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Left-Wing Veto Players and Agenda Setters: Economic Reform in Developing Democracies of Latin America

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ABSTRACT

Why do some states implement economic liberalization policies while others fail to do so? In this paper, I show that the number and ideological positions of the veto players and their interactions with each other explain differences in economic reform efforts and outcomes. Using several indicators of the veto players and their partisanship, I conduct empirical tests of the effects of the number of veto players and their ideological policy preferences on budget balances, as an indicator of reform effort, using panel data analysis of developing democracies from 1978 to 2000. Also, I test the veto players partisanship against an indicator of reform effort outcomes for Latin American countries. I find that the left-wing partisans hinder economic reform efforts while the right-wing veto players, which usually include the agenda setter in these samples, promote economic reform efforts.

Key Words: economic reform, veto players, agenda setters, budget deficits, left-wing in Latin America

INTRODUCTION

Since the 1982 beginning of the debt crisis in Latin America, economic liberalization has been the agenda of the day for most developing countries, and it became a more important issue with the democratization of post-communist countries in 1990. While some adopt economic adjustment successfully, others fail or have less successful results even though economic

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liberalization or structural adjustment is set as a condition for financial assistance by most international agencies such as the World Bank and the IMF. In this paper, I investigate why countries adopt different levels of economic liberalization by looking at differences in institutional settings in the framework of a veto players argument: when there are a large number of veto players, it is hard to change the status quo unless the veto players have very similar preferences (Tsebelis 2002). This can imply that it is hard to implement drastic policy changes, resulting in unsuccessful economic adjustment outcomes when there are a large number of veto players.

I argue that if any veto players oppose reform, the agenda setter (mostly the executive) cannot propose radical reform packages and can only propose minimal reform policies that are close to the status quo, thus leading to slow economic adjustment.[1] It is more difficult to reform when any of the veto players (including the agenda setter) are left-wing because their main constituents ―the labor and the popular sectors― oppose liberal economic reform that usually leaves them as losers (Haggard and Kaufman 1995). Thus, although the agenda setter proposes economic liberalization measures, countries will have less successful economic adjustment outcomes if there is any veto player that is left-wing. This implies that, first, even a small left-wing party can block reform if it is in the coalition or it is in the opposition coalition and has veto power. Second, it implies that the number of veto players does not matter if there are no left-wing veto players because as veto players, the left-wing veto players will more likely than the right-wing to contest drastic measures such as decreasing government subsidies or privatizing public utilities.

No literature on economic reform has yet tested whether the interactions between the agenda setters and veto players affect economic reform efforts. I employ measures of the policy position of agenda setters and veto players, and investigate how their interactions and different institutional settings affect policy making. I test this more sophisticated version of the veto player argument, using a dummy variable of left-wing veto player and an ordinal variable for the position of agenda setter. I test parts of the argument on the level of budget balance ―an outcome of austerity measures― with a larger data set of developing democracies. Next, I test

1 Of course, the executives can use decree power to implement policy reform in some countries. Different degree of decree power also changes the bargaining process between the agenda setters and the other veto players. Some presidents can break the gridlock in the legislature by using their decree power. But in this paper, I only focus on policy reform through law-making.

my argument on Latin American countries, where reasonably good data on economic reform are available, using several economic liberalization indices.[2] The empirical tests show that left-wing veto players do not have a clear effect on economic reform when they interact with reformist agenda setters. Also, I found that the reformist agenda setters have positive effects on reform efforts and their positive effects decrease by the existence of the left-wing veto players in the legislature.

LITERATURE ON ECONOMIC LIBERALIZATION

Economic liberalization is defined as a process of privatization, enterprise restructuring, price liberalization, foreign trade liberalization, exchange rate liberalization, introducing or transitioning to a competitive market, banking reform, securities market reform, tax reform, and legal reform. In theory, economic reform should bring ideal market conditions, and accordingly, liberal economies should allocate resources more efficiently, which should lead to faster development.[3] Economic adjustment is usually set as a condition for foreign aid or financial support from the World Bank or IMF, and delay in reform is inefficient since it will increase necessary adjustment costs (Alesina and Drazen 1991). However, economic adjustment in most developing democracies has been slow, and some reverse the course.

What is the cause of delay in economic reform, if most economists and economic advisors claim that a liberal economy is necessary to recover from economic or financial crisis in an increasingly globalized international economy? Some scholars argue that it is partly due to time-inconsistency problem (Sachs and Warner 1995). It takes time for a liberalized market to fully operate and increase output, but the public does not see the positive effect of new policies in the short run; thus the new policies are perceived as "bad" or even "worse" than the status quo. Additionally, this brings another problem of short-term costs to the public. As the

2 Morley, Machado and Pettinato (1999) have constructed economic reform indexes on reform in general, capital account liberalization, financial market reform, tax reform, and privatization.

3 Of course, some countries like South Korea had remarkable economic growth through heavy state intervention, and the Soviet Union and the Communist East European countries' economic growth in the early Cold War era should not be ignored. Also, not every liberalized economic reform brings positive growth. However, in general, economists accept the idea that a liberal economy is better for economic growth in the long run.

most economic reform measures bring reductions in government spending and subsidies for public goods and utilities, the public ¬especially the poor¬ have to suffer the immediate loss, such as an increase in bus fare or gas price. Then, the government faces threat of electoral loss or even popular uprising. For example, in 1989 when President Pérez of Venezuela announced a reform package called *The Great Turnaround*, bus fare increased to the point where workers could not ride the bus to work. This led to a popular uprising, which killed at least 300 people (Pérez-Liñán 2006). Eventually, Pérez was impeached, and the subsequent governments could not impose drastic liberal economic reform.

Other scholars have looked at institutions in developing democracies to explain differences in reform efforts (Alesina and Drazen 1991; Haggard and Kaufman 1995; Hellman 1998; Rodrik 1996; Sachs and Warner 1995; Wibbels 2000; 2005).[4] Traditionally, the spatial model of left-right policy dimension predicts different policies for ideologically driven parties (Alesina et al. 1997; Alt 1985; Barro 1981; Boix 2000; Drazen 2000; Franzese 2002; Hibbs 1977; Hibbs 1987; Imbeau et al. 2001; Schmidt 1996; Schneider and Frey 1988; Woldendrop et al. 1998). Haggard and Kaufman (1995) find that left-wing or populist governments are more reluctant to implement economic reform.[5] The left-wing parties' economic platform includes stronger role of governments in redistribution and development, and they are closely associated with the working class, one of the main initial losers from economic reform (Coppedge 1997).

Then, in an exciting new turn in economic reform literature, scholars began to study the effect of individual players in economic policy making. First, since economic reform redistributes economic benefits, some groups will lose from the change and will try to pressure governments not to implement economic liberalization. Hence, change in economic policy

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4 As an anonymous reader pointed out, many scholars are skeptical about using an institutional approach to understand the political economy of developing countries because their democratic institutions are not as stable as are those in OECD countries. However, research on institutions is essential in understanding economic policies because policies are changed or sustained through institutions. By changing the institutional setting, we affect the policies and may have better outcomes: better economic performances and economic development in developing democracies.

