

Paraguay

Status Index (Democracy: 2.8 / Market economy: 2.6)		5.4	Management Index		3.5
System of government	Presidential democracy		Population	5.6 mill.	
Voter turnout	60.8 % (2000) ^b		GDP p. c. (\$, PPP)	5,210	
Women in Parliament	2.5 % (2003)		Unemployment rate	10.0 % (2000)	
Population growth^a	2.9 %		HDI	0.751	
Largest ethnic minority	3.0 %		UN Education Index	0.84	
			Gini Index	57.7 (1998)	
Data for 2001 – if not indicated otherwise. ^a Annual growth between 1975 and 2001. ^b Vice presidential election August 13, 2000. Source: UN Human Development Report 2003.					

1. Introduction

On March 28, 1999, President Raúl Cubas Grau resigned to avoid impeachment. Cubas, of the Colorado Party, had taken office in August 1998 and was considered the puppet of General Lino Oviedo—who because of a failed 1996 coup attempt was banned from the May 1998 presidential elections, which he otherwise would presumably have won. The president thwarted judicial arrangements to arrest Oviedo, who mobilized his adherents in the party and the army. There were open threats against the judiciary, Parliament and opponents within the party.

On March 23, 1999, Vice President Luis María Argaña was murdered. Argaña had been considered Oviedo's main opponent within the ruling Colorado Party, and Oviedo was therefore thought to have been behind the assassination. After mass protests, especially by youths that resulted in deaths and injuries, Cubas and Oviedo eventually left the country (for Argentina and Brazil), requesting political asylum. Yet Oviedo remains a destabilizing power factor in Paraguayan politics, especially because repeated demands for extradition by the Paraguayan courts have been refused.

The head of the Senate, Luis Angel González Macchi, was sworn in as the new president for the remainder of the term until August 2003. Because of his lack of democratic legitimation (he is unelected) and the fragmented nature of the ruling Colorado Party, González was in a weak position. So it is no surprise that planned economic reforms could not be implemented. The past five years have been characterized by political stalemate, economic backsliding and a clear deterioration of the social situation.

2. History and characteristics of transformation

The transition to democracy in Paraguay was initiated in 1989, after 35 years of dictatorship under General Stroessner. The transition was the result of power struggles within the political elite. Initially, the political opposition and civil society played no role in the transition process. Thus the transition to democracy was characterized by extensive continuity among the elites in politics and officialdom (administration, military, judiciary). Stroessner had used the Colorado Party as a tool in safeguarding his rule. Party membership was a prerequisite for a career in the administration or military.

Through the party, the country was covered with a close-meshed network of control and patronage. Even after the transition to democracy, the Colorado Party remained in power. It is now the longest-governing party in Latin America (since 1947). While it is true that a process of democratization in political institutions was initiated under Presidents Rodriguez (1989–1993) and Wasmosy (1993–1998), with a new constitution in 1992, the military still played a troublesome role: It was highly politicized, viewed itself as part of the Colorado Party and openly took partisan positions. President Rodriguez, as leader of the coup against Stroessner, had formerly been commander in chief of the army; General Oviedo, the commander in chief under President Wasmosy, tried to use his position as a political springboard.

3. Examination of criteria for democracy and a market economy

3.1 Democracy

In transforming its political order, Paraguay has made progress in political institutions. There are still transformation deficiencies in political participation, political representation and the rule of law. Some progress has been made in democratic stability (actors with veto powers have been neutralized), but these advances cannot be consolidated.

3.1.1 Political regime

(1) *Stateness*: The state's monopoly of violence has been established in principle nationwide, but it does not prevail untrammelled, especially in frontier areas. In the "tri-border area" (where Paraguay, Argentina and Brazil meet) around the frontier city of Ciudad del Este, the state's power has failed in the battle against smugglers and drug dealers. Security experts consider the region a potential refuge for international terrorists.

