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# Politics, Policies and the Dynamics of Aggregate Productivity in Colombia

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**Abstract**[1]

This paper describes private actors' involvement in Colombia's policymaking process. While more transparent and formal channels are used to discuss horizontal policies, they are also less effective. The adoption of targeted policies, however, follows a faster track and depends more on political power than on those policies' potential as engines for productivity growth. Data on policies and political characteristics across sector-region units are used to further characterize the different groups' weight in policymaking, and the effect of the implied unbalance on aggregate productivity. Electoral weight and being represented by business groups and associations are found to be important determinants of the policy benefits received by a sector in a region, especially when activities are located in regions affected by armed conflict. It is also found that the resulting imbalance of policies damages aggregate productivity.

**JEL Classification:** O43, O25, P16
**Keywords:** Productivity, political economy, interest groups, targeted policies.

[1] We are grateful for the comments of Rafael Pardo, Carlos Scartascini, Mariano Tommasi, Mauricio Santa María, and participants at the IDB seminars of the project on the Political Economy of Productivity and at the 10th Annual Meeting of LACEA's Political Economy Group. This paper was undertaken as part of the IDB Latin American and Caribbean Research Network project "The Political Economy of Productivity."

## 1. Introduction

The vision that has guided economic policy making in Colombia during the last two decades has highlighted well-functioning markets as the basis for development. The 1991 Constitution set the stage by endorsing this vision, and a series of subsequently adopted reforms moved the regulatory framework in that direction.[2] In a context where the import substitution model was seen as having eroded Colombia's potential for continued growth, one of the main goals of the reforms was to boost productivity growth as an engine for overall economic growth.

From the point of view of creating conditions to maximize productivity growth, recognized as the basis for long-run economic growth, much of the economic literature suggests the policy vision reflected by those reforms was on the right track. This literature shows that two types of regulations inhibit aggregate productivity growth: i) policies that discourage firms from investing in new technologies, such as weak property rights and weak competition (e.g., Pavcnik, 2002, and Fernandes, 2007); and ii) regulations that inhibit the process of reallocation of activity towards high productivity producers. Besides rigidities in factor markets and overall weak competition, targeted policies are also leading examples of regulations that block reallocation, since they frequently protect low-productivity establishments from having to downsize or disappear (Melitz, 2003; Hsieh and Klenow, 2007; Restuccia and Rogerson, 2008; Eslava et al. 2009b).[3] In line with this conceptual framework, the reforms of the early 1990s sought to increase both competition and factor market flexibility.

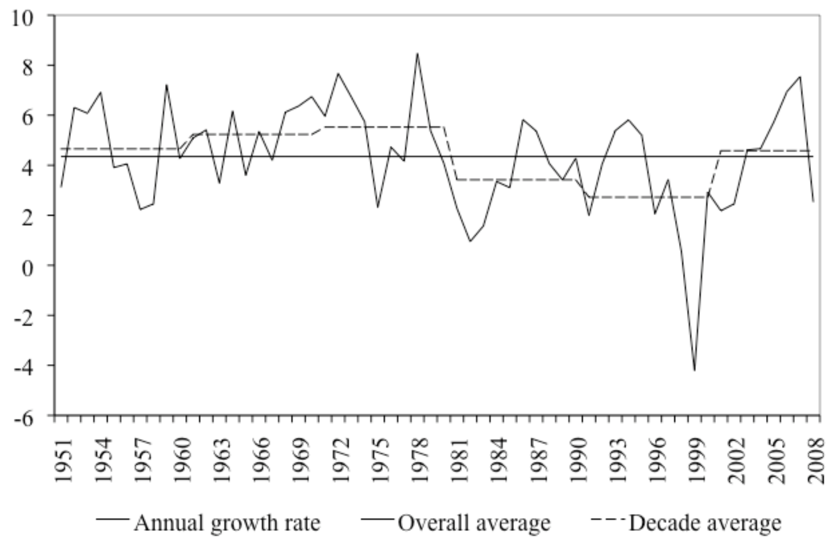
Despite the adoption of this market-oriented policy vision, the productivity performance of the country after the wave of reforms has not been as dynamic as was expected. Overall GDP growth has not been higher in the last two decades compared to previous ones, as shown in

[2] Economic freedom, private property, and free competition have the standing of constitutional rights, while free enterprise is considered the engine of development (Article 333). Moreover, promoting productivity growth is one of main duties the Constitution assigns to the government (Article 334). A series of wide-ranging economic reforms adopted around the time of the 1991 constitutional reform further reflected the spirit of the new model of economic policy. Barriers to international trade were reduced, while measures were adopted to give labor and financial markets greater flexibility.

[3] Targeted policies may harm aggregate productivity even if more productive firms are targeted, as these firms may be led to grow beyond the size they would reasonably reach given both their productivity and the demand they face (Restuccia and Rogerson, 2008). Of course, targeted policies may be productivity enhancing if they contribute to the solution of other distortions originating outside regulations. For instance, the need to stop production to install new machinery discourages investment and hits harder firms in sectors where the technology frontier has recently moved, since they would need greater investments. Regulations that encourage investment in these specific sectors are likely to boost productivity. This is also true of policies addressing the sources of sector-specific coordination failures.

Figure 1. For instance, the annual growth rate averaged 3.6 percent over 1991-2008, compared to 4.6 percent over 1971-1989. Similarly, estimates of productivity after the reforms show relatively modest overall productivity growth. Figure 2 shows aggregate productivity for manufacturing, estimated by Eslava et al. (2006) for 1982-1998. Average annual growth is very similar for 1991-1998 compared to 1982-1990.

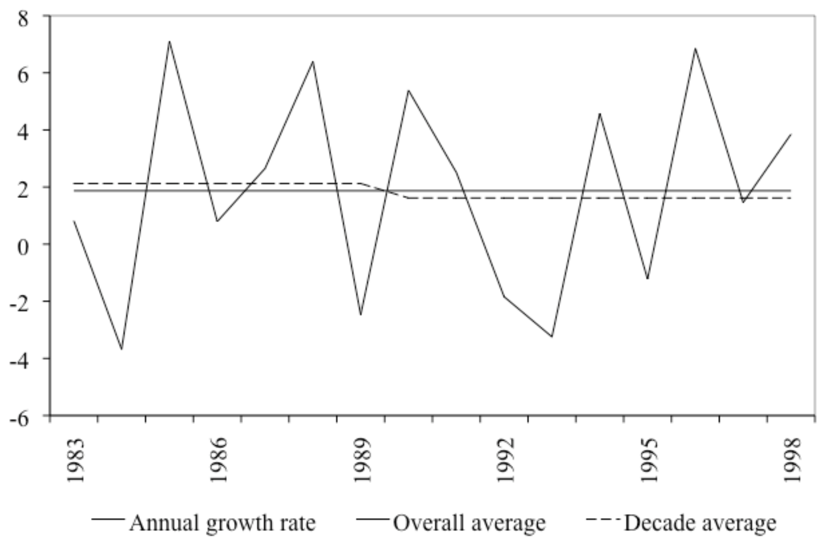
**Figure 1. Annual GDP Growth Rate (%): 1951-2008**




*Source:* Departamento Nacional de Estadística (DANE), from Banco de la República web page.

Performance similar to that of previous decades is suggestive of a modest growth effect of the reforms, especially striking considering that achieving higher growth was an explicit goal of that wave of reforms. The comparison, of course, is subject to the criticism that in the absence of reforms growth could have been much slower than previously. However, Eslava et al. (2009a) reach a similar conclusion in a formal measurement of the share of potential gains from the reforms that has been realized. Concentrating on productivity gains from the increased flexibility of factor markets, the authors compare actual and potential gains in aggregate productivity for incumbent firms. They estimate what aggregate productivity would be if these firms faced no barriers to adjusting their use of productive factors. Their estimates suggest large potential gains of close to 30 percentage points at any given point in time. However, only a negligible share of this potential increase has been realized as a consequence of more dynamic adjustment after the reforms of the early 1990s.[4]

**Figure 2. Annual Growth Rate of manufacturing TFP (%): 1983-1998**




*Source:* Table 6 of Eslava et al. (2006).

If Colombia has been able to implement dramatic policy changes in the right direction, then why has this not resulted in a more dynamic aggregate performance? Why have the gains in productivity not been as expected?

Several authors have suggested that the policies actually adopted have not been fully consistent with the overall vision of a market economy (for instance, Edwards, 2001, and Alesina, 2005). Within that general statement, our view is that a set of potentially productivity-enhancing policies has coexisted with a large set of sector or firm-specific policies that distort the allocation of resources. These micro regulations have likely eroded the positive effects on aggregate productivity of economy-wide deregulation efforts, by distorting the mechanisms that translate a firm's poor performance into incentives to exit the market or reduce the scale of its operations.[5] Interestingly, many of these targeted policies have emerged as ways to compensate losers of the reforms, partly undoing their intended effects (Edwards and Steiner, 2008).

[4] Some specific reform areas have been found to be more effective than others. Eslava et al. (2009b) find that trade liberalization contributed to weeding low-productivity plants out of the market, raising aggregate productivity.

[5] This effect would be consistent with models where idiosyncratic distortions, for instance from sector-specific regulations, affect aggregate productivity (e.g., Hsieh and Klenow, 2007; Restuccia and Rogerson, 2008).

What is the political equilibrium that explains the coexistence of economy-wide regulations aimed at increasing productivity and targeted policies with an opposing effect? The very nature of targeted policies suggests understanding the balance of political forces across groups of firms is key to understanding the emergence of these policies.

In this paper we aim to shed light on the extent to which the influence of specific interests on the Policymaking Process (PMP) may have favored the adoption of targeted policies with detrimental effects on aggregate productivity.[6] We characterize the way in which specific interests have influenced policymaking in Colombia over time, with an emphasis on economic policy in general and productivity/competitiveness policy in particular. Our description shows that a series of channels open spaces for the participation of private actors in the design of policies. The relevant channels vary depending on whether horizontal or targeted policies are under discussion. While more transparent and formal channels are used to discuss horizontal policies, those channels are also less effective. As a result, the adoption of targeted policies follows a faster track and depends on the balance of political power across groups more than on the potential of these policies as engines for growth.

To complement our description of the Colombian PMP, we characterize the winners and losers of the PMP in Colombia in an empirical setting, as a function of the determinants of political participation that matter according to our description of the PMP. We find that sector-region groups with significant weight in terms of the votes they contribute to the Senate are able to influence policies in their favor, as are sectors represented by a business association or a business group—and much more so when their activity is located in regions affected by the armed conflict. High- productivity sectors are not found to be favored. We then use the estimated coefficients to produce a measure of the political strength of each sector-region group and examine the effect of the imbalance of political power on aggregate productivity. The results lend support to our hypothesis that aggregate productivity is harmed by the persistence of targeted policy benefits granted without a clear microeconomic rationale and rather associated with the political grip of particular groups.

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[6] The ongoing civil conflict has evidently challenged investment decisions in both rural and urban areas (see Harker and Meléndez, 2008), and is probably part of the explanation for the poor performance of aggregate productivity. While not our main focus, we explore this dimension in part of the empirical work we conduct, described in Section 4 of this paper. However, other explanations are also worth considering.

The paper proceeds as follows. We begin by describing the actors who participate in the economic PMP (Section 2). Section 3 then explains the ways in which these actors interact. Section 4 characterizes winners and losers of the PMP in Colombia as a function of differential political power and examines the effect of the latter on aggregate productivity performance. Finally, as a conclusion, Section 5 presents a synthesis of our research and a discussion of the issues that our analysis suggests shape the making of policies that impact productivity in Colombia.

## 2. Actors in the Policymaking Process

We begin by defining and characterizing the different actors that participate in the PMP in Colombia. We divide our discussion into state and private actors.

### *2.1 State Actors*[7]

#### *2.1.1 President and Cabinet*

In Colombia the President is the main agenda setter in most policy areas. While he depends on Congress and the Constitutional Court (which revises that the legislation conforms to the Constitution) for adopting policies that require a law, within that limit his power and independence are considerable given his influence over Congressmen and given first-mover advantage. In Congress, the President has the exclusive right to introduce bills concerning the structure of the ministries, salaries of public employees, foreign exchange, budget, trade and tariffs, and national debt, and has control over the legislative agenda by means of a discharge or urgency petition that enables him to prioritize bills. The president may also veto legislation, although he can be overridden with a simple majority.  The President can declare states of "internal commotion" or of "economic emergency" that give him the ability to issue decrees on areas of policy that normally require the adoption of laws.[8]

[7] Cárdenas, Junguito and Pachón (2006) provide a complete description of the state actors that participate in the general PMP in Colombia. Here we present a summary of the aspects of that analysis that apply when considering policies that affect productivity, and complement it as necessary for the purpose of this study.

