

Electoral Oscillations in Argentina*

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Abstract

The mean voter theorem suggests that all parties should rationally converge to the electoral center. Typically this leads to an outcome which is unattractive to the rich. This paper develops a general stochastic model of elections in which the electoral response is affected by the valence (or quality) of the candidates. Contributions made by policy-motivated activists can influence valence. The model is then applied to the presidential elections in 1989 and 1995 in Argentina, to suggest why Carlos Menem, who won in 1989 with a populist platform, was able to win in 1995 with quite different policies that favored the upper middle class.

Key words: elections in Argentina, valence, activists.

1. Introduction

It has often been remarked that Latin America polities seem to swing in a random fashion between pro-market and anti-market democracies (Dominguez, 1998). When democracy returned to Latin America, in the 1980s, the governments in Argentina and Brazil resisted the so-called “market-oriented reforms”. However, later, in the 1990s, Argentina, Brazil, Mexico, Uruguay, Chile and Peru all implemented fundamental economic reforms. The pendulum has swung again, and there is a move to the left (Castaneda 2006 and Vargas Llosa 2005). Because the literature generally provides only descriptive analysis, two important questions remain unanswered. First, what rationale explains a country’s swing from left to right and back again? Second, is there some mechanism that causes swings in one country to infect its neighbours?

While these questions have an obvious intrinsic interest, they also pose a theoretical challenge for formal models of electoral competition. Consider the first question about one country’s oscillation between left and right. Such a phenomenon is very difficult to obtain using the standard model of political competition, principally because non-centrist policy platforms will generally not be in equilibrium, according to this model. Even if this problem is dealt with, it would still be necessary to relate the oscillations to changes in exogenous parameters. The only obvious way would be to assume that the electoral preferences or the institutional rules change radically for some unexplained exogenous reason. In this paper, we offer a model that provides an endogenous reason for the afore-mentioned oscillations. Moreover, the case study presented here makes clear that the cause of this oscillation is not *directly* due to a change in electoral preferences.

Previous work (Schofield and Cataife, 2007) suggests that the understanding of Latin American polities may require (i) dealing with more than one policy dimension, and (ii) taking into account the heterogeneity of interests within the polity. Indeed, the work points out the importance of currency as a second policy-dimension, and focuses on the winners and losers created by specific policy positions on the currency dimension. To the best of our knowledge, the second question about the contagion mechanism operating across the region has not even been addressed in any formal model. Indeed, almost by definition, the standard spatial model is usually constructed with reference to a single polity, and is thus ill-equipped to deal with matters such as contagion.

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Rather than discussing these questions abstractly, we consider the case of the Argentinean elections of 1989, 1995 and 1999. The study of a particular polity allows us to provide a better motivation for the analysis as well as an evaluation of the empirical implications of our model. We study Argentina rather than one of the other polities in the region because the sequence of events in Argentina shows that the causal connection is from political strategies to voter preferences rather than from preferences to strategies, as is usual in formal models. Indeed, the analysis of the Argentinean elections of 1989 and 1995 suggests that political candidates do not simply respond to the wishes of the electorate. Instead, the incentives of the candidates themselves induce the oscillation between winning policies. We give an account of these elections and their effects together with a suggestion about the role played by international financial institutions, as well as the US government. Section 4 presents an outline of the formal model (based on Schofield and Cataife, 2007). Section 5 gives a brief conclusion.

2. Argentina 1989: From Populist Promises to Neoliberal Policies

In 1989, Carlos Menem, the candidate of the PJ (Partido Justicialista), was elected President of Argentina with almost 50% of the votes. Menem's populist platform, which included a universal rise in salaries (*salarioazo*) and a big push to the productive sector (*revolucion productiva*), was supported by the working class, and was the key to Menem's electoral victory. In contrast, the middle and upper class generally supported the historical rival of the PJ, namely the UCR (Union Civica Radical). The Argentinean upper middle class probably regarded Menem as a demagogue from the countryside. From their perspective, Menem lacked both the values and the skills to lead a country that had suffered under a harsh military dictatorship (1976-1983) followed by an incompetent democratic government (1983-1989) whose economic mismanagement had brought about hyperinflation. It was believed that Menem's electoral promises, if implemented, would lead to a highly redistributive policy, with a strengthening of the labour unions and a weakening of private property.

Surprisingly, once in office Menem implemented policies that were opposite to his electoral promises. The new policies included the liberalization of trade and the labor market, and the privatization of several state companies.. More importantly, in 1991, Menem established a currency board that pegged the Argentinean peso to the dollar, by legally forcing the Central Bank to hold dollar reserves to cover its Argentinean peso liabilities in a 1-to-1 ratio. Although this policy (soon known as the "Convertibility Plan") succeeded in controlling inflation, it led to three major problems. First, the financial system became very fragile, since the Central Bank lost its role of lender of last resort for the economy. Second, the government sacrificed its control over the real exchange rate. Third, the resulting monetary policy was not accompanied by any measure of fiscal discipline. This was because the discretionary allocation of fiscal resources by the federal government in Argentina was crucial for the manipulation of political and electoral support at the local level. These problems made the economy especially vulnerable to exogenous shocks, particularly those resulting from "contagion" from the international economy.

