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Privatization Bolivian Style: A Cautionary Tale*

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On October 17, 2003, President Sanchez de Lozada resigned from office and boarded a plane for Miami in the face of protests that left over 70 civilians dead. The protests, popularly referred to as the 'gas wars', began when the government announced plans to allow private firms to install a pipeline to Chile to transport gas destined for US markets. The public rejection of the plan grew out of the increasing perception that natural resources, which many Bolivians believed held the key for economic development, were being transferred to international firms. Following constitutional procedure, Vice President Carlos Mesa assumed the presidency with a promise to reconsider fundamental neoliberal policies.

The gas wars were the third time in as many years that massive numbers of Bolivians had taken to the streets against neoliberal policies designed along the lines of the Washington Consensus (Williamson, 1993). In 2000, the 'water wars' erupted in Cochabamba, the country's fourth largest city, when a consortium headed by the US construction company Bechtel took control of the local water company and raised water rates, sometimes as much as 400% (Finnegan, 2002). Bechtel left the country after the government rescinded the contract. In February 2003, the military fired on striking police protesting a tax increase that had been proposed to meet International Monetary Fund deficit goals. By the time the dust settled on the confrontation the uprising had spread throughout the country leaving at least 23 dead and hundreds wounded (*La Razón*, 2003).

Not only did each cycle of protest form increasingly broad coalitions, but each cycle of protest was based on an increasingly clear critique of privatization and other neoliberal policies imposed by globalization from above.

Privatization has been a contentious issue in Bolivia since the imposition of the first World Bank Structural Adjustment Program that led to the closing on some state mines and the firing of more than 25,000 workers in 1985. The state mines, which had been nationalized after the 1952 revolution, provided the focal point for organized labor in Bolivia and the leading opposition to the imposition of neoliberal policies (Morales, 1992). The decimation of the mining unions was a profound blow to traditional social movements that were unable to prevent the subsequent increase in private sector participation in mining (Farthing and Kohl, 2001). Opponents to privatization claimed that it was little more than a transfer of resources that should serve all Bolivians to a select few.

In his first term, Sánchez de Lozada passed an innovative law that both called for the privatization of the largest firms and promised to distribute the benefits of private

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corporations among all Bolivians. The 1994 Law of Capitalization, as the partial privatization was called, was supposed to be privatization with a 'social content'. The government sold 50% of the five largest state-owned industries to multinational firms with the remaining 50% to provide a pension for a new class of Bolivian shareholder-citizens over 65 (Peirce, 1997; Whitehead, 1997). Capitalization formed the economic core of the first presidential term (1993–7) that also saw the reorganization of national and local government, a new constitution, and the restructuring of the judicial, educational and pension systems (Graham, 1997). Using neoliberal economic theories, Sánchez de Lozada predicted that capitalization would attract international investors to bring new capital, technology and management systems to Bolivia, fueling economic growth and creating hundreds of thousands of jobs along the way (MNR-MRTK-L, 1993). The underlying premise was that the adoption of economic liberalization policies, commonly referred to as the 'Washington Consensus', would promote economic growth and strengthen democracy (Williamson, 1993; Bedregal Gutierrez, 1994).

Yet in Bolivia the outcome was not as predicted by neoliberal theorists. While rates of foreign investment did increase, especially in oil and gas exploration and pipeline construction following capitalization of Yacimientos Petrolíferos Fiscales de Bolivia (YPFB), the state-owned oil and gas company, these investments provided little stimulus to the broader economy. The informal sector continued to be the primary sink for labor, workers lost jobs in the privatized industries, and economic growth remained sluggish. Most important, although the government imposed significant increases in energy consumption taxes, which provoked considerable social unrest, it still was only able to partially replace the 60% of its revenues that came from telecommunications and YPFB. In early 2003, the IMF demanded the Bolivian government reduce the deficit by US $240 million, from 8.5% to 5.5% of GDP. The government agreed to cut spending by US $30 million, and to raise US $80 million from additional hydrocarbon taxes and US $90 million from a new universal income tax (*La Razón*, 2003). It was this proposal that led to the tax wars in February.

The results of capitalization have come closer to those predicted by scholars and activists who warn that 'disciplinary neoliberalism' is part of a 'long range political project to lock in the power gains of capital on a world scale' (Gill, 2000: 6). Popular resistance to this project should come as no surprise. Fifty years ago Polanyi wrote that 'the dynamics of modern society was governed by a double movement: the market expanded continuously but this movement was met by a countermovement checking the expansion [by those] most immediately affected by the deleterious action of the market' (1957: 130). The almost constant uprisings, strikes and roadblocks by peasants in Bolivia since capitalization are all manifestations of this resistance to market forces (Farthing and Kohl, 2001; Shultz, 2001; Finnegan, 2002).

This article puts the Bolivian experience within a comparative framework by looking at recent research on privatization worldwide. I specify the innovations Bolivia's 'capitalization experiment' brought to privatization and demonstrate that the lack of regulatory control combined with a poor understanding of the logic of private firms contributed to Bolivia's worsening economic position. I demonstrate that rather than reduce corruption, the locus of 'rent seeking'[1] has shifted from the public to the private sector. Instead of providing a foundation for faster economic growth and social development, I contend that the Bolivian model of privatization reduced the ability of the government to design economic policy and increased political instability as mobilizations against economic restructuring grew. In fact, the overwhelming public rejection of the sale of gas to the United States led not just to the resignation of Sanchez de Lozada but threatens to undermine neoliberal restructuring in Bolivia.