[8] See Articles 212 to 215 of the Constitution. Presidential decrees issued under the umbrella of internal commotion or economic emergency must address the problems that motivated the declaration of the special state. They remain in force once the state of emergency has ceased only if confirmed by Congress during the year after they are issued. Both the declaration of the special state and the decrees issued under it must be approved by the Constitutional Court to be valid.

In terms of the President's relationship with other levels of government, the 1991 Constitution determined that mayors and governors were to be elected, rather than appointed by the President as was formerly the case. From the point of view of the Executive's ability to pass legislation, the change implied a loss of bargaining power for the President, who often used these appointments as political currency to strike deals with parties in Congress. The Cabinet and the heads of all autonomous agencies, however, are still appointed by the President. Those officials execute projects arising from laws enacted by the legislators and design and execute policies directed to the specific sectors under their influence. Cabinet members differ in their political power across governments, and may or may not be empowered by the President to lead policymaking in their respective sectors of influence.

Until 2004 the President could only be re-elected after spending at least one period out of office. Since that year he may be reelected for consecutive terms, resulting in increased presidential power. On the other hand, the President's power has decreased with respect to the pre-1990s era. The 1991 Constitution gave the Constitutional Court effective veto power by strengthening the process of constitutional revision. In regard to the relationship with Congress, besides stripping the President of the powers of appointment that had served as a tool for coalition building, the Constitution timed congressional elections to take place before presidential election, resulting in a greater role of legislators in the election of the President and in a pattern of post-electoral coalitions to pass legislation (Cárdenas et al., 2006). As we will see, there has also been increasing intra- and inter-party fragmentation. All of these changes have led to increasing difficulties in the passing of legislation, creating the need for alternative coalition-building mechanisms; in this context the delivery of "pork," or targeted policies as we have termed them, acquires more importance.

The President and his Cabinet set the route for the four-year presidential period in terms of policies and public expenditure through a National Development Plan. The Plan, written by the government, is subject to consultation with different groups of society by Constitutional mandate, and then brought to Congress during the first semester of the presidential period, to be enacted as law.[9] If Congress delays approval more than three months, the President is authorized

[9] The figure of the National Development Plan was created in 1958 (Law 19) and the first National Development Plan Law was enacted in 1961. Since 1991, by constitutional mandate these plans have two components: a general statement about the "long-run national objectives, the medium-run goals and priorities of governmental action, and the strategies and orientation of the economic, social and environmental policies that will be adopted by the

to enact the Plan through a "decree with force of law" (Constitutional Article 341). Action plans of all public entities for the presidential period are then developed under the provisions of the National Development Plan Law. The fact that expenditures not considered in it are not possible during the corresponding presidential period often results, in fact, in the inclusion of broad provisions in National Plan Laws, meant for flexibility to accommodate a wide range of unforeseen expenses.

### *2.1.2 Congress*

While the national agenda is implicitly delegated to the President and the cabinet members both by a personalistic electoral system and the substantial legislative powers of the Executive, Congress is a key player in the process of implementation of all government policy initiatives for which a presidential decree is not sufficient. In Colombia's bicameral legislature, the House of Representatives has a minimum of two members per Department (a geopolitical division akin to province or state) and the Senate is of a National constituency since 1991. Seats in the Senate are, however, still gained mostly by obtaining regionally concentrated votes, and senators are consequently inclined to advance policies that serve regional interests.

Chambers are each divided by broad legislation topics into seven permanent committees whose leadership is determined by internal elections. A proposed bill is first discussed in the committee most relevant to its main theme, and only after committee discussion goes on to plenary sessions. The latter, however, rely heavily on committees' assessments. Committee membership, moreover, determines the relative hierarchy of congressmen; the economic, budgetary and constitutional committees offer legislators an incumbency advantage and their members are natural leaders of Congress. As party membership is necessary to join one's first choice of committee, party structures play a role organizing legislative activity. In addition to determining hierarchy and sponsorship of key bills, party membership has gained further importance since the 2005 introduction of the "Ley de Bancadas" (Parties Law), which requires members of a single party to vote as a bloc.

Congressmen's ability and need to deliver pork to their constituencies has changed over time. Until 1991 congress members were openly assigned a fraction of the budget to fund projects of their interest (the so-called "*auxilios parlamentarios*"). The 1991 Constitution

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government," and a public investment plan containing the budget allocations required by the main programs and investment projects of the national government, as well as the corresponding sources of financing (Article 339).

eliminated these assignments, generating incentives for legislators to negotiate their approval of government projects in exchange for projects targeted to their constituencies.[10] In addition, the fact that senators started to be elected nationally increased the need for campaign contributions. Since these contributions are sometimes rewarded with targeted benefits to particular sectors or firms, there are further incentives for congressmen to negotiate alliances with the government in exchange for the enactment of these targeted projects.[11] All these factors have, as discussed above, made it increasingly difficult for the government to pass projects in Congress.

### *2.1.3 Political Parties*

The Colombian party system has been characterized by high intra-party competition, especially since the introduction of the 1991 Constitution. Although in the last several years reforms have been introduced to strengthen parties and reduce intra-party competition, their effects are still to be fully assessed. Small parties and factional "movements" proliferate, partly due to electoral rules that introduce financial and other incentives for party fragmentation. Fragmentation in turn is reflected in weak political leadership: regional and local political machines do not depend on centralized political parties, and parties have no means of controlling their local leaders' career paths.

Until 2003, seat quotas in Congress and local legislatures were calculated dividing the number of votes by the number of seats, and seats were allocated first to lists that surpassed the quota. Remaining seats were then allocated to the largest remainders (Hare largest remainders system). This system generates incentives for large parties to fragment into factions, as large parties are able to fragment into factions of optimal size that allow them to obtain multiple seats assigned by remainder (see Cárdenas, Junguito and Pachón, 2006, for an example). The 1991 Constitution introduced further incentives for intra-party fragmentation via state campaign funding given directly to candidates, as opposed to parties, and by limiting the role of parties in the mechanics of elections. The Constitution also aimed at increasing competition across parties

[10] Olivera, Pachón and Perry (2009) develop this idea in the analysis of fiscal policy and regional transfers.

[11] Many Congressmen are also entrepreneurs who themselves benefit from policies targeted to the sectors in which their private activities concentrate. This further adds to their incentives to trade their support of government projects for targeted benefits to certain sectors. Consider, for instance, the assignment of tax benefits in the context of the Free Trade Zones (FTZ) policy. Of the 45 FTZs that had been approved as of April 2009, five involve businesses in which Senators or former Senators and/or their families have ownership.

by opening spaces for the emergence of new parties, which needed to fulfill only weak requirements to become legally recognized.[12]

A reform to the electoral rules dictated by the Constitution was approved in 2003 with the purpose of strengthening parties. After the reform, a party must obtain at least 2 percent of votes in elections to continue being legally recognized and is required to present a single list for elections, in contrast to the previous possibility of presenting factional lists (Ossa, 2006a). A requirement for parties to vote as a bloc in the legislature was also introduced by the reform, although it became active only after its regulation in 2005 through the "Ley de Bancadas" (Parties Law). Moreover, the rules for allocating seats in Congress and local legislatures were modified, again to reduce intra-party competition. After the reform, quotients are calculated dividing the votes obtained by a list by a series of whole numbers, with seats allocated to the resulting quotients until all are filled. Under this system parties cannot win more seats by fractioning into several lists. Parties can present either closed or open lists. The ranking of candidates in closed lists is determined by the parties, while ranking in open lists is determined by voters, who are asked to check their preferred candidate when voting for an open list.

The effects of the 2003 reform have not yet been fully understood. However, a few studies suggest it has had effects on intra- and inter-party competition, as well as on the way party members vote in legislatures. First, the number of lists and candidates has decreased in the elections after the reform (Ossa, 2006b). Moreover, Pachón and Shugart (2008) find that the reform resulted in a greater balance in the number of parties across districts; they also find that in districts where intra-party competition increased intra-party fragmentation decreased, and vice versa. In turn, Ossa (2006b) finds that after the reform parties in Bogota's Council show greater intra-party cohesion in the presentation and discussion of bills.

#### *2.1.4 The National Planning Council*

The National Planning Council, composed of representatives of regions, economic sectors and other groups of society, is the arena in which the preliminary drafts of the National Development Plans are first discussed (Article 340). Its members are selected for eight-year periods by the President from lists presented by regional authorities and legally constituted organizations (e.g.,

[12] The attempt to increase inter-party competition was partly a reaction to the low competition that characterized the party system between 1956 and 1991 as a result of the Frente Nacional agreement, whereby the two main parties agreed to alternate in power and hold balanced representation in bureaucracy.

producers' associations and similar groups representative of different sectors of society), and half are replaced every four years (Law 152 of 1994). The National Council seats representatives of business, labor, the regions, indigenous groups, Afro-descendents, the young, women, consumers, universities, environmentalists, and others. There are also regional Planning Councils that provide a space for direct consultation of the National Development Plans with the regions. These spaces for consultation were added to the planning process by the Constitution of 1991. Once adjusted to incorporate the feedback from this first debate, National Development Plans are brought to Congress.

#### *2.1.5 CONPES and DNP*

The National Economic and Social Policy Council (CONPES henceforth, for its acronym in Spanish); and the Administrative Department of National Planning (DNP henceforth, for its acronym in Spanish) were conceived as vehicles for the development of National Development Plans (Law 19 of 1958).

The CONPES, a council that operates under direction of the President, has the function of "studying and proposing the government's economic policy" and "coordinating all of its aspects, as well as the activities of the entities that undertake its implementation." According to Decree 627 of 1974, and until 2005, this council was made up of the President and four full-time advisors—two appointed by the President, and two elected by the Senate and the Chamber of Representatives (one each) from lists presented by the government. Election of CONPES members was supposed to occur every four years with terms set at the beginning so that every two years two members were renewed. Ministers, Central Bankers, the President of the Coffee Federation (Fedecafé) and any public employee invited by the President could participate in the policy debate within CONPES. Interviews with participants at CONPES meetings, however, suggest that full-time advisors have in practice been substituted for by Ministers since at least 1990. In 2005, President Uribe issued a decree formally modifying the structure of CONPES; the four full-time advisors were replaced by Ministers, the President of the Central Bank, the President of the Coffee Federation,[13] and the presidential advisors for Afro-descendent

[13] CONPES is the only instance we know of in which the President of Fedecafé still has a formal role as private sector representative. However, his designation in this role is simply an inheritance from the previous CONPES design, and in practice he is rarely involved in the discussions. As we discuss below, for much of the twentieth century Fedecafé and ANDI (the Spanish acronym for the National Association of Manufacturers) effectively

communities and women. Meanwhile, the DNP Deputy Director serves as Secretary to the council since its inception.

CONPES organizes the policy debate around written documents prepared under the coordination of the DNP that contain a motivation, usually in the shape of a problem diagnostic, and a set of proposed policies. These proposals comprise both strategies and concrete actions that sometimes involve decrees to be enacted, or bills to be presented to Congress that may or may not be approved in the form originally proposed. Policy courses of action approved by the President, along with their motivation, are made available to the public through these CONPES documents. Passing through CONPES gives coherence to government initiatives and policies and is meant to force the government to follow a course by planning and directing its most important policies. The influence of CONPES, however, depends in practice on the relevance the President in turn grants it, and on the political grip of the DNP director.

The DNP is the government authority coordinating and supporting all activities related to the formulation of national policies. Its responsibilities include the following: i) compiling and analyzing economic studies relevant for policy design; ii) leading the preparation of National Development Plan drafts; iii) keeping CONPES informed of the country's economic performance; iv) advising other national and regional government authorities about the organization of their offices in charge of investment planning; v) determining the studies required for adequate policy design and performing these studies when they cannot be undertaken by other public offices or subcontracted to third parties (mixed or private); vi) consulting with business associations and academia on national economic problems and National Development Plans; and vii) presenting policy projects for debate at CONPES. Appointed by the President, the DNP Director has Cabinet-level status.

While DNP has historically been a realm of the Colombian technocracy, its weight relative to other Ministries in the policy debate is no longer what it once was. As with CONPES, the role this institution plays in practice is largely shaped by the President in office.

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encompassed Colombia's private interests, a fact that has changed greatly with the diversification of the country's economic structure.