2.1 The Two Periods of the Convertibility Plan

As long as the value of the dollar did not appreciate with respect to Argentina's major commercial partners, and the government was able to finance itself either through foreign debt or counter cyclical funds, the economic plan succeed in providing the stability required for economic growth. Indeed, the absence of exogenous shocks in the period 1991-1995 provided Argentina with high rates of economic growth (over 8% on average between 1991 and 1994) and a widespread optimism both at home and among foreign investors. As soon as the international conditions changed, Argentina's vulnerability to external shocks proved to be very high. The principal shocks were the Tequila crisis in 1995, the East Asian crisis in 1997, the devaluation of the Brazilian real in 1998 and the appreciation of the dollar relative to the European currencies after 1995. An analysis of the consequences of each particular crisis on Argentina is beyond the scope of this article. It is enough to say that although the Convertibility Plan survived all these shocks, the cumulative effect was to make Argentina's economic scheme unsustainable.

The Argentinean peso appreciated by 25% in real terms between 1990 and 1998 (the appreciation reached 32% by 2000), making Argentina an expensive country even by European and U.S. standards.

Given that the Convertibility Plan outlawed the printing of money without dollar backing, the fiscal imbalances in Argentinean currency had to be financed through foreign debt. In addition, the appreciation of the currency magnified the levels of debt when denominated in dollars. Consequently, between 1991 and 2001, the public debt increased from U.S. \$87 billion to U.S. \$145 billion. Thus, the Convertibility Plan succeeded in controlling hyperinflation, but when the external conditions became unfavorable, it forced the government to replace monetary laxity with foreign debt. Of course, this strategy paid off from an electoral point of view, at least as long as the government managed to refinance the short-term debt.

Argentina's economic performance over the 1990's could be said to have two different periods. The period 1991-1995 was characterized by sustainable fiscal deficits, high economic growth and a reasonable (although perhaps not competitive) real exchange rate. In contrast, the period 1995-2001 was characterized by a much lower economic growth (indeed with economy contraction in 1995, 1999, 2000 and 2001), high unemployment rates, large fiscal imbalances and an increasing foreign debt. All of these were the product of the inflexibility of Argentina's economy. In retrospect, it seems clear that sooner or later a severe enough external shock would occur, forcing a political decision to abandon the Convertibility Plan and to allow the market to re-establish some sort of equilibrium. The longer the exchange rate correction was postponed, the greater the private and public sector dollar-denominated loans. In sum, postponing a devaluation would only increase the probability of default and bankruptcy of both sectors. It is hard to see, then, how the merits of the Convertibility Plan in 1991-1994 could be dissociated from its costs in 1995-2001. The seeds of the crisis of 2001 were already present in the early apparent success of the Plan.

2.2 Losers and Winners

We can easily determine who were the domestic winners and losers over the ten year cycle of the Plan. Carlos Menem and his entourage were in office for these ten years. In this period, Menem managed to control a plurality in both chambers of Congress. By increasing the Supreme Court of Justice five to nine, and by maneuvering these appointments, he also obtained an "automatic majority" in the Court. This maneuver could guarantee immunity from later accusations of corruption over the U.S. \$20 billion federal fund collected from privatizations. In order to increase the real value of assets and profits, it was in the interest of the foreign companies hoping to acquire publicly owned companies that Argentina maintain an appreciated currency. Because the interests of the corrupt politicians were aligned with those of the foreign companies, they also wanted Argentina to stick to the Convertibility Plan.

The Argentinean upper-middle class also benefited from the economic scheme. After years of complete absence of credit (a consequence of a high-inflation and closed economy), the Convertibility Plan brought about a consumption boom of imported goods. Argentineans could be found among Japanese, European and American tourists traveling around the world. The political elite in office was perceived by the upper-middle class citizens to be corrupt itself and to condone corruption at all levels of government. Although this corruption violated the ethical standards that might have been dominant earlier, the benefits associated with the new consumption habits proved to be irresistible. In 1995, Menem was re-elected with a percentage of the votes similar to 1989. Although he lost 10% of the left votes to a new party, FREPASO (Frente Pais Solidario), he gained 10% of the center-right votes.

