' needs, as evidenced by a rightist's election after 20 years of leftist coalition rule and "strong feelings of injustice and indignation…among the young as their grievances were not properly addressed by successive governments" (Guzman-Concha, 2012: p. 408).

Faced with this near-constant demonstration of public opposition, Piñera's administration still managed to achieve economic policy successes under the inflation-averse paradigm. At the end of his administration, he highlighted the creation of almost one million new jobs, high inward flows of investment, and inflation under 2% (El País, 2013; La Tercera, 2014). But voters disregarded these achievements, and in 2013, reelected Michelle Bachelet for a second term. Bachelet won her return through her promises to change the inflation-averse, political austerity policies that had dominated Chile and caused such social upheaval. Her popularity came from an explicit recognition that Chile was living "a social moment that wants to reformulate the representative system to take up the new demands of citizens", namely, universal education (Mardones and Toro, 2014: p. 27).

It remains to be seen if Bachelet in her second term will be able to overcome these entrenched financial constrictions. The answer may lie in the third mechanism of forced centricism, Chile's rentier space, to which I now turn.

III.1.c: Natural Resources and Extractives

A very large portion of Chile's economy is based on natural resources. In 2013, 27% of Chile's GDP came from mining alone, according to the Banco Central de Chile. A 2009 estimate found close to an additional 10% relied on either raw materials or processed natural resources like fruits, fisheries, and forestry (Solimano, 2009). If one factors in the fraction of services in the economy that are oriented to or dependent on mining, then extractives play an even larger role than the brute statistics can show. The main mineral mined in Chile is by far copper; in fact, Chile leads the world in copper production and export (Korinek, 2013). Furthermore, Chile's copper reserves are the most extensive, with 190 billion tons as of 2014. This was more than double the second highest reserves, in Australia (U.S. Geological Survey, 2014).

International institutions like the OECD have long held up Chile's resource governance as a model for other resource-rich nations (e.g., Korinek, 2013). These praises have tended to focus on the stability of Chile's resource taxation regime and, equally as importantly, its management of those revenues. In terms of tax rates, Chile has a progressive rate that is designed to boost revenues when copper prices are high, and reduce the pressure on mining companies when prices are low. When natural disasters or other major shocks have required boosts in government revenue, the government has always consulted with the private sector to arrive at "gradual" and "consensual" processes for policy change (p. 28). In terms of managing government revenue, a detailed 'structural balance rule' enacted in 2006 requires that government expenditures be based on a long-term structural calculation of the economy. This policy includes a variety of exceedingly important governance measures. It prevents rising copper prices from appreciating the exchange rate, the primary mechanism of 'Dutch disease' (Humphreys, Sachs, and Stiglitz, 2007. It provides counter-cyclical insulation from global booms and busts, reduces both the need and the cost of government borrowing, and ensures that social spending remains at a sustainable level (Rodriguez, Tokman, and Vega, 2007).

One key aspect of Chile's resource governance is the state copper company, CODELCO. CODELCO was created in 1976, from the nationalization of copper that took place in 1971. Since its creation, CODELCO has been the main source of governmental revenue from copper exploitation, dwarfing tax revenues from other copper firms. Indeed,

> In the last 20 years, Codelco [sic] has been the main provider of mining income and tax revenues to the country. Its transfers have averaged 13.5%42of the annual fiscal budget, and the company has played a key role in supporting Chilean economic stability and social development during the last decade... In addition to its direct contribution to government revenues; Codelco [sic] has promoted linkages with local firms and supported smaller mining-related companies, has generated demand for local service providers and has formed qualified national professionals (Sigam & Garcia, 2012).

Well-designed resource governance institutions and policies like these can help keep the rentier space civil, by reducing the stakes and therefore the vehemence of contention for political control. As José Pablo Arellano, a Harvard-educated former Minister of Finance and CEO of Chile's state copper company, explained:

> Moreover, they strengthen fiscal discipline by rendering budget outcomes that deviate from the level set by the fiscal rule costlier. These mechanisms contribute

> to the sharing of political responsibilities and make it easier for policymakers to bear the political burden of not being able to meet social demands in a low-revenue environment and to limit the benefit of spending revenue windfalls in boom years. By setting a formal budget target, the rule reduces discretion, since it can always be argued that the special circumstances of each economic cycle would justify a more expansionary policy (2006: p. 123).

Indeed, Buxton (2008) named Chile a “singular exception” to the Latin American trope of the rentier state, due to its institutionalized resource rent usage (p. 212).

Good institutions, however, do not completely insulate a state from the temptation represented by such large, unrealized rents. Problems can begin to emerge if this institutionalized system itself becomes a source of social and political discontent, for example, by being seen as primarily benefitting some classes or social sectors more than other. This may be beginning to occur in Chile.

As a practical example, one can consider the most significant ‘withdrawal’ of these saved funds: Bachelet’s stimulus package at the beginning of 2009. This widely lauded usage of fiscal stimulus in the face of the global economic crisis carried a price tag of more than US$4 billion. But that major deployment of accumulated state wealth was still circumscribed within the anti-inflation, fiscal conservatism previously discussed. As Bachelet herself explained in a 2008 speech, “We have these tools because at the time we knew to be firm and prudent. When so many were demanding that we spend incessantly, we did the same as so many matriarchs do in their households in Chile: we saved for a difficult year.” As the previously cited quote from Arellano showed, Chile’s resource discipline is a way to tie policymakers’ hands in the face of social pressures for greater social spending. It is still primarily a “signal of sustainability to financial markets” (p. 123), a system designed to be “transparent, predictable, balanced and within a range acceptable to the firms with international reach that inhabit the sector" (Korinek, 2013: p. 5). In other words, Chile's resource governance system prioritizes the copper extracting companies, and is oriented towards encouraging them to make the necessary investments to develop Chile's copper resources.

Despite the macroeconomic rationality of Chile's rent management, it was insufficient to avoid the previously discussed protests. This may suggest that Chilean society is no longer willing to accept the status quo. Before, the electorate accepted these political restrictions on resource income in favor of "an equilibrium that generates more growth and better incomes [rather than] a specific, more progressive redistribution of income…Perhaps they implicitly think that redistribution, if accompanied by higher taxes, will affect incentives for investment and growth, harming employment" (Solimano & Torche, 2007: p. 60). This is the standard calculation for an inflation-scarred populace, according to Kaplan's thesis, as explained above. However, natural resource wealth can provide an 'out' to these restrictions, and as it becomes increasingly clear that the current regime governing the use of these resources replicates income inequality and structural restrictions to progressive social policies (Solimano, 2009), this 'out' is likely to become more highly demanded. Indeed, the four most recent Chilean social movements around extractive issues, as identified by Barton, Román, and Fløysand (2012), all revolve around a common tension between government institutions, the national growth model, and "local justice" (p. 114).

