

## Paraguay: A Shift to the Left under Lugo?

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**Theme:** President Lugo's swearing-in as the President of Paraguay marks a major turning-point in the country's history.

**Summary:** In the presence of the Presidents of all Mercosur members plus those of Chile, Bolivia, Ecuador and Venezuela, Fernando Lugo was sworn in on 15 August as President of Paraguay for 2008-13. The high profile of President Hugo Chávez of Venezuela during and after the ceremony heightened speculation that Paraguay would now join the regional alliance of nations identified with '21<sup>st</sup> century socialism'. Such a view is premature, given the composition of Lugo's cabinet and the weak representation of the left in the new Congress. Rather, the opening up to Venezuela and Bolivia should be seen in the wider context of Paraguay's move away from its longstanding 'pendulum diplomacy' *vis-à-vis* its two giant neighbours, Brazil and Argentina – a move that is motivated more by the demand for renegotiation of major hydro-electric contracts with both countries than by ideological affinity–.

**Analysis:** The victory of Fernando Lugo in the presidential election on 20 April 2008 marked a turning point in the political history of Paraguay, one of the least industrialised and most unequal countries in Latin America. Lugo scored three 'firsts' with his convincing victory: (1) it put an end to the 61-year rule by the *Partido Colorado* (PC), which had been in continuous power since 13 January 1947, the longest of any political party in the world; (2) this was the first-ever peaceful change of government from one political party to another in the history of Paraguay; and (3) he became the first former Roman Catholic bishop to assume the presidency of a country.

Lugo won a convincing victory with 40.9% of the votes cast in a 66% turnout. Blanca Ovelar, the defeated PC candidate, scored 30.6%. Lino Oviedo, a maverick former army chief and leader of the populist and rural-based *Partido Unión Nacional de Ciudadanos Éticos* (PUNACE), scored 21.9%. He had been released from jail in September 2007 – where he was serving a 10-year sentence for an attempted coup in 1996– in an attempt by outgoing President Nicanor Duarte to split the Lugo vote. In a striking demonstration of the changing political mood in the country, Pedro Fadul, founder and head of the modernising pro-business party, *Partido Patria Querida* (PPQ), with strong links to conservative sectors of the Roman Catholic Church, saw his vote slump to only 2.4%, compared with 21.3% when he stood in the 2003 presidential election.

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Through much of its 61-year rule, the PC proved an effective electoral machine for maintaining elite power and entrenching social injustice through a combination of rampant corruption, control of a bloated state bureaucracy and a nationalist rhetoric that builds on Paraguay's involvement in two of the three post-independence wars in Latin America. By comparison, Paraguay's main opposition party, the *Partido Liberal Radical Auténtico* (PLRA) proved ineffectual in building an alliance against the PC during and after the Stroessner dictatorship (1954-89), when Paraguay became a by-word for corruption, smuggling and the gross violation of human rights. Despite a new democratic constitution in 1992, the legacy of the past weighed heavily against efforts for improved governance. Corruption escalated under a succession of venal and inept *Colorado* Presidents as a powerful elite that had emerged during the dictatorship jostled to retain its power in the new democratic environment, often through buying congressional votes. Three bouts of military instability (in April 1996, March 1999 and May 2000), the assassination of a Vice-president (in 1999) and the indictment of two former Presidents on corruption charges provided additional obstacles to democratisation.

After two decades of economic stagnation, the Duarte presidency (2003-08) coincided with a period of gradual but sustained growth, reaching a provisional 6.8% in 2007. This was largely the result of rapid expansion of soybean and meat production for export in response to soaring world prices. Paraguay now ranks as the fifth-largest soybean producer and the fourth-largest exporter of soybeans in the world. However this faster economic growth was built on one of the most unequal structures of land tenure in the Americas and so its benefits were captured by a small elite of soybean farmers, cattle-ranchers and corrupt politicians. According to the National Statistical Office, by 2007 35.6% of the 6.2 million population was still living in poverty and the share of those living in extreme poverty had actually increased from 15.5% in 2005 to 19.4% in 2007. Yet this was at a time when the value of exports trebled in just three years –from around US\$1 billion in 2005 to US\$3 billion in 2007. As young, poor rural Paraguayans failed to see the fruits of growth, from 2002 there was a sudden surge in migration to Europe. By 2007 there were an estimated 100,000 Paraguayans living in Spain, of whom only 11,000 were legal immigrants.