Despite their initial aversion, the upper-middle class felt more than satisfied with Menem's government. Indeed, Menem's policies created an excellent business environment, starting with economic stability and a regressive tax structure. Indeed, members of this class also became business partners in Argentina's modernization and infrastructure projects. For the working class, the real wage remained practically unchanged from 1990 to 2000. On average, the unions had organized one general strike (across the different industrial sectors) every six months during the presidency of Raul Alfonsin of the UCR. Menem, Alfonsin's successor, avoided this problem by giving the union leaders control over the resources of the health plans of their respective industrial sectors. As a result, Menem only faced one general strike on average every fifteen months.

As a consequence of the Convertibility Plan, the per-capita public debt increased by U.S. \$1750 in 1991-2001. This money would eventually have to be paid through taxes by the citizens. Any devaluation would make the burden of the foreign debt even heavier. Eventually Argentina defaulted on part of its debt (although not its debt with the international financial organizations). Two points need to be considered. First, the default was the product of the circumstances, not a plan devised ahead of time.

Second, the country did have to pay the costs of the devaluation and default, and the ensuing crisis may well be considered the most profound that the country has had to face in recent history.

At least theoretically, the upper middle class was able to insure against the damages of an eventual devaluation, by saving in dollars and sending their money out of the country. Of course, although this strategy was in principle available to everyone, the working class was unable to use it. They received meager benefit from the consumption boom, and had to face the full consequences of the per-capita increase in the public external debt.

3. The Role of the IMF and the U.S. government

Cavuto: What's the advice here? I mean does the United States stand by a strong dollar?

That must be the consistent policy, but it's never consistently said.

Brady:¹ But I think you've fallen into the trap, Neil, if I can say. It's not strong or weak.

It's lower or higher against other currencies, and, if it is the largest reserve currency in the world, if it's the highest held currency by all central banks, it's got to be...

Cavuto: Yes, but it's not the most happening currency right now.

Brady: Now you're right. It is the largest one in reserves and all that. The euro has been gaining a considerable amount of steam. It's back to levels when it first started a few years ago.

Cavuto: Many are saying that the dollar's days as the premier currency maybe a decade from now could be numbered.

What do you think?

Brady: I don't think so. I think if the country's strong, the dollar will be strong, too. It will fluctuate some, and the people that have the most to do with it are the central bankers in the world.²

Domingo Cavallo, Argentina's Economy Minister in 1991-1996, and architect of the Convertibility Plan, has stated (Cavallo (2004) that although some of the policies implemented by Menem and himself were aligned with the so-called Washington Consensus (namely privatization, trade liberalization and deregulation), other recommendations of the Consensus (fiscal discipline, a competitive exchange rate, and tax reforms) were not. Cavallo mentions that, in the beginning, the technical staff of the IMF did not support Menem's package of policies, because they were not fully aligned with the Consensus. Nonetheless, adds Cavallo, the intermediation of Clinton's administration in favor of the Argentinean government induced the endorsement of the IMF. In other words, the initial support of the IMF for the Convertibility Plan was not due to the technical recommendation of the staff, but to pressure from the U.S. government. Later on in the 1990's, the IMF repeatedly supported Argentina's economic reforms and, in particular, asserted that Argentina's currency board was an example of a credible and viable regime. In the words of the Independent Evaluation Office of the IMF, "the IMF had been almost continually engaged through programs [with Argentina] since 1991" and "IMF resources were provided in support of Argentina's fixed exchange rate regime, which had long been stated by the IMF as both essential to price stability and fundamentally viable." (IMF, 2004).

Throughout the crises induced by external contagion, the IMF backed Argentina in two ways. First, it provided the financial aid that would prevent a run on Argentinean financial resources. Second, it helped the Argentinean government cope with both short-term public debt and the pressure to devalue. Although from 1994 onwards, Argentina failed to accomplish the fiscal targets agreed with the IMF, this failure was systematically ignored so that the country could receive extra financial aid. In the 1992-2001 period, the IMF granted loans of \$22 billion. Indeed, in 2000, the IMF further approved what in Argentina became popularly known as *blindaje financiero* (financial shielding), namely a loan for \$40 billion, which was composed of loans from the IMF (U.S. \$14 billion), the World Bank and the IADB (\$5 billion), the government of Spain (\$1 billion) and a further \$20 billion that came from the private sector. Needless to say, the crisis of 2001 was triggered despite the efforts of the IMF. It seems natural to ask the following: why would the U.S. government support a package of reforms that did not fully comport with the technical recommendation of the IMF?

The two recommendations (fiscal discipline and a competitive exchange rate) of the Washington Consensus that were neglected by Cavallo's plan seem to have had a key role in the collapse of the Argentinean economy. We can examine the consequences of these missing components. The U.S. government followed an *official* policy of a "strong dollar" at least from 1995. Clinton's Treasury Secretary, Robert Rubin, was perhaps the main advocate of this U.S. policy. The benefits for the U.S. from a strong dollar are three-fold. First, it helps finance the large current account deficit by means of capital inflows. Second, it nurtures the U.S. stock market. Third, it reduces inflationary pressure. These benefits had been sought since the administration of Ronald Reagan, even though there was, on occasion, some concern about the undesired result of a strong dollar, namely the trade consequences of a less competitive exchange rate.