All citizens have the same civil rights, even indigenous groups—but in practice the latter assert their rights inadequately, in part because they are numerically few

and poorly organized. 95 % of the population is mestizo. Constitutionally, Paraguay is a multicultural, bilingual country. Guaraní and Spanish are the official languages. Church and state are largely separate, and religious dogma has no influence worth mentioning on policy or law. The state has a basic infrastructure (administrative institutions, officials, fundamental administration of justice, making and implementing political decisions) in place throughout the nation, but corruption and political colonization of the administration have made performance spotty.

(2) *Political participation*: While national elections largely satisfy democratic requirements, the party primaries to nominate candidates have repeatedly involved irregularities. Moreover, patronage practices and political dependencies (for example, in the civil service) influence the election process, so that the Colorado Party is structurally favored. Democratically elected representatives now have the effective power to govern, and the influence of actors with veto powers—especially those in the military—has waned.

Independent political and civil-society groups can generally form freely. However, the possibilities of union organization have been hindered bureaucratically by the state. The level of unionization is around 15 %. During the period under study, the state sometimes reacted with exaggerated severity to union protests. Farmers and those who own no land are also organized. Their mobilization in favor of state subsidies, land allocation and land ownership is often suppressed violently by the state and para-statal actors. Nevertheless, during the period under study, road or street blockades and demonstrations were frequent both in the country and in the capital, Asunción.

Freedom of opinion and freedom of the press are guaranteed. There is a pluralistic media sector, including private and public radio and TV broadcasters. The press's access to information is restricted at times by the behavior of politicians and the administration. Critical journalists are sometimes physically threatened, especially if they report on corruption. In political-crisis situations, there can likewise be trespasses against institutions of the press. The independence of the press is further hampered by the extensive influence of business interests and politicians over the media—for example, in the issuing of broadcasting licenses.

(3) *Rule of law*: Fundamentally, Paraguay has separation of powers and mutual checks and balances. This is particularly the case in relations between the president and Congress. The judiciary as well, especially the Supreme Court, has a relatively independent position in form, though it cannot be considered politically neutral. In political crises during the period under study, the judiciary performed a function of stabilizing democracy, although the principles of the rule of law were not always duly observed in prosecuting the adherents of General Oviedo. Apart from professional criteria, judges are appointed very much on the basis of political criteria as well. At the lower and middle levels, there are

problems with professionalization and a severe vulnerability to corruption and political influence in trials.

Further deficiencies in the rule of law result from the duration of proceedings and prolonged investigative arrest. The introduction of a new code of criminal procedure (1999) accelerated proceedings and better protects the rights of the accused. At the level of political leadership, corrupt officials have been prosecuted in isolated cases—for example, former President Wasmosy—but they often take advantage of political, legal or procedural loopholes. The vast majority of cases of political corruption are not prosecuted.

Civil freedoms are largely secure, especially basic political rights. There are no political prisoners. Conditions in the hopelessly overcrowded prisons have repeatedly sparked criticism. There are repeated reports of excesses by the security forces (including torture and extralegal executions) against prisoners and those suspected of crimes, and against draftees. Multiple cases are known in which minors were forcibly drafted, which is against the law. The government appointed an investigative commission in 2001. The violations of human rights from the Stroessner era were criminally prosecuted in a few spectacular cases. But most cases have not been processed yet, even though the office of the prosecutor general includes a special advisor for human rights who actively works to prosecute crimes under the dictatorship. Victims of the dictatorship have not been indemnified comprehensively as yet.

3.1.2 Political patterns of behavior and attitudes

(1) *Institutional stability*: Fundamentally, democratic institutions perform their functions, but grave inefficiencies arise in the interplay between the president and Congress. This is because the ruling Colorado Party, which has an absolute majority in both chambers, is splintered into several factions, and except in election periods intramural competition undermines the party's coherence, hobbling government action.