1 Rent-seeking refers to attempts by public or private actors to take advantage of their position for financial gain or profit beyond what is accepted in their society as fair compensation or normal profit. It encompasses activities that include but are not limited to taking or paying bribes and using influence to shape regulations or avoid oversight.

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Privatization and the practice of neoliberalism

Since the mid-1980s privatization has figured as the lynchpin of international development policy. The push to privatize followed a massive privatization drive in England under Thatcher and in the United States under Reagan (Vickers and Yarrow, 1995). Driven by international financial institutions, more than 100 countries have privatized state-owned enterprises (SOEs) representing, as of 1998, a market value of US $735 billion (Nellis, n.d.: 1). In Eastern Europe and low-income countries, privatization has been part of a political strategy to redefine the role of the state (Feigenbaum and Henig, 1994; Appel, 2000). The economic arguments for privatization, embedded in the assumptions of neoliberalism, are simple. Private firms have greater incentives to operate efficiently and therefore can process information, respond to markets and allocate resources more efficiently than public ones. The more efficient allocation of resources at the firm level, when translated to the national economy, will lead to faster economic growth. SOEs are also susceptible to corruption, offering opportunities for rent-seeking public employees to enrich themselves at public expense, which proponents argue will not happen in private firms operating in a competitive, well-regulated free market. Privatization, then, should perform the triple function of creating more efficient firms, reducing corruption, and leading to faster economic growth (World Bank, 1996).

To date, however, the benefits from liberalizing state-controlled economies have not spread automatically to the broader society. While increases in the efficiency of individual firms are common, average annual GDP growth from 1989–95 was negative throughout Eastern Europe and inflation exceeded 1,000% per year in some countries (World Bank, 1996: 18). Privatization typically results in net job loss, which should not be surprising as private managers strive to cut costs. In Mexico, for example, hundreds of thousands of jobs were lost after the sale of SOEs (Ramiréz, 2000). Privatization frequently takes place in an environment where weak supporting legal and political institutions are incapable of monitoring and regulating firms, leading, in the case of Russia and China, to what some authors call 'gangster capitalism' (Holmstrom and Smith, 2000).

Schamis (2002), focusing on the institutional aspects of privatization and economic restructuring in a study of five countries in Latin America and Europe, demonstrates how privatization failed to eliminate rent-seeking behavior. He argues that new opportunities for rent-seeking arise when firms with political connections acquire public assets at a discount or buy inadequately regulated monopolies that provide public services (*ibid*.: 4). Privatization does not reduce corruption, but, instead, privatizes it as has been the case in Pinochet's Chile and Russia's 'nomenklatura privatization'. Other scholars agree, pointing to cases from Latin America (Ramiréz, 2000) to Eastern Europe (Tarkowski, 1990; Nellis, n.d.).

While the World Bank, perhaps the greatest booster of privatization at a global level, acknowledges the inherent problems, it accepts them as part of the cost of achieving broader political agendas (Nellis n.d.; World Bank, 1996; 2002). The Bank identifies the rewarding of 'insider stakeholders' as one of the key difficulties. Nellis (n.d.: 3), an ex-bank staffer, writes that in Eastern Europe this was accepted 'for what seemed excellent political reasons … The reasoning was that one needed to cut the links between the enterprises and the state, and to create swiftly a mass of private property owners; and that the only feasible way to do this was by offering substantial ownership stakes to workers and managers in the firms being privatized'. In many cases this quickly led to a concentration of ownership as a few individuals accumulated massive economic power (Holmstrom and Smith, 2000). Nellis explains that the Bank believed a problematic transition, with regressive redistributive aspects, was still preferable to the continuation of a communist-controlled eastern block.

As a key component in the broader project of neoliberal economic and political restructuring, privatization is seen by some scholars as a means to 'shrink' the state (Feigenbaum and Henig, 1994; Strange, 1996). Schamis (2002) poses a counter

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argument that as privatization is consolidated as a broader part of market restructuring, states expand their role in protecting private property, enforcing contracts, collecting taxes to pay for services and controlling economic policy. He maintains that this process 'can hardly be associated with less state but, rather, with more' (*ibid*.: 177–8) as state institutions develop their ability to protect the property rights needed for markets to function. In this context privatization is one component of 'marketization', which Schamis sees fundamentally as an 'institution building' project (*ibid*.: 178). While a state may strengthen or develop institutions as markets are given more power in an economy, it is not clear if this is really 'more' state or simply a 'different' one.

In a more nuanced analysis, Feigenbaum and Henig (1994: 51) describe three dimensions of what they refer to as 'systemic privatization'. First, a 'power shift', where privatization leads to 'a substantial and not readily reversible decrease in the power of working classes relative to that of economic elites'. Second, a 'perceptual shift' that serves to change the arenas that citizens perceive are proper for state intervention. The effect here is to 'delegitimize the public sector' and break down class bonds. Third, an institutional shift that moves policy decisions from the public to the private sector and from the sphere of politics to the sphere of economics. For example, a state-owned water company can choose to subsidize water as a social good — a political decision — whereas a privately-owned company may choose to set higher tariffs based on marginal cost of service — an economic decision.