Given this economic and political background, such was the utter disillusionment with traditional politicians that when Fernando Lugo, an ex-bishop, led a march in Asunción in March 2006 to protest at alleged violations of the constitution by President Duarte, he was immediately catapulted to the national political arena. In July 2008 the PLRA agreed to support Lugo's candidacy in exchange for the Vice-presidential ticket, a tacit admission of its own weakness and a decision that provoked the ire of the two other opposition parties. Prospects for a united opposition ended when Oviedo (PUNACE) and Fadul (PPQ) reiterated their intention to stand for the presidency. Instead, the Lugo-PLRA ticket, known as the *Alianza Patriótica para el Cambio* (APC), attracted only a myriad of small left-wing parties, strong in militancy but electorally weak in Paraguay's patronage-based political culture.

#### *The Itaipú Card*

From the moment that Lugo set out on his presidential bid, he promised to renegotiate the terms of Paraguay's involvement in two mega bi-national hydro-electric projects –Itaipú with Brazil and Yacyretá with Argentina–. The Itaipú hydro-project, jointly owned by Paraguay and Brazil, is the largest in the world, with an installed capacity of 14,000 MW, generating around 90 million MWh in 2007. Under the terms of the Itaipú Treaty, signed in secret in 1973 between the military dictatorships that ruled in both countries at the time,

Paraguay must 'cede' the unused portion of its 50% energy share to Brazil. Sales to third countries are prohibited under the 50-year treaty, which expires in 2023. Paraguay currently uses only 7 million MWh per year and must cede its remaining 38 million MWh to the Brazilian state electricity corporation, Eletrobrás, at cost price. As 'compensation', Paraguay receives only US\$2.7 per MWh, equivalent to a miserly US\$103 million per year. This compares with a wholesale price inside Brazil of around US\$60 per MWh for sales of Itaipú energy by Eletrobrás to Brazilian electricity distribution companies and a price of around US\$100 per MWh paid by Argentine electricity companies to Brazil for purchases during its 2007 energy shortage. The sale price of Paraguayan energy from Itaipú is clearly derisory and totally de-linked from the soaring world price. The current arrangement is of enormous economic benefit to Brazil.

The gigantic Itaipú hydro-electric scheme is crucial for the Brazilian economy, providing 19% of all its electricity consumption in 2007. For over three decades the Brazilian government has adroitly paid off the Paraguayan political and economic elite in order to maintain this lucrative arrangement. Despite the legal obligation for 'alternating directorships', ever since the project came on stream in the mid-1980s the finance and technical directorships of the bi-national hydro company, Itaipú Binacional, have remained exclusively in Brazilian hands and the Paraguayan National Audit Office has not been allowed to examine the company accounts. Lugo repeatedly denounced 'Brazilian colonialism' and has vowed to take the matter to the International Court of Justice if its neighbour refuses to renegotiate the grossly unequal terms of the treaty. This was the first time that a Paraguayan politician had ever made such a threat and his move set off alarm bells in Brasilia. Lugo also criticised Argentina over the 3,200 MW bi-national Yacyretá hydro-electric plant, under which a similar inequitable arrangement exists for the sale of Paraguay's energy share.

Lugo's focus on Itaipú during the election campaign captured the mood of the population at large and the other candidates, all of whom had earlier criticised him for raising the issue, were forced to reposition themselves behind the call for renegotiation. A national consensus has now emerged in Paraguay on the issue of renegotiation but the response of the Brazilian government has been intransigent. The Foreign Minister, Celso Amorim, has repeatedly stated that no renegotiation can take place before 2023, when the 50-year treaty expires. In his congratulatory message to Lugo, President 'Lula' da Silva even took the opportunity to remind him publicly that renegotiation of the treaty was out of the question.

Relations with Brazil over Itaipú are also linked to the vexed question of land reform. Rural social movements emerged during the 1990s to protest against the growing land shortage for poor farmers. At first they demanded expropriation of large landholdings that had been awarded illegally to army generals and political acolytes during the Stroessner regime under the guise of 'land reform'. But from the mid-1990s the movement became radicalised as Brazilian farmers, spurred by the disparity in land prices between the two countries, bought up large tracts of land for mechanised soybean production. Over 100 rural protestors were killed by the security forces or hired gunmen over the decade 1995-2005 and these rural protests have now assumed an overwhelmingly anti-Brazilian stance, with the burning of Brazilian flags and growing condemnation of Brazilian 'imperialism'.

Most Paraguayan soybean is now produced by Brazilian immigrants. Paying no direct taxes, using non-minimum wage labour and deforesting fertile virgin land at will, these *brasiguayos* have begun to exercise their powerful economic muscle while showing scant regard for environmental protection. On several occasions from the late-1990s they successfully blocked major highways with thousands of tractors in order to halt legislation that would bring them under the tax net. Claudia Ruser, head of the powerful soybean growers association, has been an outspoken critic of Lugo, accusing him of fomenting invasions of private property by land-hungry peasant families, whose communities are increasingly becoming islands of poverty surrounded by enormous soy plantations. At a time when a trebling of world soy prices over the past 18 months has driven the area under cultivation to a new record in 2007/2008, Lugo has a strong mandate to begin taxing what is now the richest economic group in the country. But the powerful *brasiguayos* could well dig in their heels and appeal to Brazil for help.