Democratic institutions are supported by the relevant actors, but in the case of the governing party (or some of its factions) some doubt remains whether this support is solely a matter of principle or a matter of the one's own prospects of getting elected. Hitherto there has been no transfer of power between the government and the opposition at the national level. Additionally, in Paraguay there is a latent risk that free and fair elections might bring antidemocratic politicians into power.

(2) *Political and social integration*: The Paraguayan party system is dominated by two parties, the Colorado Party and the Liberal Party. Each is more than 100 years old. They will continue to dominate the country's politics for at least the medium term. The party system is extremely stable, impeding innovations. The Colorado Party is unquestionably the stronger of the two. After 55 years in power, the party

has a close-meshed patronage network that favors populist policies in opposition to a free market. Many of the 200,000 government employees owe their jobs to their party affiliation.

Both parties are broad-based within society. Direct elections for executive offices in the party and to nominate candidates for elective office generate a high capability for mobilization in both parties. But the parties work only sometimes as instruments for articulating and aggregating social interests; they are more likely to serve as tools to mobilize voters for party caudillos. Hence the internal fragmentation of the two parties among competing party leaders is also typical, though stronger in the Colorado Party.

Compared with the parties, the system of social-interest groups is weak, not very cooperative and dominated by only a few interest positions. There is no link to the parties in terms of collateral organizations, although one of the umbrella labor organizations is close to the Colorado Party. Support for democracy is low (between 30 % and 50 %), and has been receding in the past few years. Compared with the rest of Latin America, a large percentage of the population is open to the idea of authoritarian solutions. Voter turnout has recently shrunk sharply (60 % in the election of a new vice president in August 2000 and 50 % in the municipal elections of November 2001). Autonomous organization in civil society runs up against political-culture and socioeconomic barriers and is uneven. Trust among the population is rather low.

3.2 Market economy

Paraguay is stagnating in the transformation of its economic regime. Transformation deficiencies exist in the organization of competition, the role of state enterprises, bank supervision, controlling the shadow economy, providing an assurance of justice and combating corruption.

3.2.1 Level of socioeconomic development

The relevant indicators (HDI) indicate a medium level of development. There is extensive social exclusion. The richest 10 % of the population has more than 90 times as much disposable income as the poorest 10 %. According to poverty statistics (CEPAL), up to 60 % of the population lives below the poverty line, half of it in extreme poverty. There is also an urban-rural gradient. The proportion of the poor in rural areas is more than 70 %. Paraguay is a highly agricultural country (around 30 % of jobs are in the agrarian sector). By contrast, the industrial sector is weak.

3.2.2 Market structures and competition

The foundations of market economy-based competition are safely assured. However, there is a strong state sector in telecommunications, electric power generation, oil refineries, cement production and water utilities, which are thus closed to foreign investment. Free competition and the protection of property rights are furthermore limited by endemic corruption and political influence in the administration and judiciary, and by a large shadow economy that includes smuggling into neighboring countries and illegal products (narcotics, pirated products such as music CDs, stolen automobiles, weapons, etc.).

“Minor border traffic” in goods re-exported duty-free to Brazil and Argentina still accounted for 4.5 % of the Paraguayan GDP in 1998, despite a declining trend. The informal sector is thought to include 45 % to 50 % of all persons gainfully employed; the IMF estimates the informal sector contributes between 15 % and 19 % of GDP.

Prices for public services (water, electricity, telecommunications), gasoline, pharmaceutical products and public transportation are politically controlled. The government also sets minimum wages. At the same time, Paraguay has a low burden of taxes and social contributions (income from labor and services is not taxed). Foreign trade has a medium level of protection.

Membership in MERCOSUR has largely liberalized trade with Argentina, Uruguay and Brazil; an average duty of 13.5 % applies for the rest of the world. The banking sector went through crises in 1995, 1997 and 1998. Many banks had to close. The central bank was also involved in corruption scandals. The costs of the banking crisis were around 10 % of GDP, and had to be absorbed mainly by the public sector. The bulk of deposits (80 %) are now in foreign banks. Banking supervision has improved since the crises, but is still inadequate because of scarce qualified personnel and because of political influence over banking decisions.

