14 Mixed Blessing: Preliminary Conclusions

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The premise of this book has been that the quality as well as the quantity of cross-border capital flows makes a difference to emerging market countries. The particular characteristics of greatest interest have been the institutional forms of foreign capital, ranging from foreign aid to portfolio flows. The outcomes this volume has focused on have been political, as well as economic. This conclusion attempts, in a very preliminary fashion, to draw generalizable lessons from the country cases. I look at country cases illustrating each type of capital flow to see whether the expected consequences manifest themselves. Since no country case is a pure example of a single type of capital flow, these remarks should be understood as impressionistic.[1] Furthermore, since all types of capital inflows tend to strengthen incumbents, while all financial crises tend to weaken them, the most important predictor of the political consequences of net foreign capital inflows is the characteristics of the incumbent political regime. The discussion, summarized in Table 14.1, thus distinguishes between authoritarian and democratic capital importers that have experienced each type of inflow.

Foreign Aid

Our expectations of *foreign aid* (see row 1 of Table 14.1) were that it would make a rather small contribution to economic growth in the recipient country, that the locally-relevant political influence of donor governments (or international organizations) would be strengthened, as would governing incumbents, and that this form of foreign capital transfer posed a comparatively low balance-of-payments risk. External actors would be relatively unlikely to pressure the sitting government for specific economic reforms, neoliberal or otherwise. The consequences of official grants and credits for democracy in emerging market countries thus mainly hinged upon the goals of the main donor government(s) and the pre-existing characteristics of the government in the recipient country.

United States' aid to the Philippines under Ferdinand Marcos through the late 1970s illustrates foreign aid to an authoritarian government. In return for secure leases for military bases that the US considered essential to its East Asian strategy, the US gave generous aid commitments and for many

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Table 14.1 Types of capital flows and democracy: country cases

Prominent financial instrument	*Authoritarian capital-importing country*	*Democratic capital-importing country*
Foreign aid	• Philippines under Marcos • Zaire under Mobutu	• India under Nehru • Russia under Yeltsin
Foreign direct investment	• Indonesia under Suharto • Vietnam in 1990s	'*Pessimistic*' *outcome*: • Chile under Frei, then Allende (1964–73) • Brazil under Kubitschek, Quadros, Goulart (1956–64) '*Optimistic*' *outcome*: • Argentina, Brazil in late 1980s, 1990s • South Africa under Mandela
Bank loans to govt.	• Argentina, Brazil, Mexico in 1970s	• India in 1980s
Bank loans to private firms	• Chile, Argentina, Brazil in 1970s	• ??
Portfolio investments with govt.	• Mexico under Salinas (1988–94)	• Argentina under Menem (1990s)
Portfolio investments in private firms	• South Africa under apartheid • Singapore in 1990s (equity) • Indonesia in 1990s (short-term debt)	• India, Chile in 1990s (corporate bonds, portfolio equity) • Thailand, South Korea in 1990s (short-term debt)

years downplayed credible reports of human rights abuses. Moreover, the Marcos administration apparently used its overall control of resources and influence (although not necessarily foreign aid dollars in a traceable fashion) to perpetuate dense networks of patronage and to corrupt many government-business links. The US government avoided pressuring the Philippines for significant economic reform, although the multilateral development banks sporadically tried.[2] However, in the early 1980s the US altered its perception of 'US interests' in the area and gave important support to the 'people power' movement of democracy campaigner Corazon Aquino. The

large sums of bilateral and multilateral aid to the Philippine government, along with the strong historic ties of the islands to the *de facto* ex-colonial power, gave the United States government substantial influence over the progress of the eventual democratic transition. In the Philippines, then, foreign aid began to contribute to the circumstances promoting democracy only when this became an outcome important to the country's major aid donor.

Zaire provides a second case of aid to an authoritarian regime. American, French, and other foreign aid from the 1970s through the early 1990s to Zaire under President-for-life Mobutu Sese Seko pursued goals of anti-Communism, strengthening post-colonial francophone ties, and assuring access to huge copper and mineral reserves for commercial uses and possible military contingencies. With such a full agenda of strategic goals, human rights and democratic concerns were consistently and thoroughly downplayed in the relations of the major donors with the authoritarian government.[3] Although Zaire admittedly was an extreme case, it provides a textbook example of the contribution of foreign aid to government economic mismanagement and the propping-up of an oppressive government and political regime.

An example of a democratic recipient of foreign aid is India in the 1950s through the 1960s, during these years one of the largest aid recipients among all developing countries, albeit one of the smallest in per capita terms. Aid from western democracies, both from multilateral sources such as the World Bank and through bilateral programs like the US Food for Peace donations, provided important budgetary support to the Indian government in its first decades, becoming at least one of the factors that enabled Indian democracy to survive. Large quantities of foreign aid to India not only strengthened the ability of elected rulers to deliver some of the material goods their constituents desired. Foreign assistance also reinforced the government's freedom to pursue its preferred economic policies, which it described as 'democratic socialism'. These policies included construction of a huge state productive sector, and extensive affirmative action and regional redistribution programs, all intended as a way of enhancing citizen support of the incumbent democracy (and the long ruling Congress Party) within a multiethnic state riven with deep caste and class inequalities. They were the antithesis of neoliberal policies. With hindsight, the majority of Indian economists agree that many of India's statist economic policies also were rather inefficient. However, because the population by and large perceived their redistributive element as just and moral, they played an important role in legitimating democratic government in a setting that many observers initially thought would be an unlikely home for it.[4]

The experiences of the Philippines, Zaire, and India generally confirm our expectations of foreign aid. Few observers believe that external assistance

made great contributions to economic efficiency in any of these countries. Nor did foreign aid, even from democratic donors, necessarily make great contributions to hastening the transition to democracy. Instead, aid resources gave incumbent governments additional room to manuever, both economically and politically (so long as the foreign patron government could achieve its *de facto* core goals), without greatly increasing policy-makers' worries that a sudden foreign exchange crisis might develop. More recently, the newly and precariously democratic Russian federation has received large quantities of multilateral assistance, especially – and unusually – from the International Monetary Fund. Randall Stone's chapter in this volume puts a compelling, and rather darker, twist on the likely consequences of massive quantities of foreign aid coming to a young and weak democracy. The political incumbent, President Boris Yeltsin, indeed has been strengthened, Stone argues, but at the cost of both sound economic policy and institutionalizing democracy.

Foreign Direct Investment (FDI)

Foreign direct investment (row 2) should have a significant positive impact on economic growth, should heighten the political and policy influence of multinational corporations, and should not be prone to sudden capital flight. I assume that multinational corporations (MNCs) always become players in the domestic politics of the host country, however much they may publicly disavow having any such intent. Most often their political involvement is limited to discreet lobbying on behalf of a 'good' investment climate. Thus, MNCs may intrigue against what they view as 'politically-motivated regulatory red tape' or 'irrational' restrictions on their right to hire and fire at will, and so on. If the country's current rulers are authoritarian leaders, they should be strengthened by FDI inflows. However, authoritarian regimes also may experience subtle pressure from foreign corporations to liberalize politically, for example, by expanding freedom of the press. Policy-makers may also find multinational direct investors urging them to liberalize the economic policy regime.