While they may disagree as to whether the state is growing or shrinking, the institutional shift in policy decision-making from the political to the economic sphere described by Feigenbaum and Henig (1994) fits with the 're-formed' state Schamis describes. Privatization leads to new institutional arrangements needed not only to protect certain types of property but also to limit the areas of action deemed appropriate for state intervention.[2] Turning control of investment from the public to the private sector may not so much shrink the state as change its mission, and reinforce certain class relations and privileges.

Privatization and capitalization in Bolivia

Bolivia sought to avoid some of the rent-seeking and regressive redistributionary aspects associated with privatization by ameliorating its most common negative social costs. Rather than simply replace the government as the economy's primary actor with the private sector, the 1994 Law of Capitalization was designed to widely distribute the proceeds from the sale of SOEs and create a new class of Bolivian citizens loyal not just to the political party of the day, but also to the market economy in general. Government planners believed that investments made by the private sector plus funds from nascent privately managed pension funds would drive economic development and create an employment boom over a four-year period (MNR-MRTK-L, 1993).

Pressure to privatize Bolivian SOEs began in 1985 during the International Monetary Fund (IMF) stabilization plan that led the Paz Estensorro government (1985–9) to institute the 'New Economic Plan' (NEP). The NEP cut back government spending and imposed a rigid monetary policy, which succeeded in bringing hyperinflation under control (Sachs, 1987). The government closed most state mines and fired almost 25,000 unionized miners. While privatization of state-run enterprises was a fundamental pillar of this policy, despite pressure from the World Bank and the IMF, Paz Estensorro did not initiate privatization during his administration.

2 Schamis (2002), for example, reports that in Mexico, Chile and Eastern Europe, institutions to protect property rights were created *after* the majority of state property was transferred to a national economic elite.

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This began to change in 1992, when the Paz Zamora government (1989–93) passed the Law of Privatization, authorizing the sale of 30 small state firms.[3] Typically, national investors purchased these firms (Villegas Quiroga, 1997: 48). But the World Bank and other bilateral and multilateral funders along with some members of Bolivia's center-right political parties continued to press for the privatization of the largest government industries.

US-educated mining entrepreneur, Sánchez de Lozada, a long-time proponent of privatization and Planning Minister under Paz Estenssoro, proposed the partial sale of the six largest state-owned firms during his 1993 presidential campaign (MNR-MRTK-L, 1993). The government would retain 51% of the shares in the firms and distribute them to Bolivian citizens over 21. Sánchez de Lozada hoped that this redistributive measure would lower resistance to privatization and strengthen the faith of ordinary Bolivians in the market (MNR-MRTK-L, 1993; GOB, 1994).

The government proposed selling the remaining 49% of the shares, whose value would be determined by public auction, to international firms (MNR-MRTK-L, 1993: 19). Rather than directly pay the government an estimated US $2 billion for these firms, the purchasers would commit to double the book value of each business within seven years. Having brought the firms' value to a total of US $4 billion, the Plan assumed that the new owners would leverage these funds to borrow an additional US $6 billion dollars on international financial markets (MNR-MRTK-L, 1993: 21).

The idea of increasing working capital from US $2 billion to US $10 billion in less than seven years more closely resembled a pyramid scheme than a coherent economic plan. Yet Sánchez de Lozada's economic policy hinged on its success. Government planners projected that the flood of capital would drive GDP growth from 4% in 1993 to 11% by 1997, as private investment grew to 24% of GDP (MNR-MRTK-L, 1993: 23). This rapid growth was expected to create 287,000 new jobs and improve another 212,000 jobs over the same period. These optimistic projections also assumed that domestic investment fueled by contributions paid into newly-created pension plans would complement foreign investment.

Implementation of capitalization

When the Law of Capitalization was drafted, debates raged on how to distribute the proceeds from the sale of shares and expected dividends from the privatized firms. Plans to distribute the shares to all citizens along the lines of the Russian privatization model or to transfer the funds directly to individual retirement accounts were discarded (Bauer and Bowen, 1997). Instead, the government initially decided to use the proceeds to fund the Bonosol, an annual social security payment of about US $250, for Bolivians over 65 (Estellano, 1995; CEDIB, 1995; 1997). The government contracted two pension fund administrators (AFPs), each comprised of a consortium of foreign firms with minority Bolivian partners, to administer the system. To protect the investments of Bolivia's citizens, these private AFPs had management oversight through minority representation on the Board of Directors of the newly privatized firms.

The government estimated that the AFPs would initially need between US $60 and $75 million per year from a combination of dividends and the sale of stock to finance the Bonosol. As the government knew that dividend income alone would be insufficient for this, a percentage of shares were to be sold through the newly formed Bolivian stock market. Stock sales would continue until the fund was depleted in 2050 when all Bolivians would be covered by individual pension plans.

3 Not only did the Paz Zamora government actively promote privatization, but also the concept of partial privatization was suggested as a way to attract private capital, while maintaining domestic control of the firms, at this time (ILDIS, 1992: 89).

