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Technocracy questioned:

Ideology and interests in Nicaragua's economic policies

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ABSTRACT

At first sight, the Chamorro government in Nicaragua is a classic example of technocracy: both for the a-political background of the persons ruling the country, and for the dominant influence of IMF and World Bank on economic policies. The paper aims to show that this superficial stereotyping is not correct and that ideology and interests play a role. Recommended structural adjustment policies by IMF and World Bank *do* determine economic policy, but they cannot be considered technically optimal solutions to macroeconomic problems. Furthermore, the aid that is conditional upon these policies allows discretionary government behaviour. Finally, *de facto* government leader Lacayo rapidly became a politician.

INTRODUCTION

At first sight, the Chamorro government in Nicaragua is a classic example of a technocratic administration. Ms. Chamorro came to the presidency after the 1990 elections. Ms. Chamorro appointed her son-in-law, Antonio Lacayo, as minister of the Presidency. Until then, Lacayo had been a capable entrepreneur and manager. Like some of his fellow businessmen, he had continued making money in the country during the Sandinista government, although taking part of his capital abroad. Gradually, Lacayo became the most powerful person in the country. Lacayo thus seems to satisfy the definition of a technocrat (Sicat 1985): a highly educated person (in economics, management or engineering) who has no links with political parties and who has a powerful position within the government, or is a powerful economic advisor on a permanent basis. The other members of the cabinet also lack a political background. Most ministers are lawyers or engineers. For these reasons Stahler-Sholk (1995, 10) considers the Lacayo administration a 'technocratic government par excellence.'

A second reason why the Chamorro government is often called technocratic is the influence of the international financial institutions (IFIs), World Bank and IMF, on domestic economic policies. Since 1991 the country has signed two ESAFs (Extended Structural Adjustment Facilities) with the IMF. This means the country has been carrying out stabilization and structural adjustment measures as recommended by IMF and World Bank. For this reason, it is alleged that economic policies are impartial since they are based on the working of a 'free market.' In this sense, Nicaragua satisfies another definition for a technocratic government: policies seem to follow the 'technical mode' instead of the 'political mode.'[1]

The aim of this paper is to show that this superficial typing of the Chamorro government as technocratic is not correct. In fact, economic policies of the Chamorro government are based on ideologies, sometimes foreign-inspired, and on personal and political interests. A first part of the argument is that Lacayo is a politician acting as many Latin American politicians did before him: he uses his political power to expand his economic wealth and that of his constituency, in view of staying in power after next elections. The main thrust of this paper consists of questioning the assumed link between the influence of the IFIs with their structural adjustment programmes, and technical necessity and assumed impartiality of economic policies. The standard recipe of structural adjustment, emphasizing liberalizations and privatizations, does not lead to the ideal 'liberalized' society with equal opportunities for all. As is well known, the (free) market tends to favour the haves above the have-nots, as well as the present generation over future generations. Although important, these consequences are increasingly recognized and will not be dealt with in this paper. My aim is to show that recommended stabilization and structural adjustment policies may not be optimal, even from a (limited) macroeconomic viewpoint. Stabilization and structural adjustment policies may be inconsistent among themselves, and the benefits of liberalization and privatization measures are not always straightforward. These measures are often carried out without taking the institutional situation of the country into account. Furthermore, the aid that is conditional upon these policies may have perverse effects on the implementation of liberalization measures, allowing continued distortions and discretionary policies.

The structure of this paper is as follows. First the role of ideology and interests in Nicaraguan economic policies before 1990 are examined. Then the extent of foreign influence on these policies is investigated, both before 1990 and in the period of the Chamorro administration. I show that the present influence of the IFIs is considerable, in spite of their small relative share in Nicaragua's outstanding debt. In the next section, I examine the policies generally recommended by the IFIs, and the ideology behind these supposedly 'technocratic' advices. Finally, economic policies of the Chamorro government and their effects are analyzed. It is shown that these policies are not always successful, nor in bringing macroeconomic growth nor in bringing about a free market and impartiality.

IDEOLOGY AND INTERESTS BEFORE 1990

From 1936 through 1979 the Somoza family was almost uninterruptedly in power. Nicaragua was ruled by a dictatorship. Consecutively, Somoza and his two sons used their control of state power to enrich themselves. In 1979, the family proved to own economic assets that produced 25% of GDP. Apart from the Somoza family, there were two other 'business groups' in Nicaragua (Strachan 1976). In the early 1970s, they controlled about 20% of GDP. The Somozas carried out policies to promote economic growth, in particular the expansion of agricultural export production. This benefitted businessmen of all groups, but it increased income differences. More and more small peasants were expelled from the fertile land on the west coast, and had to go to less well arable land. They could not make a living there, and were economically forced to work in the harvests of coffee, cotton and sugar. Whole families lived and worked on the plantations in miserable conditions during part of the year.