#### *Support in Congress*

However, the political challenge facing President Lugo is considerable, given that his government lacks majority support in a conservative Congress. Despite their strong support for the Lugo campaign, Congressional representation by left-wing parties remains the same –three senators and two deputies– as in 2003-08. A major reason was the failure of 10n different left-wing parties in the APC, including Lugo's own *Movimiento Popular Tekojoja* (MPT), to agree on fielding a single list of candidates. Given the poor showing of his left-wing supporters, Lugo will be dependent on support from the PLRA – whose Federico Franco occupies the Vice-presidency– in order to push through reforms. But many powerful groups inside the PLRA are deeply opposed to the introduction of personal income taxation and land reform, both of which are central to Lugo's reform programme.

Furthermore, Lugo's victory was greatly assisted by a deep split in the PC. The former Vice-president, Luis Castiglioni, was narrowly defeated by Ovelar for the presidential nomination in a December 2007 primary that was widely regarded as fraudulent. His refusal to endorse Ovelar as the official party candidate produced a haemorrhaging of *Colorado* votes. Many of these deserters switched their votes to Lugo or Oviedo. Despite losing the Presidency, the PC retained its position as the largest party in Congress. This was the result of tactical voting by Castiglioni supporters, who continued to vote for *Colorado* candidates for Congressional seats. In the 45-member upper house the PC has 15 seats, only one less than in 2003-08, followed by the PLRA (14), UNACE (9) and PPQ (4). In the Chamber of Deputies the PC has 30 seats, seven less than in 2003-08, followed by the PLRA (27), PUNACE (15) and PPQ (3).

On a more positive note, Lugo will benefit from the bitter recriminations inside the divided *Colorado* camp, following its electoral defeat. The out-going President Duarte is widely blamed for having imposed Ovelar as his candidate to succeed him against the wishes of party activists. Although Duarte engineered his place as head of the party list for the upper house, his controversial presence as senator for the 2008-13 term would do much to split the PC in congress, something that will be greatly to the advantage of the APC when pushing through reform legislation. Castiglioni, the defeated candidate in the December 2007 PC primary, said that his *Vanguardia Colorada* faction will not recognise the leadership of Duarte. It will operate as a separate block in Congress but is likely to adopt a robust opposition to Lugo's reform programme as Castiglioni projects himself as candidate for party leader in the elections scheduled for 2010.

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### *Plans for the Future*

President Lugo's commitment to addressing inequality represents a potentially serious challenge to the status quo. However, his programme remains imprecise. His inaugural speech was strong on rhetoric (recognising his intellectual debt to liberation theology) but surprisingly weak on specific policies. He repeated the main priorities of his government – land reform, targeted poverty-reduction programmes, combating endemic corruption in the public administration and renegotiation of the Itaipú Treaty– but failed to announce any specific policies in these areas.

President Chávez of Venezuela adopted a high profile during and after the ceremony. In a cultural event that evening he danced and sang arm-in-arm with Lugo. The next day he accompanied Lugo to the poverty-stricken Department of San Pedro, where Lugo had served as bishop for nearly 11 years. Here Chávez stole the show, making a lengthy anti-US speech and signing a package of 12 aid projects for Paraguay. These included a strategic reserve stock of petroleum to overcome the shortages in recent months that had been caused by the cut-off of suppliers' credits to Petropar, the loss-making state petroleum corporation. The high profile of Chávez plus intense criticism of the media from Rafael Correa and Evo Morales heightened speculation that Lugo would align himself with the current of populist and anti-American governments in the region. However, both domestic and foreign policy considerations suggest that such an interpretation is both premature and simplistic.

On the domestic front, Lugo has named a broadly centrist cabinet, especially for the key ministerial posts. Despite strong pressure from the PLRA for its 'fair share' of ministerial posts, most senior appointments have so far been based on merit rather than political favours. His Finance Minister, Dionisio Borda, engineered a successful IMF-supported programme that avoided a debt default during the first two years of the Duarte Frutos government from 2003-05. He is committed to the introduction of the twice-postponed personal income taxation in 2009 and is toying with the idea of a tax on agricultural exports, given the windfall gains to soybean exporters. The Nobel prize winner Joseph Stiglitz was officially invited to Paraguay for the inauguration. His speech to an invited audience at the central bank called for new taxes to raise Paraguay's low tax yield –only 11% of GDP– in order to fund much-needed improvements in health and education and targeted anti-poverty programmes. His comments unleashed a barrage of criticism from rural landowners and industrialists.