3.2.3 Stability of currency and prices

Inflation control and a fair exchange-rate policy are recognized goals of economic policy, but have not been pursued consistently over time, and do not have adequate institutional safeguards. The inflation rate of 14.6 % in 1998 was reduced to 5.4 % for a short time, but had returned to its original level by the end of the observation period. Close ties to its two big neighbors in MERCOSUR (Argentina and Brazil), which both devalued their currencies massively, put severe pressure on the Paraguayan currency during the period under study, causing it to drop substantially against the U.S. dollar.

The government's inadequate democratic legitimacy and the short- to medium-term electoral interests of major actors in both the opposition and government

campus have caused problems with goal-setting and performance in regard to a continuous policy of stability. Consequently the budget deficit rose significantly until 2000; after that, the trend was reversed only briefly. The principal causes are rising personnel expenses in the public sector, deficits at state enterprises and in pension funds, and the cost of restructuring the banks.

3.2.4 Private property

Property rights and the regulation of the acquisition of property are fundamentally well-defined, but there are problems with implementation under the rule of law (not least of all because of deficiencies in the judicial system). Land titles are often ill-defined, especially in the agricultural sector. A latent and sometimes violent conflict exists between (1) the interests large agricultural corporations (some of them foreign-owned) have in consolidating and expanding their holdings and (2) the demands of the landless and small farmers for agrarian reform and land redistribution. Protesters often occupy land, with subsequent conflicts, which both sides often conduct outside the law. While private enterprises are the backbone of the economy, in some sectors state enterprises exercise a monopoly or subvert fair competition.

3.2.5 Welfare regime

There are rudimentary measures to avoid social risks, but they are sharply segmented in terms of territory, class and sector. The social security systems extend only to those employed in the formal sector of the economy. Social insurance for employees in private business is still relatively young, and manages to keep its budget balanced, though it has been adversely affected by the banking crisis. The pension fund for state employees runs chronic deficits, and must rely on injections of cash from the government budget.

Because of the size of the challenges involved, the state's limited resources and poor economic performance, the country is unable to combat poverty systematically on its own. Society is severely segmented, and there are hardly any institutions to make up for gross social discrepancies. There are particularly marked differences in the delivery of health care. Women have rather little access to higher education and public office. There is a sharp urban-rural gradient here. Violations of labor law and other legal protections (children, health, etc.) are not adequately monitored or sanctioned by the government. At the operating level, because of business people's opposition, collective bargaining agreements are often impossible.

3.2.6 Strength of the economy

Real per capita income shrank considerably in the period under study. With one exception (2001), the economy showed consistently negative growth rates. The other macroeconomic data also declined overall. Urban unemployment rose substantially, most recently to nearly 11 %. According to the World Economic Forum's competitiveness index, Paraguay scored 72nd both times, out of 75 countries examined in 2001 and out of 80 in 2002.

3.2.7 Sustainability

Ecologically compatible growth is given only sporadic attention and has hardly any institutional roots. This is particularly evident in regard to the ecological impact of the country's large hydroelectric plants. Reducing air and water pollution is not a priority. In spite of an improving school enrollment rate during the last years, the educational system has great deficiencies. Only rudimentary research and development facilities exist.

4. Trend

(1) *Rule of law and democracy*: Stateness, political participation and the rule of law maintained their earlier levels. The degree of consolidation of democracy improved slightly. The observation period began in general with advances, but they proved less than stable, and some have been reversed. The presidential (1998) and vice presidential elections (2000) met democratic standards; the transfer of office was peaceful; and in the follow-up elections for vice president, the opposition won its first victory. To some extent, however, it owed this victory in part to adherents of Oviedo. The "cohabitation" of a president from the Colorado Party and a democratically legitimized vice president from the Liberal Party, who furthermore has presidential ambitions, had a stalemating effect on the political process.