Indonesia and, very recently, Vietnam are authoritarian countries that have captured large direct investment inflows (see Winters and Haughton in this volume). Loudly anticommunist and authoritarian, Indonesia under General Suharto received large amounts of FDI from the late 1960s through the 1990s. Communist and politically-authoritarian Vietnam has garnered truly astonishing pledges of foreign investment since its embarkation on the path of economic liberalization in the early 1990s. There are some interesting similarities between these otherwise diverse cases. The symbolic vote of confidence from outside, and the economic stimulus, have helped each economy. In both cases generous foreign investment apparently bolstered the political fortunes of the authoritarian incumbents, arguably encouraging

them to continue suppressing political dissidents. Foreign direct investment thus did little or nothing to promote democracy. Multinationals have insisted upon some economic reforms, generally ones aiming to make the internal economic regulatory environment more predictable and more similar to business conditions prevailing in advanced industrial countries.

Nonetheless, the political incumbents were perhaps encouraged to perpetuate certain economic irrationalities, such as large-scale corruption in the management of public-sector investments, that did not negatively affect foreign investors' profits. That is, direct investors, like local big business actors, in both countries have been more concerned with ensuring their own freedom of action than with increasing the overall efficiency of the economy. In addition, Jonathan Haughton notes that Vietnam's Communist government has required joint ventures between state-owned enterprises and MNCs, thus strengthening government incumbents more than with ordinary FDI, while diluting the presumed 'efficiency effect' of having foreign capital inflows spent by private, rather than public, actors.[5] FDI has the advantage of not being highly volatile. The spread of the 1997 East Asian financial crisis to Indonesia, but not (as of mid-January 1998) to Vietnam, probably can be attributed to the much greater role of liquid portfolio investment in the former. FDI also gives the host government useful friends: western and Japanese direct investors in Indonesia have used whatever influence they have over their home governments to encourage them to participate in the rescue package.

If the incumbent government is instead democratic, and if it can limit the political and lobbying activities of foreign businesses to actions that are not regime threatening, then the additional private investment and growth provided by FDI should strengthen democracy. However, emerging market country governments are not always able to control the domestic political activities of foreign business. Chile in the early 1970s illustrates the case of foreign direct investors – who originally had entered the country under a succession of politically and economically conservative though mostly democratic previous administrations – confronted with a newly elected, politically weak, democratic government espousing radically redistributive, populist economic policies. Officers of American multinational companies actively intrigued with representatives of the US government and the Chilean military to overthrow President Salvador Allende, who lost his life in the coup that initiated 17 years of often brutal military rule (Treverton, 1990). The Chilean experience illustrates the pessimistic hypothesis about the increased influence of foreign business in host country politics. Similar events transpired with the João Goulart administration (1961–64) in Brazil and the second Peronist government (1973–76) in Argentina, each of which the country's military officer corps, with the tacit support of traditional politicians and business leaders, also displaced by force.

There is another possible twist on these stories, however. Most contemporary economists, including many on the left, probably would agree that the economic policies of Allende, Goulart, and Isabel Perón were, in fact, unsound and unsustainable. Each of the three presidents, for example, raised civil service and public sector union wages when the treasury had no funds to back this move. Arguably, had multinational investors successfully pressured these governments to adopt less radical economic policies, then economic conditions would have improved and the excuse for a military coup could have evaporated. This second line of argument, the optimistic hypothesis, also plausibly applies to the more recent experiences of new democracies in emerging markets that have decided to welcome foreign direct (and portfolio) investors. These include Argentina and Brazil from the mid-1980s, or South Africa in the 1990s. In each case, the policy-makers in the new government who historically had been associated with economic nationalism gradually adopted many of the programs of neoliberals (on Argentina, see Armijo, 1994 and Gibson, 1997; for post-apartheid South Africa, see Daniels and Daniels, 1995). Also in each case, this shift in the overall tenor of public policies was initiated by technocrats, politicians, and other policy elites from the 'top down,' had to be sold to sceptical voters whose first preference was for classically populist economic policies, and was at least partly a response to political incumbents' perceptions of the need to attract foreign capital, especially in the form of direct investment.

Commercial Bank Loans to the Public Sector

The third category of international investments is *commercial bank loans to the public sector* of the emerging market country (row 3 of Table 14.1). I argued that bank loans to government should have a lesser impact on economic growth, while expanding the resources available to the political authorities to use for either developmental or directly electoral purposes with, in practice, comparatively little creditor oversight or external pressure to follow 'sound' economic policies, however defined. The risk of a balance-of-payments crisis, however, is higher with loan finance than with official credits or FDI. During the 1970s the authoritarian governments of Argentina and Brazil, and the civilian, semi-authoritarian government of Mexico, each received large quantities of foreign bank loans. In all three cases, foreign loans to non-democratic incumbents shored up unrepresentative political regimes by allowing political leaders to extend favors to politically crucial groups.[6] Interestingly, another consequence of foreign borrowing was to increase the *de facto* economic policy autonomy of governments from both foreign and domestic pressure to reform.[7] Finally, capital account surpluses due to foreign borrowing in all three Latin American countries served to make large current account deficits surprisingly painless, at least for

upper-income groups, and thus probably deprived the democratic opposition of many potential allies among salaried workers and the business community. Until the 1982 debt crisis, the incumbent regimes in each of these countries continued to claim, with some plausibility, that they should be maintained in office because of their singular success in national economic management. Foreign loan inflows not only insulated the military regimes in these countries from foreign pressures to alter their regulatory regimes; they also protected authoritarian incumbents from criticism from domestic political opponents.

However, bank loans, even long-term ones, are a more volatile form of capital flow than foreign aid or direct investment. In Argentina, Mexico, and Brazil the effect of the 1982 financial crisis was a loss of credibility for authoritarian incumbents leading to dramatic changes of regime in Argentina in 1983 and Brazil in 1985, as each country returned to procedural political democracy. However, had the international environment of the 1980s been less favorable to democracy, the successor regimes in Brazil and Argentina might well also have been authoritarian. Mexico's civilian 'soft' authoritarian regime experienced no sudden, dramatic crisis, but rather a gradual erosion of public confidence (important to authoritarian as well as democratic regimes, albeit in somewhat different ways) throughout the 1980s. One consequence was to give previously feeble opposition parties a opportunity to press for fairer, more genuinely democratic, rules of the national political game (see Elizondo in this volume).

