

Article

Fiscal Reform, Economic Modernization and Paradiplomacy in *Ceará* State, 1987-2006: An Experience of Internationalization outside the Richer Southern And Southeastern Regions of Brazil

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Abstract

This article aims to examine the experience of paradiplomacy in *Ceará*, one of the Brazilian states remarkable for an endogenous modernizing reform that led to economic dynamism, driven by an active strategy of internationalization of its economy and external projection. The article does a brief review of the concept of paradiplomacy in the International Relations area and then presents the experience of *Ceará* state with paradiplomacy, with its practical outcomes in an uninterrupted period of 20 years. Finally, it concludes with the warning on the importance of the politics for continuity or reversal of paradiplomacy.

Key words: Paradiplomacy; internationalization, modernization, fiscal responsibility and subnational entity.

Introduction

Amid the process of internationalization or globalization of flows of goods, services, capital and information that has been observed at least since the early of 1990s, the academic literature and practical experience indicate that the issue of international participation of subnational governments has gained visibility and may assume greater importance in future in different countries. In the global context, its growth is perceivable for at least two decades, and literature and the media increasingly deal with case studies that show this tendency.

Several authors who have researched on the role of subnational governments outside the borders of their countries approach experiences already consolidated of foreign activity of such governments, particularly in the countries of the Organization for Economic Cooperation and Development (OECD). However, the process of extroversion of subnational governments is not restricted to developed countries and is increasingly present among emerging market countries, particularly those with large surface area and federal form of government.¹

In Brazil, debate on the issue of decentralization and/or the so called paradiplomacy (international proactivity of sub-national governments) has not yet been consolidated, but it will tend to grow in the future. The expanded powers of states and

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¹ For more on OECD countries' paradiplomacy experience see: DESMET, An and DEVELTERE, Patrick. *Sub-National Authorities and Development Co-Operation in the OECD Member Countries*. OECD and Katholieke Universiteit Leuven, January 2002.

municipalities established by the 1988 Federal Constitution and the measures towards greater fiscal responsibility open perspectives that strengthen the capability and effectiveness of international activity by decentralized government units. Indeed, the specialized literature of the 1990s extended the concept of paradiplomacy and suggested the involvement of other government organizations beyond the nation-state in international activity, which is linked to the classic debate on sovereignty and federalism. The challenge for Brazil is therefore how to match the potential interest in external relations by decentralized governments (state and municipal ones) with the interests of the nation-state as a whole.²

In fact, contribution of subnational units in promoting exports and attracting public and private resources remains a complex issue in the debate on federalism and national foreign policy-making, given that it often entails a variety of prejudices and reservations. Its purpose and effectiveness inspire great controversy while its operation includes concerns about the image and credibility of the country abroad, the sharing of powers between central government and its subnational counterparts as well as feared risks to macroeconomic instability because of eventual external debt overhang by subnational units.³

In general, the ability of state governments and municipalities to act proactively in the international arena is still perceived more as some sort of fad of globalization than a genuine and permanent trend of greater autonomy of federated governments and internationalization of their economic relations. However, as the participation of these entities in international economic relations in Brazil increases, including in the areas of commercial paradiplomacy – export promotion – and financial paradiplomacy – external fund raising–, it becomes relevant to undertake extensive research on such a phenomenon and assess in more detail the scope and outreach of its impact on some domestic relevant variables.

The theoretical and empirical importance of the paradiplomacy issue is therefore associated with external activity of Brazilian subnational governments in opening markets for exports, in attraction of foreign direct investments and the straightforward external fund raising (loan agreements) from multilateral and bilateral sources to complement their needs for public investment financing. Incidentally, the significant volume of flows of external funding already raised by such governmental entities, about US\$ 36.8 billion or 37.9% of the total provided by international organizations to the country in the period 1989-2006, and the commitments to austerity (Federal Fiscal Responsibility Law or Law n^o 101/ 2000) and compliance with fiscal targets and debt control of such entities by the Federal Government (Federal Law N^o. 9496/1997)