5 In the literature of political economy of the developed countries, left-wing parties are defined as communist, socialist, or social democratic. Right-wing parties are parties that are conservative or Christian democratic (Keefer 2004). The liberal economic policies are associated with the right-wing parties as the liberal policies are against state intervention and the main constituents are the elite. Haggard and Kaufman (1995) also discuss the populist movement and popular sector support of the populist parties, but they assume that the populist movement is ideologically close to the left-wing.

will face resistance from the groups that will lose from policy reform. Even the less-powerful poor or the labor can exert their opposition through a mass uprising and street protests. Accordingly, policy makers representing their constituency will veto any change in the status quo, fearing an electoral defeat from the discontented losers of the reform.[6] Hellman (1998) uses the concept of "inclusive government" –a government that does not listen to special interests but listens to the public in general– and tests his argument on ex-communist countries. As the number of parties in government increases, the number of actors and groups whose agreement must be coordinated for policy increases as well. Hellman's test actually confirms the veto players argument that the large number of veto players will obstruct changes – once reform is initiated, the reversal of reform will be blocked as the number of parties in coalition increases. On the other hand, Wibbels (2000) finds that fractionalization in a party system, which he uses as a proxy for number of veto players, is associated with worse outcomes of economic restructuring. Fragmentation of party systems impedes coordination for both initiating and sustaining of new policies because it is harder to generate electoral and legislative support for policy changes when there are many parties in the legislature (Haggard and Kaufman 1995). Of course, a measure of fractionalization in a party system used by Wibbels and the number of parties in coalition used by Hellman differ. Yet, it is puzzling how their theoretical arguments based on the veto player theory give the empirically opposite results.

AGENDA SETTER AND POWER OF THE LEFT-WING VETO PLAYER

The two empirical tests by Hellman (1998) and Wibbels (2000) present a starting point for an in-depth study of institutions in developing democracies. Both Hellman (1998) and Wibbels (2000) fail to present the bargaining process between the veto players and agenda setters. Unlike the literature assumes, the executive (president, prime minister, or finance/economic minister) and the government party/coalition sometimes have different preferences. When the economic crisis hits, the public

6 Here, one needs to assume that policy makers care about re-election. There are some countries like Mexico where a politician cannot be re-elected. Still, politicians strive for other political and governmental posts, so one can assume that all politicians usually care about re-election or getting other jobs in politics.

becomes more willing to mandate the government to act (Haggard and Kaufman 1995).[7] The agenda setters receive a demand for change from the public and demands for more liberal policies ¬that are usually platforms of the right-wing or the centrist¬ from the IMF or the World Bank. Then, regardless of their party origins, preferences of the agenda setters can deviate from those of parties in government coalition. This is more so when government is a minority government, when president is from a different party from legislative majority or when government coalition is formed with parties with different ideological positions in policy space. Therefore, one has to consider whether the left-wing parties are veto players and look at interaction of agenda setters with veto players.

The power of agenda setters is well recognized in the literature (Alemán and Schwartz 2006; Alemán and Tsebelis 2005; Tsebelis 2002; 2006). The agenda setter has the advantage because he or she often knows where the preferred policy position ¬the indifference curves[8]¬ of other players are located in advance and can make a proposal moving the status quo closer to his or her own policy position that will be accepted by others as better than the status quo. However, the fact that the agenda setter has the power to propose a bill does not mean that the agenda setter can move the status quo any time. The positions of other veto players and of the status quo are also important.

Now, for veto players, if the usual veto players' preferences were close to those of the agenda setter on economic reform policy dimension, their veto power would not matter in this instance of bargaining. In other words, their role as veto players loses its effect (Tsebelis 2002). Decision to use veto power depends on how ideologically distant parties are from the status quo and from agenda setters, not on how many parties compose government.[9] The correct model specification should include the interaction between agenda setters and veto players because the power of the veto players will depend on their own positions in the policy space and the position of the agenda setter. Also, I divide

7 It also depends on the depth of the crisis and on the extent of the failed efforts by the previous administration.

8 In terms of Tsebelis' theory, it is the "winset" of veto players. The "winset" of the status quo is "the set of outcomes that can defeat the status quo" (2002).

9 Ideally, the best policy position of an agenda setter is the center of the policy dimension so that his/her proposal will not be vetoed (Tsebelis 2006), but regarding economic reform, I assume that the agenda setter, if he/she proposes an economic reform bill, is more to the right of the policy dimension because most of liberal economic adjustment packages are right-wing policies. Also, policy change depends on how many policy dimensions are salient. In this paper, however, I assume that policy dimension is one-dimensional.

the left-wing parties as veto player and non-veto player because the usual test of partisanship, using the percentage of left-wing parties in the legislature, might overestimate the power of left-wing parties that do not have veto power, or underestimate the power of left-wing parties that have veto power (although small in numbers).

The left-wing parties are veto players when the government party is left-wing, the government coalition includes left-wing parties, or the government is a non-left minority government and the opposition parties are left-wing.[10] The left often has veto power in economic policy bargaining because the status quo is usually to the left of the reform policies proposed by the executive. Thus, a left-wing party will either be able to limit reforms if its ideal point is between the agenda setter's and the status quo (Figure 1), or it will be able to cause stalemate if its preferences are to the left of the status quo[11] (Figure 2). Figure 1 and Figure 2 below illustrate these interactions.

If the veto players' policy position is far from that of agenda setter, veto players are likely to oppose reform, and the agenda setter can only propose minimal reform policies that are close to the status quo so that the veto players will not veto the change. The agenda setters have to implement policies that are inside the indifference curve of the veto players so that veto players would not veto and policies that are, at best, closest to their own ideal position. This can result in minimal reform outcomes or further deadlock once the status quo is moved a little bit. Alemán (2004), in his study of Latin American presidents, shows that minority presidents passed as many bills as majority presidents did, and most of the presidential bills were passed after being amended by the legislature. He explains that the minority presidents were able to pass as many bills as majority presidents because the minority presidents only proposed bills that would pass. The agenda setters would not propose a bill, which would not have passed because the agenda setters know the preferences of the veto players beforehand. Once the status quo is changed to some degree, the agenda setters and the veto players might face a stalemate again. Still, any change ¬even if it is a small amount¬ is preferred to stalemate by the agenda setters, who are pressured to implement neo-liberal policies by the international institutions.[12]

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10 The last case is very unlikely. The president usually puts together a majority coalition no matter how small his own party is.

11 If the veto players have different preferences and the status quo lies between them, there is a stalemate (Cox and McCubbins 1997).

12 This can actually explain why there are incremental changes in the economic adjustment process rather than sudden and radical change in economic policy in most countries.

Figure 1 shows the case where the ideal point of left-wing veto players (*L*) is located between the agenda setter (*P*) and the status quo (*SQ*). Knowing the ideal position of the veto players and their indifference curve (winset), the best proposal for the agenda setter will be *Z*, which is still better than *SQ* – closer to his own ideal position. The veto players (*L*) will not veto the proposal *Z* because *Z* is inside their indifference curve. Figure 2 illustrates the gridlock between the president and the legislature. The preference indifference curves of each veto players (*L*) and agenda setter (*P*) only intersect at the status quo (*SQ*). Thus, there will be no policy change because the agenda setter (*P*) will not be able to propose any proposal (*Z*) closer to him than the status quo (*SQ*) that will not be vetoed by the left-wing veto players (*L*).