Finally, beyond the unsatisfied social demands, there are other "unsettling features of the Chilean growth pattern" (Solimano, 2009: p. 11) that are necessary to understanding how Chile's golden age of sage resource-based growth may be threatened in the near future. In addition to some of the topics already described, Solimano identified the extreme pressures such an extractive-intense economy can have on environmental sustainability, especially the demand for energy, land, and fresh water resources, which are extremely limited in Chile. Similarly, other studies have found that even though Chile may have avoided a traditional, national-level case of 'Dutch disease', at the subnational level, much evidence exists that the resource curse is taking hold in different Chilean regions (Rehner, Baeza, & Barton, 2014). Arroyo and Edmunds (2010) suggest that the previous successes of Chile's extractives-based, export-led growth model may have "lulled the country into complacency", and that now this strategy "may be reaching a point of diminishing returns". If these concerns become reality, the political equilibrium may become even more likely to crumble.

In conclusion, even though Chile has expertly navigated all three forces, it may be approaching the limits of its success. Open, pro-trade growth policies, prudent macro-financial management and economic policies, and excellent, institutionalized resource wealth stewardship all may not be enough to satisfy the demands of the 'left', Chilean society. As one interviewee put it, when asked if Bachelet would be able to find a compromise solution for the country, "Bachelet won on a campaign recognizing that Chile needed a transformational change of model. But she did not say anything about royalties. What kind of change of model can there be without [addressing] royalties?" (Paredes, interview with the author, May 7, 2015).

Next, I turn to the Brazilian case. As a growing global economic powerhouse, Brazil should shed additional light on the effects of these three forces, and the utility of FE.

III.2: Brazil

Brazil alone makes up nearly half of what is considered Latin America; indeed, it is the fifth largest country in the world both by landmass and by population. The IMF's World Economic Outlook Database ranked Brazil seventh in terms of nominal GDP, with an economy of almost $2.4 trillion in 2014. It is unsurprising, then, that the chapter on Brazil in a recent primer on modern Latin American political history bore the name "The Awakening Giant" (Skidmore, Smith, & Greene, 2010: p. 306).

Contrary to the stable model of Chile, Brazil faced severe economic strain upon emerging from its dictatorship in 1985, and since then has survived wild booms and busts of growth and inflation. From 1985 to 2013, the average annual inflation rate in Brazil was about 380%, although in the period since 2000, that average rate has fallen below 8%. Brazil weathered the 2008 financial crisis well, at least in nominal terms, only contracting in 2009 by 0.3% and rebounding in 2010 with a growth rate of 7.5%.

Similar to Chile, however, Brazil has continued to suffer from high levels of inequality. In 2013, Brazil's GINI coefficient was 54.7, higher than Chile and higher than Brazil's 2012 score of 52.7, when it earned the place of 14th most unequal country in the world. Despite this hiccup, the recent trend has been a slow but steady decline in inequality since the 2000 peak of almost 60.

This decrease has been attributed in large part to the efforts of President Luiz Inácio "Lula" Da Silva (Skidmore, Smith, & Green: p. 346), and contributed to his record-breaking approval ratings of 78% in his final year in office (Datafolha, 2010). What is more, Lula achieved this popularity (and reelection) despite a campaign finance scandal in his third year in office. Yet his successor, Dilma Rousseff, only barely won a second term in 2014 in the "closest and most bitterly fought election in recent memory"

(Leahy, 2014), and her own campaign finance scandals resulted in a 64% *dis*approval rating (Passarinho, 2015).

Given Brazil's status as an emerging global leader, the size and makeup of its economic potential, and the turbulence of its recent politics, considering the three FE channels for the Brazilian case will test the basic utility and robustness of the theory.

III.2.a: Trade

Brazil is a large domestic economy, and as such, relies relatively less on international trade. From 2000 to 2014, goods and services exports as a percentage of Brazilian GDP averaged 13% according to World Bank data. For comparison, the entire Latin American region averaged 24% on the same measure during that period.

Despite this seemingly low percentage of importance of trade for Brazil's economy, trade has been a principal international diplomatic focus for the country. As Doctor (2012) explained, Brazil was an original member of the International Trade Organization, the General Agreement on Tariffs and Trade (GATT), and the GATT's successor, the WTO. Brazil was recognized as a leader in the Doha Development Round in 2001, and a vocal advocate for resisting manufactured goods liberalization without agricultural liberalization in return. "In fact, Brazil's overall aspiration to become a v'rule-maker' and not a mere 'rule-taker' in the international arena was first evident in international trade" (p. 800). In other words, contrary to Chile's unilateral liberalizations and conciliatory multilateral approach, Brazil has wielded its economic heft to help write and sometimes challenge the rules of the international trading game.

The WTO efforts, however, were just one aspect of a "triple-pronged trade liberalization drive" in Brazil in the early 1990s (Veiga, 2004: p. 177). The second prong was a series of unilateral liberalizations from 1990 to 1993, born from the lessons learned from the failure of import substitution models in the 1960s and 1970s, and the limitations of the “managed” liberalizations of the 1980s (Costa Vaz, 2004: p. 235). The third prong was MERCOSUR, the Common Market of the South, which emerged from “the political decision to promote liberal economic reforms unilaterally and to coordinate [Argentina and Brazil’s] response to the Enterprise of the Americas Initiative” proposed by the U.S. in 1990 (p. 235).

But this drive for liberalization quickly slowed. Mexico’s Tequila Crisis in 1994 provoked a serious deterioration of Brazil’s trade balance, and the unilateral tariff reductions completed in 1993 were magnified by the exchange rate policies associated with the price controls of the Real Plan, explained in more detail in the finance section below. From 1995 on, “trade policy increasingly reflected the idea that the negative effects of trade liberalization were significant and had not yet been absorbed by industry”, as well as a “perception of the comparative fragility of Brazilian industry” promoted by the import competing sectors (Veiga, 2004: p. 178-179). Brazilian trade policymakers therefore decided that “Brazil should take time to ‘digest’…pruning from its external agenda any initiatives that might result in any additional commitments to further liberalization” (p. 179). MERCOSUR’s development became “bogged down” by this “ever-growing protectionist trend”, and limited itself to enforcing existing multilateral obligations with no additional, ‘WTO-Plus’ commitments (Costa Vaz, 2004: p. 252).

Due in part to this “neo-activist stance” (Veiga, 2004: p. 178), Brazil has been an extremely active participant in the WTO, but conditionally so. Driven by a perception that the Uruguay Round liberalizations benefited developed countries disproportionately, Brazil instead focused its WTO agenda on industrialized countries’ agricultural subsidies and trade remedies rules like anti-dumping (Veiga & Ventura-Dias, 2004: p. 119). It therefore took on many leadership roles for representing developing country interests and has made extensive use of the WTO's formal procedures. According to the WTO website as of April 2015, Brazil had appealed for WTO dispute settlement as a complainant in 27 cases, 20 of which involved Canada, the United States, or the European Union. It had responded to 15 cases, and participated as a third party in 93. Many of the cases resulted in victories for Brazil. A ruling in 2013 repealed U.S. anti-dumping measures on Brazilian orange juice products despite the avid protestation of Florida's politically powerful orange growers (Reuters, 2013). In 2014, the U.S. paid Brazil $300 million to drop its victorious cases against American cotton subsidies (Bjerga, 2014).