## *2.2 Private Actors*[14]

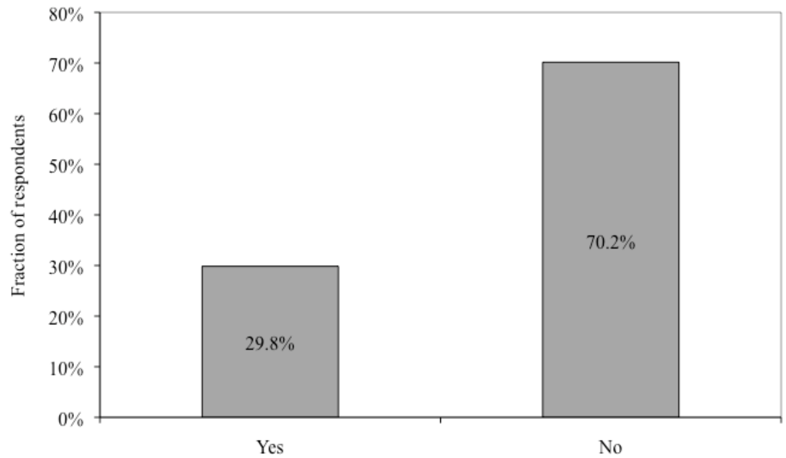
### *2.2.1 Individual Businesses*

Individual firms are at the highest end of disaggregation of private business actors that seek to participate in the PMP. A specific firm's influence on policy depends, obviously, on its characteristics. Larger firms, those belonging to sectors of strategic importance (e.g., oil, utilities), those within business groups, and large multinationals have a higher chance of intervening in policymaking.

According to responses to Fedesarrollo's October 2008 Entrepreneurial Opinion Survey (henceforth EOS, described in footnote 14), 30 percent of businesses participate in the design of policies that affect them (Figure 3). Of this share, 55 percent have had direct involvement through a high-ranking official of the firm, while 64 percent have participated indirectly through a business association (Figure 4; note that the different possible responses are not mutually exclusive). It is worth mentioning that large firms frequently have offices in charge of relationships with government.

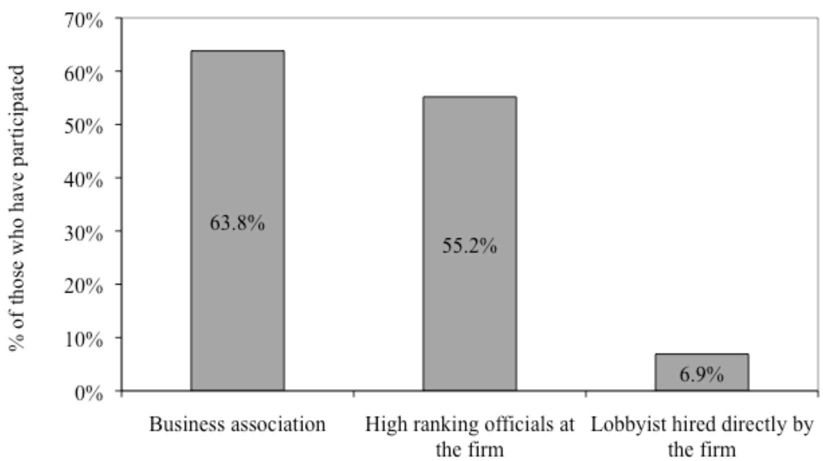
[14] Our description is based both on government documents and other sources. The former include the National Development Plans and CONPES policy documents. We also make use of existing literature, of a series of interviews we conducted between October 2008 and January 2009, and of a recent survey on policy participation responded by executives at private firms. We interviewed former National Planning Department directors and deputy directors, economic advisors to the government, heads of offices of government relationships at large firms, high-ranking executives of multinationals, and members of the Private Council of Competitiveness. The survey we use is part of a section on productive development policies added to the October 2008 round of Fedesarrollo's Entrepreneurial Opinion Survey (EOS), designed by Marcela Meléndez and Guillermo Perry as part of an investigation on the policies available to mitigate restrictions for productive investment, and businessmen's means and channels of influencing policies. We are extremely grateful to Guillermo Perry for giving us access to the results on policy participation. The EOS surveys a representative sample of business managers and owners from the manufacturing sector. A total of 202 firms responded to the full survey, and 105 firms responded the questions on policy participation. A detailed description of the design of the survey, and a complete presentation of results, can be found in Meléndez and Perry (2008).

**Figure 3. Responses to the Question "Have You Participated in the Design of Policies that Affect your Business?"**




*Source:* Fedesarrollo Entrepreneurial Opinion Survey (2008).

**Figure 4. Means of Participation in Policymaking**




*Source:* Fedesarrollo Entrepreneurial Opinion Survey (2008).

*2.2.2 Business Groups*

These groups of companies, held together through common and/or mutual ownership, are often largely owned by a single family. An interesting feature of these groups is that they hold companies in multiple sectors (though they usually have a flagship company dedicated to a specific activity), with the potential implication of diverse policy interests along the sector dimension brought together in the same group.[15] In Colombia, four economic groups have been particularly important for their participation in economic activity: Santodomingo, Ardila-Lülle, Sindicato Antioqueño, and Sarmiento-Angulo. Sindicato Antioqueño sales alone represented 5.5 percent of the country's GDP in 2007, while the four groups together accounted for more than 12 percent of GDP in 1998 (Rettberg, 2001).[16]

Business groups have been a particularly important player in policymaking during the last two decades. The mere fact that these groups represent such a large share of output and employment makes them a natural counterpart for the government in the private sector. However, their influence over policies has other roots as well. For one, business groups are one of the most important sources of private contributions to political campaigns (De la Calle, 2003).[17] Interestingly, they frequently contribute similar (and high) amounts to different campaigns in the same elections (De la Calle, 2003). Second, business groups also own media, including the two largest television stations and radio channels (Rettberg, 2005). Media control allows economic groups to influence public and government opinion (Dye, 2000), and also constitutes an important asset in negotiations with politicians, who are permanently interested in obtaining maximum visibility. Finally, since some of the largest companies in specific sectors are part of economic groups, these groups also exert great influence over some sector-specific business associations (Rettberg, 2005).

*2.2.3 Business Associations*

As mentioned above, most businesses that participate in policymaking do so through business associations. In fact, since non-members cannot be excluded from the benefits of policies business associations lobby for, in a way all firms in sectors represented by business associations participate in the PMP. However, it is also clear that larger firms and those belonging to business groups have greater influence over the views and activities of business associations. This is so because the associations' main source of funding is the contributions of its affiliates, set in

[15] Colombia presently has a quite diversified economic structure. See below for further illustration.
[16] The 2007 number for Sindicato Antioqueño was published in *El Espectador* on May 25, 2008.
[17] According to official statistics, private contributions represented 28 percent of the total funding of political campaigns in 2002 (Torres, 2008). The share of these contributions that comes from economic groups has not been measured precisely, but anecdotal evidence clearly suggests that it is large. For instance, in the Samper 1994 campaign, Grupo Santodomingo was the main donor after (sadly) the Cali drug cartel. Ardila and Sarmiento also provided large funds (Rettberg, 2005).

proportion to firm employment or output (Losada, 2000). This gives large firms and business groups effective power over many business associations; in some cases, these firms effectively appoint the association's head or pay some of the high-ranking officials at the association (Rettberg, 2005).[18] Interestingly, even though business groups have direct influence over the PMP, they also frequently participate through business associations. One advantage of this strategy for groups is that other actors and the public at large see business associations as representative of interests that are more general than those of business groups; the views promoted by associations are thus more easily "sold."[19]

Business associations have the primary purpose of representing the interests of their affiliates in the policy debate. In a survey of heads of business associations, Losada (2000) inquired regarding the objectives pursued by these associations. "Obtaining favorable regulations" was the objective most frequently mentioned (77 percent of respondents). Losada additionally conducted a survey of business association members, who indicated that having a representative of the sector (presumably to interact with state officials) was the main reason why they joined a business association.

There are several types of business associations in Colombia. First, specialized associations represent producers in a narrowly defined sector. Specialized associations are, in turn, represented by "peak associations." For instance, the Society of Agriculture brings together more than 20 specialized associations within agriculture. As of 2000, there were five peak associations in Colombia: a "super-peak" association—the Consejo Gremial Nacional[20]—and peak associations for agriculture, tourism, cooperatives, and transportation. A particularly interesting and important association that cuts across several sectors is Analdex, which represents the interests of exporters. It is worth mentioning, however, that more than 70 percent of specialized associations are not members of peak associations (Losada, 2000).

Though larger and more encompassing business associations are obviously more influential, their policy domain is at the same time limited by a traditional collective action problem: larger associations bring together more diverse interests, sometimes opposed to one

[18] Rettberg (2005) cites one interesting example: the nephew of the head of the Ardila group has quasi-permanently held the presidency of *Asocaña*, while the group owns two of the largest sugarcane refineries.

[19] Interestingly, sector-specific regulations are not generally perceived by Colombian voters as favoring specific interests over the general interest. In many instances, these policies are successfully presented as mechanisms for protecting employment in sectors that represent a large share of jobs in the economy.

[20] Interestingly, the Consejo Gremial Nacional was founded in 1991 as a response to the government's request to have a unique counterpart to consult with on trade negotiations (Schneider, 2004).

another. It is thus difficult to create a unified front regarding policy issues with concentrated benefits and costs. As a consequence, the issues addressed by large associations tend to be transversal in nature. This implies that specialized associations continue to play an important role, even for sectors also represented by peak or other inclusive associations.

The heads of several business associations are extremely vocal, frequently consulted by media, and in general influential on public opinion. Such is the case of, among others, the presidents of ANDI and Analdex (the associations of manufacturers and exporters, respectively), and the presidents of the associations of flower growers, cattle farmers, retail sellers, and the peak association of agriculture. Obviously, both their visibility in the media and the strength with which they voice their views depends on specific circumstances. As an example, Analdex and the flower growers (mostly exporters) were particularly vocal during the peso appreciation episode of 2006 and 2007.

Two particularly powerful associations, ANDI and Fedecafé, deserve especial mention. ANDI, the National Association of Manufacturers, presently aims to represent the private sector at large, with its membership nowadays including firms from the retail, services, and financial sectors. Believed to have been founded partly as a response to President Lopez's request to have one spokesman for industry (Urrutia, 2003), it has played a large role in policymaking, so much so that it represents Colombian private producers in international organizations such as ILO and has played an important role in official negotiations of trade agreements between Colombia and other countries. Fedecafé, on the other hand, was created under the auspice of the government and funded through a dedicated export tax, its main funding source even today (Schneider, 2004). Fedecafé was for decades the most important business association and one of the most important players in the PMP. Its power came partly from the fact that it represented what was for many years the country's most important productive activity. It administered a stabilization fund for coffee prices, and its chairman participated in several government boards and committees, usually as the representative of private businesses at large. While both ANDI and Fedecafe remain powerful, their influence over the PMP has changed. Fedecafe, in particular, is no longer a representative of the private sector at large; it is now perceived as representing the specific interests of coffee, still an important sector but far from the main engine of the economy. The decreased presence of Fedecafé reflects the decreased importance of coffee in the economy: while in 1965 coffee exports represented close to 80 percent of total Colombian exports (Arango, 1997), they now represent around 7 percent (authors' calculations using publicly available data from Banco de la República).

Business associations have been traditionally a key player in the Colombian PMP. Schneider (2004) presents Colombia as the case of the most well-organized business participation in the Latin American context. Colombia has had relatively strong associations, compared for instance to Argentina and Brazil, where organized business representation has not flourished. Also, in comparison to other countries with strong business associations, such as Chile and Mexico, the main associations in Colombia are found to be much larger in terms of staff (over 3,000 in Fedecafé and 150 in ANDI, compared to less than 100 in the large associations of other countries), and to represent more concentrated interests by being sector-specific rather than economy-wide.[21]

The state played a key role in the foundation of the main associations in the first half of the twentieth century. Governments helped organize business interests as a means of supporting the development of strategic sectors and delegating some policy responsibilities to entities that had greater technical capabilities and were subject to less political pressures (Schneider, 2004). Between 1940 and 1990, business associations were granted authority to administer import licenses and sector-specific development funds created and financed by the government, and they participated in a myriad of consultative bodies created by successive governments. Urrutia (1983), in fact, partially credits the strength of business participation in Colombia for the relatively successful macroeconomic performance of the country.

Traditional business associations continue to be key players in the Colombian PMP.[22] However, they have lost importance in the aftermath of market-oriented reforms. Several reasons explain this phenomenon. Business associations were particularly important in a context of strong government intervention, where development programs were naturally targeted to specific sectors, and some of the associated policy responsibilities were delegated to sector associations. The reforms, though, dismantled many sector-specific benefits that were administered by specialized associations.