A convenient strategy for the U.S. government at the time Argentina implemented its currency board would have been to attempt to appreciate the dollar without affecting the rate of exchange relative to key U.S. commercial partners, like Western Europe, China and Japan. In fact, this reasoning is in line with the thoughts of Nicholas F. Brady, U.S. Treasury Secretary during the time Argentina implemented the Convertibility Plan. As the earlier quotation suggests, the relevant questions are (i) whether the dollar is higher or lower with respect to other currencies and (ii) to what extent the dollar is held as a reserve currency. We suggest that at the beginning of the 1990's there was an alignment of interests between the Argentinean upper middle class, the politicians of that country and the U.S. government. Several years of the Convertibility Plan were the product of this alignment. The evolution and effect of this alignment and its collapse can be presented briefly.

By 1989 the Argentinean state was bankrupted and forced to finance itself via a monetary laxity that produced hyperinflation. In order to enrich themselves, members of the political elite would first have to enrich the state, and the best way to achieve this was to privatize the publicly-owned companies. However, to make the bankrupted state companies attractive enough to foreign investors, the whole economy would require some modifications, beginning with macroeconomic stability and a strong currency.

This package of policies was beneficial to the Argentinean upper middle class. Nonetheless, given Menem's party affiliation and personal background, he had no chance of being elected in 1989 by targeting this class. Instead, he targeted the working class with promises that, we suggest, he had little intention of implementing. Once in office, Menem needed the endorsement of the IMF. In this respect, the sole challenge was to get the support of the IMF for two mainstays of his plan, namely a loose fiscal discipline (helpful for political and electoral purposes) and a non competitive exchange rate (required to make privatization an attractive proposition for foreign firms). The remaining policies fitted with the Washington Consensus, and would therefore induce no opposition.

The currency board proposed by Cavallo happened to be in line with the interests of the U.S. Treasury. (The opinion of Nicholas F. Brady, U.S. Treasury Secretary at that time supports this view.) In turn, the support of the U.S. government would facilitate the endorsement of the IMF. Thus the Convertibility Plan could be implemented.

Five years later, Menem had the opportunity to try for the re-election. This time, the strategy of targeting a social class different from the one to be benefited was unnecessary. Menem's platform, as described above, was supported by a new electoral coalition that included the upper middle class and gave him the electoral victory. After ten years and a failed attempt by Menem to obtain a second re-election, a new President, Fernando De La Rúa, was elected in 1999. Although De La Rúa belonged to the opposition (UCR), in his electoral platform he committed himself to maintain the economic scheme implemented by Menem. De La Rúa kept this promise once in office. However, the negative consequences of the Convertibility Plan were so severe that they became impossible to ignore. The public debt was already too high, and the economy showed serious symptoms of high unemployment, fiscal imbalance and stagnation. The prestige of Cavallo, who had succeeded in the fight against hyperinflation, was so high among the electorate that the new administration was compelled to appoint him as Minister of the Economy in March 2001. Despite Cavallo's efforts, the Argentinean economy fell into crisis in December 2001. After the resignation of De La Rúa and a chaotic sequence of interim presidents, Nestor Kirchner, candidate of the PJ with leftist leanings, was elected in May 2003. The backlash to the crisis in Argentina may well be the reason there has been a strong move toward the left, together with a spread of anti U.S. sentiment, in many countries in Latin America.

The story that we have presented above leaves unexplained an important political question: by what mechanism was Menem able to desert the populists who supported him in 1989 and obtain the support of a new group of the upper middle class voters in 1995? It is improbable that an argument based on a median voter will suffice. It is possible that Menem was close to a median voter position on the left-right axis in 1989. However, the economic pain caused to populist voters by the Convertibility Plan, together with the benefits for the middle class voters from the same plan, both suggest that Menem's position in 1995 was not at the median. We present a formal model of the election that posits that the Convertibility Plan induced a second dimension of policy, defined essentially by the hard currency position underlying the plan. We propose a stochastic model of the election, where the presidential election depends on two kinds of *valence*. The first is *exogenous* and characterizes the perceived quality of the candidates (Ansolabehere and Snyder, 2000). The second is *endogenous*, and is associated with the financial support by activists. In the model, this support provides the financial means by which the candidate affects the perception by the voters of the candidate's quality.³ Note that a candidate might also use these resources to influence the voters adversely about the opponent's quality.