Much of this liberalization-slowing shift was carried out under Lula's administration, who touted that during his tenure Brazilian trade policy:

> made a qualitative shift favoring South-South trade… He decided to abandon negotiations with the USA for a hemispheric free trade agreement and resisted WTO+ disciplines (e.g. investment issues, intellectual property, government procurement, labor and environment standards) in trade negotiations. (Doctor, 2012: p. 801)

This statement, taken with the above observations, would seem to suggest that Brazil's trade policymaking rests on a rational consideration of the benefits and costs to trade liberalization. Such a conclusion would further suggest that the FE phenomenon does not exert much pressure on Brazil via the trade mechanism.

But Vieira (2014) argued that these trade policymaking choices were mostly reactionary, responding to external constraints and shifts in the global trading system. As he explained, "Systemic trends, however, triggered and governed most of the process of diversification of partnerships…systemic factors constrain not only the set of choices available for domestic policy-makers, but also the impacts of the adopted option" (p. 153-

154). Further, the MERCOSUR project and Brazil's leadership therein could be interpreted as a strategic attempt to resist demands for further liberalizations "viewed as potentially reducing the margins of freedom of the federal and state governments with respect to development policies" (Veiga, 2004: p. 181). But as Costa Vaz underscored, even MERCOSUR policy decisions rested on the logic of "preserving some margin of policy discretion to deal with domestic and external constraints…rather than strict submission to imperfect collective trade disciplines" (2004, p. 243.)

Perhaps the difference, then, is that Brazil is a sufficiently large economy, especially with its regional bloc of MERCOSUR, to maintain policy freedom and eschew liberalization. Therefore, while Brazil does face equilibristic pressure via the trade mechanism, it has the sheer economic power to resist.

III.2.b: Finance-Linked Economic Policymaking

According to Kaplan's model, Brazil's elections and economic policy choices since the 1990s have alternated between inflation-averse political austerity cycles and, when credit has been tight, full political austerity cycles.

Inflation data from the World Bank shows the depth of the crisis leading up to the first inflation-averse political austerity election cycle in 1994. In 1980, annual inflation was at 87%; by 1984, it was at 213%; it broached 1200% in 1989; and the average from 1990 to 1994 was over 1600%. Responding to this "economic bedlam" (Kaplan, 2013: p. 244), Finance Minister and presidential candidate Fernando Henrique Cardoso launched an ambitious austerity program called the Real Plan.

The Real Plan, as explained by one of its architects, attempted to defeat inflation via three stages. First, the government introduced mechanisms to balance the budget, and convinced economic actors that it would respect these mechanisms. Second, the Plan indexed prices in the economy into 'Real Units of Value', or URV. Finally, the government converted the URVs to the new, stable currency. The Plan was unique in its full indexation; lack of price, salary, or asset freezes; and avoidance of recession (Bacha, 1995). The Real Plan succeeded in taming inflation, which fell from over 2200% in 1994 to 93% in 1995, and 17% in 1996. Cardoso handily won election on the widespread popularity of the Plan.

Cardoso designed his first term policies for two principal groups: domestic voters concerned that the reprieve from inflation would not hold, and international investors worried that Brazil would default on its debt (Kaplan, 2012: p. 268). While Brazil's nominal public debt was not particularly high, interest rates averaged a real rate of 22% from 1995 to 1998 (Giambiagi & Ronci, 2004), reflecting this lender concern that Cardoso attempted to assuage. But political resistance to the reforms Cardoso sought succeeded in impeding the adjustments. A deteriorating fiscal deficit brought contagion from the East Asian crisis, and interest rates soared further. With the Russian default of 1998 and the near complete desiccation of international funding, Cardoso finally imposed a full political austerity cycle in 1998 (Kaplan, 2012). Cardoso won reelection, despite the pervasiveness of social ills, landless protests and squatter massacres (Ondetti, 2006), and low growth rates, due to the "fear that there was no alternative to Cardoso's orthodox economic policies" (Skidmore, Smith, & Green, 2010: p. 344).

In the 2002 campaign, Lula Da Silva challenged Cardoso's record on rising unemployment, stagnating wages, and continued slow growth. Further, Lula attacked what he called Cardoso's prioritization of credit payments over wage payments. But in the aftermath of a fierce economic crisis brought about by international financiers fears of Lula, the former revolutionary began to soften his tone. He even penned an open letter promising to maintain most of Cardoso's macroeconomic policies (Kaplan, 2012).

Upon winning, however, Lula's own supporters began to resent what they perceived as his caving to international investors. As Bruhn (2008) explained:

> [Lula's] honeymoon was painfully short; in a matter of months, long before any positive changes could have been expected, the celebratory banners of his inauguration day were replaced by banners proclaiming him a traitor to the cause of the workers and peasants who elected him…groups seized upon his election as an opportunity to increase their demands. For example, the Landless Movement [a supporter of Lula's party]… more than doubled its rate of land invasions in the first year of his administration (p. 2).

This imposed strategy of subordinating domestic interests to the demands of international economic interests is very similar to the strategy Humala undertook, and exemplifies the finance mechanism's power for equilibrism.

Regarding specific policies, Lula's two terms from 2002 to 2010 can best be described as eclectic or "liberal neo-developmentalism" (Ban, 2012). While Lula attempted to reduce expenditures on public pensions, he did so via very moderate and relatively small changes to make the system more equitable and financially sound, but without any major structural transformation (Niedzwiecki, 2014). Expansionary policies like raising minimum wages and cash transfers were carried out, and successfully reduced at least the intensity of poverty in Brazil (Bither-Terry, 2014). But these policies were never deficit-based and "hardly posed any risks to macroeconomic stability"; the famous *Bolsa Familia* conditional cash transfer program only cost 0.026% of GDP (Ban, 2012: p. 305). While economically pragmatic, such conditions were also imposed by Brazil's financiers. As Kaplan argued, "Whereas Brazil nominally had the credit access to fund a politically timed expansion… [this] would have risked raising Brazil's risk premium and undermining economic confidence in the nation" (2012: p. 247).

Dilma Rousseff, Lula's successor, continued much of Lula and Cardoso's pro-poor but pro-stability macroeconomic political legacy, although she did make some additional shifts in favor of organized labor (Ban, 2012). But Rousseff's most enduring legacy from her two terms may be the extended social protests that began in 2013 and reemerged in 2015. The 2013 protests were "the largest and most significant protests in Brazil for a generation", resulting from an initial increase in the cost of public transit fares (Saad-Filho, 2013: p. 657). But the protests quickly grew from students and young activists to include predominant middle-class representation, and the points of contention grew from the fare increase to include general public services, administrative ineptitude, and corruption. Indeed, as Saad-Filho explained,

> The deep and contradictory frustrations expressed by those protests were symptomatic of a social malaise associated with neoliberalism… the limitations of the federal administrations led by the Workers' Party (PT), the rapid growth of expectations in a dynamic country, and the atrophy of traditional forms of social representation (p. 657).