After the December 1972 earthquake of Managua, a conflict began to appear among the entrepreneurial groups. Somoza controlled the aid money that flowed in, and he benefitted much more than other wealthy persons from the boom in construction activities after the earthquake. Many businessmen began to rally with the opposition against the dictatorship. The FSLN (Frente Sandinista para la Liberación Nacional, Sandinista Front for National Liberalization), which had begun in 1961 as a small guerrilla group in the mountains, now became stronger and stronger. In 1978, after Somoza had ordered the killing of Pedro Joaquín Chamorro, director of an opposition newspaper, almost the whole population joined the opposition. In July 1979 the FSLN took over the government.

In general, we can conclude that until 1979, economic policies were mainly influenced by 'interests' and not so much by 'ideology.' After 1979 this changed. The ideology of the FSLN, 'Sandinismo,' was based on Latin American stucturalist thought, and on idealistic ideas about socialism. The catchwords were anti-imperialism, fulfilling the basic needs of workers and peasants, and non-capitalist forms of economic organization, with an emphasis on cooperatization (Dijkstra 1992, 72-73).

The Sandinistas installed a 'mixed economy.' This meant that the banks, foreign trade, and the possessions of Somoza and his closest associates were nationalized. The rest of the economy remained in private hands. But the state heavily intervened in the (private) economy, centrally allocating credits and foreign exchange, and establishing prices for many products. The government aimed at improving social services, and set up large investment projects. At the same time, real wages were to be protected and profit margins of private producers maintained. In combination with the costs of fighting a civil war against U.S. supported *contras*, these policies produced severe macroeconomic imbalances (table 1).

Inflation climbed to very high levels, especially after 1984, and the deficits on trade balance and current account increased. While in the 1970s imports and exports more or less equalled at about 700 million dollar, in the 1980s imports first doubled and later tripled exports. This implied that Nicaragua was increasingly dependent on foreign loans and grants in order to finance its imports (table 2).

Table 1. Some macroeconomic indicators of Nicaragua, 1980-1990

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Growth GDP (%)	4.6	5.4	-0.8	4.6	-1.6	-4.1	-1.0	-0.7	-11.0	-2.9	-1.5
Growth GDP p.c. (%)	1.5	2.0	-4.0	1.2	-4.8	-7.3	-4.3	-4.0	-14.0	-6.1	-4.1
Inflation (%)	25	23	22	33	50	334	747	1374	33000	1300	13490
External sector, in millions of dollars:											
Exports	495	553	447	471	431	344	287	325	273	341	392
Imports	909	1037	826	901	921	924	837	895	857	667	682
Trade balance	-414	-484	-379	-430	-490	-579	-549	-570	-583	-326	-290
Current account	-491	-563	-557	-635	-727	-839	-803	-814	-846	-531	-507
External public debt (in billions of dollars)	1.6	2.6	3.1	3.8	4.4	4.9	5.8	6.3	7.2	9.7	10.6

Sources: ECLAC/CEPAL 1986, 1988, 1989, 1993.

Towards the end of the Sandinista period, interests became more important as determinants of economic policies. While corruption, nepotism and patronage had been limited in the early 1980s, these phenomena became more frequent towards the end of the decade. Some Sandinista leaders began to act as capitalists, using party or state power to expand their investments and wealth. The 1990 election result came to almost everybody's surprise. The many party cadres and faithful government functionaries who until then had worked for a decent salary, now realized that they would soon lose their jobs and stay behind without any source of income. In the few months between the elections and the change in power, many state possessions, notably cars, were illegally given to FSLN followers. While the FSLN had still gained almost 50% of the votes in the election, after this '*la piñata*'[2] their popularity decreased.