4. A Formal Model of Elections

The electoral model presented here is an extension of the standard multiparty stochastic model, modified by inducing asymmetries in terms of valence. Details are given in Schofield (2006, 2007) and Schofield and Cataife, (2007). The key idea underlying the formal model is that party leaders attempt to estimate the electoral effects of party declarations, or manifestos, and choose their own positions as best responses to other party declarations, in order to maximize their own vote share. The stochastic model essentially assumes that party leaders cannot predict vote response precisely, but can estimate an expected vote share. In the standard spatial model, only candidate positions matter to voters. However, as Stokes (1963) has emphasized, the non-policy evaluations, or valences, of candidates by the electorate are equally important. In empirical models, a party's valence is usually assumed to be independent of the party's position, and adds to the statistical significance of the model. In general, valence reflects the overall degree to which the candidate is perceived as able to govern effectively.

Over the last decade a new literature has developed that considers deterministic or probabilistic voting models including valence or bias towards one or other of the candidates.⁴ In the model with valence, the stochastic element is associated with the weight given by each voter, i , to the average perceived quality or valence of the party leader. Recent work has developed an empirical and formal stochastic electoral model based on multinomial conditional logit methods (MNL), as given in Train (2003). In this model, each political candidate, j , was characterized by an intrinsic or exogenous valence. It was possible to obtain the conditions for existence of a local Nash equilibrium (LNE) under vote maximization for a parallel formal model using the same stochastic assumptions as the MNL empirical model. A LNE is simply a vector of candidate positions with the property that no candidate make a small unilateral move and yet increase utility (or vote share). Note also that a pure strategy Nash equilibrium (NE) is a vector of candidate positions so that no candidate has a unilateral incentive to deviate so as to increase vote share. Thus any NE must be a LNE.

The mean voter theorem (Hinich, 1977) asserts that all candidates should converge to the electoral origin (where the electoral origin is the mean of the distribution of voter preferred points). This paper offers a more general model of elections that is based on the assumption that there are various additional kinds of valence. The first is referred to as *activist valence*. When party, or candidate adopts a policy position z_j in the policy space, X , then the activist valence of the party is denoted $\mu_j(z_j)$. Implicitly we adopt a model originally due to Aldrich (1983). In this model, activists provide crucial resources of time and money to their chosen party, and these resources are dependent on the party position. Each candidate then uses these resources to enhance his image before the electorate, thus affecting his overall valence.

We assume voter utility is given by the equation

$$u_{ij}(x_i, z_j) = \lambda_j + \mu_j(z_j) + (\theta_j \cdot \Pi_i) + (\alpha_j \cdot \Gamma_i) - \beta \|x_i - z_j\|^2 + \epsilon_j \quad (9)$$

$$= u_{ij}^*(x_i, z_j) + \epsilon_j$$

constant term, λ_j , is the *intrinsic or exogenous valence* of party j , The function $\mu_j(z_j)$ is the component of valence generated by activist contributions to candidate j .

The term λ is a positive constant, called the *spatial parameter*, giving the importance of policy difference defined in terms of a metric induced from the Euclidean norm, $\| \cdot \|$, on X . The vector

$$\epsilon_j = (\epsilon_{j1}, \dots, \epsilon_{jn}) \tag{10}$$

is the stochastic error, whose multivariate cumulative distribution is the Type 1 extreme value distribution, denoted by Ψ . The terms (θ_j, η_i) are individual specific scalars giving the influence of sociodemographic characteristics of the voter on vote choice. Similarly the terms (α_j, τ_i) model the influence on voter choice of the voter's perceptions of the character traits of the candidates. The term $\mu_j(z_j)$, is j 's activist support function. We suggest that we can indirectly estimate $\mu_j(z_j)$ by modelling the election.

In the theoretical model just proposed, activist valence is affected by party position. As party j 's activist support, $\mu_j(z_j)$, increases due to increased contributions to the party in contrast to the support $\mu_k(z_k)$ received by party k , then (in the model) all voters become more likely to support party j over party k . The problem for each party is that activists are likely to be more extreme than the typical voter. By choosing a policy position to maximize activist support, the party will lose centrist voters. The party must therefore determine the optimal marginal condition to maximize vote share. Theoretical results give this as a (first order) balance condition. Moreover, because activist support is denominated in terms of time and money, it is reasonable to suppose that the activist function will exhibit decreasing returns. When these activist functions are sufficiently concave, then the vote maximizing model will exhibit a Nash equilibrium.

It is intrinsic to the model that voters evaluate candidates not only in terms of the voters' preferences over intended policies, but also in terms of electoral judgements about the quality of the candidates. These judgements are in turn influenced by the resources that the candidates can raise from their activist supporters.

In the activist model the term influences every voter and thus contributes to the electoral motive for candidate j . In addition, the candidate must choose a position to balance the electoral and activist support, and thus change the position adopted.