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Table 1 Purchase price of capitalized firms

Sector/Firm	Date of transfer	Principal shareholder	Country of origin	Bid for 50% of firm US $ millions
Hydrocarbons (YPFB)				
Petrolera Chaco	4/97	Amoco	US	306.7
Transredes	4/97	Enron	US	263.5
Empresa Petrolera Andina	4/97	YPF	Argentina	264.8
Telecommunications				
ENTEL	11/95	STET	Italy	610.0
Transportation				
LAB (airlines)	10/95	VASP	Brazil	47.5
ENFE (railroads)				
Andina	3/96	Cruz Blanca	Chile	13.2
Oriental	3/96	Cruz Blanca	Chile	25.9
Electricity (ENDE)				
Corani	7/95	Dominion Energy	US	33.0
Guaracachi	7/95	Energy Initiatives	US	35.0
Hermoso	7/95	Constellation Energy	US	30.0

Source: Villegas (1997: 33–4)

The Law of Capitalization, signed in March 1994 with little debate in Congress, led to the sale of the government's oil and gas, telecommunications, airlines, power generation and railroad companies.[4] At the time, the capitalized industries accounted for about 12.5% of GDP and 60% of government revenues — oil and gas alone accounted for 80% of those revenues. The sales were not quite under the conditions initially proposed. The government sold 50% not 49% of the stock as the bidding companies insisted on majority ownership to guarantee complete managerial control.

The five firms, divided into ten independent units, were sold between 1995 and 1997 through public auction (see Table 1). One remaining portion of YPFB was fully privatized during the Banzer administration (1997–2001). In all, the bids totaled US $1.67 billion, in a combination of commitments for future investment and cash. The remaining shares were distributed between the pension fund administrators (AFPs) and workers who converted their pensions to stock. The winning bids typically required purchasers to pay only a fraction of their investment commitment at the time of the sale. For example VASP (Viacao Aérea Sao Paulo), the second largest Brazilian airline company, took control of Lloyd Aero Boliviano (LAB), with a payment of US $5 million to company accounts and a commitment to invest an additional US $42.5 million in LAB over five years (Prefectura de La Paz, 1995).

As the contracts assigned the government's 49% of the shares to the AFPs the government was neither able to use the influx of cash to reduce the deficit, as was done in Mexico and Brazil, nor able to count on future earnings from the companies, all of which were initially destined for the Bonosol.

4 Vinto, the national smelter, the sixth industry on the block, had no bidders in the first round of capitalization. The British firm, Allied Deals, bought the smelter for US $14 million in December 1999 (Rubín de Celis, 2001). Vinto reverted to government control in 2002 after going into receivership. COMIBOL, the national mining corporation, was the one large firm exempted from capitalization as the nationalized mines were considered part of the national patrimony and their sale or transfer to private firms constitutionally prohibited

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Capitalization evoked a visceral political, popular and intellectual response from across the political spectrum (CEDIB, 1994; Torres Obleas, 1997; Altos Estudios, 2000). The traditional left accused the government of handing over the country's wealth to transnational corporations and called it unconstitutional (CEDIB, 1994; *El Mundo*, 5 February 1994: 57; Vargas, 1994). The right also opposed the sale of enterprises it considered strategic. The military, remembering its defeat to Chile in the War of the Pacific in 1880, took special offense at the sale of the railroads to the Chileans, arguing that it was a threat to national security as well as an insult to the country's honor (*El Diario*, 4 March 1996: II, 1). Many economists of both the left and the right criticized the assumptions of capitalization and argued that it would lead to the loss of 12,000 jobs while hindering the government's ability to direct economic development over the long term (CEDIB, 1995).

Public opposition to the sales of the firms began even before Sánchez de Lozada took office. Protest primarily consisted of daily marches and demonstrations in La Paz, with the members of each union striking or marching in protest as their firm was sold (CEDOIN, 1996). While union members took to the streets and regularly clashed with riot police, the constant demonstrations became incorporated into the daily routines of La Paz life and halted neither the sale of state firms nor the 14,795 layoffs that followed (Torres Obleas, 1997).

The majority of the population, most of whom earned less than the unionized workers losing their jobs, expressed only limited sympathy with the workers' plight.

Impacts of capitalization

Capitalization's ambitious economic goals rested on five basic assumptions. First, investments made by the capitalized companies would, by themselves, have a multiplier effect on the rest of the economy and lead to faster growth. Second, Bolivian entrepreneurs would absorb the available capital and use it to create jobs. Third, the AFPs would initially sell off shares of the capitalized companies to finance the Bonosol, and dividends from the companies would generate a cash surplus for investment at low interest rates. Fourth, the share price of the capitalized firms would increase due to the ongoing investments and increases in productivity. Fifth, taxes generated from rapid economic growth would compensate for the immediate loss of oil and gas revenues. To date, these assumptions have not been proven. The nature of these failures in Bolivia gives practical and theoretical insights into market restructuring, privatization programs and the changing nature of the state.

Capitalization has achieved part of the first assumption: new owners met, and often exceeded, investment quotas. Villegas estimates foreign direct investment before capitalization at US $169 million (Villegas Quiroga, 1997: 52); in 1996, a single firm, the Italian-owned STET, invested that much in ENTEL alone. By June 2000 the capitalized firms had invested about US $2 billion, the lion's share stemming from US firms in the hydrocarbon sector (*Los Tiempos*, 15 September 2000: A9; Barja and Urquiola, 2001). The majority of these investments, however, has been in capital-intensive goods of foreign manufacture and has not had a large multiplier effect on the economy. In 1996 four of the capitalized firms were among the top six largest importers in the country (Villegas Quiroga, 1997), and the oil and gas producers continued to be among the largest importers through the end of the decade.