FOREIGN INFLUENCE ON ECONOMIC POLICIES

In the period of the Somoza dictatorship, foreign influence on the political and economic situation in Nicaragua was limited. Although the external debt increased towards the end of the 1970s, the interest rate was still low and debt was not perceived as a problem. Politically, it was the era of the cold war. Nicaragua was in the camp of the 'west.' In the international forums Somoza always closely imitated the U.S. position. He was 'rewarded,' so to speak, by non-intervention of the U.S. in domestic affairs, in spite of his bad record in human rights issues. The fact that from 1976 onwards Carter took over the U.S. presidency certainly helped the change in power in Nicaragua. Carter's emphasis on 'human rights' led him to limit the political and military support for Somoza.

In the period of the Sandinista mixed economy, foreign influence became much more important. On the one hand, the U.S. government stopped aid in 1981 and began financing the opposition against the Sandinistas, the *contras*. On the other, foreign aid from many different sources prevented the collapse of the economy.

As of 1981, loans from multilateral organizations (World Bank and Interamerican Development Bank) stopped because they were effectively vetoed by the U.S. government. But many Western European countries and Latin American countries continued to give aid on a bilateral basis. In the course of the decade, aid from these countries diminished. As for the Latin American countries, the main reason was that they had debt problems themselves and could not afford to continue lending to Nicaragua without ever seeing the debt repayed. Western European countries, which had financed many large big investment projects in the early 1980s, became worried about the damages done to these projects by the civil war, and about economic policies and the bad economic situation in general. Aid from these western sources was more or less replaced by aid from the former socialist countries. The Soviet Union became Nicaragua's main oil supplier after Mexico (and earlier Venezuela) stopped supplying oil on credit.

A large part of grants and loans in the 1980s was tied to projects and to specific supplies. In the case of the former socialist countries, tying of aid often implied that not very useful goods of dubious quality had to be purchased. This was one of the reasons that the economic crisis became more severe towards the end of the decade.

External relations not only influenced the economic situation, but also Nicaragua's economic system and economic policies. The combination of state intervention in prices and (mainly) private ownership, offered many opportunities for obtaining financial gains from the differences between official and black market prices and the scarcities. In other mixed economies, contradictions of this kind caused an early end of the system. Or there would be a return to a market economy - as in Chile in 1973 -, or these contradictions led to more nationalizations and to the introduction of a centrally planned economy - as in the Soviet Union in 1929 - (Dijkstra 1992). It is remarkable that the FSLN did not do the latter in Nicaragua. The main reason was that maintaining a mixed system guaranteed the support from many Latin American and European countries.

Table 2. Foreign aid to Nicaragua in relation to exports and imports

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Credits (in millions of dollars)	529	729	499	438	628	925	201	229			288	605	412	199	364
Grants (in millions of dollars)	148	74	99	181	144	272	317	156			202	844	379	291	204
Total (in millions of dollars)	677	803	598	619	773	1197	518	385			490	1449[1]	790	490	568
Aid as % of exports:	137	145	134	131	179	348	180	118			125	537	359	183	162
Aid as % of imports:	74	77	72	69	84	130	62	43			72	210	107	74	81

[1]Includes an amount of 376 million dollars for debt repayment and of 259 million dollars for debt foregiveness. In the other years these categories are empty, except for debt foregiveness in 1992 and 1993 of 53 million dollars.

Sources: For aid figures: Vos (1996), and for exports and imports: tables 1 and 4. This means for 1990-1994 exports and imports do not include services.

Although financial support from these countries decreased during the 1980s, their political support was still important. Nicaraguan leaders perceived that maintaining a mixed economy could at least prevent a direct U.S. invasion in the country. However, the contradictions of the mixed economy and the economic crisis which resulted from it, can be considered important causes for the 1990 election defeat of the Sandinistas.

After the change in power the kind of aid changed, as well as its origins and conditions. Aid from the former socialist countries stopped, and aid from West European countries increased again. In addition, the U.S. and multilateral organizations restored aid. The US AID started to give loans to Nicaragua in June 1990, under the condition that the country set up a stabilization plan. Further conditions were added in subsequent loans in 1990 and 1991 (Evans 1995, 178-1979). In September 1991, the IMF, the World Bank and the Inter-American Development Bank began to lend again, after arreared debts with these institutions had been cleared. The loans from these institutions were conditional upon the strict stabilization and structural adjustment measures.

Table 2 shows that total aid exceeded the country's exports in each year since 1980. In most years, aid financed more than half of imports. After 1990, exports hardly recovered while imports increased. On average, aid dependency, defined as the relation of aid to exports, or aid to imports, was even higher under the Chamorro government than under the Sandinistas.