Because each candidate is supported by multiple activists, we extend the activist model by considering a family of potential activists, $\{A_j\}$ for each candidate, j , where each $k \in A_j$ is endowed with a utility function, U_k , which depends on candidate j 's position z_j , and the preferred position of the activist. The resources allocated to j by k are denoted $R_{jk}(U_k(z_j))$. Let $\mu_{jk}(R_{jk}(U_k(z_j)))$ denote the effect that activist k has on voters' utility. Note that the activist valence function for j is the same for all voters. With multiple activists, the *total activist valence function* for candidate j is the linear combination $\mu_j(z_j) =$

$$\sum_{k \in A_j} \mu_{jk}(R_{jk}(U_k(z_j))).$$

Bargains between the activists supporting candidate j then gives a *contract set* of activist support for candidate j , and this contract set can be used formally to determine the *balance locus*, or set of optimal positions for each candidate. This balance locus can then be used to analyze the pre-election contracts between each candidate and the family of activist support groups.

We use the following Theorem, based on a stochastic valence model, denoted $E(\lambda, \mu, \epsilon; \Psi)$. This model incorporates exogenous valence, the average perception of the competence of the candidates. In addition, resources contributed by activists can also influence these perceptions. The *balance solution* for each candidate is the locus of positions that balances the centripetal electoral attraction against the gradient generated by the desire of activists to pull the candidate towards more radical positions desired by activists.

The first order condition for the candidate positions (z_1, z_2) to be a Nash equilibrium in the vote share maximizing game is that the party positions satisfy a *balance equation*. This means that, for each party, $j = 1$ or 2 , there is a *weighted electoral mean* for party j , given by the expression

$$z_j^{el} = \sum_i \mu_{ij} x_i.$$

This is determined by the set of voter preferred points $\{x_i\}$. The coefficients $\{\mu_{ij}\}$ for candidate j will depend on the position of the other candidate, k . The *balance equation* for each j is then given by:

$$z_j^{el} - z_j + \frac{1}{2} \left. \frac{d\mu_j}{dz_j} \right|_z = 0.$$

Here we call $z_j^{el} - z_j$ the *electoral gradient for party j*, since in the absence of activist resources, the equilibrium condition would be given by the condition

$$z_j^{el} - z_j = 0.$$

The second term in this expression is called the *activist gradient for party j*. This first order condition will guarantee that the vector z^* will then be a *pure strategy Nash equilibrium of the vote maximizing political contest*.

The term *balance solution* for the candidates is used for a pair of positions (z_1, z_2) satisfying both balance equations. Theorem. (Schofield, 2006) Consider the electoral model $E(\lambda, \mu, \Psi)$ based on the Type I extreme value distribution, and including both exogenous and activist valences. The first order condition for z^* to be an LSNE is that it is a balance solution. If all activist valence functions are highly concave, in the sense of having negative eigenvalues of sufficiently great magnitude, then the balance solution will be a Nash Equilibrium of the vote maximizing political game.

Figure 1 shows the proposed balance loci and weighted electoral means and contract curves for the two parties, UCR and PJ in the two elections of 1989 and 1995.

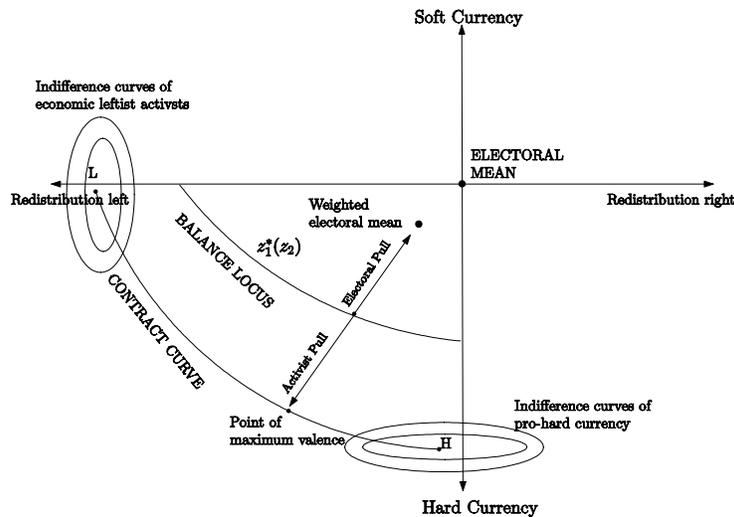


Figure 1: The balance locus and weighted electoral mean for Menem in 1995.