[21] In the case of ANDI, diversification away from manufacturing has limited its ability to push for some specific policies. We discuss this issue in greater detail below.

[22] A telling episode occurred in the context of a major scandal surrounding the financing of president Ernesto Samper's campaign by the Cali drug cartel. The Consejo Gremial Nacional publicly asked for the president's resignation. This stands in contrast to the passive attitude of the business community during the scandals that affected Brazil's Collor de Mello and Argentina's Menem (Schneider, 2004).

It is also the case that business interests have become increasingly fragmented, as the productive structure of the country has become more diversified. As an example, consider a Herfindahl-Hirshsman index of exports at the three-digit level of sector disaggregation. This number went from 0.48 in 1980, to 0.08 in 2007 (authors' calculations from Banco de la República data). Probably as a reflection of the greater fragmentation of business interests, the number of business associations in Colombia has grown from just a few in 1950 to more than 220 in 2000 (Urrutia, 1983; Losada, 2000), and their reach has extended to many more sectors. The proliferation of business associations has also implied that the presence of the private sector in policymaking has become disperse. Different associations have begun to compete for access to the government, another factor behind the weakening of their power.

Moreover, business groups, not subject to the collective action and free rider problems that plague business associations (Giacalone, 2005), and with greater financial capability to make campaign contributions, have overshadowed increasingly atomized associations. In the words of Revéiz (1997), "presidential power is exerted now more around business groups than around business associations." In fact, Losada (2000) finds that heads of business associations perceive "competition from business groups and multinationals" as one of the main threats to their associations. Of 164 mentions to threats affecting these organizations, 5 percent referred to this type of competition, the same share as "disperse interests of members."[23]

#### *2.2.4 Private Council for Competitiveness*

A final private-sector actor worth mentioning is a recent initiative to organize participation in the PMP, the Private Council for Competitiveness. The Council was founded by a group of private businesses with the purpose of promoting competitiveness-enhancing policies, following the model of the Council on Competitiveness in the United States.

Several characteristics make the Council interesting and likely influential in future policy initiatives on productivity. First, the Council represents a selected set of large firms, both national and multinational, allegedly interested in pressing for transversal policies and the elimination of distortions from targeted policies, rather than for protectionist policies or other preferential treatment. Its main purpose thus suggests a shift in the lobbying activities of private

[23] Competition by other associations and disperse interests of members rank fifth among the more than 20 "threats" perceived by heads of business associations. The four factors mentioned by most heads of business associations were bad economic performance of the country as a whole, bad performance of the sector, weak government support of the association, and hostile regulation of the sector.

interests that in the past, as discussed above, did not have policies designed to increase aggregate productivity as a priority.[24] Second, the Council has gained a privileged position as a member of the technical secretariat to the National Competitiveness Commission (see Box 1), together with the National Planning Department. The secretariat is in charge of preparing the policy documents for discussion at the NCC. As one of its members, the Private Council for Competitiveness has a leading voice in the policy debate in that arena. Third, the president and vice president of the Consejo Gremial Nacional—the presidents of ANDI and SAC, respectively—have seats on the Competitiveness Council's board of directors.

These features make the Private Council for Competitiveness likely to become influential in the PMP. In fact, since its foundation in 2007, it has had a great deal of influence on some policy initiatives specifically targeted to increase competitiveness (with expected consequences on aggregate productivity as well).[25] The Private Council for Competitiveness may prove fundamental to guaranteeing the continuity of some of these programs, and of other initiatives that have emerged in the context of the National System for Competitiveness (see Box 1).

### *2.2.5 Labor Unions in the PMP*

There are three "peak" labor unions, each composed of smaller unions representing group-specific labor interests. The Confederación de Trabajadores de Colombia (CTC), founded in 1937, is the oldest labor union in Colombia. The CTC presently includes 250,000 workers from 10 regional and six national worker "federations" and has offices ("*seccionales*") in three cities. Workers from agricultural, manufacturing (agro-industry, textiles, metal-mechanics, chemicals, wood) and services sectors (telecommunications, construction, transport) are represented, as well as informal workers and government employees. The largest peak union, however, is the Central Unitaria de Trabajadores (CUT), founded in 1986, made up of 800,000 workers from all economic sectors organized into 11 "federations" and four sector unions. CUT has offices in all Departments of Colombia. Finally, Confederación General del Trabajo (CGT), founded in 1971, has a membership of 300,000, including workers in the flower and sugar sectors. Presently,

[24] This does not mean that the lobby for targeted policies has lost steam in the very last years. Only a few firms and associations are active members of the Private Council for Competitiveness, and even those members continue lobbying for interests that are specific to them. However, organized private action to promote policies of general interest is an encouraging sign.

[25] For instance, a recent government initiative seeks to support sectors of high productivity growth and strategic interest in developing their international operations. The Private Council participated in the selection of the sectors to be considered "strategic" under this program.

however, unionized workers amount to only 5 percent of the active workforce, down from their highest level of 13 percent in the 1970s (Cuesta, 2005).

### *2.2.6 Universities and Think Tanks*

One peculiar aspect of economic policymaking in Colombia has been the major influence of well-trained economists. There have been various avenues for the transmission of their expertise. First, economists at universities and think tanks participate actively in the policy debate. Their views are frequently reported by the media, and many write regular columns for the most widely read newspapers and magazines. Many of those views end up shaping policy proposals, partly due to their impact on politicians' views as a result of media coverage and subsequent public pressure.

Moreover, technocrats have frequently held high-ranking positions in government. Meisel (1996), for instance, documents that 50 of the 55 people in top economic policy positions between 1974 and 1996 pursued graduate studies abroad, and 13 held PhD degrees in Economics from universities in the United States or Northern Europe.[26] Moreover, economists trained both abroad and in the best economics departments in the country also frequently go to work for the government. The flow of highly trained economists between academia and government works both ways. The heads of Fedesarrollo and the Department of Economics at Universidad de Los Andes, for instance, frequently have had previous experience as ministers or deputy ministers. Interestingly, the revolving door also has stops at business associations, frequently headed by highly recognized technocrats who have held or eventually come to hold government positions.[27]

## 3. Arenas and Modes of Interaction

In this section we describe the manner in which different actors participate in the PMP. While in the main text we refer to the "economic" PMP in general, Box 1 describes aspects specific to the making of policies directed at promoting productivity growth.

[26] Meisel (1996) includes in this list of top positions the minister of Finance, the president of the Central Bank, the director of the National Planning Department, the advisors to the Monetary Board (up to 1991), and the members of the Board of Directors of the Central Bank (since 1991).

[27] As an example, the current president of the association of insurance companies is a US trained economist who previously was Minister of Finance and director of Fedesarrollo. Similarly, the current president of the association of pension funds was previously dean of the department of Economics at the Universidad de los Andes and director of the National Planning Department.

### *3.1 Interaction among State Actors*

The rules of the game set forth out in the Constitution of 1991 and subsequent legislation imply some interesting features of the PMP in terms of the interactions between different state actors. Given the agenda-setting power of the president, policy projects frequently come from the executive. These initiatives then make their way to Congress, where the government needs to build support for the project. Appointments to public positions and budget allocations for targeted projects are used to build coalitions in Congress, and the increasing degree of fragmentation in Congress has made this process more costly after the adoption of the 1991 Constitution (Cárdenas, Junguito and Pachón, 2006). Moreover, the fact that Congress can modify bills presented by the government opens an additional space for coalition-building. For instance, Congress included in the 2002 Labor Reform bill articles that increased the demand for students graduating from SENA, the public institution in charge of training blue-collar workers. As SENA has traditionally been used by career politicians to serve their clienteles, this change helped to make the bill politically feasible (Echeverry and Santamaría, 2004).

Another interesting feature of the interaction between Congress and government is the fact that the costs and feasibility of coalition-building depend on a combination of political and business cycles. As policies that impose greater structural changes demand more political muscle, they are frequently adopted during the initial years of the government (a "honeymoon" effect). For instance, the Labor Reform adopted in 2002 (the first year of President Uribe's first term) closely resembled a bill that was proposed to Congress but defeated in 2001 when the Pastrana government was coming to an end. Coalition-building also appears to be less costly during economic downturns, when the government is known to be short on resources to deliver pork. Moreover, economic downturns are particularly good times to propose policies intended to solve structural problems of the economy. At such times congressmen need to convince their constituencies that they are seeking solutions to the crisis, and they are therefore more prone to accepting the advice of government technocrats.[28]

[28] This feature of the Colombian PMP is consistent with part of the theoretical literature on the timing of reforms. In many of these models reforms are undertaken when further delaying them becomes sufficiently costly (e.g., Alesina and Drazen, 1991). Crises are likely to be times of this type.

**Box 1. Arenas for the Interaction of Political Actors in the Context of Productivity Policies**

In the context of the increasing liberalization of the early 1990s, and aware of the need to promote the adjustment of the country's productive structure to compete in international markets, the government included in the National Development Plan for 1994-1998 a chapter entitled "Competitiveness for Internationalization." This chapter gave way to a change in the policy-making of policies explicitly designed to increase productivity and competitiveness by introducing new actors and arenas to this particular policy debate.[29] The most notable change was brought about by the creation of a National Council for Competitiveness in 1994 (Decree 2010), an advisory council to the President on all matters related to "quality, productivity and competitiveness improvement for the country and its regions." In its first version, the Council included seven representatives of the entrepreneurial sector, three representatives of the academia, and three representatives of the workforce, all appointed by the President. This Council was to operate under the coordination of a "Presidential Advisor for the economy and competitiveness," and to "work with the relevant authorities in each particular matter, promoting the creation of regional Competitiveness Councils as necessary." According to the rulings of this Council, the government entered the negotiation of Competitiveness Agreements with selected sectors, whereby both parties committed to particular actions for competitiveness improvement.

In 1998, to eliminate duplication across arenas, the functions of the National Council for Competitiveness were assigned to the Trade Mixed Commission, an instance of similar composition and purpose assigned to the Ministry of Trade since 1976. The Trade Mixed Commission was expanded to include two representatives of academia and two of the workforce, appointed by the President, to match the original structure of the previous Council (Decree 2222).

Subsequent National Development Plans continued to underscore productivity and competitiveness enhancement as enginesfor economic growth. Following the mandate of the 1998-2002 National Development Plan to strengthen and revise the national policy for productivity and competitiveness, in 1999 CONPES approved the proposal of the Ministry of Trade to articulate public and private efforts through actions on three fronts: transversal, sector-level and regional. The transversal policies front brought with it another arena for policy debate: the discussion of transversal policies was assigned to specialized thematic networks within the wider Colombia Competes Network, which brought together government authorities, entrepreneurs, workers, academia, legislators and representatives of the judiciary. The sector-level front continued to be covered with the figure of Competitiveness Agreements described above. The discussion of regional policies, in turn, was assigned to Regional International Trade Advisory Committees (CARCEs for their acronym in Spanish), new groups created in a spirit similar to that of the regional Competitiveness Councils that they would replace.

This national policy for productivity and competitiveness resulted in increased knowledge about bottlenecks, and was somewhat successful in bringing regional actors closer to the policy-making process. It, however, was unsuccessful in influencing transversal policies, because sector Ministries did not abide by its recommendations and the Ministry of Trade did not have the hierarchical stature to influence the policies implemented by other Ministries. Coordination across the multiple actors and arenas involved in the policy-making process also proved difficult.

In 2004 CONPES created the Domestic Agenda for Productivity and Competitiveness with the objective of defining short-run and medium-run plans, programs and projects to "take advantage of the opportunities and mitigate the risks associated to increased integration under the

[29] "Productivity" and "competitiveness" have often been used alongside one another—and even interchangeably—in public discourse. These semantics are not innocuous to the extent they reflect upon the types of policies that emerge in equilibrium.

Free Trade Agreement with the U.S.," under negotiation at the time (CONPES, 2004). This Domestic Agenda, to be coordinated by the DNP, would rely for policy design upon open dialogue with all interested public and private actors, in all three dimensions: transversal, sector-level and regional. The overlap with the objectives and activities of the policy for competitiveness and productivity run by the Ministry of Trade is evident.

The Domestic Agenda was an input for the 2006-2010 National Development Plan, and to that extent proved an effective venue for putting forth particular policy requests. Under the new institutional setting of policymaking for productivity and competitiveness (described below), it is no longer a relevant venue.

In 2006, and with the purpose of giving coherence to the institutional setting of policymaking for productivity and competitiveness, CONPES approved the organization of a National System for Competitiveness. The system was to be the set of "guidelines, regulations, resources, programs and public and private institutions that foresee and promote the design and adoption of a policy for productivity and competitiveness" (Decree 2828 of 2006).