These types of social exhaustions with the status quo are exactly what the FE concept predicts when international economic interests predominate, even when that predomination is supremely pragmatic.

The conundrum facing Brazil's finance-underpinned economic policymaking is perhaps best understood by comparing two quotes from the same article praising Brazil's successes and "transformation" (Trebat, 2013: p. 127). On the one hand, Trebat pointed out that: "the binding constraints on economic growth in earlier eras, particularly inflation, have been eradicated. Yet there are new constraints… Chief among them is education. Success on the educational front could well be the determinant of whether or not Brazil will continue on the path to developed country status" (p. 132). But just a few pages later, the author warns that "there are enough reminders…of the painful historical legacy of poverty, inefficiency, and low levels of education to think that other, less optimistic outcomes are also possible such as stagnating levels of income and inequality, a turn toward economic populism, and a retreat from global engagement in trade" (p. 140).

In other words, the policies that Brazil needs to undertake or expand to satisfy social demands may not be palatable for the international financial system. At the time of writing this work, Rousseff found herself embattled in an attempt to pass "austerity with a social focus… to reduce Brazil's gaping fiscal deficit and save the country's coveted investment grade rating from credit agencies" (Boadle & Soto, 2015). Partly as a result, Rousseff's popularity ratings fell to 12% in April 2015. As one former central bank governor cast the conundrum, "The fundamental question is whether the government, weakened by low approval ratings, will be able to impose the minimum dosage of adjustments that are necessary to correct the macroeconomic imbalances" (Leahy, 2015). The Economist put it even more directly: "Ms. Rousseff's policy levers are jammed" (Economist, 2015). This is the FE phenomenon at work.

III.2.c: Natural Resources and Extractives

According to Weyland (2009), Brazil does not have a rentier economy based on its immense natural resource wealth. When it comes to appropriating and politicizing extractive rents, "Brazil has recognized a basic claim of the political right, namely, the need to respect constraints, especially the limitations arising from global capitalism and domestic market reform and from liberal, representative democracy" (p. 146). But a deeper analysis using the lens of FE illustrates that there are some worrying characteristics around Brazil's natural resource dependency, and therefore, some resulting policymaking constraints.

The two most important primary product export categories for Brazil are minerals and agricultural goods. Almost a fourth of Brazil's exports are mineral-based (Petras, 2013), and iron ore is the most significant within that group, with about 80% of the world's iron exports originating in Brazil (Aguilar Sánchez, 2012). Within agricultural goods, soy beans are the most important product. However:

> Brazil [has become] more dependent than ever on a single market. From 2000 to 2010 exports of soy to China… represented 40 percent of Brazil's total exports; exports of iron to China…constituted over a third of the total exports of that sector…As China's growth slows, demand declines and increases Brazil's economic vulnerability (Petras, 2013: p. 473-475).

Even more concerning within Brazil has been the behavior of the industry leaders in these two sectors and their political allies. For example, "Despite their political rhetoric in favor of family farming, the Lula and Rousseff regimes have been among the biggest promoters of agribusiness… The largest share of state resources allocated to agriculture, finances agro-business and large landowners" (Petras, 2013: p. 474). Further, in 2012 a Swiss non-profit called The Public Eye awarded Vale, Brazil's largest mining company, the distinction of the company with the "most contempt for the environment and human rights", citing its activities in the Amazon and on other indigenous lands (Chaudhuri, 2012). Vale was privatized in 1997 but still receives heavy government support, most obviously through relatively low royalty rates. The government raised royalties in 2013, but despite pro-business criticism that the Rousseff administration was "keen to squeeze the sector until it squealed", the maximum rates only rose to 4%, or one third of the maximum rate charged in Australia (Economist, 2013).

However, on the Brazilian domestic front, it is oil that has been the most politically charged extractive industry. Although Brazil is often associated with oil, and is in fact the largest oil producer of Latin America, Brazil's petroleum exports have been declining significantly due to its inability to satisfy its internal energy demands (U.S. Energy Information Administration, 2014a). But this has not decreased the political importance of petroleum to Brazilian society, especially in the form of the mega-company Petrobras.

Petrobras was created in 1953, as part of the Brazilian government's drive to develop a local base for heavy industry. Until 1998, Petrobras held a government-granted monopoly of the oil and gas sector, which included all licenses for exploration and production in the national territory. It also "had the mandate to develop the oil industry from scratch, investing in technology and human capital, and giving priority to the participation of the domestic supply industry" (Sigam & Garcia, 2012: p. 27). Petrobras's history is therefore one of "creation in the face of energy insecurity, a highly insecure Cold War world order in which self-sufficiency was the only viable solution, and the growing need to address domestic energy consumption" (Nem Singh, 2012: p. 221-222).

Despite this national importance, at the end of the 1990s the Cardoso government pushed to end Petrobras's monopoly and privatize the company. Labor unions and oil sector workers carried out mass demonstrations against the policy change throughout the entirety of Cardoso's presidency. Although in the end the government did open Brazilian oil production to foreign capital, it did not privatize Petrobras completely. Petrobras remained the dominant player in Brazilian petroleum production, and most foreign companies opted to work with Petrobras rather than try to compete against the giant (Nem Singh, 2012).

Several popular, semi-protectionist policies were included as part of opening oil production, or have since been tacked on as additional reforms. For example, Brazil has several policy instruments designed to channel some petroleum proceeds into research and human capital development through linkages with universities' curricula and scholarship structures. An independent agency oversees concessions and establishes clear local content requirements to stimulate local industry (Sigam & Garcia, 2012).

However, there are some more malevolent results of this close government—Petrobras relationship that Brazilian society is beginning to forcefully reject. At the time of writing, an ongoing scandal involving illegal campaign contributions, money laundering, bribery, and other forms of corruption had brought down more than 100 high-level politicians and Petrobras executives. As Bloomberg Business categorized the case in May 2015, "Brazilians are facing some stark truths: The powerful and connected are still dividing the country's riches among themselves. The past decade's economic miracle was in large part a mirage. And the future is again on hold" (Smith, Valle, & Schmidt, 2015). As a result of the scandal, Rousseff's approval rating fell to the lowest point ever recorded for a sitting president: 9%. Hundreds of thousands of people took to the streets to demand an end to corruption and calling for Rousseff's impeachment, despite there being no evidence that Rousseff herself was involved.