To assess the donor's possible leverage on economic policies it is also important to look at the sources of total debt outstanding. Table 3 shows that debts from commercial banks were not very important for Nicaragua in 1993. In 1995 this debt was further reduced by a "government buy-back" at eight cents to a dollar. Most debt was with bilateral donors, of which the former socialist countries were still the largest group. Loans from these countries were on soft conditions, and by far the largest part will be written-off (Latin America Monitor 1995).[3] The debt with former East Germany is now included in the Paris club debt.

The debts with multilateral organizations are relatively small compared to the situation in other highly indebted countries, due to their lack of involvement in most of the 1980s. However, these institutions, and in particular the IMF, play a dominating role in setting the conditions for debt restructuring, debt forgiveness, and for giving new loans (Evans 1995). IMF staff was heavily involved in the design of the 1991 stabilization plan, and, together with World Bank staff, continues to be involved in the design of structural adjustment policies. The first condition of the other international financial institutions, World Bank and IDB is always 'compliance with the conditions set by the IMF'. The IMF has also been assigned the task of monitoring the compliance with the agreements. The recommended structural adjustment policies are discussed in bi-annual meetings of the 'Consultative group of lending agencies and donor countries', in which all important bilateral donors and multilateral organizations participate. But the other donors generally follow the proposals of the IMF and World Bank. This means that a large part of aid is no longer tied to projects or to goods, but to policies.

Table 3. Composition of Nicaragua's foreign debt, by source, 1993 (in %)

Paris club	15	
Former socialist countries	33	
Other bilateral	22	
Total bilateral		70
Multilateral organisations	12	
Commercial banks	16	
Suppliers	1	
Total	100	

Source: Vos (1996), figure 6.3

THE 'IMPARTIALITY' OF STRUCTURAL ADJUSTMENT POLICIES

Many authors have pointed to weaknesses of stabilization and structural adjustment policies, and to negativ and unintended consequences of the aid that is conditional upon these policies. A first problem is th combination of internal stabilization, directed at price stabilization, and external stabilization and structura adjustment which are directed at improving the trade balance. Internal stabilization usually involves expenditur reducing policies, such as cutting the budget deficit and limiting monetary expansion. Sometimes it also involve expenditure switching policies: a devaluation of the exchange rate. However, if a country has suffered fron inflation for a long time, prices tend to be indexed to foreign prices. A devaluation then fuels the increase ir domestic prices, and a fixed exchange rate is often used as a 'nominal anchor' which helps to fight inflation. But if some inflation continues, the exchange rate becomes overvalued which hampers exports and stimulate imports. In this situation, there is a trade-off between achieving internal (price stability) and external (balance of payments equilibrium) stabilization.

Apart from a devaluation, structural adjustment typically includes 'supply side' measures, such as deregulation of domestic prices, liberalization of foreign trade, liberalization of financial markets and reducing the role of the government by privatization. These measures aim to increase domestic supply, in order tc improve the balance of payments in the medium and long run. These standard recipes of the IFIs for structural adjustment are based on the assumption that reduing governmnet intervention in the economy always enhances production, exports and so economic growth.

These recommendations are based on 'neoliberal' *ideology*. Although it is often true that markets work better than governments, it is not always true. In particular, if markets are characterized by many distortions at the same time, it is not at all clear whether liberalization and deregulation are 'first-best' solutions, leading to Pareto optimality (Van Dijck 1995). Furthermore, there does not exist a 'theory' of structural adjustment, in the sense of prescribing the order of liberalization of different markets (McKinnon 1993).

Empirical studies conducted so far often lead to questioning the benefits of liberalizations and privatizations. Mosley (1993) evaluated structural adjustment programs in many countries, and concluded that privatization and foreign trade liberalization, were not very relevant for such positive macroeconomic results as have been achieved in these programs. After carefully examining the arguments in favour of trade liberalization, Rodrik (1992) concluded that there is no proof that trade liberalization increases efficiency or productivity growth. Privatizations of state owned enterprises are often carried out under the pressure of paying internal or external public debts. If so, prices for these SOE's are often set too low which leads to a net loss in discounted government revenues (Rodrik 1990). Other authors showed that the experience of South-East Asian countries is often wrongly interpreted as being cases of liberalization, while in fact, a lot of import substitution and selective government promotion were applied (Westphal 1990, Amsden 1994, Lall 1994). Further, premature liberalization of financial markets has led to financial crises in many countries, for example in the Southern cone countries in the early 1980s (Corbo *et al.* 1986, Paus 1994), and in Mexico at the end of 1994. Empirical studies seem to indicate that it is better not to implement financial liberalization, both domestic and the liberalization of the capital account, until all other reforms are well in place (McKinnon 1993).