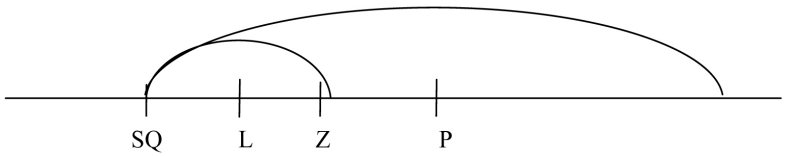

Figure 1. Bargaining and Interaction between the Agenda Setter and the Legislature

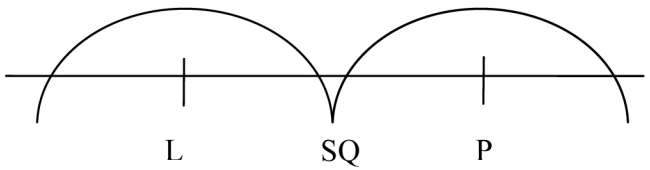

Figure 2. Deadlock between the Agenda Setter and the Legislature Regarding Economic Reform

The first implication of my argument is that when there are one or more left-wing veto players, existence of veto players will have negative effects on economic reform efforts. The second implication is that agenda setters can only propose a moderate, if any, reform due to interaction with left-wing veto players. Nonetheless, agenda setters positively affect the reform efforts. In other words, the effect of reformist agenda setters will be greater when there is no left-wing veto player. The existence of left-wing veto players would decrease the positive effect of agenda setters' reform efforts because agenda setter would propose only a small change inside the indifference curve of the veto players (Figure 1), or because there is a stalemate when the status quo is located between the

agenda setter and the veto player (Figure 2).

EMPIRICAL TESTS

I test the implications of the bargaining between veto players and agenda setters, using a dataset on developing democracies from 1978 to 2000.[13] I only look at democratic countries because the argument is based on an assumption that elected officials are responsive to their constituents and face re-election or re-appointment in other government jobs. The dataset starts from 1978 because it was after the second oil shock of 1979 that international agencies recognized the need for liberal economic policies. It is important to look at years before 1982 when the debt crisis hit Latin American countries so that I can assess if there is any difference in government or policy before the crisis and after the crisis. I limit the data to the year 2000 because of limited data on economic reform efforts index. I use a pooled time-series regression with a panel-corrected standard errors estimator with assumptions that disturbances are panel-level heteroskedastic and that there is no contemporaneous correlation across panels.[14]

Economic reform as a dependent variable is difficult to operationalize for a large N-study. Even if an economic reform bill is passed, its implementation could be hindered, so a scholar would need to monitor its implementation and outcomes. Furthermore, it is necessary to look at non-crisis cases and see why some countries do not even experience the crisis and sustain economic development. One of the ways to measure economic reform efforts is using indicators of macroeconomic performance such as budget balances. It could be misleading to use such an indicator since it is hard to discern whether good economic performance is due

13 All the variables and data sources are listed in Appendix I.

14 Beck and Katz (1995) argue that OLS with PCSE, panel-corrected standard errors estimator is better than FGLS, feasible generalized least squares estimator for comparative political science data. OLS estimates of time-series cross-section model parameters are more likely to be biased because OLS estimates of standard errors will be inaccurate due to contemporaneous correlations and panel heteroscedasticity. PCSE retains the estimates from OLS but corrects the standard errors. By doing that, PCSE gets rid of contemporaneous correlations and heteroscedasticity. FGLS does the same thing and its estimates are more efficient than PCSE, but the estimates of standard errors become downward biased, producing too optimistic coefficient statistical significance. Assuming that the covariance matrix is unknown ¬FGLS estimator depends on the assumption of known covariance matrix¬ it is advisable to run with PCSE to avoid bias in estimates of standard errors.

to successful initiation and implementation of neo-liberal economic policies. Besides, bad economic performance could be due to external shocks or failures of general economic policies rather than failures of economic adjustment. Nevertheless, the performance indicators are the only viable data available for a large number of developing countries, and the success of any reform effort should, on average, be reflected in the indicators of economic performance.

Luckily, an economic reform index does exist for 17 Latin American countries.[15] Morley, Machado, and Pettinato (1999) created several indexes of economic liberalization, including the level of reform in general, capital account liberalization, financial market reform, tax reform, and the level of privatization. The general reform index is a percentage of completion of reform, averaging five specific reform areas: capital account, financial market, tax system, and privatization. It ranges from 0.343 to 0.891, and the standard deviation is 0.142. The extent of privatization is measured by the percentage of privatized public enterprises.

As a supplement to tests on Latin America economic reform index, I use level of budget balances (*Budget Balance*) as one of my dependent variables because agenda setters (executives) propose the budget and the legislature votes on it every year, and it is one of the performance indicators monitored by international financial institutions in their efforts to hold countries receiving aid and loans to certain benchmarks. In using *Budget Balance*, I follow Wibbels's operationalization of economic reform effort and extended data using the IMF's *Financial Statistics*.[16] Wibbels (2000) measures fiscal balance as a "percentage of government expenditures and lending minus borrowing". The variable ranges from -194.40 to 83.17 (in percentage) with the standard deviation of 23.56. Using time-series data for a large number of countries allows test of the non-crisis cases as well.

My main explanatory variable is the existence of left-wing parties as a veto player. For operationalization, I constructed a dummy variable using several sources: Keefer's *Database of Political Institutions* (2004), Coppedge's classification of Latin American political party ideology (1997), and the *Political Database of the Americas* by Georgetown University (2006). If a government party is left-wing, if there is a left-wing party in coalition government, or if there are left-wing opposition parties against minority

15 The countries are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Paraguay, Peru, Uruguay, and Venezuela.

16 I want to sincerely thank Erik Wibbels for providing his entire data set.

government, *Left-Wing Veto Player Dummy* is 1, and 0, otherwise. Figure 3 shows that parties that consist less than 10% of the legislature can have veto power while parties that consist more than 50% can have no veto power, confirming that not all left-wing parties in legislature could be veto players.

Figure 3. Relationship between Left Veto Player Dummy and Percent Left Parties in Legislature

To test a competing hypothesis of the conventional spatial model of partisanship, I also include *Percentage of Left-Wing Parties* in the legislature. I use this variable to test whether discrepancies in economic liberalization efforts come from just partisan difference or from strategic bargaining between agenda setters and left-wing parties working as veto player. I calculated the percentage of the seats held by the left-wing parties.[17]

17 Most developing democracies have multi-party systems, and there is no information on partisanship of very small parties. This requires extensive data collection to identify the small parties. Identification and even counting the number of seats held by these small parties are disputed among the scholars. I have identified the small parties to the extent information exists except for some countries like Venezuela where different sources disagree on identification and even on the number of seats held by the parties. Even though the data set is not complete, it will give a fair estimation of the power

Left-Wing Veto Player and *Percentage of Left-Wing Parties* are highly correlated. Correlation comes out to be about 0.74. In order to test the veto player argument against the alternative spatial model, I include both variables although I will have a multicollinearity problem.

Testing the hypothesis using *Left-Wing Veto Player* is a better specification than using the number of veto players, but I also include *Number of Veto Players*. I use the data constructed by Keefer et al. (2002) for the entire set of developing democracies.[18] Andrews and Montinola (2004) have put together a dataset on the number of veto players for Latin American and post-communist countries and claim that they have counted both the institutional and partisan veto players following Tsebelis' method of counting veto players. Thus, I include their index of number of veto players when I test reform outcomes in Latin America. I expect that the number of veto players does not have much effect by itself because the number only matters when veto players are left-wing.