Commercial bank loans to a democratic government can also augment its resources and bolster its credibility. In the 1980s India, a democratic country which had resisted the blandishments of international bankers throughout the 1970s, became a large commercial bank borrower. Tellingly, one of the hopes of Indian politicians and policymakers was that, by borrowing from the foreign private sector, they could escape the economic policy conditionality imposed by public sector lenders, such as the International Monetary Fund, to which Prime Minister Indira Gandhi very reluctantly had had to turn for a large loan in 1981. As had been the case with Latin American sovereign borrowers of the 1970s, the foreign resources gave additional room for fiscal maneuver (or irresponsibility) to the incumbent government – though this time the incumbents were democratic. India experienced another external payments crisis in 1991, which led the country to another reluctant turn to the IMF and provoked policy-makers into beginning long-needed economic liberalization.[8] Fortunately for the long dominant Congress (I) Party, it was a short-lived coalition government of the non-Congress left parties that made the politically unpopular decision to turn to the IMF in early 1991; the Congress itself, under newly-elected Prime Minister P.V.N. Rao, took the onus of devaluing the rupee by 22 per cent in July of that year. Overall, since the external crisis was contained, access to foreign loan capital

served to support both the political incumbents during most of the 1980s, that is, the Congress (I) Party, and also India's democratic political regime.

The cases of three large Latin American borrowers in the 1970s, and of India in the 1980s, thus generally confirm our suspicions that cross-border private bank lending to the public sector in emerging market countries increases both the economic and the political bargaining power of incumbent governments – unless and until a serious external payments crisis causes the economic management skills of the political leaders suddenly to be called into question.

Commercial Bank Loans to the Private Sector

This volume has suggested that the effects of *commercial bank loans to the private sector* (row 4), are likely to include a greater stimulus to economic and industrial growth and an increase in the political weight of large borrowing firms in domestic policy councils. The inflows should increase the bargaining chips of big business *vis-à-vis* the incumbent government. If local big business firms bring in significant quantities of foreign commercial bank loans, then authoritarian regimes should experience pressure from their entrepreneurs to liberalize, at least in the areas of respect for property, legal and predictable regulatory enforcement, and sometimes human rights. Of course, many of the most closed regimes, from China to Burma, during the 1970s heyday of commercial lending to developing countries lacked a business class that could directly attract foreign bank loans. Other authoritarian countries with private firms that might have borrowed abroad, such as the East Asian tigers like South Korea, operated domestic regulatory and financial environments that strongly encouraged local firms to depend on state banks instead.[9]

As it happens, the main examples of developing countries whose private firms directly contracted large quantities of medium and long-term commercial bank loans abroad are precisely those Latin American countries whose governments also were large borrowers, thus confounding our attempts to distinguish the effects of government versus private sector long-term borrowing. One proposition I suggested in Chapter 1 seems not to hold true in these cases, however. There does not seem to be evidence that countries that had a particularly large share of direct private sector borrowing abroad, such as Chile or Argentina, spent their borrowed funds, on average, more wisely than those with relatively smaller shares of private in total foreign borrowing. In fact, most observers have considered that Chile, along with Brazil, apparently invested with a reasonable degree of efficiency, while Argentina wasted a large portion of the funds it borrowed (Frieden, 1991, p. 80). One plausible explanation that is consistent with the logic developed in chapter one, however, is that the private sector in many of these countries, but perhaps in

Argentina particularly (see Lewis, 1990), was characterized by what has come to be known as 'crony capitalism,' in which firms' profits depend less on competitive efficiency and more on political connections that give them access to economic rents. Under these political conditions, private borrowers may expect that any exchange rate or other losses they experience are likely to be 'socialized' by the central government.

The expectation that big business would increase its bargaining power with the authoritarian central government, and then would tend to push for political liberalization if not full democracy, seems to have described outcomes in Brazil (where business dissatisfaction with military rule was crucial in accelerating democratization, as Peter Kingstone notes in his chapter in this volume), but not in either Chile (where big business could not even protect itself from waves of bankruptcy when the debt crisis hit in 1982–83, much less impose a liberalizing political agenda on military incumbents) or Argentina (where crony capitalism prevailed, linking military officers and big business in non-productive rent-seeking). In these three countries taken together, there is not strong evidence that big businesses used their ability to attract foreign loans to enhance their politically-relevant domestic resources, or even that big business' political preferences tended toward political liberalization, though not always the transition to full mass democracy. If the expected effect is present, it has been swamped by other, more powerful, influences.[10]

I do not know of a good empirical example of a democratic developing country whose private firms directly tapped multinational commercial banks for large quantities of long-term loans. This cell in Table 14.1 is thus empty.

Portfolio Flows to the Public Sector

This fifth category of international financial flows is shown in row 5 of Table 14.1. Our expectations of their effects on the borrowing country's political economy were quite similar to those postulated for commercial bank lending. *Portfolio inflows to the public sector* should provide a lesser stimulus to economic growth than those going to the private sector, but a greater political resource for the sitting government. As noted, portfolio flows differ from bank loans in one important respect: balance-of-payments crises provoked or exacerbated by large-scale overnight capital outflows are much more likely to occur with securities explicitly marketed to their purchasers as being highly liquid.

Mexico during the early 1990s provided a reasonably clear example of several hypothesized consequences of portfolio flows coming into government coffers (see the chapters by William C. Gruben, Carlos Elizondo, and Walter Molano).[11] The substantial portfolio capital inflows to the government, beginning in the very late 1980s and accelerating in 1993, on the whole

strengthened the semi-authoritarian regime, and its domination by the Mexico's longtime ruling political party, the Partido Revolutionário Institucional (PRI). Foreign purchases of portfolio capital inflows in the Mexican government peso-denominated *cetes* securities, and later the dollar-indexed *tesobonos*, enhanced the freedom of maneuver of the PRI political incumbents, just as the earlier commercial bank loans had done in the 1970s. As Mary Ann Haley and Jeffrey Winters emphasize in their contributions to this book, foreign portfolio investors seek political stability. However, as Carlos Elizondo notes in his essay, sometimes a preference for political stability, in practice, can be a preference for a process of gradual, orderly democratization to continue. Thus, in 1994, the enhanced visibility of Mexican politics in the US as a consequence of the North American Free Trade Agreement (NAFTA) had made US investors aware that a possible source of instability in Mexico was popular protests against the continuing legacies of soft authoritarianism in Mexico, such as election fraud. That is, the need to retain the confidence of notoriously fickle foreign investors put pressure on the out-going Salinas administration to run clean elections. Business confidence prior to the election, of course, was helped by the fact that it looked as though the leftist PRD, whose standard bearer, Cuauhtémoc Cárdenas, had come close to winning the 1988 election, had no chance in 1994. In August PRI candidate Ernesto Zedillo, as expected, won easily.