The System is supported by the National Competitiveness Commission (CNC for its acronym in Spanish), a consultative body of the government. The Commission was designed to articulate the participation of public and private actors in the formulation of policy recommendations to CONPES. The CNC acts under direction of the President and is composed of the Ministers and representatives of the regional governments, private sector, workforce and academia. The Presidential Advisor for Regions and Competitiveness coordinates the Commission (Decree 2828 of 2006), and there is a Technical Secretariat shared by the National Planning Department, the Trade Ministry, and the Private Council for Competitiveness. Regional chapters of the CNC, which are in the process of being organized, will coexist with CARCEs.

The description above should illustrate the variety of venues whereby private actors might participate in the design of policies aimed at increasing productivity.[30] It should also show how unstable and difficult to understand those mechanisms have been. Frequent changes and the lack of a stable and powerful head of productivity policy have implied lack of coordination and several instances of duplication that render these mechanisms largely ineffective.

### *3.2 Modes of Participation of Socioeconomic Actors*

An interesting feature of the PMP in Colombia, of great importance for our analysis, is the existence of ample formally established spaces for the participation of private actors in the process. For instance, the Constitution requires National Development Plans to be formally discussed with different groups of society before being approved.[31] As described above, the

[30] Besides the arenas for participation described above, since 2002 the Uribe government runs Communal Councils, not directed at policies for productivity, but frequently arenas for the discussion of policies with side effects on productivity. These Communal Councils are meetings conceived with the purpose of facilitating interaction between citizens, and regional and national authorities to promote dialogue about problems facing the community and to reach agreements about potential solutions. They take place every Saturday at a different municipality, with the presence of President, Cabinet members, and local and regional authorities. The Presidential Advisor for Regions and Competitiveness is responsible for organizing these meetings and setting their agendas. National Development Plans for presidential periods 2002-2006 and 2006-2010 provide the guidelines for this government program.

[31] Private participation in the discussion of policies is taken seriously. For instance, in 2008 the Constitutional Court decided that a "Forests Law" approved by Congress did not abide by the Constitution. The reason was that the bill was not discussed with indigenous and Afro-descendant communities, the main inhabitants of the forests, before being brought to Congress (Constitutional Court, Press Release 1, January 23, 2008). The Constitution states that one goal of the State is facilitating the participation of citizens in decisions that affect them.

national and regional Planning Councils are bodies created with this purpose, and include private sector representatives. Moreover, in some policy areas there are specific consultative bodies designed to open a window of participation for the private sector and other socioeconomic actors (see description of the National Competitiveness Council in Box 1 as an illustration). There are also ad hoc commissions for the discussion of specific policy initiatives. One example is the Discussion Roundtable created in 2000 for the discussion of the labor reform then in progress; business associations, labor unions, universities and political parties were part of that roundtable. Another example is the Domestic Agenda for Productivity and Competitiveness, an initiative to channel policy requests from sectors and regions in the context of the negotiation of the Trade Agreement with the United States.

### *3.2.1 Business in the PMP*

The private sector intervention in policy-making follows a two-track strategy. The first is a "formal track" whereby firms use the formal mechanisms of participation described above (representation in the boards of government agencies and in government-led consultative committees). There are also less formal venues for participating in the PMP. In fact, as we discuss below, in recent times the latter avenues of participation are perceived as more effective and seem preferred by private producers for discussing the policy issues they consider most pressing.

*The formal track.* As described above, one characteristic of the Colombian PMP is the existence of ample channels for private-sector participation. In principle, the existence of these formal vehicles for participation provides direct access to policymaking. The effectiveness of these mechanisms and the actual access of private firms to them is, however, an open question. The evidence at hand actually downplays the importance of these formal mechanisms, or at least suggests they are not the main avenues private producers use to try to influence policies.

Consider, for instance, Table 1. The table reports the types of events of participation mentioned by firms that responded to the EOS' Policy Participation questions (Meléndez and Perry, 2008). The reported figures indicate that less than 40 percent of the instances of participation occur using these formal channels. When firms are divided into size categories, large firms follow roughly the overall pattern mentioned above. Medium-sized firms, meanwhile, report using formal channels even less often: less than 20 percent of their instances of participation occurred within the context of the formal consultative mechanisms. Small firms are the ones that use most often formal mechanisms: over 70 percent report having participated through one of the formal mechanisms mentioned in the survey (Competitiveness Agreements negotiations, National Development Plan discussions, Domestic Agenda discussions, and Communal Councils).

**Table 1. Mechanisms of Participation**

| | % of participation instances | | | |
|---|---|---|---|---|
| | All firms | Large | Medium | Small |
| | (1) | (2) | (3) | (4) |
| Specific formal mechanisms of participation | 39,0 | 41,5 | 18,2 | 71,4 |
| Initiatives of business associations | 54,9 | 52,3 | 72,7 | 28,6 |
| Others | 6,1 | 6,2 | 9,1 | 0,0 |

*Notes:* Surveyed firms are asked what types of mechanisms of participation they have used. They can indicate more than one type of mechanisms. We report the share of responses that indicate each type of mechanism. "Specific formal mechanisms of participation" are: Competitiveness Agreements negotiations, National Development Plan discussions, Domestic Agenda discussions, and Communal Councils. All of these mechanisms are described in the text. Column (1) reports overall figures, while columns (2)-(4) divide firms into large, medium-sized, and small.
*Source:* Fedesarrollo Entrepreneurial Opinion Survey (2008).

There seems to be a whole host of reasons why firms do not use these mechanisms of participation as actively and exclusively as one might expect. First, the types of policies discussed in these arenas are frequently less pressing to private sector interests; specific interest groups give priority to policies whose costs or benefits are concentrated on the corresponding group, especially if those costs or benefits are felt in the short run. With few exceptions, however, the "formal track" provides a space for consultation on government initiatives that frequently originate from recommendations by government's technocrats, and the policy priorities of governments and their technocrats often do not correspond to the (narrow and short-run) policy priorities of private producers. In a related manner, the policies discussed in these arenas are frequently transversal in nature, and consequently tend to have benefits and costs that are not sufficiently concentrated to make them of central interest to specific private actors.[32]

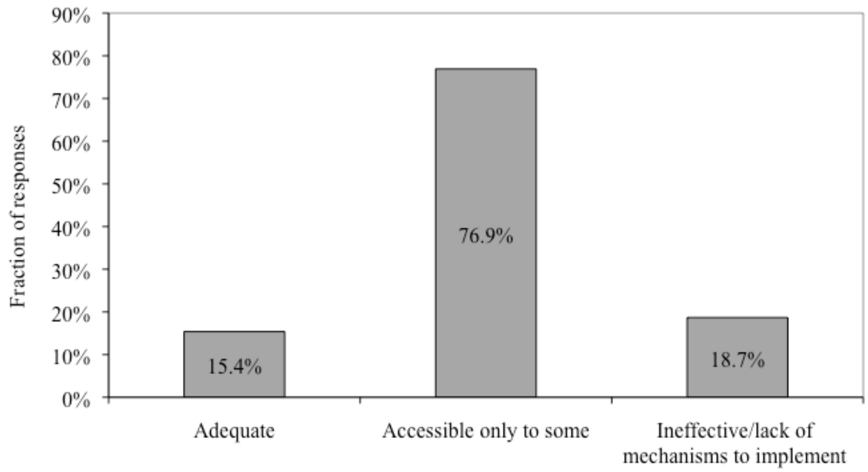
[32] An exception is the Domestic Agenda, designed precisely to identify the policy priorities of different productive sectors. Also, debate in the National Competitiveness Council is apparently following another logic so far, but that seems associated more to momentum than to structural conditions. This arena is still too recently created to judge its efficacy.

Second, our interviews suggest that private producers consider existing mechanisms for participating in the PMP to be ineffective. In the case of policies directed at improving productivity, this perception may derive from the somewhat chaotic evolution of the system for competitiveness (see Box 1). This perception of ineffectiveness also appears to be a natural consequence of the fact that, while many of these mechanisms offer opportunities for private sector actors to present their positions, there is no clear mandate to incorporate those positions into policies.

The EOS also asked firms' opinion on formal means of participation. Only 15 percent of respondents find them adequate, while the remainder characterize them as either restricted or ineffective due to a lack of mechanisms to implement the policies derived from consultations (Figure 5). Interestingly, around 60 percent of respondents see affiliation with powerful business associations as important for having access to formal participation channels (see notes to Figure 5).

It is also worth mentioning that the formal spaces of participation are often an arena for consensus building around government initiatives. Officials are aware of the fact that these initiatives, many of which have origin in technical advice, need to be "sold" to socioeconomic actors before their passage through Congress. For instance, the debate initiated in the Discussion Roundtable for the Labor Reform of 2000 was instrumental for the final adoption of the reform in 2002 (Echeverry and Santamaría, 2004). The Discussion Roundtable brought labor reform, which was not a policy priority of either political parties or socioeconomic actors, to the forefront of the policy debate. It also gave technocrats the opportunity to explain arguments in support of the reform. Making gains from the reform explicit in the public debate empowered winners and gave them incentives to defend the initiative. Finally, the Discussion Roundtable was also a space for striking deals that made the reform politically feasible (such as the creation of an unemployment subsidy as part of the bill).

**Figure 5. Opinion of Formal Mechanisms of Participation**




*Source:* Fedesarrollo Entrepreneurial Opinion Survey (2008). "Accessible only to some" includes accessible only to: large firms (33 percent), firms associated with important business associations (57 percent), and firms within businessgroups with political power in region (29 percent). Possible responses to this question are not mutually exclusive.

*The informal track.* The discussion above implies that formal mechanisms of participation are by no means perceived as sufficient by private producers and their representatives. Besides their relative ineffectiveness, the very fact that they seek to bring together diverse perspectives within the private sector, sometimes including opposing points of view, makes these inappropriate spaces for the discussion of initiatives with highly concentrated benefits and/or costs. Therefore, the private sector also uses informal channels to influence the PMP at different stages. These informal mechanisms most frequently take the form of trying to establish direct contact with either government officials or congressmen. For instance, Losada (2000) presents evidence that these direct contacts are the instrument that business associations use most frequently to influence policy. In a survey of heads of business associations, he finds that almost all of them (93 percent) establish direct contact with congressmen and government officials to present the sector's point of view. Interestingly, this occurs despite the fact that 91 percent of those associations report being able to participate in formal consultative bodies created by the government.

The form that these direct contacts take depends on various factors, among them: i) whether the intention is to have a private initiative included in the policy agenda, or rather block, support, or modify an initiative already under way; ii) the access that the particular private group has to different levels of government and Congress; and iii) the personality and governing style of the president in office.

Bringing policy initiatives to the forefront of the policy agenda is one of the main objectives of lobbying activities by private actors. Note for instance, that according to the EOS more than half of the instances of participation in policymaking by private businessmen consist of initiatives by business associations, which represent only one form of private policy initiative (Table 1). Given that most policies in the economic sphere must be either proposed or endorsed by the executive, establishing direct contact with the executive is the preferred avenue for private groups to present their own policy initiatives. For instance, the EOS asks firm managers to identify their counterparts in policymaking. Figure 6 shows that 83 percent of the firms that reported having participated in policymaking since 2002 mentioned government officials as their counterparts; 65 percent interacted directly with cabinet members, and around 33 percent interacted directly with the president.