A related group of criticisms of structural adjustment programs focusses on the lack of attention for institutions, market failures and for the working of the government bureaucracy. As Geddes (1995) concludes in a review article, the quality of the state bureaucracy is very important, also and perhaps even more when state intervention is reduced. Liberalization and privatization may lead to increased concentration and market failures if there is no appropriate regulatory framework, and if there are no business laws that can be enforced nor appropriate business customs (Due 1993, Stein 1994, Zattler 1993). Lack of, or uncertainty about these institutions may seriously affect private investment and so reduce the effects of structural adjustment measures (Borner *et al.* 1994). More in general, uncertainty about the sustainability of reforms hampers their success and so their sustainability (Rodrik 1990).

The fact that aid money is conditioned upon structural adjustment programs may have various other negative and unintended consequences (De Vylder 1994a). The aid money can be used to finance the government deficit and the trade deficit. This may reduce the incentives for reducing these deficits. The government may increase expenditure or reduce taxes, which opens up the possibility for granting exemptions to individual cases, in contradiction with the agreed adjustment program. Credits can be given at lower costs, wages for certain government officials can be raised, etc. etc. So the very fact of having an agreement on structural adjustment provides the opportunity not to implement it, due to increased foreign aid inflows. The government may also feel less stimulated to carry out policies for promoting exports and reducing imports. If this happens, the dependence on aid continues. Two dangerous relationships appear from this: The more aid a country receives, the more it will remain dependent on aid *and* the more it is possible to deviate from the strict liberalization rules, applying discretionary policies. A country that agrees to the structural adjustment conditions is likely to become a 'donor's darling.' This in turn, allows it not to carry out the structural adjustment program as agreed.

Summing up, the standard recipes for stabilization and structural adjustment suffer from some weaknesses. Stabilization policies may conflict with measures to improve the trade balance. Policies for structural adjustment, such as liberalization and privatization, are presented as unavoidable, technical solutions but there is no theory underpinning this and at least part of the evidence points to a less extensive and more careful implementation. Secondly, the recommended policies often lack attention for institutions in a broad sense. And thirdly, the fact that a lot of aid money is conditional upon the agreements on structural adjustment policies, threathens to reduce the incentive for implementation of these policies and to open up the possibility for discretionary government intervention. This means that:

- Foreign intervention (of the IFIs) in economic policies cannot be considered objective and impartial technical advice, but contains elements of ideology;
- Foreign aid coming in as a result of structural adjustment programs permits deviations from the agreed policies, in particular, discretionary action in favour of politically powerful groups.

STRUCTURAL ADJUSTMENT IN NICARAGUA

After some failed attempts at stabilization in 1990, the Chamorro government carried out a successful stabilization program in March 1991. The reduction of runaway inflation was mainly due to (Acevedo Volg 1993, De Vylder 1994b, Dijkstra 1996):

- in the short run: an agreement with the labour unions to fix nominal wages during several months after March 1991;
- a very tight monetary policy: in keeping with IMF monetary programming, domestic money supply can only increase commensurate with the increase in foreign exchange;
- a reduction in the government deficit, mainly by reducing state employment, by abolishing free education and increasing the fees for health services, and by increases in excise taxes and the value added tax.
- the availability of external finance for financing the remaining deficit of about 8% of GDP.

The new government also immediately began the transition to a market economy. It started the privatization of state enterprises. By April 1995, 345 of the 351 state enterprises had been privatized (Nicanieuws 1995). Intervention in domestic prices was reduced, although the government maintained fixed prices for some basic goods and services, like transport. The foreign trade sector was liberalized. The state monopoly on exports of the traditional crops came to an end. Imports were also liberalized, and import tariffs were rapidly reduced. In 1993, a common external tariff within the renewed Central American Common Market came into effect, of 20%. Private banks were allowed to function along with state banks. In sum, almost all state intervention related to the former mixed economy has been abolished. The market was to determine the allocation and distribution of economic assets again.

The Nicaraguan government was a perfect adherent to the IMF's and World Bank's ideas on stabilization and liberalization of the economy. Nicaragua received a lot of aid again in the early 1990s. As table 4 shows, the large amount of aid continues to be necessary, given the large deficit on the balance of trade and the need to finance the external debt. Apparently, it took a long time until stabilization and structural adjustment provoked some increase in production and exports. Private investment only increased from 4% of GDP in the 1980s to 9% in the 1991-1993, while state investment decreased from 20% to 8% between the same periods (Dijkstra 1996). Negative GDP growth rates continued until 1994, when there was a slight increase. Exports and total gross investment also increased in 1994 (IDB 1995).