Unfortunately, the story did not end there. For a variety of reasons, both economically sound and politically opportunistic, outgoing President Carlos Salinas chose not to devalue despite a widening trade deficit.[12] His administration convinced world markets that it would not precipitously devalue by replacing peso-denominated treasury securities, as they came due, with dollar-indexed bonds offering an attractive interest rate. In December 1994, Zedillo's economic team finally devalued the peso by 15 per cent, an intrinsically reasonable amount in terms relative to price inflation prevailing in Mexico as compared to the US Nonetheless, the markets panicked. By early February 1995, the peso's value stabilized at 40 per cent below its earlier level, only stopping there due to the firm backing of a $50 billion rescue package engineered by the Clinton administration.[13] The Mexican population, which had endured a drop in the real urban minimum wage of more than 50 per cent following its 1982 international debt crisis,[14] and only had begun to see economic recovery in the early 1990s, was stunned to discover that further years of austerity were in store.

The consequences for Mexican democracy over the subsequent three years of the peso crisis were fairly consistent with our theoretical expectations. On the one hand, the PRI stopped looking like a miraclemaker, and the stock of opposition parties rose. Greater transparency of political activity, and incremental progress towards fairer formal rules of the game (election procedures and campaign financing, for example) resulted.[15] These trends were

democratizing, and contributed to the opposition victories in the mid-1997 elections. On the other hand, the economic consequences of the peso crisis clean-up have, as also theorized, undercut the social and economic positions of several groups whose active participation in writing new 'rules of the game' might be expected to ensure full and fair mass participation in democratic processes. As has happened in country after country, middle class unionized civil servants and public sector industrial workers were laid off in large numbers, weakening these groups as political actors. Post-crisis structural adjustment also has made the poor, both urban and rural, more desperate than ever, encouraging the twin responses of apathy and resignation for the majority, along with a turn to violent protest for a minority.[16] The interim bottom line is thus something like this: Mexico's peso crisis has brought greater political freedom and competitiveness, but has heightened economic insecurity and inequality. The fact that government short-term debt was a large part of the problem has put the public sector on a particularly tight rein.

Turning to the case of portfolio capital inflows to the government of an already democratic emerging market country, we could expect many of the same outcomes: the direct positive impact on economic growth probably would be limited because public sector borrowers have a political as well as an economic investment agenda; while they lasted, portfolio purchases of government bonds could provide a welcome source of fungible resources to the political incumbents – but portfolio inflows would be prone to sudden reversals, possibly bringing political as well as economic crises for the country and/or its rulers. Argentina in the early 1990s, under President Carlos Menem of the Justicialist (Peronist) Party, was a newly-democratic country that allowed itself to sell large quantities of government debt to buyers bringing capital from abroad.[17] As it happened, the Menem team had occasion to regret its reliance upon portfolio inflows for government deficit financing. When Mexico's peso crisis exploded in late December 1994, first-world investors, as had happened in 1982, tended to generalize their pull-out across other emerging markets, especially in Latin America, without a great deal of regard for the possible differences among countries. In early 1995 Argentina, Ecuador, Brazil, and others experienced the 'tequila effect' of a backlash from Mexico's crisis.[18] While Menem, along with Argentina's decade old democracy, survived the dramatic ebb of capital, the government budget (which thereafter incorporated much higher interest rates on the public debt) and the Argentine economy (where an incipient recovery from the recession of the 1990s was dashed) paid the price.

The tequila effect was not sufficiently severe to have unbalanced Argentina's new democracy. However, it is not too difficult to imagine a scenario in which it might have. President Menem himself was quite lucky in the timing of Argentina's narrowly averted financial crash: the movement to

alter the Constitution to allow him to run again, and his victory in that election, already had passed by early 1995 when the run on the Mexican peso began to batter the Argentine peso. Had the Argentine electoral calendar been otherwise, he might well have lost his bid for reelection.

Portfolio Investments to the Private Sector

The final type of cross-border capital flow is *portfolio investments in private sector securities* (row 6). With an authoritarian regime in the capital-importing country, our expectations would be that such flows would make a potentially large contribution to private investment by the country's largest firms (that is, those whose shares constitute the blue chip investments in the local stock exchange, or who are able to issue bonds or commercial paper in global markets), that the heads of these firms would tend to join foreign direct investors overtly or covertly in pushing for greater political liberalization (in the sense of a rule of law and civil liberties protections) without necessarily risking too much to call for full democratic elections, and that the desire to avoid the ever-present potential of a major capital outflow would lead to a fairly cautious and deferential attitude on the part of the authoritarian rulers towards their business supporters. Preemptive neoliberal economic policy reforms also should be likely.

South Africa in the 1970s and 1980s provides an interesting case. Rich in diamonds, gold, and minerals, it long had one of the most active stock and securities exchanges outside the major industrial democracies. It also had a special kind of authoritarian political system, one that provided liberal democracy for a minority, but used apartheid to exclude the black majority from economic, social, and political power. Generalizing very roughly, in recent decades black Africans were the workers and small farmers, Afrikaaners the civil servants and commercial family farmers, while English-speaking whites dominated the liberal professions and upper reaches of business. British capital was long the largest source of foreign investment, both direct and portfolio, in a tradition dating back to the late nineteenth century. Under these circumstances, foreign capital inflows to the local private sector on the one hand tended to strengthen the white minority, the elite who benefited from authoritarian rule over all non-white residents. At the same time, business links to the outside probably strengthened the English-speaking minority within the overall white minority that ruled the country. Under these particular demographic circumstances, the predicted politically liberalizing effect of capital inflows to the business class was muted by the solidarity of the white community as a whole. Nonetheless, the English-speaking white community was somewhat more open to a gradual transition to democracy than the Afrikaaner one, perhaps partly because of its greater familiarity with the larger world through international business links. As was

the case in our examination above of commercial bank lending to the private sector in authoritarian Latin America, there does not seem to be compelling evidence that private portfolio inflows to the South African private sector during the 1970s and 1980s was a great source of pressure for economic efficiency, although my judgment on this point is quite impressionistic (see Daniels and Daniels, 1995).

Another obvious case is that of Singapore, in the 1980s and early 1990s both an Asian 'tiger' and a hot emerging stock market. As of the mid-1990s, Singapore's longtime strongman and patriarch, Lee Kwan Yew, was respected at home and throughout the region because of the country's great economic advances under his tutelage. At the same time, Lee and his proteges, including Prime Minister Goh Chok Tong, could not afford to alienate their business leaders, on whom the country's prosperity and ultimately their own political tenure depended. In the case of Singapore, many business families within the country also had extensive ties with the overseas Chinese community around the world, including those who had located in the advanced industrial democracies. The Singapore business community was quite far from sharing, for example, the political opinions of radical students who wished to move rapidly to full democracy. However, the internationally competitive business community also was sensitive to its image abroad, collectively wincing when, for example, a Japanese popular song mocked Singapore as the place where chewing gum was a banned substance.

Financial globalization in Singapore had resulted in a somewhat freer press, a dawning but vigorous debate over the pros and cons of paternalistic government, and signficant moves toward political liberalization – stopping well short of formal representative democracy – over the decade ending in the mid-1990s. Interestingly, Singapore to mid-January 1998 had escaped serious damage from the East Asian financial crisis, at least by comparison with its neighbors. This was probably because there are important distinctions among the various types of new cross-border portfolio investments in the emerging market country's private sector, beyond the obvious differences between portfolio flows and the other less-volatile flows discussed in this book. Singapore, although an important emerging stock market, did not suddenly in late 1997 reveal large amounts of short-term foreign borrowing by local banks – a major source of trouble in Thailand, Indonesia, and South Korea.