Another main explanatory variable is the variable identifying whether agenda setters propose economic reform. I have constructed a 5-point scale ordinal variable from -2 to 2. I have looked at Economist Intelligence Unit's *Country Profile* and *Country Report* to identify agenda setters and their economic policies and proposals for each year from 1978 to 2000. *Agenda Setter* is coded 2 if the agenda setter proposes many or extensive liberal reforms or pursues radical liberal policy. 1 indicates that the agenda setter proposes a few minor liberal reforms or maintains the liberal policy as the status quo. 0 indicates that the agenda setter proposes no liberal reform. -1 indicates that the agenda setter proposes minor reversals in liberal reforms or maintains the non-liberal policy as the status quo. -2 indicates that the agenda setter proposes major reversals in liberal reforms. I coded *Agenda Setter* as 2 only if Economist Intelligence Unit reported that reform was "radical" or "extensive", or the agenda setter proposed reform in many areas. When agenda setters propose any reform, a country may experience a change in policy outcomes, and I expect the indicator *Agenda Setter* to have positive effects on the level of budget balance and performance of economic adjustment (for Latin America).

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of left-wing parties because unidentified small parties actually hold less than 1% of the total seats on average. Besides, parties that hold one ore two seats are not usually in government coalition.

18 Keefer's measurement of checks and balance in government is not an exact measurement of veto players defined by Tsebelis (2002). Keefer has developed an indicator of veto power as the number of checks and balances, adjusting for each veto players' independence from each other (it is not very clear how he adjusted it). However, limited resources and time constrained me to use his variable for the time being.

In addition to my main explanatory variables, I include variables to control for other factors that might influence the level of budget balance and performance of economic adjustment (for Latin America). My first control variable accounts for the type of electoral system to test whether or not an "inclusive government" (one that is more responsive to the general public and less responsive to special interests) is better at implementing economic reform. Rogowski (1987) shows that governments with large electoral districts and list-system PR (Proportional Representation) are more insulated from regional and sectoral pressure and from special interests that could lobby for certain economic policies, which leads to faster reform or persistence of reform. I use a dummy variable for *Proportional Representation*. When the electoral system is PR, the country will have more balanced budget.

The variable of *Democracy* is included to test whether greater democratic accountability makes economic reform more or less likely. Although all countries in the data set are democratic, some governments are more insulated from popular pressures than others. A more democratic country should be more accountable to the general public; thus it is more likely to implement reform despite the pressure from special interests. On the other hand, if democratic governments respond to wide-spread anti-reform interests because they are accountable to citizens' interests, we expect less impressive economic reform outputs. I use the indicator of *Democracy* (*Polity*) from the Polity IV Project (2003).

My third control variable is *Federalism*. Wibbels (2000; 2005) and Treisman (2000) argue that federalism negatively affects outcomes of economic adjustment because of a collective action problem. It is also a collective action problem. Subnational governments have incentives to default their international borrowing at the expense of national governments, not following the stabilization package. Because subnational governments can receive transfers when their budget runs out, federalism often creates a "fiscal illusion", which in turn leads to over-demanded public goods and bigger budget deficits. Finally, federalist states often need to take care of heavy provincial debt because federal oversight of spending by local government is difficult (Treisman 2000; Wibbels 2005).

A dummy variable for the *Executive Election Year* is included to account for the argument of the political business cycle (Alesina et al. 1997). It is argued that government increases inflation and public spending in order to boost economic growth just before an election.

Lastly, a dummy variable for *Civil War* is included. A state in the middle of interstate or intrastate warfare will find it unusually hard to implement

or continue sound economic policies. During civil war, it is unlikely that the economy functions well, any liberal reform policy is halted, and government runs high budget deficits because its military spending increases. I include a variable of war, coded by Fearon and Laitin (2003).

To control for economic conditions, I include the *Logged GDP Per Capita* and the *GDP Growth Rate*. I include the *Logged GDP Per Capita* to control for the expectation of a wealthy country getting more lenient treatment by international investors. Larger budget deficits are likely when there are less international investors who can discipline the market (Wibbels 2000). I expect a positive coefficient of the *Logged GDP Per* Capita variable for budget balances. *GDP Growth* is used to control for economic performance of a country. Stronger economic performance will correlate with budget balances positively.

I test my hypotheses with the following equation[19]:

$$\begin{aligned}\text{Economic Reform Outcomes}_{it} = {} & \beta_0 + \beta_1\text{Left-Wing Veto Players}_{it} \\ & + \beta_2\%\text{Left in Legislature}_{it} \\ & + \beta_3\text{Number of Veto Players}_{it} \qquad (1) \\ & + \beta_4\text{Agenda Setter Position}_{it} \\ & + B_k\text{Controls}_{it} + \varepsilon it\end{aligned}$$

Then, I test the interaction between agenda setters and left-wing veto players controlling for the *Percentage Of Left-Wing Parties* in the legislature with the following equation[20]:

$$\begin{aligned}\text{Economic Reform Outcomesit} = {} & \beta_0 + \beta_1\text{Left-Wing Veto Players}_{it} \\ & + \beta_2\%\text{Left in Legislature}_{it} \\ & + \beta_3\text{Agenda Setter Position}_{it} \qquad (2) \\ & + \beta_4\text{Left-Wing*Agenda Setter}_{it} \\ & + B_k\ \text{Controls}_{it} + \varepsilon it\end{aligned}$$

Implication 1 implies that the more left on the policy dimension any veto player is, the veto players have more negative effects on economic reform efforts. The veto players on the left will induce bigger budget

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19 β is a coefficient of the estimator; i is a country; t is year from 1978-2000 or 1978 to 1995 (for economic reform indices of Latin America); k is a coefficient of controls. ε_i is an error term.

20 I do not include the *Number Of Veto Players* for the final equation after I prove that the number of veto players is not necessary in the equation when I include the *Left-Wing Veto Players Dummy*.

deficits than when the veto players are more right on the policy dimension.

Implication 2 implies that when there is a left-wing veto player, the agenda setter will propose a more moderate policy because that is all he or she can achieve, resulting in larger budget deficits and slower reform.

Table 1. Effects of Left-Wing Veto Players and Number of Veto Players on Level of Reform (Latin American sample only)

	Model 1A with # VP on reform	Model 1B with dummy on reform	Model 1C with % left on reform	Model 1BC with dummy and % Left	Model 1ABC # VP, dummy, and % Left	Model 1D interaction
Explanatory Variables						
Left-Wing Veto Player (dummy)		-0.073*** (0.011)		-0.040** (0.016)	-0.054** (0.027)	-0.079 (0.053)
Percentage of Left (% left)			-0.16*** (0.020)	-0.117*** (0.024)	-0.112*** (0.028)	-0.103*** (0.029)
Number of Veto Players (# VP)	0.005 (0.005)				-0.003 (0.004)	-0.006 (0.006)
Interaction Terms						
Left-Wing* Number of VP						0.009 (0.010)
Control Variables						
Federalism	-0.023*** (0.00)	-0.010*** (0.003)	-0.004 (0.003)	-0.007** (0.003)	-0.025*** (0.002)	-0.024*** (0.002)
Electoral System-PR (PR)	0.043*** (0.03)	0.035* (0.015)	0.047*** (0.016)	0.044** (0.018)	0.063*** (0.022)	0.066*** (0.022)
Democracy (Polity)	0.004 (0.003)	0.003* (0.002)	0.005*** (0.002)	0.005*** (0.018)	0.006 (0.005)	0.006 (0.005)
Executive Election	-0.023** (0.023)	-0.011 (0.013)	-0.013 (0.013)	-0.012 (0.013)	-0.018 (0.024)	-0.019 (0.024)
Civil War	-0.002 (0.009)	-0.016* (0.010)	-0.008 (0.008)	-0.016* (0.010)	-0.039*** (0.014)	-0.040** (0.016)
Trend	0.03*** (0.00)	0.024*** (0.001)	0.024*** (0.001)	0.024*** (0.001)	0.035*** (0.00)	0.035*** (0.001)
Intercept	0.19*** (0.04)	0.370*** (0.014)	0.362*** (0.019)	0.365*** (0.018)	0.231*** (0.05)	0.23*** (0.053)
Adjusted R-squared	0.60	0.65	0.66	0.67	0.69	0.69
Wald Chi-squared	950.81	3181.27	4559.18	4286.02	27281.01	32099.51
Prob > Chi-squared	0.00	0.00	0.00	0.00	0.00	0.00
Number of Cases	143	238	238	238	140	140

Note: *** indicates |p|<.01; ** indicates |p|<.05; * indicates |p|<.10
Statistical significances are based on two-tailed tests. Panel Corrected Standard Errors are reported in parentheses.