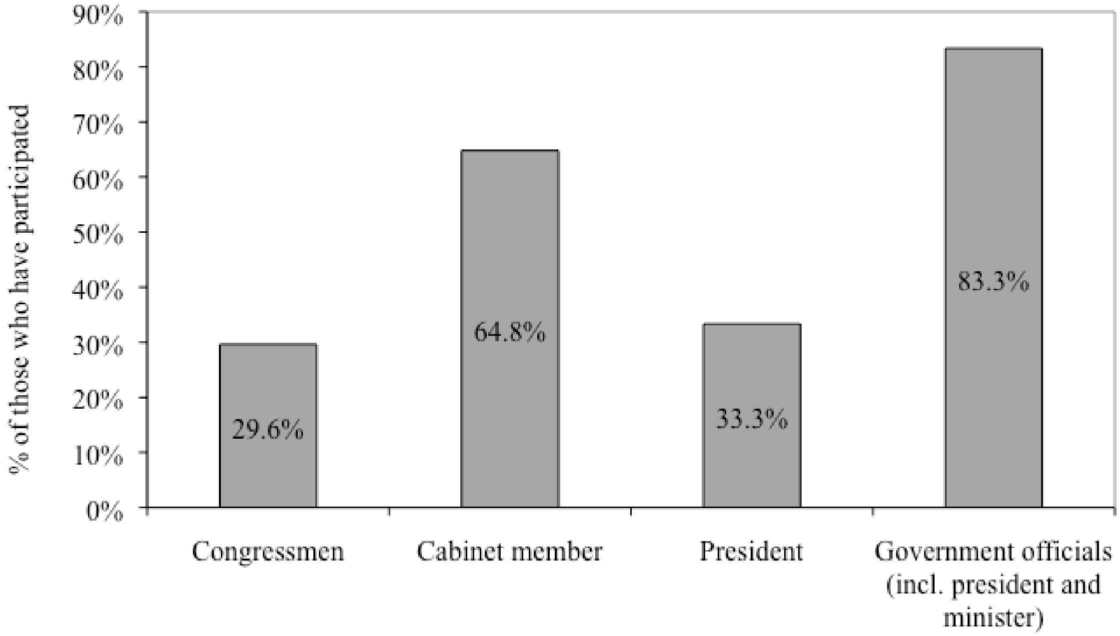
The specific manner in which a private sector representative interacts with the executive depends, of course, on whether he has direct access to high-ranking officials, including the president. For instance, each president has an inner circle of private businessmen who are close to him; members of this group tend to share geographical origin with the president, or come from sectors or business groups to which the president has personal ties. The views of these businessmen are highly valued by the president; they are also likely candidates to be Ministers or presidents of Ecopetrol (the main oil company, largely owned by the government). Modes of interaction with the executive also depend on the way in which the government in office conducts business. To illustrate differences between governments, consider Presidents Pastrana (1998-2002) and Uribe (2002-present). While during the Pastrana administration cabinet members had large room to propose and take forward their own initiatives, President Uribe tends to handle a large number of issues directly. Therefore, during the former administration there was a rationale for the private sector to try to channel its initiatives through high-ranking officials in the Ministries. Meanwhile, President Uribe has appointed a High Economic Advisor whose office directly handles and takes to the president concerns put forward by private sector representatives.[33]

Besides including their own initiatives in the government's policy agenda, private interests also intervene in policymaking to support, block or modify initiatives already being discussed by Congress. Thus, direct contacts with congressmen are also a frequent strategy among private sector representatives. Close to 30 percent of the firms that reported having participated in policymaking in the EOS indicated congressmen were among their counterparts in policymaking activities (Figure 6).

A variety of instruments are used by private sector representatives to influence government officials and congressmen. In his survey of heads of business associations, Losada (2000) attempts to identify lobbying activities frequently conducted by these associations. A large number of respondents mention intervening directly in the drafting of a bill or decree, and presenting the group or sector's position on a given issue to congressmen and government officials (either by handing position papers to them, or via direct conversations and presentations) as two of the most important activities. In contrast to business groups, campaign contributions are only marginally important as a lobbying instrument for business associations. Less than 10 percent of the business associations surveyed by Losada indicate they have contributed to political campaigns.

[33] It is perfectly clear to the business community that the most effective channel to policymaking during the current administration is the president himself. A direct line to the High Economic Advisor is a highly valued political asset. Also, the president is now a key participant in regular meetings of business associations, which have become venues for the private sector to present its demands.

**Figure 6. Who Has Been Your Counterpart?**




*Source:* Source: Fedesarrollo Entrepreneurial Opinion Survey (2008). Possible responses to this question are not mutually exclusive.

It is interesting to compare the perceived effectiveness of different informal channels of access to policymaking. Table 2 summarizes responses to a question about the outcomes of participation events in the EOS. Private sector representatives who have had the president among their counterparts seem quite successful in shaping policies: none of these respondents characterized their participation as unsuccessful, and close to 40 percent of them indicated that a policy similar to the one they requested was adopted "in most cases." Next in line are those who have interacted with cabinet members: 17 percent report their requests were unsuccessful, while 20 percent report a policy similar to the one they requested was adopted in most cases. Of those interacting with congressmen, 25 percent characterize their participation as unsuccessful, and roughly another 25 percent report that a policy similar to the one requested was adopted in most participation instances. The least successful seem to be those who interacted with lower ranking government officials: 46 percent say they were unsuccessful, and 23 percent said they obtained a policy similar to that requested in most cases.

**Table 2. Counterparts and Outcome of the Interaction**

| State actors | Respondents who have had this counterpart as % of those who have participated in policy-making | Outcome of the interaction (% of those who have interacted with this counterpart) | | | |
|---|---|---|---|---|---|
| | | Policy similar to the one requested implemented in most cases | Policy similar to the one requested implemented in some cases | Policy requested not implemented, but a compensatory one adopted | Policy requested rejected by policy-makers |
| | (1) | (2) | (3) | (4) | (5) |
| Congressmen | 30% | 25% | 25% | 25% | 25% |
| Cabinet members | 65% | 20% | 29% | 34% | 17% |
| President | 33% | 39% | 50% | 11% | 0% |
| Other government officials | 24% | 23% | 15% | 15% | 46% |
| Others | 15% | 38% | 25% | 25% | 13% |

*Notes:* Column (1) summarizes responses to the question of who has been the respondent's counterpart in events of participation in policy-making. Each respondent was allowed to check as many responses as he deemed appropriate. We report the number of respondents who indicated having had contact with the corresponding state actor, as a share of the respondents who indicated that they have participated in policy-making. Columns (2)-(5) summarize the outcomes of events of participation as reported by respondents. We present the respondents that choose each type of outcome, as a fraction of those who have indicated a given state actor was among their counterparts.
*Source:* Fedesarrollo Entrepreneurial Opinion Survey (2008).

To place these results in a comparative perspective, consider scores in the Global Competitiveness Report (2007) section on institutions, where respondents to the World Economic Forum's Executive Opinion Survey are asked for their view on different institutions. In a question that asks to what extent legal contributions to political parties have a direct influence on specific policy outcomes, with 1 being equal to "a very close link" and 7 being equal to "little influence in policy", Colombia scores below the mean. With a mean score of 4.1, Colombia scores 3.2, close to Argentina (3.1), Venezuela (3.2) and the United States (3.4), and far below Chile (5.3). A similar picture arises from a question on how much influence individuals or firms with close personal ties to political leaders had on recently enacted laws and regulations with substantial impact on business, with 1 being equal to "enormous influence" and 7 being equal to "no influence." The mean score is 4.3, and Colombia's is 4.2, this time closer to Mexico (4.0), Peru (4.0) and the United States (4.2), and far from Chile (5.2). Overall, compared to other countries executives in Colombia seem to have a perception of greater importance of personal political connections and contributions to political parties.

*3.2.2 Other Private Actors*

*Labor unions and other social groups.* As is the case with business representatives, labor unions and representatives of social groups also hold seats in many policy consultative bodies and commissions. Labor unions, for instance, participate in the committee in charge of negotiating minimum wage increases. They also participate, together with representatives of women, Afro-descendants and indigenous people, and other social groups, in the National Planning Council.

Similar to business, labor unions and other social groups also intervene in the PMP through informal channels. Informal participation in their case takes the form of trying to exert pressure through strikes and street protests. This form of participation was legitimated by the Constitution of 1991 that through its statement of fundamental rights gave workers the right to participate as a political force. The influence workers have achieved through this type of pressure is, however, limited by the abstract and general nature of the views they express. Besides quite general labor demands, unions frequently call for the protection of human rights, public education, and state ownership of firms, among other demands. The emergence of ethnic pressure groups that have overlapping interests with labor unions, has contributed to broaden the range of issues in which unions are interested.

*Technocracy.* The active participation of business representatives and technocrats in the making of economic policies in Colombia has been partly credited for the relatively successful and stable economic performance of the country over the twentieth century. The influence of these groups placed economic stability as a policy priority (Urrutia, 1983). Moreover, it helped in insulating the economic policy-making process from partisan politics (Schneider, 2004). Scholars have also argued that high-level technical advice and the strong technical and/or entrepreneurial background of policy-makers improved the quality of policies (Meisel, 1996).

Nonetheless, worrisome signs of a deterioration of the quality of the bureaucracy have appeared in the last few years.[34] President Uribe tends to handle issues directly and disregard technical advice, taking decision power away from ministers and technocrats. In a related development, a number of newly created special agencies under the direct supervision of the

[34] We attempt to make a general characterization of the PMP, beyond the specificities characterizing the government of a given president. However, it is impossible to not focus at times in the current administration. The Uribe administration has been in power for seven years, out of the less than 20 that have passed after the reforms; meanwhile, before this administration the Constitution banned presidents for remaining in power for more than four years at a time. Moreover, a new Constitutional Reform to allow president Uribe to remain in power for an additional four-year period is under discussion as this paper is written.

president have absorbed responsibility for the design and implementation of key policy programs (and their associated budget), historically under the scope of action of DNP and other ministries.[35] Besides making much of the work by the government technical agencies futile, this shift in duties has also resulted in the appointment of people with less technical strength than used to be required for key positions, as well as an increasing reluctance on the part of many highly trained economists to work for government agencies.

## 4. Quantifying Group Influence as a Function of Political Characteristics

The above description of formal and informal elements of the PMP makes clear that different private interests (firms, sectors, regions, business groups, etc.) participate in that process at different stages and through different mechanisms. Their ways of participating make them more or less influential in the actual policies adopted, and the resulting imbalance implies that policies are generally not transversal to these groups. Here, we focus on that characteristic of the political equilibrium—the fact that different groups have different degrees of influence over the PMP—and try to measure their political strength, defined as their ability to affect policies for reasons related to their participation in the PMP (as opposed to what could be characterized as "legitimate economic reasons," at least following the logic of public debate). Then, we examine the effect of the distribution of *political strengths* on aggregate productivity.

### *4.1 Measuring Political Strength*

#### *4.1.1 Model and Data*

We focus on groups defined as sector-region combinations. We define a sector at the three-digit level of sector disaggregation, and only for sectors in manufacturing, due to data availability. Our regional unit is the *departamento*. Following our description of the PMP, there are several reasons why the region and sector dimensions are relevant as a focus for policy targeting. First, a variety of policies are inherently directed at specific sectors or even products; import tariffs and tax exemptions are examples. Second, business associations, many of them sector-specific, are important representatives of business interests in the PMP. Along the regional dimension,

[35] An outstanding example is the Presidential Agency for Social Action and International Cooperation ("Acción Social"), created by Decree 2467 of 2005, to "channel and execute all social programs that depend on the Presidency," that is in fact responsible for crucial poverty alleviation policies and programs as well as for all policies and programs aimed at vulnerable population affected by drug dealing and violence. A complete list of the programs currently under direct control of the presidency can be found at http://web.presidencia.gov.co/programa/.

congressmen are elected on votes concentrated in specific regions (even senators, who in principle are elected nationally), so that the regional dimension captures the constituencies of the different congressmen. Moreover, some of the targeted policies adopted in Colombia over the last few years have been directed at overcoming the obstacles violence has imposed to development; many such instruments are targeted at specific regions, given the regional concentration of violence.

Our aim in this section is to measure the political ability of a (sector-region) group to influence relevant policies. For this purpose, we run a "policy index" of group-specific policies against indicators of group participation in the political process and alleged economic determinants of group-specific policies; the part that is explained by participation in the PMP is what we will call political strength. The strategy is summarized in equation (1) below:

$$\tau_{s,r,t} = \alpha + \beta' * PMP_{s,r,t} + \gamma' * Ec_{s,r,t} + \varepsilon_{s,r,t} \quad (1)$$

where $\tau_{s,r,t}$ is the policy index for firms in sector *s* and region *r* during year *t*, $PMP_{s,r,t}$ is a vector of variables that measure the group's involvement in the policymaking process, and $Ec_{s,r,t}$ is a vector of economic characteristics that are usually seen as the legitimate determinants of whether a sector in a given region is favored by government protection. All of these variables are explained in greater detail below. Our estimation covers the 1998-2006 period.