Indonesia is another authoritarian country that in the 1990s received increasing amounts of portfolio capital inflows into its private sector, particularly the banking system. Like Lee in Singapore, Indonesia's Suharto benefited from large portfolio capital inflows, in that they made his regime and government look like excellent economic managers. However, and unlike Singapore, Indonesia has had a serious financial crisis; as of this writing the currency had dropped 80 per cent against the US dollar,

compared to its level in early 1997. What are the apparent implications for democracy? Jeffrey A. Winters, who was able to revise his chapter on Indonesia, is struck by the much more facile and effective social and political response to the financial crisis in democratic Thailand and South Korea, as compared to authoritarian Indonesia. President Suharto's initial response to the crisis seems to have been to promise the IMF whatever it wanted, and then, in his government's budget of early January, as well as his plans to be succeeded by his high-spending Vice President Habibie, to have attempted to continue with crony capitalism – with large areas of the economy reserved for his own family – as usual. The incumbent authoritarian government was proving extremely resistent to neoliberal economic reform, even after a violent balance-of-payments crisis and the forced retirement of Suharto in May 1998. Unfortunately, the first few months of the Habibie government did not result in significant structural reforms of Indonesia's underlying political economy. Perhaps because Indonesia's poor and middle sectors, but not yet its top elites, had thus far paid the bulk of the costs of the crisis.

I close the case studies with a look at portfolio flows to the local private sector in three democratic or democratizing emerging market countries: India, Thailand, and South Korea in the 1990s. Although all types of foreign capital inflows tend to assist political incumbents – so long as a balance-of-payments crisis is avoided – I argued in Chapter 1 that those flows whose local disposition is in the hands of the private sector could be more problematic for the often weak or fragile democratic governments in emerging market countries. Portfolio flows controlled by private entrepreneurs should stimulate productive investment while empowering local big business as a potential counterweight to the national political leaders.

India had been securely democratic for decades. Its portfolio flows to the private sector in the 1990s, in contrast to most of the East Asian countries that had trouble in late 1997, had been mainly in the form of equity and bond flows, particularly those associated with large Indian firms raising funds directly by securities floated in international markets, global depository receipts (GDRs). Although even limited entry by private investors directly into Indian capital markets has had an important influence on the shape of Indian financial regulations, as detailed by John Echeverri-Gent in his essay, the Reserve Bank of India, the country's central bank and main commercial bank regulator, placed strict limits on the amount of short-term foreign loans and deposits that commercial banks could contract, resulting in a regulatory regime with substantial capital controls still intact. This regulatory caution appears to have paid off; through mid January 1998, India had not yet caught the 'Asian flu'.

India also is a case where our predictions about the political and policy consequences of capital inflows to private big businesses provide a plausible description of reality. On the one hand, the private sector became increas-

ingly important to the balance of payments in the 1980s and early 1990s, both as a source of exports and as an investment destination for foreign funds. Economic policies, meanwhile, became more market-oriented, particularly since 1991, and the profession of businessperson, by all accounts, has higher status and greater attraction for the 'best and the brightest' than it did in the first three decades after independence in 1947. There is a chicken-and-egg problem here, as it is hard to know whether businesspersons have become more politically and socially prominent as a consequence of economic policy changes initiated by government bureaucrats and senior politicians, or whether the generally pro-market preferences of an increasingly confident private sector wield more influence than previously. Both are probably true. The causes of India's recent economic liberalization are in any case overdetermined (Varshney, 1996; Echeverri-Gent, 1997). In his carefully nuanced contribution to this volume, Echeverri-Gent suggests a new twist on the 'optimistic hypothesis' about the effects of private foreign capital flows: by forcing greater regulatory transparency and breaking up cosy oligopolies, democratic integrity is preserved and deepened, as small businesses and small investors get a more level playing field and, most importantly, a corrupting influence from the crony capitalists to the government is dampened. At the same time, he concedes that trade and financial globalization in India in general already have widened interregional income disparities – and probably will continue to do so, with potentially ominous implications for democratic and political stability.

The final examples are Thailand and South Korea, newly-democratic countries that received large amounts of portfolio capital inflows to their private sectors in the 1990s, with particularly large flows of short-term hard currency debt, often borrowed by local banks who then would relend in local currency, making their profits on the spread.

Danny Unger's chapter summarizes Thai political economy since the mid-1970s. While agreeing that local big business prefers political liberalization to full democratization, Unger sees the strengthening of local private capital in Thailand in the 1980s and 1990s as an important counterweight to a still very powerful military-bureaucratic-civil service complex, which the proliferating clientelistic political parties had utterly failed to rein in. That is, given Unger's assessment of the stage of Thai democratization, he sees redistribution of economic and political power in the direction of local big business prior to the financial crisis as, on balance, having increased political competition and accountability. Moreover, although he is less explicit on this point, Unger tends toward the 'optimistic' interpretation of the post-crisis increased indirect influence of foreign institutional investors on Thailand's economic policy choices, suggesting that sounder macroeconomic and regulatory policies may result. It is also possible to imagine that the balance-of-payments crisis could weaken Thai democracy, at least in the short-run, by

reinforcing the impression that civilian politicians are both incompetent and corrupt, and implying that the Thai military is neither. However, as both Winters and Unger note, Thai adjustment to its financial crisis in late 1997 and through January 1998 was reasonably rapid, arguably *because of* its comparatively democratic political game.

A related dynamic seemed to be at work in Korea. That country's balance-of-payments crisis hit before the December 1997 presidential election, in contrast to events in Mexico in 1994, and served to discredit both the conservative government of incumbent President Kim Young Sam (a former dissident who owed his election to a rapprochement with the outgoing military rulers) and the *chaebol*, powerful and long-favored oligopoly business conglomerates (Kim, 1996; Amsden, 1989). Long-time dissident Kim Dae Jung won a plurality in a three-way race and used the opportunity given him by the crisis to win striking early negotiating victories even before formally assuming office.[19] As in Thailand, the financial crisis may prove to have a silver lining in that it gives reforming democratic governments some leverage to reduce some of the cosy ties between big business and the state. However, as in Mexico, those who suffer most in the short run will be those in the lower, and to a lesser extent the middle, income groups. Political democratization may be accelerated, but the economic pain will be considerable. Furthermore, if the Rueschemeyer, Stephens, and Stephens (1992) analysis is correct, then the apparent weakening of groups such as labor unions during the transition to democracy might hold worries for the future. The alternative hypothesis is that, by being flexible and 'reasonable' in this time of crisis, Korean union leaders may permanently earn themselves a place at the table. Moreover, to the extent that the foreign investor community sees cautious progress in democratization as a key indicator of that highly-desired quality, 'political stability' (see Elizondo in this volume), then the financial crises in Thailand and South Korea may work to secure those countries' democratic openings.