Table 2. Power of Left-Wing Veto Players and Number of Veto Players on Budget Balance 1978-2000

	Model 2A with # VP	Model 2B with dummy	Model 2C with % left	Model 2AB # VP and dummy	Model 2AC # VP and % Left	Model 2BC with dummy and % left	Model 2ABC with # VP, dummy and % Left	Model 2D interaction
Explanatory Variables								
Left-Wing Veto Player (dummy)		-4.35** (2.06)		-4.89** (2.10)		-0.81 (2.37)	-0.96 (2.47)	-3.14 (3.97)
Percentage of Left (% left)			-11.21*** (3.98)		-12.30*** (4.10)	-10.19** (4.75)	-11.13** (4.98)	-10.56** (4.97)
Number of Veto Players (# VP)	0.54 (0.45)			0.81* (0.47)	0.51 (0.47)		0.51 (1.56)	0.15 (0.79)
Interaction Terms								
Left-Wing* Number of VP								0.61 (0.90)
Control Variables								
Federalism	-4.88*** (1.42)	-3.80*** (1.48)	-4.17*** (1.50)	-3.92*** (1.50)	-4.19*** (1.53)	-3.60** (1.53)	-3.64** (1.56)	-3.69** (1.54)
Electoral System-PR (PR)	-4.05 (2.54)	-7.14*** (2.72)	-6.48** (2.76)	-6.02** (2.85)	-5.67* (2.88)	-6.93** (2.80)	-6.09** (2.93)	-6.27** (2.94)
Democracy (Polity)	-0.54* (0.33)	-0.32 (0.38)	-0.30 (0.40)	-0.51 (0.40)	-0.47 (0.42)	-0.29 (0.39)	-0.46 (0.42)	-0.43 (0.43)
Executive Election	-1.43 (1.36)	-2.55* (1.47)	-2.30* (1.43)	-2.08 (1.47)	-1.92 (1.43)	-2.59* (1.45)	-2.19 (1.44)	-2.21 (1.44)
Civil War	-2.42 (2.20)	-3.77* (2.30)	-4.52* (2.37)	-3.43 (2.34)	-4.18* (2.41)	-4.68** (2.36)	-4.37* (2.39)	-4.40* (2.37)
East Asia	5.81* (3.50)	1.05 (4.00)	0.61 (3.89)	0.45 (4.04)	0.13 (3.91)	0.79 (4.04)	0.21 (4.09)	0.62 (4.09)
Latin America	8.84*** (2.89)	7.47** (3.06)	8.11*** (3.03)	7.42** (3.09)	7.93*** (3.08)	7.39** (3.10)	7.19** (3.15)	7.13** (3.10)
Middle East-North Africa	-0.68 (3.85)	-7.52* (4.65)	-5.75 (4.68)	-6.30 (4.84)	-5.68 (4.85)	-6.28 (4.96)	-5.79 (5.11)	-6.04 (5.06)
South Asia	-4.32 (5.06)	-7.29 (5.23)	-5.58 (5.26)	-8.54 (5.41)	-6.68 (5.45)	-6.86 (5.39)	-8.01 (5.60)	-8.48 (5.58)
Sub-Saharan Africa	7.77** (3.51)	10.49*** (4.02)	12.25*** (4.09)	10.50** (4.23)	11.88*** (4.31)	11.49*** (4.13)	11.10** (4.35)	10.97** (4.35)
lnGDP Per Capita	7.17*** (1.48)	7.16*** (1.76)	6.97*** (1.76)	6.97*** (1.88)	6.76*** (1.87)	6.77*** (1.79)	6.52*** (1.92)	6.44*** (1.90)
GDP Growth	0.42*** (0.11)	0.45*** (0.12)	0.37*** (0.11)	0.47*** (0.12)	0.38*** (0.12)	0.41*** (0.12)	0.42*** (0.12)	0.42*** (0.12)
Trend	0.99*** (0.17)	1.09*** (0.20)	1.12*** (0.19)	1.07*** (0.20)	1.11*** (0.20)	1.08*** (0.20)	1.07*** (0.21)	1.07*** (0.21)
Intercept	-80.18*** (10.93)	-75.84*** (13.79)	-73.78*** (13.28)	-76.35*** (14.89)	-72.94*** (14.32)	-71.12*** (13.87)	-70.02*** (15.00)	-68.28*** (15.06)

Adjusted R-squared	0.21	0.24	0.23	0.24	0.23	0.24	0.24	0.25
Wald Chi-squared	197.98	247.78	239.70	241.97	231.32	235.59	227.26	231.41
Prob > Chi-squared	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Number of Cases	740	613	648	599	634	613	599	599

Note: *** indicates |p|<.01; ** indicates |p|<.05; * indicates |p|<.10
Statistical significances are based on two-tailed tests. Panel Corrected Standard Errors with AR1 correction are reported in parentheses.

Table 1 presents the results of tests on 17 Latin American countries. First, I present a model with just *Number of Veto Players* as the only explanatory variable (*Model A*), just with *Left-Wing Veto Player* (*Model B*), and just with *Percentage of Left-Wing Parties* (*Model C*). Then, I conduct tests by adding each explanatory variable to each other to control for others.[21] The model number indicates the combination of certain explanatory variables. For example, Model 1AB indicates that the model has *Number of Veto Players* (*Model A*) and *Left-Wing Veto Player* (*Model B*) in Table 1.[22] After adding all the explanatory variables (*Model ABC*), I test the hypothesis that the number of veto players does not matter unless the coalition includes a left wing member, by using an interaction term between *Number of Veto Players* (# *VP*) and *Left-Wing Veto Player* (*dummy*) (*Model D*).

The results for the whole sample are presented in Table 2 using *Budget Balance* as dependent variable with *Number of Veto Players*, *Left-Wing Veto Player*, and *Percentage of Left-Wing Parties* as explanatory variables to see which argument better predicts the ideologically driven parties' behaviors regarding economic adjustment. The model specification is the same as for Table 1 with the corresponding alphabets, A, B, C, and D. I include the economic control variables, GDP per Capita and GDP Growth.

Models 1A and *2A*, which represent the usual way to test the veto players argument, show that *Number of Veto Players* (# *VP*) by itself has no effect on either *Budget Balance* in the full sample (*2A*) or *Level of Reform* in Latin America (*1A*). When included with *Left-Wing Veto Player* or *Percentage of Left-Wing Parties*, it still has no effect on budget balances (*Models 2AC* and *2ABC*). Tested on Level of Reform in Latin America, Number of Veto Players (# VP) has almost no effect (Models 1A and 1ABC).[23]

21 All three variables are highly correlated.

22 For a robustness check, I run the same model specification without regional dummies and just with the explanatory variables, and with other control variables. The results do not vary much and can be obtained from the author upon request.