Our policy index summarizes policies in four dimensions: trade policy, the tax regime, export incentives, and policies derived from the Domestic Agenda. Our trade policy measure is the average nominal tariff for goods that the group produces calculated from National Planning Department records. Our tax-regime measure is the income tax exemption rate that results from subtracting the income tax rate effectively paid by each sector from the nominal corporate income tax rate in force at each point in time.[36] Our measure of export incentives is the ratio of the value of CERTS (a type of tax reimbursement instrument for exporters) to group output reported by each group in the EAM (the Annual Manufacturing Survey);[37] we calculate this ratio for the group adding firm-level CERT values and output values for the firms in a group. Finally,

[36] The income tax rate effectively paid was computed as the product of the nominal tax rate and the ratio between the effective tax payment and the tax payment that would have resulted in absence of exemptions. These variables were calculated from data made available by the Ministry of Finance (DIAN) disaggregated by ISIC three-digit sector and year.
[37] More precisely, CERTs are tax reimbursement instruments available to exporters and granted at differential rates over exports across goods. We use the value of these reimbursements reported by firms in the EAM.

our measure of policies derived from the Domestic Agenda is a variable that takes the value of 1 when there is record of a sector participating in the discussion tables in a specific region and requesting policies that were later incorporated into the 2006-2010 National Development Plan, and zero otherwise. This variable is made always equal to zero before 2004, when the Domestic Agenda discussion roundtables took place.[38] We average these four measures to obtain an index that varies between 0 and 1 and increases with benefits received by the group. Note that our measures of tax and trade regulations vary by sector and year, while our measure of export incentives varies by sector, region, and year, and participation in the Domestic Agenda varies across sectors and regions (and over time only because before 2004 it takes the value of zero for all groups). Table 3 contains summary statistics of these policy variables across groups.

**Table 3. Summary Statistics, Policy Variables 1998-2006**

| Variable | Number of observations | Mean | Standard deviation | Min | Max |
|---|---|---|---|---|---|
| Nominal tariff rate | 2209 | 0.139 | 0.041 | 0.069 | 0.203 |
| Income tax exemption rate | 2209 | 0.056 | 0.069 | 0.000 | 0.310 |
| CERT/output | 2209 | 0.001 | 0.004 | 0.000 | 0.076 |
| Policy Index with Domestic Agenda | 2209 | 0.066 | 0.069 | 0.017 | 0.361 |
| Lagged vote weight measure | 2209 | 0.003 | 0.006 | 0.000 | 0.042 |
| Lagged (log) employment | 2209 | 5.693 | 2.131 | 0.000 | 11.054 |
| TFP (log) | 2209 | 2.417 | 0.528 | -0.769 | 5.918 |
| TFP growth | 2183 | 0.011 | 0.292 | -2.367 | 4.564 |
| Lagged average plant output (log) | 2209 | 14.974 | 1.832 | 8.503 | 22.926 |
| Armed conflict (log) | 2209 | 3.184 | 1.414 | 0.000 | 6.047 |
| Dummy business association | 2209 | 0.715 | | 0 | 1 |
| Dummy business group | 2209 | 0.294 | | 0 | 1 |

Following our discussion of the policymaking process, the variables that we include in $PMP_{s,r,t}$ are the following:

- A dummy variable indicating whether there is a specialized business association representing the sector (taken from Losada, 2000, using information from the end of the 1990s).

[38] Data to create this variable come from the Domestic Agenda dataset provided by the National Planning Department. The dataset lists all the petitions by sector and region representatives, and the policy consequences they have had.

- A dummy variable indicating whether one of the four main business groups owns firms in the sector (taken from Gutiérrez et al., 2005; the authors list companies in different groups based on information for different years, all close to 2000).
- A measure suggested by Quintero (2006) that summarizes the sector's weight in regional employment and the region's importance in providing votes for senators. More specifically, the author suggests:

$$vote\_weight_{s,r,t} = S_{s,r,t} I_{r,t}$$

  $S_{s,r,t}$ is sector *s*' share of region *r*'s employment in year *t*. $I_{r,t}$ is the average share represented by region *r* in the votes obtained by the senators elected in the last election (votes in region *r* for senator *e*/total votes for senator *e*, averaged over the candidates that were elected to the Senate). We construct $S_{s,r,t}$ from the EAM and $I_{r,t}$ from 1998 and 2002 Senate election data. This variable is intended to capture the relative importance of different groups in generating votes.

For $Ec_{s,r,t}$ we follow the rhetoric of industrial policies. One frequent argument is that particularly productive sectors, and those that show rapid productivity growth, must be protected to boost long-run aggregate growth. As discussed in the introduction, theory does not support in general the argument that benefiting more productive sectors or firms increases aggregate productivity, but different models at least consistently show that favoring less productive units is damaging to aggregate productivity. It is also argued that groups that employ large numbers of workers must be favored as a means of protecting employment.

We thus include in $Ec_{s,r,t}$ measures of total factor productivity (TFP), average growth of total factor productivity, and total employment, for sector *s* in region *r* in year *t*. We obtain these measures from plant-level data from the Annual Manufacturing Survey for each year in the period 1995-2006. The survey has sector and region (department) identifiers for each plant, which we use to aggregate at the group level. Our average sector-region TFP measures are calculated from micro data, where plant-level TFP is a residual from a standard production function. We use estimates of factor elasticities from in Eslava et al. (2006); those estimates are obtained using instrumental variables methods and the EAM data for 1982-1998. In alternative model specifications we also include in $Ec_{s,r,t}$ a measure of average plant size in terms of output for each sector *s* and region *r* at time *t* (constructed from the EAM), intended to capture whether larger firms have privileged access to policymaking after controlling for other determinants of political power.

Finally, we estimate a second set of equations intended to capture the role of the civil conflict in granting political power to particular groups. In these regressions we include as an additional regressor a measure of regional violence from the conflict: the number of armed-contact events recorded by the Departamento Administrativo de Seguridad (DAS), obtained from the Observatorio de Derechos Humanos y Violencia of the Office of the Vice President of Colombia. We also interact this measure with the business associations and business groups' dummies.

After estimating equation (1), political strength for each sector-region group can be estimated by projecting:

$$\hat{\tau}_{s,r,t} = \alpha + \hat{\beta}'*PMP_{s,r,t} \qquad (2)$$

*4.1.2 Estimation Strategy and Results*

All models include year dummies as controls for omitted variables. To mitigate biases in estimation, variables with potential endogeneity problems enter the equations lagged. Model specifications vary slightly, including and excluding the average firm size.

Table 4 presents estimation results for the simpler set of regressions, where we do not include the potential effect of the armed conflict. Table 5 presents the estimation results for the second set of regressions, including our measure of regional violence and its interactions with the business association and business groups' dummies.

Our main focus on these regressions is the role of the "political" determinants of group success: our *vote_weight* measure and the dummies for business association and business group. The coefficient on the vote-weight measure is always significant and has the expected positive sign, indicating that sector-region groups that are important in providing votes are able to influence policy making tilting policies in their direction. The estimated coefficient implies that a one standard deviation change in the vote-weight measure has an effect of 0.02 on the policy index, an important effect considering that the mean of the policy index is 0.06. The results also show that sectors represented by a business association or a business group, or both—since all sectors in which the presence of a business group was identified are also sectors for which there exists a business association—are able to influence policy-making. Being represented by a business association or business group increases the policy index of a group in 0.02 or 0.01, respectively, again a sizable effect given the range for the policy index. These findings are consistent with the description of the policymaking process above.

**Table 4. Policy Benefits to a Region/Sector as a Function of Measures of Political Power**

| Dependent variable: Policy Index | (1) | (2) |
|---|---|---|
| Vote weight (t-1) | 3.302 | 3.234 |
| | (0.433)*** | (0.428)*** |
| Dummy Business Association | 0.026 | 0.024 |
| | (0.002)*** | (0.002)*** |
| Dummy Business Group | 0.013 | 0.016 |
| | (0.003)*** | (0.004)*** |
| Employment (t-1) | 0.000 | 0.002 |
| | (0.001) | (0.001)** |
| TFP (t-1) | -0.008 | -0.003 |
| | (0.003)** | (0.003) |
| TFP growth | -0.005 | -0.005 |
| | (0.003)* | (0.003) |
| Average plant size in output (t-1) | | -0.004 |
| | | (0.001)*** |
| Constant | 0.033 | 0.068 |
| | (0.007)*** | (0.011)*** |
| Number of observations | 2183 | 2183 |
| $R^2$ | 0.25 | 0.25 |
| Year dummies | yes | yes |

*Note:* Robust Standard errors. *** denotes significance at 1%, ** denotes significance at 5%, * denotes significance at 10%.

In the regressions accounting for the effect of violence, the results just described vary only slightly: a group's vote-weight continues to be important, and the effect of business associations and business groups is significant for the sector with average violence. Most interesting, interactions of regional violence with the business association and business group dummies also show positive significant coefficients, indicating that the location of a sector member of either of these groups (or both) in a region affected by the armed conflict increases its political grip. Finally, violence on its own displays a negative significant coefficient in all regressions. Sectors located in regions affected by the conflict that are not represented by business associations or backed by business groups are unable to tilt policy benefits in their direction.

**Table 5. Policy Benefits to a Group as a Function of Measures of Political Power and Violence**

| Dependent variable: Policy Index | (1) | (2) |
|---|---|---|
| Vote weight (t-1) | 3.240 | 3.169 |
| | (0.430)*** | (0.425)*** |
| Dummy Business Association | 0.010 | 0.008 |
| | (0.004)** | (0.004)* |
| Dummy Business Association and armed conflict | 0.005 | 0.005 |
| | (0.001)*** | (0.001)*** |
| Dummy Business Group | -0.001 | 0.003 |
| | (0.007) | (0.007) |
| Dummy Business Group and armed conflict | 0.005 | 0.004 |
| | (0.002)** | (0.002)** |
| Armed conflict | -0.004 | -0.004 |
| | (0.001)*** | (0.001)*** |
| Employment (t-1) | 0.000 | 0.002 |
| | (0.001) | (0.001)** |
| TFP (t-1) | -0.008 | -0.003 |
| | (0.003)*** | (0.003) |
| TFP growth | -0.005 | -0.005 |
| | (0.003)* | (0.003) |
| Average plant size in output (t-1) | | -0.004 |
| | | (0.001)*** |
| Constant | 0.048 | 0.080 |
| | (0.008)*** | (0.011)*** |
| Number of observations | 2183 | 2183 |
| $R^2$ | 0.25 | 0.21 |
| Year dummies | yes | yes |

*Note:* Robust Standard errors. *** denotes significance at 1%, ** denotes significance at 5%, * denotes significance at 10%.

In terms of "economic" determinants, our findings suggest that high or increasing productivity is not a main driver of policy in Colombia. If anything, policies tend to favor sectors lagging in terms of TFP and TFP growth. The coefficients on TFP and TFP growth measures are always negative, but significant only in the model specifications that do not control for the sector's average plant size, with which these variables have a strong correlation. Sector employment displays a positive and significant coefficient only when we control for the sector's average plant size, where the latter is found to affect negatively and significantly policy benefits. These two findings together suggest that smaller plants are targeted, but once this effect is controlled for, policy favors groups that generate more jobs. Note that the latter effect is found even though we are already controlling for the vote-weight of a group given by its participation in votes and employment.[39] Thus, the direct effect of employment found seems to suggest a genuine concern with protecting employment beyond the electoral gains that this protection may generate.

Finally, to illustrate our results, Table 6 presents rankings of the 40 sector-region groups most favored by policy according to our Policy Index, and with the greatest political strength according to the strength measure estimated as in equation (2). Our ranking is based on averages over the 1998-2006 period and is restricted to sectors within manufacturing, since we only have data for this sector.[40] Coincidences between the two rankings are striking: 37 out of 40 sector-region groups in Table 6 rank among the first 40 by both measures. These are the winners of the Colombian PMP.

It is also interesting to note in these rankings that, of the 23 three-digit sectors in our data, only five (seven) show up in the first (second) ranking, even though our measures permit in principle targeting different sectors in different regions differently. Of these targeted sectors, food products, textiles, and apparel appear in both rankings. However, in terms of the political strength that explains the targeting, textiles and apparel producers in Antioquia lead the sector; the strength of the food products sector, meanwhile, seems to come from its organization as a sector (or collection of sub-sectors) across Colombian territory, rather than the power of

[39] In turn, including total employment represented by the sector safeguards us against potential biases in our vote-weight measure, arising from its correlation with a sector's employment.

[40] Five manufacturing sectors are missing from our data, due to problems in the tax database that impeded the calculation of their Policy Indices: Beverages, Rubber products, Glass and products, Machinery (electric), and Professional and scientific equipment. We calculated policy indices for 402 region-sector groups, but estimated political strength measures for only 371 because of missing data.

producers in a specific region. Note that of the top 15 groups classified according to political strength, only four do not belong to the food products sector, and two out of these four correspond to textiles and apparel in Antioquia. Given the construction of our political strength measure, this reflects the high employment share the sector represents in a state that is important for electoral purposes.