Despite promises from President Lula that he "would aim at reforms that would allow the revenues from future deep-sea oil drilling to be put 'into the hands of the Brazilian people' in order to pay off 'the debt of 500 years owed to the poor'" (Hogenboom & Fernández Jiberto, 2009: p. 98), "until his last year in office, Lula followed political continuity with minimal changes with respect to the role of the state in the oil industry" (Nem Singh, 2012: p. 225). Rousseff has overseen slightly more dramatic changes. For example, thanks to political pressures from oil producing states (Nem Singh, 2012) as well as legal suits, Rousseff approved a bill to maintain the current royalty structure from already auctioned oil fields, but to force new concessions to pay a higher overall royalty of 15% (Aguilar Sánchez, 2012). The change also increases the proportion of royalty income devolved to oil producing states, in addition to the already relatively high percentages of its extractive royalties that Brazil devolved (ELLA, 2012).

But as the Colombian case will show, devolving royalty income may lead to central government budgetary constraints. This warning is especially appropriate given the fiscal crisis Brazil currently faces. Further, while raising royalties are a positive sign that some of the social demands described in the previous section could be addressed, "to date, the Brazilian government's position [has been] one of open defense of the commercial and corporate interests of its large national companies, especially in the effort to guarantee markets and adequate conditions for the commodities that form the base of the country's current exports" (Aguilar Sánchez, 2012: p. 5). While the government has thus tried to avoid a rentier state whereby capturing extractive resources form the primary purpose of the political system, it is telling that so many politicians have been found to have appropriated that rent to enrich themselves.

It is clear that extractive resources rents may not provide the Brazilian government with an 'out' from its current constrained economic policymaking. Further, the very efforts to maintain those rents seem to be constraining the current administration's policy choices, by placing a source of revenue off limits that could help satisfy social demands. The FE concept therefore does provide a useful analytical framework for Brazil's current crisis, or, as Aguilar Sánchez (2012) named it, "No easy miracle" (p. 1).

III.3: Colombia

Chile was a resource and trade-dependent, institutionally and politically stable medium power country. Brazil was a large country with significant internal market power. For the third case study, I chose Colombia, because as the following sections will indicate, it is resource dependent, institutionally and politically unstable, and a medium power country.

Colombia is also a useful case in this analysis for a variety of other factors. Colombia's inequality is worse than either Brazil or Chile's—it had the highest GINI coefficient of 55.9 in 2013. Annual GDP growth rates from 1990 to 2013 average 4% from World Bank data, above the Latin American and Caribbean average of 3% during the same period, but below the 5% that Peru achieved with a similar economy. Within this period, Colombia recovered from a deep political and economic crisis, pulled "back from the brink", and emerged as an "impressive" success story (DeShazo, Primiani, &McLean, 2007).

On the trade front, Colombia's trade strategy has focused primarily on its neighbors and bilaterally pursuing the two megamarkets of North America and Europe, as opposed to a relatively more general multilateral approach or more prolific bilateralism. In addition, Colombia has extremely close political and financial ties with the U.S.; for many years it has been the primary recipient of overt U.S. foreign aid in the Latin American region (Meyer & Sullivan, 2012).

Perhaps most unique of all has been Colombia's serious and ongoing civil conflict, which is also the characteristic that brought so much support from the United States. The conflict is fueled by three parts: cartel-run cocaine production for the U.S. and European market, anti-state guerrilla groups often allied with the cartels, and paramilitary 'self-defense' vigilante groups. The conflict has in large part dominated

Colombian politics (Skidmore, Smith, & Green, 2010), and with good reason; the war has cost hundreds of thousands of lives, over 80% of which were civilian bystanders (Haugaard, 2013). It has also displaced nearly 4 million citizens, destroyed over 240,000 hectares of forest, and distorted Colombia's economy, including through direct deteriorations of income equality (Silva Cano, 2010). While this paper does not address the state-undermining effects of the international drug trade, they are serious threats to state power, development, and policy space (Ambler, 2014; Ekici, 2014; Malinowska-Sempruch, 2014).

For all of the reasons enumerated above, this third and final case study will therefore complete this survey and test of the FE concept's explanatory power.

III.3.a: Trade

In 1989, President Virgilio Barco began the Colombian trade liberalization program known as '*la apertura*'. He implemented gradual unilateral removal of tariffs and non-tariff barriers, and did not stall the process even when part of his policies provoked a strong appreciation of the Colombian peso. His successor, César Gaviria, converted this passive liberalization into a program of active pursuit of trade agreements. Gaviria focused initially on the Community of Andean Nations and the 'Group of Three' initiative with Mexico and Venezuela (Vargas-Alzate, Sosa, & Rodriguez-Rios, 2012). This focus came to be known as "open regionalism" (Torres, 2011).

During the following two administrations, liberalizations began to falter. Domestic fragility and international economic crises frustrated even the best intentions of President Andrés Pastrana, who espoused a development plan that declared that exports were a motor of growth. But the administration of Álvaro Uribe in 2002 reconsolidated Colombia's free trade reforms, and alongside his efforts to extend state authority and achieve stability, began to negotiate a free trade agreement with the United States and Canada, and the European Union (Vargas-Alzate, Sosa, & Rodriguez-Rios, 2012).

The negotiations of these agreements received high levels of international scrutiny and, in many cases, criticism. Human rights activists in the U.S. delayed ratification of the agreement, pressuring lawmakers to demand lasting changes to Colombia's dark human rights record in its civil conflict (Economist, 2011). High murder rates for unionized labor figured prominently on this list of sins, as Colombia has consistently been ranked the most dangerous country for labor activity in the world (Fetterhoff, 2011). Although the final signed deal included a labor rights action plan, the plan was criticized as "too weak and too limited in its scope to have a discernible effect on human rights in the country" (Hillebrecht, 2014: p. 72).

Critics also underscored serious concerns about the effects of the FTA on Colombian farmers. One in-depth analysis found a mix of results for the Colombian agricultural sector, from export opportunities for competitive sectors like bananas and sugar, to contraction in import competing crops like corn. It also predicted large displacements of formal rural laborers, assumably to more economically efficient occupations, and the risk of serious environmental degradation from land use changes, deforestation, and scarce resource pressures. On net, the study found that "the FTA is expected to contribute to the economic growth of the agricultural sector but can adversely impact the sustainability of rural areas if appropriate measures are not implemented to protect the environment and the affected groups" (Díaz Guerrero, 2012: p. 85). Further, these measures may not be undertaken. Upon ratification of the agreement, high-profile experts like the minister of agriculture proclaimed that

Colombia was “not ready” for the agreement (Economist, 2011). Similarly, Rafael Mejía, president of the Society of Colombian Agriculturalists, stated:

> The transport infrastructure [necessary to bring agricultural goods to the U.S. market] is behind. Primary, secondary, and tertiary highways, ports and airports, they are all bad. Rivers are not navigable…There is much work to be done. The productivity of the agricultural sector has been growing. But it is one thing to be efficient and productive at the *finca* level, and another to add value [to a product] and carry it to port for shipping (Dinero, 2011).

Mejía also expressed concern with the “marked disequilibrium” between the number of contingencies included in the final plan and other concessions to the U.S. that Colombia ceded, concluding, “We were very generous” (Dinero, 2011).