*   *   *

I ended Chapter 1 with a series of expectations. Based on the evidence presented herein, how have they fared?

1. I suggested that, contrary to the too-facile expectations of many in the business and policy communities, economic growth does not necessarily promote political democracy, at least not for poor and middle-income countries. While this collaborative project has not directly addressed this link, it seems implicit in the stories told of Mexico and Brazil before the 1982 debt crisis, and Indonesia and Vietnam in the more recent period. What economic growth does do, for as long as it continues, is to

legitimize incumbents. Conversely, however, where authoritarian regimes have wrapped themselves in the flag of successful economic management, they can be denuded rapidly by financial blowups. This happened to authoritarian rulers in Argentina, Uruguay, and Brazil in the early 1980s (though Chile's General Augusto Pinochet held on), and was a factor in the overthrow of Philippine dictator Ferdinand Marcos and gradual liberalization of Mexico's civilian one-party state.

2. No contributors to this volume rigorously tried to test the hypothesis that inflows controlled by the private sector within the emerging market country, or by foreign direct investors, would be allocated more efficiently, resulting in greater increments to growth, although Stefano Manzocchi summarizes related literature, finding the links between private foreign capital and growth more tenuous than sometimes assumed. Walter Molano's contribution is implicitly provocative on this point, however, as he suggests that the long-run economic consequences of the Thai and East Asian crises of late 1997 could be more serious than the Mexican crisis of 1994–95, precisely because the borrowers in East Asia were in the private sector, whereas Mexico's peso crisis was first and foremost a crisis of the government's ability to meet its short-term debt obligations. This apparent anomaly – that capital flows coming to the local private sector might produce deeper economic crises than public-sector portfolio borrowing – is perhaps explained by the fact that many of the private borrowers in East Asia were banks and financial institutions operating in newly-liberated capital markets with inadequate regulatory oversight (see Amsden and Euh, 1997). In fact, several of the authors note that greater transparency and predictability in national financial regulation – often missing in emerging markets – would be a good thing, whether for better economic results in the capital-importing country (see Manzocchi), for foreign investors (Molano), for small investors and ordinary citizens within the emerging market country (Echeverri-Gent), or even for the institutionalization of democracy itself (Stone).
3. Different institutional forms of cross-border capital flows would, I thought, differentially promote the fortunes, and local political influence, of four different political actors: foreign governments and international organizations, incumbent governments in the capital importing country, foreign direct investors, and local big business. The evidence of increments of both political and economic influence accruing to foreign lender/donor governments and/or to borrower governments as a consequence of different institutional forms of cross-border capital flows is straightforward and consistent with these predictions. With the relative decline of foreign aid, for example, not only have borrower governments lost resources, but foreign governments (often to their surprise) also

have lost influence. It is worth pondering the consequences of the fact that the currency trader George Soros in the early 1990s gave more aid to promote democracy in Central and Eastern Europe than the US government.[20]

With respect to foreign business, my initial decision to call the influence of multinational direct investors 'political,' but to exclude the indirect influence of global private portfolio investors (before any financial crisis) from this framework seems to have underemphasized important facets of the story. Thus, for example, Haley, Porter, Stone, and Echeverri-Gent in this volume each detail some of the different ways in which the mostly neoliberal preferences of private global investors (in the case of Russia, Russian owners of wealth who had the connections to engage in capital flight) have constrained public policy choice in emerging market countries, even when the foreign investors did not actively lobby incumbents. Moreover, once a financial crisis looms, private portfolio investors may become directly involved, as in the cases of foreign institutional investors in Mexico in 1994–95, or private multinational banks who made short-term loans to domestic banks in East Asia in 1997. Tellingly, South Korean President-elect Kim Dae Jung granted George Soros an audience in the first two weeks after his December 1997 upset victory, making sure the financial endorsement of Korea implied by the meeting was well-photographed (Burton, 1998).

The findings on the political consequences of foreign inflows coming under the control of local private business firms were intriguing but difficult to generalize. In some authoritarian countries, from Chile and Argentina in the 1970s to Indonesia in the 1990s, the private business community was so dependent upon the political authorities that even an ability to attract foreign capital inflows seemed not to give it much of an independent voice. Nor was it clear that these borrowers favored even limited political liberalization. In fact, strengthening business families close to the regime has often propped up authoritarian rule indirectly – at least unless and until a financial crisis shook the system (see Winters, this volume).

In other developing countries, private business has been a vocal and somewhat independent political actor. Where private capitalists have been able to attract foreign capital without the assistance or intermediation of their government, they have often asserted themselves in domestic policy debates. In both authoritarian and democratic Brazil politicians needed business support at least as much as the reverse (see Kingstone, this volume). Private business borrowers in newly-democratizing countries such as Thailand and South Korea, or newly market-oriented democratic countries like India, were also flying high before the late 1997 crises, partly because of their importance to the balance of payments.

Danny Unger's chapter suggests that increased influence and independence for the domestic business community was a welcome source of pluralism, given Thailand's long tradition of a centralized, closed, state bureaucracy. With the late 1997 crisis, both government and business leaders lost credibility with the Thai public, although the medium-run consequences of this remain unclear. Similarly, Korea's large integrated financial–industrial conglomerates, the *chaebol*, in the mid-1990s had used their access to foreign funds as yet another advantage *vis-à-vis* small firms. The *chaebol* have been humbled by the late 1997 financial crisis, quite plausibly strengthening President-elect Kim Dae Jung's hand in enacting needed regulatory reforms.

India's business community in the 1990s both aided the country's balance of payments by being able to tap global capital markets and increased its public voice in the policy arena, although the precise connection between these two trends is unclear. John Echeverri-Gent argues that the greater transparency demanded by foreign institutional investors as a quid pro quo for bringing their monies into the country has had the salutory effect of curbing corruption in local business practices. This, he concludes, strengthens democracy, because it reduces the incentives for local business leaders to attempt to suborn politicians to cover up corruption. That is, while Indian big business has been strengthened in some ways, it also has been held to account and disciplined in other respects. We can probably conclude that direct loans to and/or investments with the local private sector do increase big business' control over politically-relevant resources. How much, and with what political consequences, cannot be answered outside of the context of individual countries.

4. There can be little doubt that balance-of-payments crises are bad for political incumbents, both in terms of the credibility of their economic policies (see Gruben) and the length of their political tenure, a point stressed by Elizondo and Kingstone in particular. On the other hand, and provocatively, democratizing polities that are relatively pluralist and open to policy debate may be more able to cope with financial crises flexibly and effectively than authoritarian regimes (see Winters).[21] Thus, in late 1997 both South Korea and Thailand changed both economic policies and chief executives while continuing their democratic opening. By January, 1998 Indonesia had not made either shift. Both China and Vietnam have been protected from the Asian financial crisis thus far by a combination of reliance on FDI rather than portfolio flows, plus continued capital controls (see Haughton). It is hard to imagine the non-democratic, secretive regimes in either country responding successfully to a financial crisis should one hit.