**Table 6. Policy Index and Estimated Political Strength Rankings, by Region-Sector Group**

| Ranking | Policy Index | | Political Strength | |
|---|---|---|---|---|
| | Department | ISIC 3-digit sector | Department | ISIC 3-digit sector |
| 1 | Valle del Cauca | Printing and Publishing | Cesar | Food products |
| 2 | Choco | Food products | Nari–o | Food products |
| 3 | Caqueta | Food products | Magdalena | Food products |
| 4 | Bolivar | Food products | Sucre | Other non metallic minerals |
| 5 | Cauca | Food products | Valle del Cauca | Food products |
| 6 | Atlantico | Food products | Antioquia | Wearing apparel |
| 7 | Valle del Cauca | Food products | Boyaca | Iron and steel |
| 8 | Nari–o | Food products | Bolivar | Food products |
| 9 | Risaralda | Food products | Meta | Food products |
| 10 | Cordoba | Food products | Huila | Food products |
| 11 | Caldas | Food products | Santander | Food products |
| 12 | Quindio | Food products | Antioquia | Textiles |
| 13 | Magdalena | Food products | Cordoba | Food products |
| 14 | Antioquia | Food products | Tolima | Food products |
| 15 | Bogota | Food products | Cauca | Food products |
| 16 | Cesar | Food products | Atlantico | Food products |
| 17 | Meta | Food products | Cordoba | Iron and steel |
| 18 | Santander | Food products | Norte de Santander | Other non metallic minerals |
| 19 | Cundinamarca | Food products | Norte de Santander | Food products |
| 20 | Tolima | Food products | Bogota | Food products |
| 21 | Boyaca | Food products | Antioquia | Food products |
| 22 | Huila | Food products | Risaralda | Wearing apparel |
| 23 | La Guajira | Food products | Bogota | Textiles |
| 24 | Norte de Santander | Food products | Cundinamarca | Food products |
| 25 | Sucre | Food products | Tolima | Wearing apparel |
| 26 | San Andres y Providencia | Food products | Caldas | Food products |
| 27 | Norte de Santander | Leather products | Valle del Cauca | Wearing apparel |
| 28 | Atlantico | Wearing apparel | Casanare | Food products |
| 29 | Arauca | Food products | Norte de Santander | Pottery, china, earthenware |
| 30 | Quindio | Textiles | Risaralda | Food products |
| 31 | Caldas | Wearing apparel | Bogota | Wearing apparel |
| 32 | Bolivar | Wearing apparel | Tolima | Textiles |
| 33 | Antioquia | Wearing apparel | Valle del Cauca | Other chemicals |
| 34 | Atlantico | Textiles | Choco | Food products |
| 35 | Tolima | Wearing apparel | Santander | Wearing apparel |
| 36 | Norte de Santander | Wearing apparel | Quindio | Food products |
| 37 | Quindio | Wearing apparel | La Guajira | Food products |
| 38 | Caldas | Textiles | Boyaca | Other non-metallic mineral products |
| 39 | Risaralda | Textiles | Sucre | Food products |
| 40 | Antioquia | Textiles | Bogota | Other chemicals |

*Note:* Political Strength measure obtained using the coefficients from column (2) of Table 4. Table shows top 40 after averaging across years.

### *4.2 Effect on Aggregate Productivity*

In this subsection we present some suggestive evidence supporting the argument that targeted policies are detrimental to aggregate productivity. We use our estimated political strength measures and measures of aggregate productivity for ISIC two-digit manufacturing sectors to examine how the relative ability of groups within them (groups being ISIC three-digit sector, region combinations) to tilt policy in their favor affects productivity at a more aggregate level. One word of caution is in order: given our limited estimation horizon and the small number of two-digit sectors, our estimations have a small number of observations. We thus consider the evidence we present here as simply suggestive of a phenomenon worthy of further investigation.

To calculate aggregate TFP from micro data we follow practices that are standard in the literature (Olley and Pakes, 1996; Bartelsman and Doms, 2000; Foster, Haltiwanger and Syverson, 2008; Baily, Hulten and Campbell, 1992). Accordingly, we calculate aggregate TFP measures at the ISIC two-digit sector level as weighted averages of plant-level TFP, where the weights are the plants' shares of output in the corresponding two-digit sector. Plant-level TFP, in turn, is calculated as explained in Section 4.1.2.

Our empirical model includes three explanatory variables: the ISIC two-digit sector standard deviation of groups' political strength measures from equation (2); the average ISIC two-digit sector political strength measure; and the ISIC two-digit sector correlation between our political strength measure and the TFP of the average plant in the group. Using these three measures, we intend to capture the extent of targeting, and the degree to which targeting is or not directed at the most productive units. Following Restuccia and Rogerson (2008), for a given distribution of plant-level TFP idiosyncratic policies harm aggregate productivity, the negative effect being stronger if less productive units are those most benefited by policies. Both the standard deviation and the mean of political strength capture the extent of targeting (as opposed to horizontal policies), since deviations from the average political strength result, as we know from the previous section, in deviations from the average policy benefits obtained. These two variables are thus expected to display a negative sign in our results. The correlation between TFP and political strength is higher the better targeting is, in the sense of focusing on more productive businesses; we thus expect this variable to be positively correlated with aggregate TFP.

Table 7 presents summary statistics for these variables. It is worth noting that TFP and targeted policies are virtually uncorrelated. The fact that targeted policies are not aimed at favoring the most productive businesses already suggests disregard for the aggregate productivity consequences of targeted policies.

**Table 7. Summary Statistics, Weighted TFP and Estimated Political Strength Variables, 1998-2004**

| Variable | Number of observations | Mean | Standard deviation | Min | Max |
|---|---|---|---|---|---|
| Weighted TFP (log) | 54 | 2.108 | 0.700 | 0.878 | 4.429 |
| Political Strength - Standard Deviation | 54 | 0.017 | 0.010 | 0.001 | 0.037 |
| Political Strength - Mean | 54 | 0.099 | 0.017 | 0.083 | 0.141 |
| Correlation of Political Strength and average TFP | 54 | 0.000 | 0.002 | -0.009 | 0.003 |

Table 8 presents our econometric results. The regression includes ISIC two-digit sector and year dummies, to control for sector-specific characteristics that may affect aggregate TFP performance, and for the macroeconomic cycle. The coefficient on the standard deviation of the political strength is significant and has the expected negative sign, confirming that deviations from a level playing field have indeed been costly to aggregate productivity in Colombia. The estimated coefficient implies that a one standard deviation change in the political strength dispersion measure affects the ISIC two-digit aggregate TFP measure in -0.63. We consider this effect large, given the 2.11 mean of the aggregate TFP measure. The coefficient on the political strength average variable is not significantly different from zero. This probably reflects that the extent of targeting is best captured by the dispersion of targeted policies, as opposed to their level—if all sectors were equally targeted, even through a different combination of specific policies, the policy stance could be considered horizontal. Finally, the coefficient on the correlation of political strength and average plant TFP is positive and significant, as expected. The estimated coefficient implies that a one standard deviation change in this correlation positively affects the ISIC two-digit aggregate TFP measure in 0.2.

While only suggestive, our results in this section lend support to our hypothesis that the less than spectacular aggregate productivity performance after the market reforms of the 1990s is partly due to the persistence of targeted policy benefits granted without a clear microeconomic rationale and instead associated with the political grip of particular groups.

**Table 8. Aggregate Productivity as a Function of Political Strength Estimates**

| Dependent variable: ISIC 2-digit sector TFP | |
|---|---|
| Political Strength - Standard Deviation | -63.210<br>(33.530)* |
| Political Strength - Mean | 41.964<br>(26.946) |
| Correlation of Political Strength and average TFP | 98.464<br>(50.037)* |
| Constant | -2.048<br>(3.110) |
| Number of observations | 54 |
| Adjusted $R^2$ | 0.74 |
| Year dummies | yes |
| ISIC 2-digit sector dummies | yes |

*Note:* * denotes significance at the 10 percent level.

## 5. Discussion

The economic Policy Making Process (PMP) in Colombia has been atypical in the context of Latin America in that there has been well-organized participation by the private sector. Business and labor representatives, universities, and think tanks have had access to policymaking in arenas clearly defined by formal rules. A wide and diverse array of interest groups has thus been formally represented in policymaking in an organized way, while technocrats have been given active and extensive roles in the bureaucracy. Such a set of institutions seems to set the stage for successful economic policies, and in many ways it has.[41] In terms of policies designed to improve aggregate productivity, the participation of diverse interests should guarantee that a wide array of preferences are aggregated into the policies finally adopted, in principle favoring general welfare over specific interests.

However, after the reforms of the 1990s there is an asymmetry in the types of policies subject to consultations with the private sector using the formal mechanisms established for

[41] Urrutia (1983) and Meisel, (1996), for instance, partly credit the active participation of business representatives and technocrats in the economic PMP for the relatively stable and conservative macroeconomic policy that characterized the country over the twentieth century. The adoption of widespread market-oriented reforms in the early 1990s is another example of successful policymaking.

private participation in policymaking: while policies that affect a wide range of interests go through these channels, more targeted policies in general do not. Moreover, the same inclusive nature of consultations with the private sector makes the adoption of general policies slow and difficult, especially in the recent context of increased fragmentation of the political actors, both private and state. As a result, the pace of adoption of general-interest policies, compared to that of targeted policies, has become relatively slower.[42]

Our descriptions and findings suggest that the imbalance between productivity-enhancing but relatively hard-to-pass horizontal policies and their targeted counterparts is part of the explanation for the modest success of the economy-wide reforms of the last two decades in reaching their goal of boosting aggregate productivity. Formal mechanisms of representation of private interests in policymaking before the 1990s were similar to those that exist today: participation in boards of public institutions, and in government-led commissions. However, representatives from only a few business associations participated (generally ANDI and Fedecafé); given the greater concentration of economic activity at that time, this was sufficient to put forth the most relevant private sector interests. Market liberalization and a new Constitution in the 1990s subsequently created arenas for private sector participation that encompass a wider range of private interests in a context of greater diversification. Despite its potential virtues, in practice this new model for the participation of private actors has been largely ineffective in translating policy requests into actual policies given the intense coordination problems that arise among increasingly fragmented actors. The relative weakening of the established spaces for participation as channels to materialize private interests into actual policies has translated into increasing participation in policymaking via direct informal contacts with government officials and congressmen. On the political side, the need of private funding for political campaigns has increased, leading to greater importance of business groups, a main source of campaign funding, relative to the more encompassing business associations.

The combination of the factors described above has led to the prevalence of policymaking arenas where the balance of political muscle by diverse private interests

[42] The greater difficulties inherent to the adoption of productivity-enhancing policies are also reflected in the relatively minor budgets allocated to horizontal programs directly designed to increase aggregate productivity, compared to some sector-specific policies. For example, in 2006 the budget of Colciencias, the public institution in charge of fostering technological innovation, was less than one third of the amount allocated through tax incentives to three manufacturing sectors. Colciencias' budget for that year was of 81,000 million pesos, while the tax benefits accruing to ISIC sectors 31, 32 and 35 amounted to 284,670 million pesos.

determines policy outcomes, and these outcomes consequently imply targeted benefits. That is, lobbying and access to high-ranking officials and congressmen are more relevant in the policymaking process than more transparent forms of representation such as participation in government-led committees. The evidence we present shows that sectors and regions represented by business associations and/or business groups, and those that have a higher electoral weight for senate elections are favored with targeted benefits. Among these benefits there are tax exemptions, and protection from international competition in the form of product-specific import tariffs. Interestingly, the influence of business groups and business associations on policy benefits to a given sector in a given region is stronger for sectors located in regions more subject to violence, reflecting attempts to create economic conditions under which violence can be more effectively addressed. The fact that different groups have different amounts of power to affect policies is reflected in the granting of directed policy benefits—many in the form of exceptions to general regulations—which we find to be detrimental to aggregate productivity.

To summarize our view of the current state of private participation in the PMP, in the aftermath of reforms there are important differences in the way the private sector participates in policymaking depending on whether the policies under discussion are horizontal or vertical in nature. Productivity-enhancing policies frequently fall in the former category, undertaken by government initiative, and the participation of private interests in their adoption tends to follow formal channels. Meanwhile, private actors propose, often successfully, the adoption of vertical policies with concentrated benefits. For this purpose, they take advantage of informal channels of direct contact with high-ranking officials and politicians. In light of these circumstances, institutions that favor formal, transparent, mechanisms of private sector participation, relative to informal channels, also tend to favor a generally productivity-enhancing policy stance. The increasing fragmentation of political actors in the last two decades and the loss of coalition-building tools for the government in Congress have made political exchanges in formal and broadly encompassing arenas difficult, increasing the relative effectiveness of informal participation. The resulting success of vertical policy initiatives that contradict the general trend of dismantling targeted benefits is, we argue, part of the explanation for the lack of success of reforms in boosting productivity growth.

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