As with the application of neoliberal programs in other parts of the world, policy makers failed to consider that the quality of economic growth, as much as the quantity, determines job creation (Ramiréz, 2000). Villegas (1997) contended that even if the capitalized firms increased production and efficiency, they would not create new jobs. In the case of the airline LAB, the company's largest single investment, the 1996 purchase of a Boeing aircraft, probably created more employment in Seattle than in Bolivia. All steel pipe for the construction of the Brazil-Bolivia gas pipeline came from

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Argentina, Brazil and Korea, and the US $435 million dollar investment on the Bolivian side directly created fewer than 600 permanent jobs. This should come as no surprise; over 40 years ago Hirschman (1958) observed that resource extraction is a poor 'growth engine' as it has poor forward and backward linkages.[5] A rise in GDP from an increase in natural gas production will create far fewer jobs than the same level of growth from labor-intensive activities such as agriculture or the transformation of tropical hardwood logs into finished products

Capitalization led to massive firings of unionized workers on a scale not seen since the closing of state-owned mines in the mid-1980s. YPFB went from a high of 9,150 workers in 1985 to fewer than 1,880 by the end of 1997. Cruz Blanca reduced the number of railroad workers in its two companies from 5,424 to 855 by 1999 while increasing the tonnage shipped (Antezana Ergueta, 2001).

Rates of economic growth at the national level hovered around 4% through 1998. Revenues from the new gas pipeline to Brazil that came on-line in 1999 provided an important cushion for an economy reeling from the fallout of the 1998 Argentinean economic crisis and curtailment in coca production. The Argentinean crisis decimated the greatest single demand for Bolivian labor and, with it, perhaps the country's greatest source of remittance income. The eradication of thousands of hectares of coca resulting from Banzer's US supported war on drugs also battered the economy. GDP grew at around 1% in 1999 and 2000, rising slightly in 2001. Poor global economic conditions have generally curtailed economic expansion in Bolivia's dependent economy, although the government predicts growth will reach 2.5% in 2003 (www.ine.gov.bo).

The second assumption, that national entrepreneurs would absorb increasingly available capital and use it to drive job growth, is derived from the notion that private sector entrepreneurs will harness the energy of an unfettered market (de Soto, 1990). The limitations of a small national market, the open borders that resulted from the 1985 New Economic Policy, the high cost of investment capital, and the perceived risk associated with doing business in Bolivia combine to make it difficult for national manufacturers to compete with those in other parts of the world. As a result, the demand for national investment capital has remained low. In part, this is due to the nature of the country's investment opportunities, which are primarily capital intensive, in mining, oil and gas, electrical energy generation, agriculture and timber extraction. With the exception of timber and agriculture, and to a lesser extent mining, the companies with the necessary technical expertise and financial and managerial capacity are all foreign (Villegas, 1997: 55–60). In a country as historically unstable as Bolivia, the perceived regulatory and political risks are higher than in much of the world. This leads national investors to look to the short term and expect to earn risk premiums, as much as 3% to 5% per month on investment capital. This expectation is incompatible with the kinds of investments needed to develop either the physical or human infrastructure that can lead to long-term productivity increases.

The third assumption — that the AFPs would both pay the Bonosol with cash dividends from the capitalized firms and generate a cash surplus through the sale of shares on the Bolivian stock market — may prove to be the most problematic of all. Due to the difficulties in establishing the Bolivian stock market, in order to make the first payment in 1997, the AFPs had to borrow about US $44 million at 11% interest. The inability to generate sufficient revenue for the Bonosol reveals some of the fundamental flaws underlying capitalization. Capitalized companies are under no obligation to distribute dividends; they can choose to pay down loans or reinvest revenues instead, and the AFPs, as minority shareholders, have no leverage over company decisions. As well, unlike publicly held companies in the United States and Europe, company accounts remain confidential and even shareholders have no ability to examine them. The introduction of publicly owned and traded companies runs counter to the way business historically has been done in Bolivia. As one businessman explained in a confidential interview, 'almost every business in Bolivia keeps a triple

5 For a more recent similar analysis see, Sachs and Warner (1999: 43–76).

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set of books to avoid taxes'. While this is accepted standard business practice, it is not conducive to the public trading of stock, which requires that information on earnings and expenses be public, believable and accessible.

While the government anticipated that dividend income would not cover all the Bonosol payments, it did expect that the AFPs could make up deficits through the sale of stock in the different companies. The open trading of stock, of course, assumes the existence of an active stock market, which has yet to take hold in Bolivia. The stock market *(Bolsa de Valores*) continues to trade primarily in government and private bonds and in shares of less than 20 stocks, making it impossible for the AFPs to raise cash needed to pay social security payments without borrowing. While shares of stock are exchanged by employees taking cash from their pension savings, these exchanges are done informally, and no matter how much is paid, they do not affect the 'market price' (Hausherr, 2002). Investors have little demand for shares whose prices are artificially inflated by the AFPs, who are paid a commission on the net value of the portfolio they control.