² Among the pioneering studies on paradiplomacy in Brazil, two master's dissertations are noteworthy: i) LEAL FARIAS, Déborah Barros. *Federalismo e Relações Internacionais*. Brasília: Dissertação de Mestrado. Brasília, Instituto de Relações Internacionais, Universidade de Brasília (UnB), 2000. (unpublished), and ii) BOGEA, Antenor Américo. *Diplomacia Federativa*. Brasília, Dissertação do Curso de Altos Estudos do Instituto Rio Branco do Itamarati, 2001. (unpublished); in addition to ABREU, Márcia Donner. *O Itamaraty e a Diplomacia Federativa*, Revista Mercosul Informativo, ano III, Março-abril 1998

³ Controversy on paradiplomacy outreach on the Brazilian federation context can be seen in the following studies: i) SILVA LESSA, José Vicente. *Paradiplomacia no Brasil e no Mundo: o poder de celebrar tratados dos governos não centrais*. Viçosa: Ed. UFV, 2007, and ii) CASTELO BRANCO, Álvaro Chagas. *Paradiplomacia & Entes Não-Centrais no Cenário Internacional*. Curitiba: Juruá, 2008

impose constraints on external fund raising by those subnational entities which are not fiscally sound.

However, for those entities that are in compliance with their fiscal targets and with a plenty of leeway in debt and payment capacity, recourse to external borrowing at reasonable costs and long term is to provide a secure and stable source of funding for their investment programs of promotion of local growth and development, with positive implications for external projection of the country and its access to best practices and innovations provided by the international financial and technical assistance.⁴

Several factors, such as decentralization of resources by the Federal Constitution of 1988 for the subnational governments in Brazil, the exhaustion of federal policy for regional planning and Brazilian admission to the globalization process, throughout the 1990s, imposed on states and large municipalities in Brazil the challenge of promoting active strategies of articulation with the outside world, to open markets, raise funds and attract investments so as to create more jobs and consolidate economic activities able to compete in domestic and foreign markets. This strategy, known as federative diplomacy, as so-called by diplomats, or paradiplomacy, as denominated by academics, was intensively exercised by the State of *Ceará* in Brazil during the 90s and the beginning of the first decade of the XXIst century. This made the state extrapolate its peripheral position on the Brazilian federation, outside the richer and more industrially developed Southern and Southeastern regions, and leading it to an increasing internationalization of its economy so far then very much closed to the outside world.⁵

This article aims to examine the experience of paradiplomacy in *Ceará*, an impoverished state of the semi-arid northeast region of Brazil, with 8.2 million people, an area of 57,500 square miles and *per capita* income of US\$ 2,380 (in 2006). The state became remarkable in the last 20 years for having adopted an extensive program of modernizing reforms that led to economic dynamism and improved well-being, boosted by a proactive strategy of internationalization of its economy and external projection.

The study undertakes an analysis of both the process of fiscal adjustment and economic modernization operated in the state of *Ceará* in the period 1987-2006, as well as evolution of its strategy of internationalization which is featured as a showcase of paradiplomacy, since the examination of its experience shows a clear and conscious policy by the state government in the fields related to its jurisdiction as a subnational state entity, namely, export and tourism promotion, attraction of foreign direct investment and raising of financial resources and technical cooperation from international organizations.⁶

⁴ For more on the amount of external funding raised by the state governments in Brazil during 1989-2006, see, BESSA MAIA, José Nelson. *Paradiplomacia: a projeção internacional dos Estados*. São Paulo: Valor Econômico Newspaper, issue of June 24th, 2008.

⁵ The operational concept of paradiplomacy was formulated by Prieto Noé Cornago and widely disseminated by publishing of the book "*Paradiplomacy in Action: the Foreign Relations of Subnational Governments*", edited by Francisco Aldecoa and Michael Keating. London: Frank Cass Publishers, 1999.

⁶ For more in-depth analysis on *Ceará*'s model of internationalization, it is advisable to see: BESSA MAIA, José Nelson and LEAL FARIAS, Deborah Barros. *Do Nacional-Desenvolvimentismo à Internacionalização no Brasil Subnacional: o Caso do Ceará*. Fortaleza: Instituto Brasileiro de Relações Internacionais (IBRI) e Edições Livro Técnico, 2006.