The number of veto players has a statistically significant estimate of 0.81 in *Model 2AB*, which includes both *Number of Veto Players* and the dummy for *Left-Wing Veto Player*. After I control for the existence of left-wing veto players, every additional veto player improves budget balances by 0.81% of expenditures, contrary to the expectations of the veto player argument. This is a substantively small effect considering the range and the standard deviation of Budget Balance.[24] Moreover, the model is not correctly specified because the number of veto players should only matter if at least one of the veto players is on the left of the status quo. Thus, I present the model with interaction terms[25] between Number of Veto Players and Left-Wing Veto Player (Models 2D and 1D). With the interaction term specifying the conditional effect of the number of veto players on the existence of left-wing veto players, the number of veto players has minimal or no effect on economic reform outcomes, which reflects my expectation that the number of veto players does not matter if they are not left-wing.

Traditional theories of how interests translate into policy would predict that outcomes associated with economic liberalism would be less likely to occur when the legislature contains large left-wing parties. In contrast, the veto player argument presents that even one very small left-wing party can prevent policy from moving to the right if it is a member of the ruling coalition. To test which of these arguments better explains shift of economic policy more to the right (neo-liberal economic policies), I use the percentage of the left in the legislature (*% Left*) as an indicator of the size of the leftist contingent. When at least one veto player is left-wing (dummy), reform achievement in Latin America will decrease by about 7% (*Model 1B*) and it is substantively and statistically significant. 7% decrease is almost the half of the standard deviation of *Level of Reform in Latin America*. *Model 1C* shows, however, that for every additional 1% of seats held by leftist parties, reform achievement declines by about 16%. Again, the effect is too huge to be credible. Additional 10% of seats held by the left will reduce reform achievement by 160%, which is way out of range. Nevertheless, the estimate seems to show that left-wing parties in the legislature actually do affect the policy making process whether

23 Table 1 does not contain Model 1AB (# VP + dummy) and 1AC (# VP + % Left) because the results are similar. *Number of Veto Players* does not have statistically and substantively significant effect on *Level of Reform* in Latin American countries.

24 It ranges from 0.343 to 0.891, and the standard deviation is 0.142.

25 I ran the models with different specification, including and excluding control variables and tested the privatization index for Latin American countries. The results are similar to the ones reported in Table 1.

or not they are veto players.[26] Evidence for the effects of left-wing veto players is weak compared to the effect of the percentage of seats held by left-wing parties in the legislature. The reason for this discrepancy could be due to the limitation of the dummy variable. The dummy variable loses a lot of information because it only ranges from 0 to 1 while the percentage of left-wing parties ranges from 0 to 100, thus allowing more variance.

From Table 2, tests on budget balance confirm the findings in Table 1. When included separately, *Left-Wing Veto Player* and *Percentage of Left-Wing Parties* (*Model 2B* and *Model 2C*) both have statistically and substantively significant negative effect on *Budget Balance*. Nonetheless, the magnitudes are distinctively different. *Model 2B* (*Left-Wing Veto Player*) suggests that having at least one left-wing veto player decreases budget balances by about 5%. In contrast, for every additional 1% of seats held by leftist parties in the legislature, budget balances decrease by 11%. Additional 10% of seats held by the left will increase budget imbalances by a 110% of expenditures. Having left-wing parties in legislature can almost transform a country's fairly balanced budget into highly imbalanced budget, considering that the minimum value of *Budget Balance* is -194.40.

The dummy variable for left-wing veto player and the percentage of the left in the legislature are highly correlated, at about 0.77. According to Western and Jackman (1994), excluding one or the other of two highly correlated variables results in a biased estimation.[27] Hence, I include both *Left-Wing Veto Player* and *Percentage of Left-Wing Parties* in the equation (*Model BC* or *Model ABC* in Table 1 and Table 2). Tested on the level of reform efforts in Latin America, both the left-wing veto player dummy and the percent seats held by the left have statistical and substantive significance (*Model 1BC* and *Model 1ABC*). After controlling for the percentage of left-wing parties in the legislature, the existence of a left-wing veto player in the ruling coalition decreases reform efforts by 4%, which is about the third of the standard deviation. Controlling for the existence of left-wing veto players, the ideological composition of the legislature itself will decrease reform efforts by 11.7% for every 1% increase in the seats held by left-wing parties, and 117% for 10% increase in the seats held by the left. Once I control for how big the left-wing coalition is, the role of veto players does not have a clear effect. Yet, this does

26 More statistical testing seems necessary to find which variable is a better indicator of power of left-wing parties. An anonymous reader suggested the Bayesian modeling.

27 Nevertheless, if I put both of them, it will destroy the standard errors. If I want to exclude either of the two, I will need a good justification (King 1986; 1991).

not mean that the effect of veto players is zero.

One of the notable findings in Table 2 is that the coefficient of the proportional representation system is negative, contrary to Rogowski's expectation. The test shows that having a proportional representation system increases budget deficits by about 7%. The variables *Executive Election*, *Federalism*, and *Civil War* all have the expected sign, and in some cases, have statistically and substantively significant effects on *Budget Balance*. Federalism is indeed associated with greater budget deficits. The control variable of *Executive Election Year* supports the business cycle argument that governments manipulate macroeconomic policies before elections. *Democracy* (*Polity*) has neither statistical significance nor the expected sign.

Table 3. Effects of Agenda Setter and Left-Wing Veto Players on Budget Balance and Level of Reform (Developing Democracies Sample for Budget Balance and Latin American Sample for *Level of Reform*)

	Dependent Variable: Budget Balance			Dependent Variable: Level of Reform		
	Model 3E with agenda	Model 3BCE with dummy % left and agenda	Model 3F interaction	Model 3E with agenda	Model 3BCE with dummy % Left, and agenda	Model 3F interaction
Explanatory Variables						
Left-Wing Veto Player (dummy)		1.95 (2.46)	0.51 (2.72)		-0.016 (0.024)	0.007 (0.031)
Percentage of Left (% left)		-8.32* (5.17)	-8.07 (5.14)		-0.096** (0.043)	-0.108** (0.046)
Agenda Setter (ordinal -2 to 2)	2.41*** (0.92)	2.27** (0.92)	1.08 (1.24)	0.065*** (0.018)	0.063*** (0.018)	0.077*** (0.018)
Interaction Term						
Left-Wing Veto Player*Agenda			2.12 (1.68)			-0.027 (0.023)
Control Variables						
Federalism	-4.58*** (1.48)	-4.44*** (1.50)	-4.52*** (1.48)	-0.013*** (0.003)	-0.013*** (0.004)	-0.013*** (0.005)
Electoral System-PR (PR)	-7.58** (3.10)	-7.56** (3.29)	-7.39** (3.25)	0.045** (0.022)	0.052* (0.027)	0.055* (0.029)
Democracy (Polity)	-0.67 (0.51)	-0.53 (0.51)	-0.50 (0.51)	-0.003 (0.002)	0.002 (0.003)	0.002 (0.003)
Executive Election	-2.18 (1.66)	-1.60 (1.61)	-1.79 (1.63)	0.011 (0.035)	0.011 (0.034)	0.013 (0.034)