The current pattern of share ownership lends itself to the manipulation of stock prices, as almost 99% of shares are held by only three owners: the multinational firms own 50%, and the two AFPs split 49% between them. Because the capitalized firms are prohibited from selling shares of stock until they fulfill their investment commitments, the AFPs are the principal source of stocks for the market, which allows them to control the availability and the stock prices. To complicate the matter further, the AFPs are primarily charged with administering individual retirement accounts for more than 500,000 workers. Therefore, confidence that stock prices reflect true values becomes even more critical as the AFPs begin to look for domestic private sector investments for the individual pension accounts they manage. The fear is that the AFPs will transfer shares at inflated prices from the capitalized firms to the new pension funds. This would provide a source of capital to help the AFPs address the solvency issue, while also providing a sink for current pension fund contributions. As of 2001, however, 72% of AFP investments remained in government bonds (www.spvs.gov.bo: Figure 11).

In addition to the lack of a viable equity market, two problems cut short the life of the Bonosol. First, the firms did not generate the expected level of dividends as they chose to reinvest their earnings rather than distribute them among shareholders. This choice allowed them both to avoid paying taxes on profits and to reach their investment obligations faster. More important, the Banzer administration, which came into office in 1997 just months after the first Bonosol payment, decided that the country could ill afford to spend US $60 million per year on a program that was targeted to help old people and would do nothing to contribute directly to economic growth.[6] On returning for a second term in 2002, Sánchez de Lozada promised to reinstate the Bonosol.

The fourth assumption, that increases in productivity brought about by foreign investors would increase share value, has also proved false. A February 2001 study showed that the combined share prices of the capitalized firms have fallen from US $1.67 billion at the time of capitalization to US $774 million, with the majority of the losses split between ENTEL (US $329 million) and the oil and gas firms (US $377 million) (CEDIB, 2001: 3).[7]

Finally, the loss of oil and gas revenues to the national treasury has not been compensated with revenues from increased production, nor from the gains from foreign investment, nor from unloading the burden of the airlines and railroads (both losing money at the time of their sale), but primarily from special energy taxes. Beginning in 1997, a 25% increase in energy consumption taxes led first to strikes by transportation drivers and then, after raising fares to cover increased fuel costs, to strikes and protests by poor Bolivians affected by the price hikes (*La Razón*, 10 December 1997: A11). By

6 The Banzer administration did use funds to pay 'Bolivida' a reduced Bonosol once during its period in office.

7 I believe that actual losses are much higher than these estimates, which are based on AFP price evaluations rather than any real market price

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the end of 1997, the fall in oil and gas revenues combined with the US $200 million it had cost to implement capitalization contributed to a US $430 million budget deficit (*La Razón*, 25 November 1997: B7). Government revenues continued to fall through 1998, leading Banzer to impose across-the-board budget cuts of 5% in 1999 (*La Razón*, 16 December 1998).

Budget deficits have continued to be a problem, with each deficit bringing on another round of negotiations with the IMF and the World Bank (IMF, 2003). Often when the government must introduce further restructuring to meet IMF goals, the proposals are rejected by a large and increasingly vocal segment of the Bolivian populace. The proposed income tax proposal that came from one agreement in February 2003 led to the 'tax wars' set off by a confrontation between police and the military.

New opportunities for rent-seeking

In general, the newly installed private owners used similar strategies to increase profitability: they reduced or rebalanced the workforce; increased capital investment; introduced new management techniques and productive technologies; and raised rates for basic services. Unlike the government, private companies had the freedom to focus on the economic maximization of the firm as an independent unit, rather than the need to negotiate with diverse political actors demanding job security, low-cost services, or revenues for the treasury. While the government had used its ownership of the SOEs as a way to subsidize electricity and water for urban consumers and rail service for residents of small towns built along rail lines, private firms were under no obligation to provide such unprofitable services. In some cases after capitalization, in telecommunications for example, the government specified service goals and rate-setting formulas. In others, such as the transportation sector, however, the government proved it was unable to provide adequate regulatory provisions to protect people dependent upon these services.

Asset stripping: railroads and airlines

In Bolivia's weak regulatory environment, the government is incapable of protecting the interest of the 'public shareholders' represented by the AFPs. Some of the actions by the new private owners, such as selling or transferring assets from the capitalized firm to the parent firm, might be considered illegal as they defraud the shareholders, but the majority was simply good business practice given a firm's imperative to maximize profits.

A good example of this practice is provided by the national railroad company, which had been losing US $4 million per month at the time of the sale and was split in two. The companies, both bought by Cruz Blanca, a Chilean firm, began to show a profit shortly after their sale. The rapid turnaround, offered as a dramatic example of privatization's success, was achieved by reducing the workforce by 80%.[8] The new management also improved operation in a number of areas, including refurbishing maintenance shops, canceling subsidies for agricultural producers and private miners, and closing unprofitable passenger services.

The success was short lived. By the end of the decade, Ferro Carril Andino (Andino), operating in the western half of the country, had begun to decapitalize, selling assets (Garcia, 2000) including land and even the railway stations themselves. The company failed to maintain the roadbed and removed sections of track between Cochabamba and Oruro, closing service to over 50 stations that had no other road access. They also

8 The Manager of Ferro Carril Andino, which ran the railroads in the western half of the country, said that the workers quit as they refused to come to work when the firm was privatized (Taborga, 1997). A representative of the labor union said the workers were fired.