Table 4. Some macroeconomic indicators of Nicaragua, 1990-1994

	1990	1991	1992	1993	1994	1995[1]
Growth real GDP (%)	-1.5	-0.2	-0.5	-0.7	3.2	5.0
Growth real GDP p.c. (%)	-4.1	-3.7	-4.5	-4.4		
Inflation	13490	866	10	26	13	13
External indicators (in millions of US$):						
Exports of goods (fob)	332	268	223	267	350	450
Imports of goods (fob)	570	688	771	660	790	850
Trade balance (goods)	-238	-420	-548	-393	-440	-400
Current account	-620	-10	-716	-644	-739	-560
External debt (in billions of US$)[2]	10.6	10.3	9.9	10.5	11.7	

[1]Estimates.
[2]For 1990 and 1991: external public debt.
Sources: For 1990 and 1991: CEPAL (1993), later years: Latin America Monitor: Central America, several issues.

One of the reasons why export production did not respond during 1991-1993 was the overvaluation of the cordoba. The government gave more priority to fighting inflation, for which it was thought better not to devalue the currency too often. In combination with the liberalization of imports, this hampered exports and stimulated imports. In 1994, the real effective exchange rate depreciated by 7% (IDB 1995) which probably helped to bring about the increase in exports.

The import liberalization caused a change in the composition of imports: the share of consumer goods increased from 17% on average between 1986 and 1989, to 31% on average in 1990-1993 (Central Bank of Nicaragua 1993). The share of durable consumer goods increased from 3 to 5%. The government established an incentive to return to Nicaragua for the businessmen who had left for Miami during Sandinista rule: they could import a luxury car free of tax. Many of them returned several times from Miami and so could resell several cars on the domestic market. These increased imports of luxury goods, and of consumer goods in general, did not benefit production.

The liberalization also led to a change in the industrial structure. The share of production (agriculture and industry) decreased, and the share of trade and services increased. Part of U.S. aid came in the form of food imports, mainly rice, which was sold cheaply on the domestic market. This affected peasant corn producers and tortilla makers in the cities. Imports of cheap second-hand clothing from the U.S., and of cheap footwear from East Asian countries, made many small producers in clothing and shoe production go bankrupt.

The liberalization of imports caused a revival of a few large private import houses owned by rich business families. They have the capital and the international contacts to set up this trading. In fact, the state monopoly on imports was replaced by a private cartel. This prevented many prices from coming down. Something similar happened to the former state supermarkets. Their privatization brought about concentrated ownership. Profit margins of the supermarkets are very high.[4]

In order to set up a private bank, an amount of 2 million dollars is needed as starting capital. Between 1992 and early 1995, 11 private banks started business. They are all small and often linked to some private companies. Until June 1993, private banks captured almost half of deposits (45%), but extended only 22% of loans (Dijkstra 1996). In addition, they only lend to low-risk activities, such as trading. The state banks still finance the lion's share of production activities. Interest rates can be freely set and are high. Except for some NGO financed credit programs with relatively limited outreach, small producers are rationed out of the credit market. The large import trading houses and supermarkets get most domestic credits. This partly explains the disappointed amount of private investment. Many private producers complained about the lack of financing for investment.[5]

The privatization of the former state enterprises was carried out by CORNAP (Corporación Nicaraguênse de Administración Pública, Nicaraguan Corporation for Public Administration). According to a law, 25% of the ownership of state enterprises should go to the workers, 25% to former soldiers, 25% to former *contras*, and 25% to former owners. If returning ownership to former owners would not be possible, they would be given indemnization bonds. By April 1995, the privatization process was almost completed. According to a study by CORNAP itself, state revenue from privatizations amounts to less than 20% of the value of the state enterprises, while about 10% of that value was spent on costs (IHCA 1995). So the state earned very little in the process, in spite of the fact that the privatized state enterprises produced about 30% of GDP. The state even ended up with a loss by having to pay out on the indemnization bonds (Stahler-Sholk 1995). One of the conditions for the 1994 ESAF was the privatization of the - highly profitable - state telecommunication company (TELCOR). The government proposals for the privatization met with serious political and union resistance, but were approved in Parliament in November 1995. The main reason why the World Bank and IMF have pushed so hard for the privatization of TELCOR seems to be that the proceeds can be used to finance the bond compensation scheme (Latin America Monitor 1995).