The Agriculture Minister, Cándido Vera Bejarano, is no radical when it comes to land reform. He remains opposed to both land occupations by landless farmers and confiscation of land that had been illegally distributed to powerful members of the Colorado party and armed forces during and after the Stroessner dictatorship under the guise of land reform. The Industry and Trade Minister, Martín Heisecke, is a right-of-centre pharmaceutical entrepreneur. In response to the serious cement shortages in recent months caused by breakdowns at the plants owned by the state-owned monopoly, *Industria Nacional de Cemento* (INC), he said that if he had his way, the company would be privatised tomorrow. The Minister of Public Works, Efraín Alegre, is an advocate of public-private partnerships for highway construction.

On the foreign policy front, Lugo now has a strong mandate to press for the renegotiation of hydro contracts. During the inauguration ceremony, President Lula was visibly shaken by the barrage of chanting addressed to him from the 15,000 strong audience, calling on him to accept the renegotiation of the Itaipú treaty and he returned home immediately



after the ceremony. Given the current intransigence of the Brazilian government, and the fact that Paraguay also seeks to renegotiate the terms of its other major bi-national hydro undertaking, Yacyretá, with Argentina, the Lugo government's increasing ties to Venezuela and Bolivia, rather than a product of ideological affinity, have more to do with a concerted effort to break away from the *política pendular* (pendulum policy) –playing off its two powerful neighbours Argentina and Brazil against each other– that has characterised Paraguayan foreign policy for over a century to the exclusion of all other Latin American countries.

Paraguay is now developing this 'third front' as a tactical move as part of its bid to renegotiate the hydro-electric contracts with both Brazil and Argentina. Lugo has been at great pains to dismiss any affinity with the broad populist movement sweeping the rest of Latin America while at the same time applauding the greater sovereignty over their country's natural resources that Presidents Morales and Chávez have promoted. His support for Venezuela's entry into Mercosur should be seen as an effort to offset the dominance of Brazil and Argentina within the block. These geo-political considerations also help to explain Lugo's development of closer ties with the Vázquez government of Uruguay, as both seek a better deal for the smaller economies with the regional block through the mechanism of enhanced regional development funds and preferential exemptions to the common external tariff (CET).

Two further pointers suggest that the 'opening up' of ties to Venezuela is a tactical rather than a strategic move with deeper ideological implications. First, Lugo has endeavoured to maintain close ties to the US and has been invited to lunch with George Bush during his trip to the September UN General Assembly. Secondly, to the surprise of many observers, President Ma of Taiwan attended the inauguration ceremony, before which Lugo confirmed that Paraguay would continue its policy of non-recognition of the Peoples' Republic of China, in spite of the fact it is now the second most important source of Paraguayan imports.

**Conclusion:** Paraguay has finally embarked on the *alternancia* stage of its democratic process, which had been postponed for nearly 20 years since the Stroessner dictatorship ended in 1989. Underlying currents of structural reform are welling to the surface, including a new pride and self-confidence in the country's Guaraní language and cultural identity. There is a new mood of optimism in a country where most people had come to despise politicians. It is no surprise that Lugo should be the catalyst for this change –the fact that he was not a 'politician' was one of his strongest electoral appeals–. This non-partisan image will stand him in good stead as he attempts to conjure up the majorities needed to push forward urgently-needed reforms.

Paraguayans have extraordinarily high hopes that he will transform the country, with an opinion poll giving him a massive 93% rating. In rural areas there are growing demands among militant peasant organisations that he should confiscate and re-distribute large Brazilian-owned landholdings. In urban areas, there are strong middle-class expectations that he will root out corruption within the public administration. But in the absence of clear policies, these high hopes are unlikely to be met in the short term, let alone the medium term. For this reason, his honeymoon period with the electorate could prove to be relatively short. As disillusionment with lack of progress on structural reforms kicks in, the power and experience of the PC will be harnessed to recover from its shocking defeat in April 2008 –a defeat that was largely of its own making–. It remains the largest political party, inside and outside congress. It could quickly re-unite and begin to re-assert its

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authority over a debilitated Presidency. Such a scenario would bode ill for 'good governance' during the coming period. But even if Lugo can press through reform legislation, his government will face an enormous challenge in delivering a poverty reduction programme, given the control that the PC still exercises over the judiciary and the public administration. Nevertheless, whatever happens on the domestic front, there is now a cross-party consensus, backed by a groundswell of public opinion, for the renegotiation of bi-national hydro contracts with Brazil and Argentina. This will have significant geo-political implications in the region for years to come.

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