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dismantled railroad bridges, reportedly transporting the materials to Chile to build spur lines to mines. The fact that the railroads were divided into two companies made it possible for Cruz Blanca, the parent corporation, to abandon Andino while continuing to operate the profitable rail lines in the eastern part of the country. Bolivia's government had no mechanisms at its disposal to affect the behavior of a firm that found it more profitable to asset-strip its holdings.

LAB, the national flagship airlines, suffered a similar fate. As with Andino, VASP integrated LAB's international operations with its own, expanded the maintenance capacity to take advantage of Bolivia's low labor costs, reduced national service, fired Bolivian managers, and stripped over US $13 million from LAB's parts inventory. Stories in the Bolivian press accused VASP of using the LAB parts to refurbish jets in other VASP-owned companies. The 'just too late' inventory system of the new owners had disastrous effects on the quality of service for Bolivians dependent on the airline for national travel and its international reputation.

Critics of VASP's management argue the underlying strategy was first to sell off LAB's parts inventory to pay for the acquisition and then sell off shares of stock to raise cash (*30 Días*, October 2001: 14–27). LAB began to report losses in 1999 and bordered on bankruptcy by 2001 (*La Razón*, 4 April 2001). In November 2001, VASP management, under criminal investigation for malfeasance in Bolivia, sold its interest in LAB to Bolivian businessman Ernesto Asbun. While the airline may survive under the new management, there is little indication that a stripped LAB will ever pay dividends to the AFPs.

Transferring profits: telecommunications

The case of ENTEL is slightly different. The Italian company STET (later bought by Telecom Italia) took over ENTEL, one of the best managed and the second most profitable of the state-owned firms, bringing in Italian management, rebalancing the workforce, and undertaking an ambitious investment plan to meet its contract obligations of US $610 million over four years. The company made a large commitment to cellular telephones, the fastest growing sector of the telecommunications market in Bolivia. ENTEL also planned to increase international service through linking Chile and Brazil with fiber optic cable.

Revenue grew at double digits through 1999 but profits, which had been about 16% when the company was state-owned, have been low. The company has been accused of shifting profits out of ENTEL and transferring them to wholly owned subsidiaries outside of Bolivia, a practice AFP-selected board members have no ability to challenge. Regulations simply do not provide controls to curtail such behavior. The impact, of course, is to lower ENTEL's profits, 50% of which are slated for the AFPs and other shareholders.

Buying discounted assets: hydrocarbons

Before capitalization, the Bolivian oil company, YPFB, was the most profitable of all state-owned enterprises. Even so, its rate of growth was limited as the government siphoned off most of its earnings, rather than reinvest them in exploration. YPFB was sold as three companies (Empresa Petrolera Chaco, Empresa Petrolera Andina and Transporte Boliviano de Hidrocarburos [Transredes]). These companies, freed from the demands of a revenue-hungry government, invested quickly after capitalization and together account for almost half of the investments in the capitalized firms. Transredes, owned by a consortium of companies including Enron and the Brazilian national petroleum company, Petrobras, invested US $435 million by mid-1999 to complete the Bolivian side of the gas pipeline to Brazil with loans provided by the Inter-American Development Bank and Andean Development Corporation (Corporación Andino de Fomento — CAF).

Exploration and production companies have found immense quantities of gas, with estimates of reserves increasing from seven trillion cubic feet (TCF) to over sixty TCF,

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giving Bolivia the second largest gas reserves in South America with much exploration yet to be done. Markets for gas, however, are lacking. The combination of an economic crisis and successful energy conservation programs in Brazil reduced the growth of demand for electricity, the primary use for Bolivian natural gas. Government negotiations to pump gas to the Pacific coast through Chile for export to US markets were the proximate cause of the 'gas wars' that led to Sanchez de Lozada's resignation. Critics noted that the deal would provide few benefits to Bolivia, as regulations written to promote foreign investment reduced wellhead royalties from 50% to 18%, with 13% directed to departmental governments.

The privatization of oil and gas has tragic implications for the country's economy. YPFB had been on the verge of completing a contract to build a pipeline to connect Bolivian gas fields to Brazilian markets before capitalization (Calle Quiñonez, 2000: 247). This single pipeline could have increased YPFB profits by at least $50 million a year for 40 years. These earnings, instead, were largely transferred to private firms that borrowed capital from the same international financial institutions that had previously offered loans to YPFB. Rather than transfer exploration and production profits to private multinational oil firms, YPFB could have continued to embark on the series of joint ventures with international petroleum firms that were well underway before capitalization.

The new laws that control oil and gas investment, written with technical assistance from oil industry representatives (Hale, 1997), were designed to attract foreign investment rather than protect national interests. The real giveaway came with the regulations that followed the 1996 restructuring of the hydrocarbon laws that reduced wellhead royalties, especially as international firms had shown themselves willing to invest in Bolivia with the higher royalty rates (Mariaca Bilbao, 2000). The lower tariffs were only to apply to 'new hydrocarbons' as a means of promoting exploration. However, the regulations defined fields that had been proven but not put into production as 'new' as well, a giveaway that could cost the nation hundreds of millions, if not billions, of dollars over the next 40 years.

The transfer of the nation's wealth of hydrocarbon reserves to private transnational corporations for pennies on the dollar severely limits the country's capacity to develop throughout the twenty-first century. While state-owned oil companies have a global reputation for being corrupt, they still have been important sources of revenue for national development. Before capitalization, Enron signed a deal to build and operate the gas pipeline to Brazil. Even though this contract was highly irregular and is still under review by Bolivian courts, the national treasury still would have received more than it will from privatized firms (Ramos, 2000).