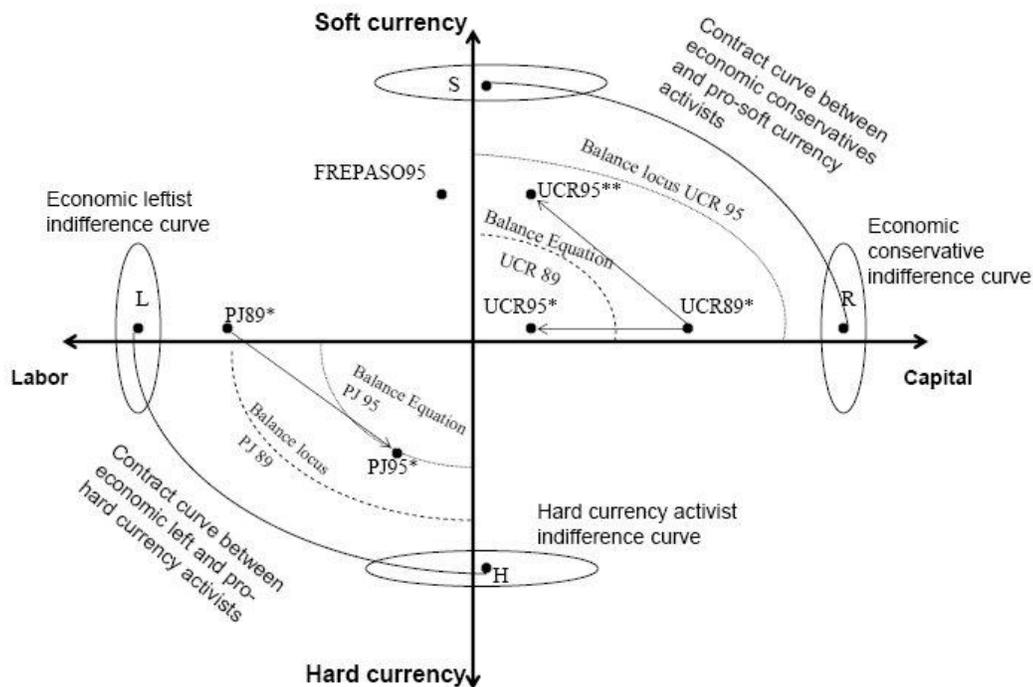
For example, the contract curve for Menem, associated with the two activist groups, centered at L, for Labor, and H, for hard currency supporter, is a catenary.

As Figure 2 indicates, the equilibrium position for a candidate for PJ will depend on the difference between exogenous valences of the PJ candidate and the UCR candidate, as well as the position adopted by the UCR candidate.

We suggest that the exogenous valence of Menem in 1995 was higher than that of the competing candidate, Massaccesi of the UCR, because of the residual sentiments associated with Peronism in the working class. Even though Menem’s move to the right on the economic axis (as illustrated in Figure 1) lost him votes, he gained from the increased resources made available from the new activist group at the hard currency position.

Support for this two dimensional model of party positioning is provided by Figure 3, which gives an estimate of the electoral distribution of voter preferred positions derived from a sample survey.⁵

Figure 2: Argentinean Presidential Elections 1989-1995



Highest density contours of the electoral distribution in Argentina

5. The Swing to the Left

After a failed attempt by Menem for re-election, a new President, Fernando De La Rúa, was elected in 1999. Although De La Rúa belonged to the opposition (UCR), in his electoral platform he committed himself to maintain the economic scheme implemented by Menem. De La Rúa kept this promise once in office. However, the negative consequences of the Convertibility Plan were so severe that they became impossible to ignore. The public debt was already extremely high, and the economy showed serious symptoms of high unemployment, fiscal imbalance and stagnation. Cavallo was appointed as Minister of the Economy in March 2001. Despite Cavallo's efforts, the Argentine economy fell into crisis in December 2001. After the resignation of De La Rúa and a chaotic sequence of interim presidents, Nestor Kirchner, candidate of the PJ with leftist leanings, was elected in May 2003.

By 2006 it became evident that left-wing politicians had won popularity not only in Argentina, but in several countries of the region. This phenomenon encouraged scholars to talk of Latin America's (new) leftward swing. (Vargas Llosa 2005, Castaneda 2006).

These countries included Argentina, Bolivia, Brazil, Chile, Ecuador, Uruguay, Peru, and Venezuela. Of course, there is significant variation in terms of the policy stances of the leftist leaders in each of these countries. There were also marked similarities among some of them. The most anti-free market position has been taken by Hugo Chavez (Venezuela). Following Chavez were Evo Morales (Bolivia), Ollanta Humala (Peru), Rafael Correa (Ecuador) and, to a lesser extent, the Kirchners (Argentina).⁶ Ideas supported by these leaders included the repudiation of national debts, suspension of review of their national economies by the IMF, re-nationalization (or even expropriation) of certain industries, etc. Chavez has either openly or allegedly campaigned for these leaders. For instance, in the case of Ollanta Humala, Chavez campaign support for him was persistent and open. In the case of Cristina Kirchner, US prosecutors have alleged in a Miami courthouse that Chavez provided a bag full of money to contribute to the campaign that gave her the presidency of Argentina in 2007.