After the political crisis was resolved early in 1999 through constitutional channels, a certain mood of new beginnings was evident in the country. There was hope that broad mobilization would lead to a revival of Paraguayan democracy. Another contributing factor was that both major parties, the Liberals and Colorados, joined with another party to form a National Unity government. But the momentum for reform did not last long. As a consequence of an attempted overthrow by Oviedo's supporters, the officer corps was purged. There was yet another small mutiny (May 2000), but in general the position of the military as an independent power broker in the political process must be considered weaker at the end of the period under study, and the risk of a takeover by the military has declined sharply. The scope of corruption, deficiencies in justice, violations of human rights and the parties' shortcomings have changed little or not at all.

According to Transparency International's Corruption Perception Index, in 1998 Paraguay placed 84th among 85 countries studied; in 2002 it was 98th out of 102, and ranked the worst of any Latin American country. A positive note is that the constitutionally stipulated office of an ombudsman for human rights (Defensor del Pueblo) was filled in October 2001. Isolated reforms are also being implemented in the judicial system. The Colorado Party remains fragmented, and its ability to act as the bearer of governmental responsibility is restricted. The Liberal Party offers no clear alternative programs and places short-term power interests above propagating democracy; it is willing to resort even to supporting authoritarian politicians in order to gain power.

The parties' deficiencies in articulating and aggregating interests have led social actors to try to impose their interests directly, through political protest. This has reinforced the political stalemate. The population's skepticism about democracy has increased. Former General Oviedo still holds considerable voter potential, and in 2002 he founded his own party, which is thought to be behind some of the mass protests and violent demonstrations against President González. Oviedo is thus attempting to influence the upcoming 2003 presidential and parliamentary elections.

Table: Support for democracy (in %)

	1998	2000	2001	2002
Satisfaction with how democracy is working (percentage of "satisfied" or "very satisfied" responses)	24	12	10	7
"Democracy is preferable to any other form of government"	51	48	35	41
"Under some circumstances, an authoritarian government is preferable to a democratic one"	36	39	43	38

Source: Latinobarómetro 1998–2002 (<http://www.latinobarometro.org>)

(2) *Market economy*: The institutional framework for working toward a market economy has improved only in some segments (e.g., banking supervision), but not comprehensively. General economic development has deteriorated both quantitatively and qualitatively since the mid-1990s. This trend continued during the period under study, and has even intensified. Paraguay is going through the worst economic recession of the past 20 years. But this has not yet affected HDI values, which even improved slightly up to 2000.

Table: Development of socioeconomic indicators of modernization

	HDI	GDI	GDP index	Gini index	UN Education Index	Political representation of women	GDP per capita (\$, PPP)	% of poverty in the population
1998	0.736	0.723	0.63	57.7	0.84	8.0 %	4,288	-
1999	0.738	0.725	0.63	-	0.83	8.0 %	4,384	60.5
2000	0.740	0.727	0.63	-	0.83	8.0 %	4,426	-

Source: World Development Report 2002; Human Development Report 2000, 2001, 2002; CEPAL, Panorama Social de América Latina 2001–2002, Santiago de Chile 2002.

Table: Development of macroeconomic fundamentals

	1998	1999	2000	2001	2002 ^a
Growth of GDP in %	-0.6	-0.1	-0.6	2.4	-3.0
Growth of GDP per capita in %	-3.2	-2.6	-3.1	-0.1	-5.4
Export growth in %	-7.2	-27.0	-15.1	3.0 ^a	-
Import growth in %	-7.0	-27.1	-6.7	-3.0 ^a	-
Inflation (Dec.–Dec.) in %	14.6	5.4	8.6	8.4	14.6
Unemployment in %	6.6	9.4	10.0	10.8	-
Budget deficit in % of GDP	-1.0	-3.6	-4.3	-1.1	-2.5
Current account balance in mn \$	-160	-86	-192	-220	-96

^a Preliminary figures

Source: CEPAL, Balance Preliminar de las Economías de América Latina y el Caribe 2002, Santiago de Chile 2002; CEPAL, Estudio Económico de América Latina y el Caribe 2001–2002, Santiago de Chile 2002.