Another factor explaining the limited response of private investment is the weak institutional framework for business in Nicaragua. The political situation is still very unstable. In the countryside some fighting continues, initiated by former soldiers and contras who did not receive their promised land and jobs. In the political arena, polarization is still the rule. For example, the whole first semester of 1995 two different Constitutions existed because of a conflict between the Parliament and the Executive. Since the differences involved the relative powers of the two, effective governance of the country stopped.

In spite of the privatization of almost all former state owned enterprises, the property situation is still not well defined. Many persons who benefited from the confiscations in the Sandinista period still don't have legal ownership titles, while their properties are often also claimed by the former owners. By November 1995, more than 2000 claims on property had been resolved, which cost the government $260 million in compensation bonds. But another 3000 claims remain (Latin America Monitor, 1995). The 'ownership rights' in a broad sense are also weakly defined. The government continues the 'ad hoc' way of setting rules of the Sandinista government. Rules and procedures are changed without consultation of the directly involved persons, incentives are announced without making them widely known. This creates a lot of uncertainty among private producers. According to Borner *et al.* (1994), this is the main factor behind disappointing private investment levels.

So far, I have shown that trade liberalization in combination with the overvalued exchange rate did not lead to an increase in exports. It did bring about more imports of consumer goods. The concentrated ownership in commerce prevented prices from coming down. Financial liberalization led to the coming into existence of too many private banks in the small Nicaraguan market. High costs lead to high lending rates, and the efficiency of allocation has not improved. The privatization of 345 state enterprises did not bring in government revenues, and it remains to be seen whether the enterprises will produce more efficiently. Private investment is hampered by high interest rates and by the uncertain political situation and the frequently changing economic policies.

Now, the question is what the impact has been of foreign aid. Foreign aid is still used for financing the budget deficit and for financing the current account deficit. The availability of external finance clearly allowed the government to give priority to the internal stabilization objective, maintaining the exchange rate overvalued. But apart from this, it is difficult to establish negative incentive effects. A little bit more can be said on the impact of aid on discretionary behaviour of the government.

Cantarero and Gaber (1994) argue that Nicaragua was ruled by the technical mode for about a year only, from March 1991 until March 1992. This was the period in which the hyperinflation came down to managable levels. In 1992, specific groups of private producers asked and obtained exceptions to the stabilization and liberalization policies. Agricultural exporters, for example, successfully requested a restructuring of their debts and renewed cheap credits in 1992. In the same year wage increases over and above the structural adjustment agreement were granted to government workers. These deviations show that Nicaragua was again ruled according to the political mode (Canterero and Gaber 1994). It can be argued that the availability of foreign aid made these exemptions possible.

In general, there does not seem to be strong private sector support for the all-out liberalization measures. The dominant organization of private producers, COSEP, had always complained about state intervention during the Sandinista government. By 1992, many executives began to ask for more credits at lower rates and for technical assistance provided and organized by the government (Spalding 1994). While theory predicts that one of the advantages of liberalization is that there comes an end to rent-seeking, in practice rent-seeking behaviour often continues (Rodrik 1990). This clearly also occurred in Nicaragua.

In 1993, the government successfully negotiated higher tariffs for certain products, in the context of the Central American Common Market. This freed the way for discretionary policies. An example can be found in an industrial consumer goods branch.[6] There are four producers in this branch. Ownership of three of them is in the hands of persons closely related to the government. In 1993, the director of the fourth received a letter from one of the others saying that he had to increase the price of his main product. He was almost forced to do so, because otherwise his colleagues would have stopped supplying him an essential input for his product. This cartel was due to two factors: the input was cheaply imported on the basis of foreign aid, and the output price could be increased because of increased external tariffs as a temporary exception granted to Nicaragua in the CACM.