Critics raised very similar concerns about the other megamarket FTAs that Colombia pursued in this time period. The EU set up an EU-Colombian Human Rights Dialogue to assuage concerns during its negotiations with Colombia, and the Colombia-Canada FTA was also “developed amid public outcry and political dissent” (Hillebrecht, 2014: p. 72). The Canadian government came under particular fire for delaying a human rights impact assessment that was a unique and lauded aspect of their FTA. Critics called this delay “a golden opportunity lost” (Rochlin, 2014).

Juan Manuel Santos, Colombia’s current president, has continued pursuing and deepened the internationalization of Colombia’s economy. Approving analysts considered his driving logic to be the need to “make up the time lost from the concentration of the country and the State in the armed internal conflict” of the past decades (Ramirez, 2011: p. 95). In this vein, one of Santos’ primary targets for a bilateral FTA was South Korea. Official documents explained the reasoning as that the agreement was necessary to allow Colombia to compete for market access with Peru and Chile, who had also signed FTAs with South Korea, in addition to being a stepping stone towards agreements with Singapore and Japan (Ministerio de Comercio, Industria y Turismo, 2011). But while the U.S.-Colombia FTA at least attracted support from large non-agrarian social groups (Dinero, 2011), the Colombia-South Korea FTA appears to have much less social approval, including from the Colombian largest unions as well as academics (Caracol Radio, 2014). It is unclear whether this opposition results from a general opposition to further free trade agreements or more specific concerns about perceived negative affects to similar countries and encouraging further extractive development (Kerguelén, interview with author, May 12, 2015).

Finally, the make-up of products that Colombia trades is an important factor to consider, although the section below on extractives will deal with his topic in more detail. In essence, Colombia's exports have tended towards a higher concentration of primary goods, and value added production has trended down (Reina, 2010). In 2014, Colombia's top five products in its export basket were crude petroleum (32%), refined petroleum (6.9%), coal (16%), gold (4.9%), and unroasted coffee (4.8%) (Jiménez Peña, 2014). Oil production, primarily for the U.S. market, is expected to continue to boom, in addition to natural gas and coal (U.S. Energy Information Administration, 2014b). It is telling in this regard that, when announcing the signing of the Colombia-South Korea FTA, the news portal for the Korean Culture and Information Service referred to "the resource-rich Colombia" (Jae-un, 2013).

Thus, while Colombia's relationship with the trade mechanism is less clear cut than the Chilean and Brazilian cases, the FE concept is still a useful lens. Since 1989, presidents have pursued liberalizations at all cost, despite economic crises and domestic or international opposition. But Colombia has not made liberalization an economic fundament to the degree of Chile. The driving ideology seems to be competition to maintain or gain market access in response to competitors' free trade agreements, also known as "competitive liberalization" (Bergsten, 2002), even when this has come at the expense of being overly 'generous' when negotiating with larger partners. So Colombia has not attempted, or been able to attempt, to rewrite rules in its favor, like Brazil.

III.3.b: Finance-Linked Economic Policymaking

According to Miles (2009), Colombia has avoided serious bouts of hyperinflation, but due to persistent, significant inflations rates, has been a "quintessential 'moderate inflation country'" (p. 65). Indeed, World Bank data indicate an average annual inflation rate of 24% from 1980 to 2000. However, in 2001, those numbers began to fall; from 2001 to 2013, average inflation rates were just 5%. At the same time, Colombia's central bank reported public debt of an average of 40.5% of GDP from 1995 to 2014. Can analysis through the lens of FE help explain this history?

Colombia adopted a new constitution in 1991. This created two important policy milestones that are necessary background for understanding how international finance has moderated Colombian economic policymaking. Among many changes that the new constitution implemented, the two most relevant for this analysis are central bank independence and fiscal and political decentralization.

With the 1991 constitution and the 1992 implementing laws, the Colombian central bank gained a high degree of independence. The laws designed a protective system of appointments for the board of directors of the bank whereby no president could 'stack the deck', although this was later undermined when presidential reelection was re-legalized. In terms of responsibilities, the bank was tasked with managing Colombia's monetary and credit policies, as well as the exchange rate policy that had previously been determined by Congress. The prime directive of the bank was instilled as maintaining the purchasing power of the Colombian peso (Meisel & Barón, 2010).

Analysts have estimated that the bank has been reasonably successful at this aim, decreasing both the overall level of inflation and uncertainty about price levels, even as the policy has contributed to the persistence of inflation (Miles, 2009). Part of this persistence results from a lack of complete credibility in the bank's inflation targeting (González G. & Hamann, 2011; Echavarría, Rodríguez, & Rojas, 2011).

The second major economic policy change resulting from the new constitution was the political and economic decentralization to Colombia's subnational departments and municipalities. Most relevantly for this analysis, the policy changes resulted in an ever-increasing importance for subnational expenditures and transfers as part of total government expenditures; subnational expenditures now hover around one third of total expenditures, and transfers to subnational governments now absorb over half of national government expenditures. At the same time, the relevant importance of subnational taxes as a percentage of total taxes has consistently fallen. Together, this has led to a significant degree of dependence on the central government, and to a resulting tension between the central government distributing resources and the local governments spending them. Due to this tension, several additional adjustments followed this major change, most recently with constitutional reforms in 2011 that attempted to make resource flows from the central government to the subnational governments less automatic, even out the distribution among recipients, and add more conditionality on how transfer funds are used (Bird, 2012).

While these two policies might imply that the dynamics of Kaplan's model do not apply, as he explained,

> the adoption of central bank independence is not a sufficient condition to check a political business cycle…in many cases they provided an insufficient check on governments' influence over monetary policy…Perhaps, for this reason, the

> scholarly evidence regarding the effect of central bank independence in Latin America is inconclusive (2013: p. 135).

While Colombia's experience with its central bank independence reforms is debatable, the additional aspect of implementing direct transfers did appear to lead to political business cycles at the local level (Páez, 2011). As well, the two policies certainly contributed to serious problems with the central government's macroeconomic policymaking (Bird, 2012; Vallejo, 2014).

These problems reached a boiling point in 1998 and 1999, during the administration of Andrés Pastrana. Pastrana had defeated his social-democratic challenger, Horacio Serpa, in 1998 mostly because of scandals shrouding Serpa's party, but also because "Serpa's populist style worried many Colombians who preferred the gradualism that had come to be enshrined in presidential politics" (Boudon, 2000: p. 45). Even though Serpa's promised budgetary prudence and his policies did not reject market economics outright, voters identified Pastrana more strongly with liberal economics (Ulloa & Posada-Carbó, 1999).

One of Pastrana's first tasks was to address the economic crisis that had helped him achieve victory, and so in 1999 the administration was forced to request a three-year, $2.7 billion Extended Fund Facility from the IMF. Colombia began pursuing this rescue as a consequence of a recessionary trend towards real GDP losses, a deteriorated and deteriorating central government fiscal position due to the subnational government transfers, record unemployment of 20%, a crisis in the Colombian financial sector, a heavy depreciation of the peso, and a series of large exogenous shocks like an earthquake that devastated the main coffee-producing region of the country (Lizarazo, 2011; Restrepo & Urrutia, 1999).