Conclusions

Whitehead, writing only weeks after the first Bonosol payment had been made in 1997, in a candidly 'prospective' evaluation, suggested that by incorporating a redistributive component, capitalization represented an attempt to move 'beyond neoliberalism' and traditional privatization programs. He asked whether capitalization might serve to legitimize a market economy through its attempt to 'underwrite universal entitlements and substantive citizenship rights' (Whitehead, 1997: 92).[9] He concludes: 'Anyone adopting a historical, comparative, or sociological perspective on the current ascendancy of neo-liberal theory and discourse should draw comfort from the thought that all such constructivist projects contain the seeds of their own synosession. Bolivia

9 Whitehead draws on Marshall's classification of citizenship rights that defines 'substantive citizenship rights' as the range of 'social' rights that include 'the right to a modicum of economic welfare and security to the right to share to the full in the social heritage and to live the life of a civilized being according to the standards prevailing in the society' (Marshall, 1964: 71–2).

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might even return to the Latin American vanguard, becoming one of the first countries in the region to advance substantively beyond the confines of orthodox neo-liberalism' (*ibid*.: 92). Whitehead's optimism has proven unfounded. Instead of moving 'beyond' neoliberalism, capitalization provides an interesting case of what Brenner and Theodore refer to as 'actually existing neoliberalism', a 'political practice [that] has generated pervasive market failures, new forms of social polarization and a dramatic intensification of uneven development at all spatial scales' (2002: 352).

Capitalization did indeed achieve its narrow goals of attracting foreign investment capital and reducing the government's role both as an economic actor and as a provider of public services. The law failed, however, to meet its broader economic, social and political agendas. The Bolivian economy has not responded as predicted to the influx of foreign investment capital and the hundreds of thousands of anticipated jobs never materialized. While private management did increase firm efficiency, this did little to improve the economic situation of the government due to the loss of revenues from YPFB and ENTEL. Moreover, the projected increases in tax revenues have yet to materialize as the now private companies choose to reinvest or transfer earnings out of the country rather than distribute profits and pay taxes in Bolivia. The long-term situation for the national government looks bleak as it is unlikely that tax revenue from the growth inspired by capitalized companies will replace previous oil and gas income as tax rates have been reduced to attract investors. The reduction in government revenue exacts an enormous social cost as public expenditures on health and education decline.

Not only did the government lose revenue but it also lost the ability to use price structures as a policy tool. For example, before capitalization, telephone and electric companies did not aim to maximize profits but, rather, to keep the cost of telephone service and electricity affordable to urban consumers. Since the sale of the oil and gas company, special taxes on gasoline and diesel, largely paid for by Bolivia's poor through increased transportation costs, have replaced much of the income that the national oil company contributed to the treasury.

As with privatization in other countries, the problems generated by the absence of regulatory and market infrastructure in Bolivia were not adequately anticipated. Unsophisticated pension fund managers and a weak regulatory structure were unable to ensure an honest accounting and distribution of profits from firms like Enron and Petrobras. The lack of market infrastructure made the task of the AFPs almost impossible, as they were unable to sell shares to diversify their investments to ensure reasonable returns. The redistributive component of privatization, which was to provide broader access to social citizenship rights and serve as the means to move 'beyond neo-liberalism', was sacrificed in part because of the economic crisis brought on by capitalization itself. Instead, as the locus of rent-seeking shifted from SOEs to private firms, capitalization became an exercise in creative rent-seeking, in part due to a weak regulatory structure. Aggressive rent-seeking cannot simply be attributed to the actions of a single villainous firm: profit maximization is an integral part of the mandate of the firm. After all, it is bad business practice to fail to take advantage of a regulatory vacuum.

Capitalization's principal legacy, however, may well be how it has redefined the mission of the state. The 1952 revolution began to change the Bolivian state from one controlled by a handful of families from the mining and agricultural elite to one with a responsibility to a broader citizenry. While an 'unfinished' revolution (Malloy, 1970), the state did extend universal citizenship rights and, through the nationalization of the mines, declare natural resources part of the country's patrimony. Capitalization as part of a project of systemic privatization has defined a new role for the state, which will be difficult to reverse given its dependence on debt assistance from the World Bank and the IMF. This new role has been successful in both shifting ever more power to favor global elites and beginning to strengthen institutions which protect their property.

Instead of balancing the contradictory goals of maintaining a legitimate state and creating a stable market economy, capitalization has threatened both the viability of the state and the market economy. The abuses of the privatized firms and the inability of the

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government to ensure that these firms paid their share of taxes led to the gas wars and Sanchez de Lozada's resignation in October 2003. On assuming the presidency on 18 October, Carlos Mesa made it clear that he would consider altering the country's basic commitment to its neoliberal policies. The hundreds of thousands of Bolivians who drove Sanchez de Lozada from office have made it clear that they will accept nothing less. Yet it is not clear how much Mesa will be able to accomplish given a divided congress and the certain opposition from the United States, the World Bank and the IMF. Mesa faces the fundamental contradiction of market-democracies: balancing the legitimacy of the state with the need to create the conditions for markets to operate.

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