Civil War	-4.69* (2.85)	-5.02* (2.77)	-4.60* (2.77)	0.011 (0.011)	-0.001 (0.012)	0.001 (0.012)
East Asia	2.42 (4.55)	1.84 (4.80)	1.51 (4.73)			
Latin America	2.76 (2.92)	2.47 (2.87)	2.49 (2.82)			
South Asia	-7.23 (5.12)	-5.21 (5.39)	-5.40 (5.33)			
Sub-Saharan Africa	5.62 (3.79)	5.98 (5.39)	6.26 (4.06)			
lnGDP Per Capita	7.26*** (1.73)	7.39*** (1.69)	7.38*** (1.67)			
GDP Growth	0.50*** (0.15)	0.48*** (0.15)	0.49*** (0.15)			
Intercept	-58.37*** (13.10)	-58.67*** (13.04)	-58.18*** (12.89)	0.578*** (0.037)	0.576*** (0.048)	0.562*** (0.050)
Adjusted R-squared	0.22	0.23	0.23	0.21	0.23	0.24
Wald Chi-squared	230.82	228.75	227.98	86.20	125.93	138.23
Prob > Chi-squared	0.00	0.00	0.00	0.00	0.00	0.00
Number of Cases	460	452	452	225	225	225

Note: *** indicates |p|<.01; ** indicates |p|<.05; * indicates |p|<.10
Statistical significances are based on two-tailed tests. Panel Corrected Standard Errors with AR1 correction are reported in parentheses for budget balance and without AR1 correction for reform. Middle East and North Africa dummy is dropped.

So far, my focus has been on veto players without specifying which of them is the agenda setter. This reflects what has been done in much of the literature, but not the real policy-making process. Table 3 actually presents the final model specification with agenda setter's reformist position as the explanatory variable (*Model E*) and with an interaction term between *Left-Wing Veto Player* and the agenda setter's position (*Model F*). In theory, the agenda setter's policy proposal should be endogenous. That is, if she knows that there is a left-wing veto player, she will propose only very moderate changes in the status quo because she knows anything else will be defeated (Figure 1 and Figure 2). I include an **interaction term** between *Left-Wing Veto Player* and *Agenda Setter's* position (Table 3, *Model F*), to test my argument that agenda setters and veto player bargain on policy-dimension, and that each player's effect on outcome will be constrained by the existence of the other.

When I add the agenda setter's position variable (Table 3, *Models 3E* and *3BCE*), *Agenda Setter* has a statistically significant and positive effect, meaning that if the agenda setter favors liberal economic policy, budget

deficits are lower. When agenda setter proposes modest economic reforms (*Agenda Setter* = 1), reform achievement will increase by 6.5%, which is almost the half of one standard deviation of *Level of Reform in Latin America*. If an agenda setter proposes radical reforms (*Agenda Setter* = 2), reform achievement will increase by 13%, which is almost one standard deviation increase in reform efforts; thus it is a big effect.

Only *Model 3F* tested on the *Level of Reform in Latin America* has the expected sign for the interaction term, which should be negative, following the implication that the effect of reformist agenda setters will be reduced by the existence of left-wing veto players (*dummy* = 1). I expect the agenda setter to choose his own preferred policy only when there is no left-wing veto player in his coalition. Hence, I expect the effect of the agenda setter's position to be greater when there is no left-wing veto player to influence his position. When there is no left-wing veto player (*dummy* = 0), the unconditional effect of *Agenda Setter* is 0.077. The fact that the interaction term is not statistically significant does not mean that the marginal effect coefficients for *Agenda Setter* and *Left-wing Veto Player* are substantively insignificant. One needs to calculate the marginal effect coefficients and their standard errors.[28]

Table 4. Marginal Effects of Left-Wing Veto Player as Agenda Setter Changes

Condition	Coefficient of Left-Wing (Model 3F on reform)	Lower 95% Confidence Interval	Upper 95% Confidence Interval
Agenda Setter Proposes Major Reversals in Liberal Reform (-2)	0.061 (0.071)	-0.078	0.200
Agenda Setter Proposes Minor Reversals in Liberal Reform (-1)	0.034 (0.050)	-0.064	0.132
Agenda Setter Proposes No Liberal Reform (0)	0.007 (0.031)	-0.054	0.069
Agenda Setter Proposes Minor Liberal Reform (1)	-0.019 (0.023)	-0.064	0.025
Agenda Setter Proposes Major Liberal Reform (2)	-0.046 (0.033)	-0.111	0.019

I calculate the marginal effects coefficients and standard errors for *Left-Wing Veto Player* with the following equation, using *Model 3F* on *Level*

28 Brambor, Clark, and Golder (2006) argue that it is wrong to interpret the constitutive elements of interaction terms as unconditional or average effects.

of Reform in Latin American sample, and the results are shown in Table 4[29]:

$$\frac{\partial Y}{\partial X} = \hat{\beta}_{left-wing} + \hat{\beta}_{left*agenda}\overline{Agenda_Setter} \quad (3)$$

Left-Wing Veto Player has different conditional effects as the agenda setter's policy position changes. When the agenda setter proposes reform, the left-wing veto players will more actively veto any change. When the agenda setter does not propose any reform, the left-wing veto players do not have to veto anything as there is no proposal for change. Thus, the left-wing veto players' negative effect on overall economic reform will be less when the agenda setter's policy position does not vary much from the left-wing veto players' policy preferences.

Figure 4 shows the marginal effects of the left-wing veto players as the policy position of the agenda setter changes and the 95% confidence interval lines. The slope of the graph shows the general trend that is expected from my argument: as the position of the agenda setter moves to the right (*Agenda Setter* proposing major liberal reform – *Agenda Setter* = 2), the conditional effect of the existence of left-wing veto player becomes more negative. However, the confidence interval crosses zero, indicating that the existence of left-wing veto players could have no significant effect on economic reform efforts. The zero effect of the left-wing veto players interacting with the agenda setters –the 95% confidence interval includes 0– might be indicating that when the two opposing forces interact, their effects cancel each other out.[30] It also could be that either the agenda setter is himself an impediment to liberal reform or his position reflects his strategic calculation of what he can get, given the existence of left-wing veto players.[31]

29 Calculation for standard errors is shown in Appendix II.

30 A unanimous reader pointed out that the zero effect might be coming from the data containing both incidents of interaction, which are compromise (Figure 1) and gridlock (Figure 2). In other words, gridlock between the agenda setter and the veto players will result in zero effect.

31 I want to thank Barbara Geddes for pointing this out.

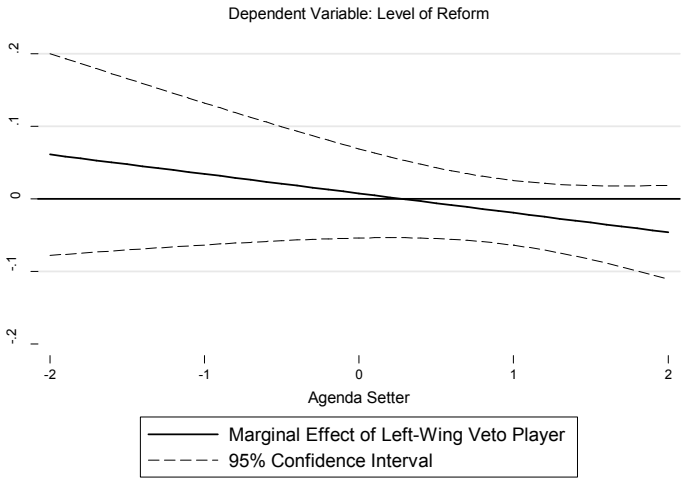

Figure 4. Marginal Effects of Left-Wing Veto Player on Reform as Agenda Setter Changes