In order to secure IMF funding, the Pastrana government had to agree to implement a series of difficult adjustments. These ranged from an initiative to enforce tax collection, curb public sector spending, and establish stricter rules for the fiscal decentralization system, as described above. Pensions, wages, and public employment were also all restricted (Restrepo & Urrutia, 1999). Public sector unions bitterly protested the reforms through strikes and marches, resulting in the deployment of security forces in Bogotá throughout 2000 (La Nación, 2000; Leech, 2000).

Despite this opposition, the economy was not the major deciding factor for the 2002 election. Uribe won primarily because of the security crises plaguing Colombia at the time; indeed, “Uribe was the only candidate who made clear throughout the campaign his opposition to the way Pastrana had handled the peace process with the FARC”, promising to take a much harder line with the militants (Ulloa & Carbó, 2003: p. 789). Still, the economic problems were still part of the national debate, and Uribe was seen as less interventionist and more conservative with public expenditures (Ulloa & Carbó, 2003).

After the initial reforms promised under Pastrana failed to stabilize the government’s finances, further, deeper tax cuts were necessary throughout 2002 and 2003. What is more, Uribe’s administration failed to win a referendum approving some of the IMF conditions, which forced him to propose alternatives to Congress (Webb-Vidal, 2003). But many members of Congress, including from Uribe’s own party, as well as representatives from various social sectors, fought rabidly against the policies.

Still, Uribe’s efforts on the security front, via his ‘Democratic Security’ platform, began to show signs of success, and violence and crime rates dropped drastically. These gains in citizen security led to immense popularity for Uribe (Restrepo & Spagat, 2005; Posada-Carbó, 2011), whose approval rating fluctuated between 65 and 80% during his administration. After a constitutional amendment allowed him to run for reelection, Uribe retained power in 2006, a result that "took almost no one by surprise" (Botero, 2007: p. 103). Other contributing factors to this fait accompli were economic gains, such as healthy growth rates partially attributed to the return of consumer confidence (Posada-Carbó, 2011) and partially due to a "favorable global economic circumstance" of high average growth rates, high primary product prices, and international incentives for foreign direct investment in Colombia (Botero, 2007: p. 98). At the same time, partly as a result of his austerity policies, unemployment remained relatively high throughout Uribe's administration (Uhl, 2013).

Although he has since shown himself to be more independent that expected, Uribe's successor, Juan Manuel Santos, won his victory in 2010 largely due to being identified as Uribe's heir and the guarantor of continued security. Indeed, Santos only declared his candidacy once the Supreme Court declared Uribe ineligible to run for a third term. What individual merit Santos did receive related to security, since he had served as Uribe's defense minister. On social and economic policies, voters did not significantly distinguish between Santos and his principal opponent (Posada-Carbó, 2011).

In conclusion, the predominance of political instability and voter preoccupation with security in Colombia has limited the utility of the FE analytical concept. FE as defined so far would predict that the Colombian electorate would not reward austerity politics, since it was not scarred by past hyperinflation. Instead, FE would predict that voters would punish repeated impositions of austerity as part of attempts to attract external funding, such as the IMF bailouts. Perhaps, then, this is a weakness of the FE model, in that it does not, as currently proposed, account for non-economic issues like citizen security and the ideological relationship between conservative security policies and conservative economic policies. An additional possible missing variable is an actively leftist portion of society, which has been weakened in Colombia due to accusations of being associated with the rebel movements (Hernández, interview with author, May 8, 2015). As a result, while considering Colombia's recent financial and economic policy history through the FE lens does provide some insight, it does not help explain political outcomes or predict crises as well as it does in more politically stable polities.

At the same time, the third FE mechanism may still be useful for analyzing Colombia's case, due to the intricate relationship between the civil conflict and natural resource extraction.

III.3.c: Extractives and Natural Resources

Colombia is wealthy in a variety of natural resources. Much of this wealth is in 'lootable' natural resources that can be extracted relatively easily at low capital or time cost and sold into homogenous bulks where the origin is difficult or even impossible to trace. In the Colombian case, the most important lootable resource is gold. At the same time, other non-lootable resources, like oil, have also featured prominently in Colombia's conflict. Finally, illegal trading and cultivation of coca leaf for cocaine production is an additional important and conflicted feature of Colombia's natural resource and extractive portfolio. Numerous studies have highlighted the connections between the various groups of actors in Colombia's civil war and these different types of natural resources.

Idrobo, Mejía and Tribin (2014) described how illegal gold mining has become a "new engine in the Colombian conflict". They compared municipalities with legal mining contracts, around 316 out of 1102, with those with a known presence of illegal gold mining activities, around 82 out of 1102. They tested these characteristics against homicide and massacre victim rates, and found a strongly significant relationship. This finding parallels more speculative or anecdotal evidence that suggests that much of Colombia's gold production is either controlled by rebel organizations or linked to the extortion or persecution from the paramilitaries (Leiteritz, Nasi, & Rettberg, 2009; Lavaux, 2006). A similar dynamic exists for emeralds—around half of the world's emeralds have come, historically, from Colombia via legal means, while an additional 10% are mined and exported illegally. Yet even the legal mines have had to depend on local private armies (Lavaux, 2006).

In the literature on conflicts over control of natural resources, oil is usually considered non-lootable, as it requires heavy investments in extraction and transport infrastructure, and costly maintenance and skilled labor. However, in Colombia, the rebel movements have successfully used threats, extortion, and kidnapping in order to raise significant funds from oil companies. In part, this strategy was made possible due to geographical coincidences in which oil pipelines must travel through rebel-controlled or contested areas before reaching port (Ross, 2004). The basic strategy is akin to a mafia security contract: oil companies pay rents to armed rebel or paramilitary groups in exchange for not having their facilities destroyed or their workers kidnapped (Lavaux, 2006). In response, some oil companies have allegedly purchased arms and other equipment to bolster state security forces in their regions of operation (Pegg, 2003). Further, though most of the studies on this topic came from the early 2000s, these attacks are still a serious issue, as evidenced by a January 2015 scandal in which high-level executives of a oil pipeline company were accused of paying two Colombian rebel groups $6 million, and of being complicit in kidnappings and murders carried out by the rebels (Semana, 2015a).

A further complication in the effect on policymaking space from extractive natural resources comes from the significance of the illegal coca crop. Angrist and Krugler (2008) analyzed the natural experiment of Colombia's coca cultivation boom as a result of better crop destruction and product interdiction tactics in other coca-producing companies. They found that increases in income from coca production was correlated with unrest and violence, and suggested that the extortion and 'taxation' from illegal armed groups was to blame. Indeed, the income link between those groups and narcotic production has been well documented, including direct smuggling as well as indirect 'taxation' via protection fees (Lavaux, 2006; DeShazo, Primiani, & McLean, 2007).