5, 6. Chapter 1 also expressed concerns over the medium-term political consequences of the worsening of income distribution that often – or always? –

accompanied post-balance-of-payments crisis structural adjustment programs. Even more ominously, the same effects on income distribution (and the subsequent distribution of political influence), I argued, might be expected from preemptive neoliberal economic reforms of the sort that emerging market country governments often have had to enact in order to head off a financial crisis that threatened. This hypothesis is hard to evaluate because it requires the construction of counter-factual scenarios, but a few concluding words may be relevant.

The post-1982 debt crisis period of structural adjustment in Latin America is the best source of data, since the waves of financial crisis associated with the portfolio flows of the 1990s occurred too recently to evaluate them. Three trends were apparent.

- First, poverty and inequality worsened dramatically throughout Latin America during the debt crisis decade. Moreover, neither poverty nor inequality was reduced in the early 1990s, even when most countries of the region began to grow again.[22]
- Second, procedural political democracy took hold and deepened throughout the region.[23] A contributing factor was the discrediting of military regimes throughout the region that had legitimized political repression in the 1970s by rapid economic growth.
- Third, the room for public policy maneuver by Latin American governments in the 1990s clearly had shrunk by comparison with previous decades, particularly the 1950s through the 1970s. The neoliberal policy preferences of the late twentieth century's global portfolio investors led them to shun countries that adopted leftist policy agendas that, for example, redistributed land or other assets, made the tax system more progressive, increased social spending, and so on (see Haley and Porter, this volume).

From the viewpoint of the distribution of political power within Latin American emerging market countries the news was thus both good and bad. On the one hand, political pluralism and the openness and competitiveness of politics increased as a consequence of the external debt crisis of the 1980s. On the other hand, those groups whose politically-relevant resources already were scarce had their *economic* power diminished even further just as the rules of the successor democratic games were being negotiated. Meanwhile, the debt crisis also had negative consequences for the international *distribution of political power* between the governments of developing countries and foreigners, both private investors and their home governments (see Porter).[24]

The optimistic comeback to these observations might make some of the following points. Latin America is not the world; there is thus no

reason to believe that its experience of structural adjustment predicts anything about East Asia, Eastern Europe or anywhere else.[25] After all, income distribution was infinitely more unequal in Latin America in 1980 than in East Asia in 1995; perhaps initial inequality is the main determinant of structural adjustment that makes the already poor relatively poorer. Moreover, international trade theory predicts that the locally abundant factors of production – typically including unskilled labor in emerging market countries – will see their relative economic returns rise as a consequence of greater integration with the global economy, because these factors will be relatively scarcer on the world stage (Stolper and Samuelson, 1941; Frieden and Rogowski, 1996).[26] The recessions and cuts in government spending associated with structural adjustment may be particularly burdensome for the poor, yet inflation stabilization, also demanded by global private portfolio investors, disproportionately benefits lower income groups since the poor and unsophisticated typically lack access to the diversified asset portfolios that upper income groups use to protect themselves from price volatility (see Stone in this volume, and Armijo, 1998). Finally, and most persuasively, neoliberal reforms, although they cause transitional pain, plausibly improve the functioning of the economy in the medium and long run. In particular, they eliminate most opportunities for politically-protected, but economically-wasteful, rent-seeking by petty government bureaucrats.[27]

7. The most important conclusion of Chapter 1, finally, was that little could be said about the likely consequences of the changing forms of foreign capital flows for democratic development in emerging market countries in the absence of knowledge about the current political system. In general, net inflows of all types boosted incumbents, while sudden net outflows destabilized them. Portfolio flows – including stocks, bonds, and short-term debt – have in the mid-1990s, unfortunately, more than lived up to their reputation for volatility.

There thus are some reasons to believe that current trends in global financial markets are not entirely favorable for the oft-heralded turn to democracy by developing countries in the late twentieth century. Still, given the conditions of global economic competition today, most developing countries would be worse off in the absence of foreign capital inflows, whatever their form. So long as they do not exit immediately, most capital inflows do promote economic growth in the recipient country, particularly when the funds are invested with an eye to market rather than political criteria. In the long-run (if not necessarily during the interim) capitalist economic growth does seem to be associated with liberal democracy. Liberal democracy ('procedural political democracy'), in turn, provides at least limited protections to the economically

disenfranchised, and is a political system superior to any variety of authoritarianism (military–technocratic, fascist, Communist, theocratic, or whatever) for all but the dictator and his or her group. This conclusion's implicit policy recommendation, therefore, is not the naive advice that emerging market countries somehow ought to resist the blandishments of foreign portfolio investors. Rather, the lesson may be that developing countries (both governments and citizens) consider opening their markets up to global financial flows at least somewhat cautiously and with an educated awareness of the risks involved.[28]

Notes

1. The countries assigned to particular cells had larger than modal capital inflows of the type indicated; however, the type of capital flow indicated, as for example 'bank loans to private firms,' was not necessarily the single most important source of foreign capital inflows for that country in that period.
2. Some observers argue that the World Bank, for example, was a significant influence moving economic policy in the Philippines in a generally neoliberal direction. See Broad (1988). In my view, the portfolio investment received by the country in the 1990s has been infinitely more effective in producing macroeconomic policy changes in an orthodox direction.
3. On US policies toward sub-Saharan Africa, see Clough (1992).
4. A plurality of bilateral donors also came in handy for India and some other aid recipients. When western foreign aid donors attempted to impose economic and political conditions that Indian Prime Minister Indira Gandhi found onerous (for example, US pressure to devalue in 1966, US opposition to Indian involvement in the war over Bangladesh in 1971), then the Indian goverment sought alternative sources of foreign assistance from the Soviet Union.
5. In general, the notion that MNC investors help promote 'sound' economic policy should not be taken too far. MNCs also can tolerate large deviations from impersonal, market-oriented economic policies when their own profits are large. For example, many MNCs have been happy to engage in high-cost, tariff-protected production for local markets.
6. Foreign funds permitted, for example, economically questionable but politically useful policies such as the purchase of new weapons for the military in Argentina, expansion of export and farm subsidies in Brazil, and extension of generous benefits to members of public sector unions in Mexico, Argentina, and Brazil.
7. In Brazil, for example, accelerating levels of inflation and public-sector debt seemed an acceptable tradeoff to governing elites as long as rapid economic growth continued and foreign capital inflows kept domestic interest rates from rising significantly (see Fishlow, 1989).
8. The payments crisis' proximate causes were the rupee's overvaluation and the sudden strain caused by the several effects of the Persian Gulf War, from higher oil import prices to the loss of substantial workers' remittances from Indians employed in Kuwait. When the financial scare hit, the main capital outflows were private portfolio investments in so-called NRI (non-resident Indian) deposit accounts; nonetheless, the fact that India's total foreign debt had risen to close to $90 billion constituted an additional worry.