5. Transformation management

5.1 Level of difficulty

At the beginning of the period under study, Paraguay was at a medium level of development socially (HDI) and economically (GNP per capita), with marked recessive tendencies in the economy and gross social disparities. Great ethnic homogeneity is certainly an advantage. The democratization process in Paraguay began in 1989, after a long phase of authoritarian rule, with a weak autonomous civil society, a weak political opposition, and great continuity among the elites in politics and officialdom. Despite these poor starting conditions, along with

persistent deficiencies in democracy and in the rule of law, the country was able to resolve its institutional crises at the beginning of the observation period within the constitutional rules.

5.2 Reliable pursuit of goals

During the period under study, the government had only a limited ability to act with a long-term orientation or in the prospective best interest of the country. Because of its weak basis of legitimation and inadequate support in Parliament, its activity was characterized by ad hoc measures, a lack of overall concepts and attempts to maximize short-term political gains, with no recognizable setting of consistent priorities. Announced reforms found only scant implementation in concrete measures. Parts of the government (or governing party) worked against one another. There was no recognizable coherence in policy. Although the government ensured a fundamental reliability of expectations for its citizens' lives, there is neither an assurance of justice nor a stable economic environment. Social and economic actors have had to contend with politically induced uncertainties.

5.3 Effective use of resources

The government uses only some of the state's available resources efficiently. The state bureaucracy is swollen (the number of civil servants has increased 25 % since 1989, and they are almost invulnerable to dismissal). Recruitment of administrative personnel puts a heavy emphasis on political loyalty. The state budget is perpetually unbalanced. A significant reduction in the deficit survived only briefly. Multiple cabinet reshufflings have brought no lasting increase in efficiency and were primarily a reaction to internal party conflicts. In November 2002, both the minister of finance and the president of the central bank resigned because Congress refused to initiate economic reforms (especially tax reforms— income tax and value-added tax) that the IMF had required as prerequisites for a loan of \$200 million. The result was problems raising the funds to pay debts to foreign creditors or to pay civil servants' salaries.

The government carries out only a portion of the reforms it announces, and cannot adhere to its own plans. For example, in October 2000, the legal basis was set up to privatize the state's water works, the telephone company and the railroad, but these moves were never carried out. Rate increases to reduce the deficit at state enterprises and prepare them for privatization have regularly led to social protests that force the government to reverse some measures. In May 2002, Congress halted the privatization of the state telephone company in order to investigate financial irregularities.

After further protests and demonstrations in June 2002, the government suspended all privatization projects that same month. The government gives no assurance of adequate public services and thus hinders any further development or transformation. The government was unable to rein in corruption during the period under study. The resources of the state are distributed on the basis of patronage networks. Corruption is a central feature of state and administrative culture.

5.4 Governance capability

The leading political actors—especially the government—have indeed reacted to setbacks and policy failures with changes, but these changes proved to be marginal more often than not, so that policies have tended to remain stuck in the same rut. Learning experiences have not penetrated into the cognitive policy-making structure. For example, there have been short-term successes in fighting inflation, reducing the budget deficit and restructuring the banking sector. But it has been impossible to consolidate these successes; thus, in some areas, the situation has deteriorated again. There has been no attempt at comprehensive, long-term reforms in the administration of the state or in combating corruption. Even the president has been linked with cases of corruption.

The interests of stakeholders are not questioned. The process of privatizing state enterprises was inaugurated but then halted, in part because of massive protests by employees. A reform of the latest state bank (BNF) is failing, in part because the bank is being plundered by politically influential individuals. The primary problem in Paraguayan politics during the period under study was that because of his lack of democratic legitimation and weak position in his own party, the president has had insufficient political authority to initiate and continue reforms.