So, although the relationship is second order, natural resources have helped constrict Colombian policymakers' agency through their prolonging of the civil conflict (Ross, 2004). If the recent leaders have had to prioritize the reestablishment of state authority throughout their territory, and combat violence and civil strife, then they have had reduced policy room for other projects such as peaceful development initiatives. And if at least some of the power of the rebel groups came from control of or threats to natural resource rents, which seems indubitable, then those natural resources helped constrain policymaking by converting at least part of the traditional policymaking space into rentier space.

Beyond the civil war, however, extractives and natural resources have constrained policymaking in other ways. Beginning during the government of Gaviria, Colombia's government implemented several structural reforms that caused a "reprimarization" of the economy (Gaitán et al., 2011: p. 33). These reforms included establishing clear legal property rights over mining concessions, large fiscal and commercial benefits for investors, stable contracts of at least 25 years in duration, and "a system of extremely lax environmental controls, [including] suppressing funds for environmental impact guarantees, legal loopholes in relation to the processes for closing mines, and a deficient treatment of mining liabilities" (p. 33).

The Colombian government's strategy became one of consolidating long-term extractive projects to promote large flows of foreign investment and boost governmental profits from royalties. But the latter part of this plan did not come to fruition. Calculations of the 'state-take' of mining profits found that the Colombian government only received 22% of the rents from extractive projects, the lowest in Latin America. In part, this results from heavy subsidies to the extractive sector, and royalties that the government has consistently lowered in order to generate more investment (Gaitán et al., 2011).

As well, Colombia's revenue sharing policies have directly contributed to narrowing policymaking space. These policies "have established systems of extractive royalty distribution that reward the producing territorial units - be that district, provinces, or regions where extractive projects are located - with larger royalty shares. This is believed to not only foster development, but also undermine a project's local opposition" (ELLA, 2012: p. 9). Although this is theoretically better for local development that the peripheral extraction model of Chile, as described in the previous section, these transfers to departments and municipalities of royalty income, to help mitigate conflicts and promote extractive activities, directly restricted the central government's ability to balance its budget and address national economic priorities from the federal level. Additionally, for the departments that receive devolved royalty income, "no significant correlation exists between receiving royalties and improvements en levels of poverty", despite requirements that departments have to use certain high percentages of this returned income for poverty reduction projects (Gaitán et al., 2011: p. 72).

In large part for these failings, in 2011 the government initiated a reform to centralize royalty revenue and direct it to more productive targets. But the limited overall scale of the reform and its control by a congress that experiences on average a third of its members falling to corruption scandals or connections to rebels or paramilitaries leaves doubt as to the efficacy of the new design (Gaitán et al., 2011). Further, one of the principal items of debate in the 2014 reelection of Santos was the topic of this new royalty discretion. Critics claimed that this would enable future political business cycles using the '*mermalada'* or marmalade to buy votes for congressional allies. Santos defended the policy, claiming "Marmalade isn't any different than investments" (Redacción Política El Tiempo, 2014).

In sum, the focus by successive Colombian governments on promoting extractives, as well as extractive and natural resources' relationship to Colombia's conflict, is leading to an increasingly inevitable crisis. Although the economy recovered under Uribe, this recovery is unstable due to its dependence on volatile but high primary resource prices and "intensive extraction of natural resources without addressing their preservation or restoration" (Ortiz, 2014: p. 216). Yet the extraction of energy resources does not significantly contribute to employment growth, and nor does it generate "quality employment" (Jiménez Peña, 2014: p. 308; Gaitán et al., 2011). As well, a political economic space that thus depends on international economic price surges therefore risks becoming a highly contested rentier space.

The current Santos administration has largely continued the policies of weakened regulations and territorial rights in order to prioritize extraction as a mechanism for growth. These decisions have led growing conflicts with indigenous and Afro-Colombian communities, some of which have been violent (Bebbington & Bebbington, 2012). Numerous scandals have emerged showing the "dramatic institutional weakness" around enforcing environmental regulation, or the appropriation of institutional oversight for personal gain (Gaitán et al., 2011: p. 24). While some protests have led to temporary halts in mining projects (Semana, 2015b), the Santos government is continuing to deepen the pro-extractive, low state-take model. In February 2015, the head of Colombia's Planning Department announced plans to "halt a decline in oil production by making its royalties system more favorable to large drillers" (Medina & Willis, 2015).

In this sense, then, FE is indeed a useful lens for analyzing the Colombian extractive and natural resource case. Unfortunately, however, the outlook is not positive. In addition to the restricted policymaking space for all the reasons previously laid out, around limited governmental resources, links to civil strife, and peaceful protests against extractive concessions, there are also macroeconomic indications that Colombia may be "starting to feel some…symptoms" of the resource curse (Gaitán et al., 2011: p. 46).

IV. CONCLUSION

In summary, the three case studies yielded the following results as tests of forced equilibrism's utility as a lens through which to analyze or explain ongoing political economic issues in Latin America.

In Chile, dependence on international trade caused that country's leaders to push for international restrictions on domestic policymaking, even though this then restricted Chile's own policy space. But extractive resources with strong legal limitations on their use and international finance heavily invested in Chile's legacy of macroeconomic prudence interacted and severely limited Chilean policymakers. As a result, the current situation in Chile is one where the FE concept is especially visible, and no clear policy consensus for how to satisfy social demands without disrupting the economic model and damaging Chile's economy exists.

In Brazil, burgeoning world power status enabled policymakers to help write the global trading system's rules, allowing Brazil to maintain policy freedom and eschew, to some degree, total liberalization. But similarly to Chile, Brazil's policymakers opted for slow economic changes within the confines of the rules of international finance and the international economy. This lack of radical improvements helped bring about the current situation, where Brazilian society is demanding policy changes that Rousseff cannot provide because of fiscal constraints. Extractives complicated the scene by forming a bastion of pro-international policies that have allowed some policymakers to privately gain and further infuriated society. In this case, as well, FE proved quite useful.

Finally, in Colombia, policymakers have taken a middle path between the two trade strategies of Chile and Brazil. They have pursued liberalizations despite political resistance in order to gain market access, but not quite to the degree of Chile, nor have they been able to influence the global trading system to the Brazilian degree. On finance, successive governments have faced budget and growth crises with deepening austerity measures in order to gain the support of international financial institutions. Domestically, however, the ongoing security crisis and civil strife predominated in all election cycles, limiting the predictive utility of FE. Still, analysis of the third FE mechanism, extractives, did provide some useful, if negative, insights into Colombia's near future.

Thus, this work has found that FE is indeed useful as an analytical tool or conceptual framework for explaining certain aspects of modern Latin American political economy. However, the idea is not without its flaws and weaknesses. Therefore, political economists should further flesh out the concept, test new cases, and criticize and adapt forced equilibrism. With these additional steps, perhaps FE will offer a strong, lasting contribution to the field.

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