Table 5. Marginal Effects of Agenda Setter on Reform as Left-Wing Veto Player Changes

Condition	Coefficient of Agenda Setter (Model 3F)	Lower 95% Confidence Interval	Upper 95% Confidence Interval
No Left-Wing Veto Player (0)	0.077 (0.018)	0.041	0.114
Left-Wing Veto Player (1)	0.051 (0.022)	0.007	0.095

The agenda setter's effect may vary, depending on whether there is a left-wing veto player or not. To test it, I calculate marginal effects coefficients and standard errors for *Agenda Setter* with the following equation, using *Model 3F* on *Level of Reform in Latin American* sample, and the results are shown in Table 5.[32]

$$\frac{\partial Y}{\partial X} = \hat{\beta}_{agendasetter} + \hat{\beta}_{left*agenda}\overline{LEFT} \quad (4)$$

The marginal effect of *Agenda Setter* is a 5.1% increase in reform effort when the agenda setter proposes modest reforms (*Agenda Setter* = 1) and faces a left-wing veto player (*dummy* = 1), reduced from a 7.7%

32 Calculation for standard errors is shown in Appendix II.

increase in reform efforts if there is no veto player. When the agenda setter proposes extensive liberal policies (*Agenda Setter* = 2) and interacts with left-wing veto players, the marginal effect of *Agenda Setter* is 10.2% increase in reform performance in Latin America, reduced from a 15.4% increase in reform performance without left-wing veto players. It is almost one standard deviation increase in the level of reform achievement in Latin American countries.

Figure 5 illustrates that the positive conditional effect of *Agenda Setter* decreases when they interact with left-wing veto players (*dummy* = 1), and the 95% confidence interval lines confirm that Agenda Setter has positive effect. The agenda setter's conditional effect is lower, though still positive, when it has to interact with left-wing veto players. It could be because the agenda setters strategically choose a moderate reform due to constraints by other veto players, or because the left-wing veto players veto their reform efforts. The negative effect of left-wing veto players is thus reflected in reform outcomes. The results show that the effect of the agenda setter's position is constrained by the existence of left-wing veto players.

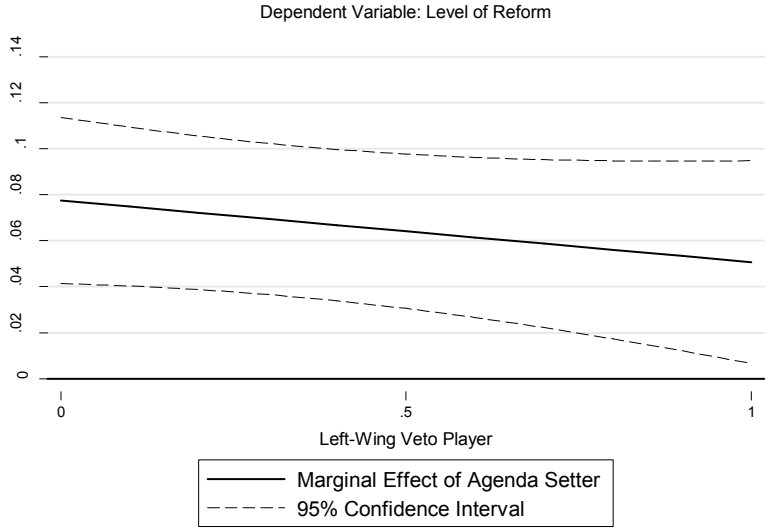

Figure 5. Marginal Effect of Agenda Setter on Reform as Left-Wing Veto Player Changes

CONCLUSION – EFFECTS OF AGENDA SETTERS, VETO PLAYERS AND THEIR IDEOLOGY

In this paper, I started with a puzzle why there are discrepancies in the efforts of economic reforms and their outcomes when a country has experienced a contracting economy. In literature studying the effects of veto players in political economy, I found five major problems. First, most of the literature does not consider the bargaining process between the agenda setter and the veto player. Second, the institutional argument of the policy change using the veto player argument is inadequate because empirical results to date have opposite empirical findings. Third, empirical tests of the veto player argument do not consider the ideological preferences of the agenda setter and the veto players; they simply count the veto players. Fourth, even though there is a consensus that the left is more anti-reform, empirical studies have inconsistent findings. Fifth, for any test of effect of ideologically-driven behaviors on policy, the consensus has been using the percentage of left-wing parties in the legislature, which is not a good way to test the effect of partisan veto players. Thus, I conducted empirical tests to see whether veto players act according to their ideological policy preferences. I did not find an effect for left-wing veto players apart from the effect of left-wing partisanship in the legislature. However, by breaking down veto players into agenda setters and other veto players, I found that the reformist agenda setters do have positive effect on economic adjustment efforts and outcomes. Also, the reformist agenda setters' positive effects are diminished by the existence of left-wing veto players. Yet, it is not clear what explains reformist agenda setters' behaviors when they face oppositions. For future research, one should test whether agenda setters strategically propose reform policies that would not be vetoed or they publicly propose reformist policies because of external pressure although their real policy positions are more to the left.

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APPENDIX I

Table A1. Variables Used to Predict Economic Reform Efforts

I. Dependent Variables
1. Economic Performance:
   a. Budget Balance: a percentage of government expenditures and lending minus borrowing
      (Source: World Bank Government Finance Statistics and Wibbels 2005)
   b. Reform: the level of reform in five areas of reform efforts (Morley et al. 1999)
   c. Privatization: the percentage of privatized public enterprises (Morley et al. 1999)

II. Independent Variables
1. Agenda Setters (-2-2): ordinal variable
   (Source: Economist Intelligence Unit. Country Profile and Country Reports)
2. Partisanship
   a. Left: (0-1) 0 – the government/coalition is composed of the right-wing parties; 1 – the government/coalition is composed of the left-wing parties or the opposition is composed of the left-wing for the minority government
   b. % Left (0-100) – the percentage of left-wing parties in legislature (Source: Keefer 2004)
3. Number of Veto Players
   a. Number of Veto Points – Checks (Source: Keefer 2004)
   b. Number of Veto Players (Source: Andrews and Montinola 2004)

III. Control Variables
1. Federalism: (0-2) 0 – no federal system; 1 – semi federal; 2 – federal system (Source: Wibbels 2005)
2. Electoral Systems: (0-1) 1: Proportional Representation (Source: Golder 2005; Keefer 2004)
3. Executive Election: (0-1) 1: the year the executive election was held (Source: Wibbels 2005)
4. Democracy: Polity (Source: Polity IV)
5. Civil War: (0-1) war = 1, no war = 0 (Source: Fearon 2003)

APPENDIX II

Calculation for Standard Errors for Marginal Effect Coefficient

Let's call the marginal effect coefficient of *Left-Wing Veto Player*, $\hat{\theta}_{left}$. The standard errors (SE) for $\hat{\theta}_{left}$ will be the square root of:

$$\begin{aligned} V(\hat{\theta}_{left}) &= V(\hat{\beta}_{left} + \hat{\beta}_{left*agenda}\overline{Agenda}) \\ &= V(\hat{\beta}_{left}) + \overline{Agenda}\, 2V(\hat{\beta}_{left*agenda}) + 2\,\overline{Agenda}\, Cov(\hat{\beta}_{left}, \hat{\beta}_{left*agenda}) \quad (5) \end{aligned}$$