President González Macchi has been able to withstand a total of three impeachment attempts only because the governing party wanted to keep the opposition vice president from assuming the presidency. The work of governing has been further hampered by the almost constant election campaigns of the past three years. After the election of a new vice president (August 2000), the election of a new head of the Colorado Party (May 2001) and the municipal elections (November 2001), political events were dominated in December 2002 by the primaries for candidates for the pending April 2003 presidential and parliamentary elections.

The government takes account of the allocative effects of its policies, but makes hardly any effort to improve the allocative efficiency of the markets. Many reforms are induced from the outside, with consequent adverse effects on their sustainability.

5.5 Consensus-building

The main political actors do agree on establishing a market-based democracy. But there are problems with implementation. The reformers are weak, and they have no control over actors with veto powers and their ability to throw up roadblocks. This has been documented by the failed process of privatizing state enterprises. There is a lack of consensus-building mechanisms—for example, between business owners and unions or between politicians and actors from civil society. Politics has been marked by dissent more than consensus. For example, the National Unity government came to a quick end in February 2000, not least because the Colorados were uninterested in any genuine power-sharing and did not keep agreements.

Although the government can prevent the structural conflicts in the agricultural sector from escalating between the occupants of land and the large landowners, it cannot mitigate existing conflicts. However, the conflict over land is not articulated along party lines. Although the government has made initial attempts to promote the population's sense of solidarity, it cannot succeed, because of its incoherent policies and weak basis of legitimation.

5.6 International cooperation

Although political actors work actively with bilateral or international donors (including the IADB and World Bank) to strengthen democracy and the market economy, projects for technical and staff collaboration yielded only very limited improvements during the period under examination. The Paraguayan government does attempt to present itself to international actors as a reliable partner, but is not considered entirely credible, not least because its weak power base restricts its ability to get things done. Important donors feel the government has neither the will nor the ability to make fundamental reforms, see little possibility of exerting influence, and do not expect any sustained continuance of the often-defective measures that have been inaugurated.

The public sector is considered too weak and inefficient to carry out projects. It also has no experience with cooperation. Consequently the risk of a further reduction in international organizations' commitment in Paraguay remains. Paraguay is a member of MERCOSUR, along with Argentina, Brazil and Uruguay. The population generally supports belonging to this common market (Asunción is the headquarters of the MERCOSUR court of arbitration), even if some voices loudly advocate the country's going its own way during periods of political or economic crisis. The Paraguayan economy is closely tied to those of the neighboring states, so that economic crises in Argentina and Brazil have direct consequences in Paraguay.

Membership in MERCOSUR has helped stabilize Paraguayan democracy in the sense that these two big neighbors have intervened diplomatically in active ways during periods of political crisis (e.g., threatened coups). Through MERCOSUR, Paraguay is also involved in negotiations on a free-trade agreement with the EU. In concert with the MERCOSUR countries, it is conducting parallel negotiations on easing trade with the United States, within the ALCA process. In 2001, for the first time in six years, the US recertified that Paraguay had an active policy to combat the drug trade.

6. Overall evaluation

In view of the starting conditions, current status and evolution achieved, as well as the actors' political achievements (management), this assessment arrives at the following concluding evaluations:

(1) *Starting conditions*: The starting conditions for transformation toward a market-based democracy were rather negative in Paraguay's case. Democracy was not achieved by fighting for it, but instead was the chance result of power struggles among the elite in the Stroessner regime. The result was a broad continuity among the elites in politics and officialdom. In economic terms, at the beginning of the transition, Paraguay was characterized by a comparatively low density of regulation and a very open economy.