9. On the role of state control of financing in South Korea, see Kim (1996), and Woo (1991).
10. Jeffry Frieden (1991) suggests what the missing variable might be. He explains variations in local business' policy preferences between Brazil, the members of whose business community competed with one another for sector-specific subsidies from government, and Chile or Argentina where business accepted radically pared down government and neoliberal policies, by reference to Chile and Argentina's higher historical levels of class conflict which made private business more dependent upon the state's repressive apparatus. Thus the Brazilian business community, less dependent upon the state for internal security, felt free to demand both more economic benefits from government – and more rapid and substantial political liberalization.
11. By early 1994 foreign participants accounted for as much as 70 to 80 per cent of daily trading in Mexico's stock market (Fidler and Frasier, 1994). They also held around 40 per cent of outstanding federal government debt, according to Banco de México figures showing a breakdown of holders of all outstanding government debt supplied to the author by the International Institute of Finance in Washington, D.C. As of February 1994, 1.4 per cent of federal government debt was held by Mexican banks, 25.1 per cent by the Banco de México itself, 40.7 per cent by foreigners, and 32.8 per cent by the non-financial sector resident in Mexico. I note again that the form in which most international financial statistics are collected makes it difficult to distinguish between portfolio flows destined for the capital-importing country's public and private sectors. My choice to assume that most short-term debt flows were destined for the private sector, as reported in the summary statistics in this volume's introduction and first chapter, will have understated the Mexican government's borrowing abroad.
12. Many observers have argued that Mexico's December 1994 crisis was more of a liquidity than a solvency crisis. If private investors had not reacted so precipitously, neither the subsequent balance-of-payments nor fiscal crises need have reached anything like the magnitude that they did. On the economic issues, see Gruben and Molano in this volume; Sachs, Tornell, and Velasco (1995); Roett (1996); Passell (1995). On the politics of Mexican international financial policies in 1994, see Elizondo in this volume; Starr (1997).
13. The package included $20 billion in loans and guarantees from the US, a then unprecedented $17.8 billion from the International Monetary Fund (IMF), and a similarly noteworthy $10 billion from the Bank for International Settlements (BIS), the bankers' central bank.
14. In 1990, the real urban minimum wage in Mexico City was 45.5, where 1980 was 100. Real average wages in manufacturing were 77.9, with the same base year. ECLAC (1993), pp. 34–5.
15. My reading of Mexican politics is that Zedillo himself is sincere about democratizing reform, although progress undeniably has been two steps forward, and one and a half back. See Dillon (1996); Crawford (1997).
16. Even the Zapatista movement in Chiapas state, which predates the 1994 financial crisis, is largely a reaction against neoliberal economic reforms, in this case mainly the land-tenure changes that accompanied Mexico's accession to NAFTA.
17. In the case of Argentina, much of the 'foreign' capital was undoubtedly returning flight capital, that is, money that Argentine citizens, often illegally, had spirited out of the country from the late 1970s through the 1980s to place in safe havens abroad. From the viewpoint of the present analysis, however, this

interesting fact is irrelevant, since the behavior of the owners of the portfolio investments is equivalent.

18. On Brazil's experience, see Kingstone in this volume. On the tequila effect, see Roett (1996), and Molano (1997).
19. The President-elect prevailed upon the outgoing incumbent to pardon two former presidents, Chun Do Hwan and Roh Te Woo, facing life sentences for corruption and abuse of power. By this act, Kim Dae Jung looked magnanimous (President Chun had planned to execute the dissident, only desisting because of vocal and high-level international pressure) and won friends among the military and traditional economic elites. In early January 1998, Kim Dae Jung got at least initial agreement from normally militant trade union leaders for their acquiesance to some layoffs, in exchange for an extension of Korea's thin social safety net.
20. The Soros Foundation spent more than $123 million in Central Europe between 1989 and 1994, about five times the US government's National Endowment for Democracy (Miller, 1997).
21. *New York Times* columnist Thomas L. Friedman (1998) distinguished among countries with modern 'transparent' domestic financial regulation, that have been hurt least (Taiwan, Hong Kong, Singapore), countries with 'democratic, but corrupt, systems,' that 'were hurt second worst' but already have begun to adjust (Thailand, South Korea), and the 'corrupt, authoritarian regime that can't adapt' and 'is going to melt down' (Indonesia).
22. The Inter-American Development Bank (1997, pp. 17–18), which favors market-liberalization and generally tries to put a positive face on neoliberal structural adjustment, put it this way: 'After falling continually throughout the 1970s, poverty increased dramatically in Latin America during the 1980s … [D]uring the 1990s, the distribution of Latin American income did not improve, though the persistent deterioration that characterized the late 1980s was arrested … [P]oorer income groups typically benefit disproportionately from economic recovery, just as they are disproportionately hurt by bad times… But the relatively well-off groups of Latin American society appear to have benefited from the recovery of the 1990s more than the poorest classes'. For more critical views of structural adjustment , see Veltmeyer, Petras, and Vieux (1997), Oxhorn and Ducatenzeiler (1998), or Boron (1995). Baer and Maloney (1997), on the other hand, conclude that neoliberal reforms will not worsen Latin American income distribution in the long run.
23. The literature is vast. See Diamond, Linz, and Lipset (eds) (1989). On democratic consolidation in the 1990s, see Domínguez and Lowenthal (eds) (1996).
24. Interestingly, the perception among policy-makers and intellectuals in *advanced industrial countries* is also that financial globalization has limited public policy autonomy in their countries, shifting 'power' abroad (see Underhill (ed.), (1997); Schrecker (ed.), (1997); Strange (1986); Cerny (ed.) 1993). The relative gainers were not emerging market countries, of course, but rather private owners of capital. Dani Rodrik (1997) provides a resolutely moderate synthesis of the overall globalization debate, that nonetheless acknowledges the increased bargaining power of capital.
25. Sub-Saharan Africa's experience of structural adjustment in the 1980s was even more depressing than Latin America's, though the causes of this failure are wildly overdetermined (Poku and Pettiford (eds), 1998).
26. For a contrary argument that is empirically rather than theoretically based, see Cohen (1998). He noted that globalization in the 1990s in Mexico, Brazil, and Argentina, Latin America's three largest emerging markets, seems to have

worsened income differentials and decreased the returns to unskilled labor, as governments undermined collective bargaining traditions in order to attract foreign capital, while local capitalists shed workers and adopt the latest (capital-intensive) technology in order to compete globally.

27. On the theory of economic 'rents,' see Krueger (1974). For arguments in favor of market reforms to eliminate corruption and rent-seeking that were written about India, but apply more generally, see Jha (1980), and Bardhan (1984).
28. The crises in portfolio flows of the mid-1990s have led to renewed interest in those countries that have retained substantial capital controls, including Chile (see Fidler, 1998) and China.

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