Very little is known about the conditions under which state enterprises have been given away or sold. This gave way to speculations about a *quinceañera* after the *piñata*: The *quinceañera* is the benefitting of both current government officials and relatives, and Sandinistas from the state possessions.[7] There is some evidence in this respect. I have been told that several Sandinista labour union leaders obtained a former state enterprise. This could occur according to the 25% share which was officially destined for 'workers.' Another example is the following. Raúl Lacayo, brother of the minister of the Presidency, was briefly director of the Central Bank in 1991. In that period, he surprised friends and foes by extending a very cheap loan to the state sugar refineries, which were in bad condition. Shortly after, when Lacayo had resigned as Bank President, these enterprises were privatized. Raúl Lacayo obtained these enterprises at a very low price.[8]

Although the evidence is somewhat anecdotical, it seems to be confirmed that the generous foreign aid allowed the government to make some deviations on the agreed structural adjustment program. In turn, these deviations from the agreed program are likely to have increased the institutional uncertainty, so that more potential investors persevered in their 'wait and see' attitude.

CONCLUSION

Before 1990, ideology and interests dominated Nicaraguan economic policies. In the period of the Somoza dictatorship (1936-1979), Nicaragua was ruled by an entrepreneurial family who used state power to promote their economic interests within a capitalist framework. During the Sandinista government (1979-1990), ideology became more important. Economic policies had idealistic aims, such as improving the welfare of poor workers and peasants. Towards the end of that period, however, economic policies came to respond also to personal interests of the Sandinistas. This occurred, in particular, in the few months between their election defeat and the change in power. In the Sandinista period foreign influence on economic policies increased. This was due to the economic crisis, which caused a huge dependence on foreign financing for imports.

According to many observers, Nicaragua under Chamorro is an example of a country ruled by technocrats. A first reason is the composition of the cabinet and, in particular, the person of Antonio Lacayo. Lacayo, a well educated former businessman with no history of political involvement, is minister of the presidency and, in fact, the most powerful person of the country.[9] A second reason is the foreign influence, in particular of the international financial institutions (IFIs), on economic policies. This foreign influence is supposed to lead to objective, impartial, and technically optimal solutions to the economic problems of the country.

In this paper I showed that Nicaragua is not ruled by technocrats. Although it is true that the IFIs dominate economic policies, this does not mean that policies are impartial and technically optimal. Secondly, although Lacayo was no politician before he came to power, he is one now and he is acting as a typical Latin American ruler: trying to serve his interests and those of his potential supporters in next elections.

Many authors have pointed to the potential negative impacts of implementing structural adjustment policies as recommended by the IFIs. In this paper, I grouped the criticisms in 1) recommended policies often suffer from an inconsistency between stabilization and structrual adjustment, and structural adjustment policies often lack theoretical justifications, 2) recommended policies don't take institutions sufficiently into account, and 3) the aid that goes with the approved structural adjustment programs has negative effects: it reduces incentives for closing the external and internal gaps, and it opens the possibility for discretionary government action. If these criticisms are true, it implies that the dominance of IFIs on economic policies does not mean that these policies are technical; instead, they contain elements of ideology.

For Nicaragua, I showed that all three factors apply. The overvalued exchange rate as a result of the priority for internal stabilization proved to harm the trade balance. The carrying out of trade liberalization, financial liberalization, and privatization brought about negative consequences for growth and investment, for government revenues, and for private producers except those active in commerce and services. Among the recommended policies there is relatively little attention for the quality of the public sector and for creating a stable business environment. These results imply that, at least to some extent, structural adjustment policies in Nicaragua seem to be the consequence of ideology rather than impartial technical advice.

The negative trade balance is financed by foreign aid, and this aid may have the expected negative incentive effects. In addition, it has been shown that certain persons and groups have benefitted from discretionary government policies. Although some of the evidence presented is anecdotical, it can be concluded that interests have been important motivating forces behind economic policies.

NOTES

1.Cantarero and Gaber (1994), although these authors do not agree that Nicaragua satisfies this condition, see below.

2.La piñata is the name of a child birthday's party, in which a puppet (the piñata) is beaten until the sweets come out and our grabbed by all invited.

3.This debt forgiveness can also be interpreted as doing justice to the new exchange rate of the ruble against the dollar, since most of this debt was denominated in 'convertible rubles' and the ruble has depreciated sharply against the dollar. I owe this point to an anonymous referee.

4.They amount to 100%, according to economist living in Nicaragua, January 1994.

5.Interviews in January 1994 with executives of private manufacturing companies and with a representative of the Chamber of Industry.

6.Interview with Nicaraguan firm executive, January 1994.

7.Quinceañera is the special celebration of a girl's fifteen's birthday.

8.Interview with economist living in Nicaragua, June 1995.

9.In view of the presidential elections coming up in October 1996, Lacayo resigned in the Fall of 1995, as did the other potential candidates for those elections.

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