Handicaps included a large sector of loss-making state enterprises, a large informal sector and institutional conditions that inhibit growth. These conditions include an inefficient, politicized state administration and a lack of an assurance of justice because of deficiencies in the legal system. Furthermore, at the start of the observation period, Paraguay was in a deep economic recession, with problems in the banking sector and a rising budget deficit. Politically, Paraguay's democracy went through a profound crisis in 1998–1999, which it handled successfully at first. This yielded opportunities to expand democracy and create a broad coalition for reform in both politics and the economy.

(2) *Current status and evolution*: Opportunities for reform at the start of the observation period went unused, so that the subsequent three years were characterized by political and economic stasis. The fact that democracy survives and that the crisis was resolved through constitutional channels, together with the weakening of the military as an actor with veto powers, can be considered an advance on the way toward democratic transformation. But this progress did not penetrate into the depths of the democratic structure. The political parties remain very inadequate in their functions of articulating and aggregating interests.

The government party is fragmented and capable of action only to a limited degree. Support for democracy has waned. The number of supporters of authoritarian solutions remains high. The distance covered in transforming toward

a market economy has been minimal. At best, the country can be credited with short-lived successes in acute challenges (inflation, budget deficit) and controlling the bank crisis. Fundamental economic reforms have either gone unattempted or were blocked.

(3) *Management:* The verdict on the actors' relative management performance is negative. The process of (economic) transformation stagnated during the observation period. This is especially true of balancing the government budget and privatizing state enterprises. Successes, as in reducing the inflation rate or cutting the budget deficit, were short-lived and could not be sustained. It remains to be seen whether the reforms in the banking sector, at least, prove sustainable.

Most macroeconomic indicators document a negative overall balance in crisis management. The president's lack of democratic legitimation has impeded any focused policy of reform. Opportunities to create a broad political and social consensus went unused. The fault can be laid on all the political actors. Ultimately, further political and economic development remains fraught with imponderables.

7. Outlook

The Paraguayan presidential democracy is characterized by a strong Parliament with a bicameral structure and fragmented parties. The consequence is that many points of the political decision-making process are vulnerable to vetoes. Deep-seated political and economic reforms must therefore draw on broad coalitions and an unequivocal democratic legitimation of the decision-makers. The still-heavy sediment of authoritarianism in political culture, combined with the country's unresolved social problems, can foster authoritarian tendencies in politics.

Paraguay's democracy suffers from the presence of a hegemonic party that was already in power during the dictatorship, and that still contains authoritarian residues. Moreover, because of its internal fragmentation, the party has been both the government and the opposition, impeding the work of the true opposition parties. For lack of a serious challenge from the opposition, there is also no real pressure on the government to make reforms. At the moment there is no indication of strong forces pushing for more economic reforms. Hence no crucial changes can be expected in the political arena. The party landscape—including internal party fragmentation—will change little and will hinder the formation of majorities able to act.

Nor can any impetus toward reform be expected from outside, because of the crisis in MERCOSUR. Where economic and social reforms do occur, they are patchwork, reacting to specific challenges. Despite multiple challenges, no general program can be expected. Socially, the question of land reform and the

creation of alternative employment opportunities for the landless and for impoverished small farmers will have to be solved. Efficiently combating poverty is closely tied with this. The Paraguayan state will not be able to manage this challenge alone.

In the economy, a socially aware tax reform would have to ensure that the state's finances remain balanced, and that resources are available for an active social and educational policy. The privatization of state enterprises is likely to face further difficulties. In part this is a matter of preserving political sinecures. Also, it has been found that privatization processes in a corrupt environment arouse justified suspicions that the process will not be genuinely transparent, and that privatization will not so much serve the interests of the population as become a further means for the elites to enrich themselves. In such an environment, it is difficult to arrive at a positive consensus about privatization. It is significantly easier to mobilize groups of the population against it.

Economically, Paraguay is dependent on the world economy and demand for its most important (agricultural) export products, as well as on developments in the neighboring MERCOSUR countries. Any leeway for independent action is rather limited.