Chavez further facilitated these leaders' resources to pursue policies in line with his recommendations. For instance, the Argentine government, lacking any access to international financial markets, has eased its financial needs by borrowing from Venezuela. Also, several accords have been signed between Chavez and Morales to boost Bolivia's recently nationalized energy industry. Venezuela's central role in the region is only possible thanks to its wealth from natural oil reserves. These resources allow Chavez to intervene directly or indirectly in the political processes of other countries in the region. It is quite possible that his control over Venezuela's state wealth and his public support may have had a significant impact on the relative valence of domestic politicians. In the same fashion that the US and IMF had affected the valences of the leaders in the 1990's, contributing to the temporary success of rightist policies and hard currency regimes, Chavez now pushes toward the implementation of anti-free market policies. Since anti-free market policies are by their very nature incompatible with the possibility of having access to financial markets to borrow money, the economic dimension is linked to the external dimension. As the Argentine case shows, once an anti-free market stance has been taken, it is no longer possible for a government to borrow money at sustainable rates.

This has two effects on the external dimension. First, non-traditional lenders become the only alternative. In the case of Argentina, Venezuela took that role, reinforcing the view of Argentina as Venezuela's ally. Second, a hard currency is no longer a viable option. This leads to conflict over whether the government supports the agricultural sector through export subsidies, or taxes it to raise revenue. In the case of Argentina, the resulting political crisis led to public confrontation between the President Cristina Kirchner and Vice President Julio Cobos. Cobos had favored the agricultural activist group that opposed an increase of export taxes on soybean and sunflower. In terms of our formal model, these political events can be understood as a positioning of the Kirchners on the north west quadrant of the policy space. According to the model, in equilibrium, any party that will oppose the Kirchners in 2011 must locate in the south east quadrant of the policy space.

6. Conclusion

In the above discussion, we suggest that in the Latin American polities, an electoral dimension is defined in terms of the external issues of the exchange rate, debt, and the relationship with the United States and other developed polities. The oscillation in one polity follows naturally from the two-dimensionality of the policy space, as activist groups are brought into prominence as a result of the links between choices made in the internal and external dimensions. As the Argentine case illustrates, the form of the support provided by both internal activists (large companies, syndical leaders, etc.) and external activists (multilateral organizations, US or European business interests or policy makers) may vary, but the ultimate goal is to contribute to the success of candidates supporting policies favourable to the activist groups. External conditions are crucial, because they influence the responses of the various activist groups, and thus the strategic responses of the political candidates.

As it is sometimes suggested, political choices in one polity, like Argentina, may trigger a demonstration effect, or belief cascade, in other polities of the region. We thus have a reason for the possibility of contagion from one polity to another. However, our model provides another, more direct, form of contagion, rooted in the democratic process. This form of contagion stems from external activist groups. Supporting similar policies across polities induces a high correlation between the electoral swings of the countries in the region. In other words, when a hegemonic power makes a policy choice on issues such as the exchange rate, savings level, openness of the market, etc., then it has an incentive to try to influence the policy of other countries, through support for any candidate who is willing to implement the preferred policy. However, the support of activists for the hegemon can induce a counter response by other activists (usually leftist). These changes in the electoral equilibria make it appear as if the domestic electoral preferences change temporally or geographically in a chaotic fashion across the region.

Our analysis suggests that this is a misinterpretation. What drives the electoral swings is not a change in preferences, but a change in the distribution of perceptions that the electorate has of the quality of candidates of left and right. Because these perceptions result from the actions of activists who respond to outside influences, we see that the electoral outcomes in Latin American polities will tend to display intrinsic uncertainty. A similar conclusion will hold for other other countries whose economies are dependent both on natural resources and manufacturing. As Edwards (2011) has recently observed in his analysis of Latin American political economy, the problems are fiscal irresponsibility and persistent corruption. The model we have proposed here suggests why these problems are so persistent.

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Notes

1. Nicholas F. Brady was U.S. Treasury Secretary in 1991, when Argentina implemented the Convertibility Plan.
2. Partial transcript from *Your World with Neil Cavuto*, Fox News June 5, 2003.
<http://www.foxnews.com/story/0,2933,88801,00.html>
3. See Aldrich (1983), Aldrich and McGinnis (1989).
4. Ansolabehere and Snyder (2000), Aragones and Palfrey (2002), Banks and Duggan (2005), McKelvey and Patty (2006).
5. The factor analysis was based on a survey. *Politics and the Presidential Election*, Romer & Associates, Survey - TOP045: Roper Center Databank
6. Not all these leaders took office. Ollanta Humala was defeated in Peru's run off election by Alan Garcia. But Nestor Kirchner not only won the 2003 election in Argentina, he was followed by his wife, Christina, in 2007.

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