The period of analysis focuses on the last two decades (1987-2006) because of the time in which the state governments and then the municipalities in Brazil, owing to further decentralization mandated by the Federal Constitution of 1988 and entry of the country into the globalization process, could not only perform greater role in search for markets but also raise funds for their own development, such as is the case of easier access to regular and direct contracting of external loans from international financial organizations. As the state of Ceará is concerned, the period of analysis is even more justified by comprising a continuous phase of modernization, state reform and international projection, all implemented by the same political elite formed around the Party of Brazilian Social Democracy (PSDB), which held power at state-level executive power branch for 20 years in five consecutive terms.⁷

The Relevance of the Paradiplomacy for Public Policy-Making

Both the academic literature and practical experience suggest that subnational governments engagement in international affairs is gaining strength and may be considered an important factor for many countries. Throughout the second half of the twentieth century, especially after the Cold War, under the theme herein discussed, the main consideration to be made in the foreign policy area of many federal countries is the fact that the international environment is no longer exclusively conditioned by strategic issues identified as high politics (security affairs), but is increasingly moving to focus on issues deemed as low politics (economic relations). This change of focus was important for the subnational governments for having directed them to a position of proactivity in the external scenery and opening the opportunity for adjustments in formulation of national foreign policy.

⁷ As a matter of fact, the so called “Changes Project” and its modernizing and reformist mystique ruled the political life in Ceará during the terms of governors Tasso Jereissati (1987-1991, 1995-1998 and 1999-2002), Ciro Gomes (1991-1994) and Lúcio Alcântara (2003-2006), all of them were then affiliated to the Brazilian Social Democracy Party (PSDB).

It is likely that the main outcome was the remarkably increasing difficulty of the central governments in controlling, in a centralized fashion, the impacts of international economic developments on the different segments and interest groups situated within its own territory. In this case, in times of globalization, centrally made and implemented foreign policy by the bureaucratic apparatus of the central government would not be either efficient or agile enough to timely respond to the dynamic economic issues faced by subnational governments.

Moreover, with increasing international competition and the difficulties caused by economic changes, the subnational governments seem to be assuming the tasks of seeking to increase exports, attracting foreign direct investment and raising funds across national borders. In this context, centralization of tasks by the nation-state, deemed necessary to deal effectively with matters related to war and peace, loses part of its role to diversified actors, requiring a more appropriate approach in coping with issues of trade and finance since the flow of goods and services and investment produces different impacts and promotes differentiated interests among the various subnational territory entities within the same country.

It is also worthy to mention that formation and consolidation of regional integration blocks had significant impact in several federations, such as the United States, Canada and Mexico under the Free Trade Agreement of North America (NAFTA), Brazil and Argentina under the MERCOSUR, as well as Germany, Austria and Belgium under the European Union (EU). The geographical borders between these countries are no longer seen as an immediate concern of national security, but otherwise observed as market opportunities for exports, investment and financing. The free movement of capital, the increasingly intense search for reduction of production costs and greater scope of choice for location of production have also brought impacts.

Therefore, the central governments are not the only ones to striving to bring new companies and assembly lines to their territory: their own subnational governments have taken initiatives and competed heavily for bringing such investments to their jurisdictions. Those subnational entities have even been often accused of promoting a deleterious competition (the so-called fiscal war) for the federal union to which they belong.⁸

The Concept of Paradiplomacy: a brief review of the literature

The researcher of Basque origin Soldatos (1990), by examining the issue of increasing involvement of subnational governments in the world scenery, coined the term "paradiplomacy" to describe the international initiatives by such substate governments. The term was also widely disseminated by the Canadian author Duchacek (1990), which abandoned its own terminology "microdiplomacy" by recognizing that

⁸ For more on the so called "fiscal war" in Brazil, it is advisable to see the following articles: i) TENDLER, Judith. *"The Economic Wars Between the States"*. Report for the Banco do Nordeste/MIT Project, 2000, and ii) ROCHA, Antônio Glauter Teófilo; AMARAL FILHO, Jair do; e MELO, Maria Angela Campelo de. *"As políticas industriais da Bahia, Ceará e Pernambuco: existe algo mais que guerra fiscal?"* In: Anais do IX Encontro Regional de Economia, 2004, Fortaleza.

the term could be considered derogatory, and preferred to adopt the denomination given by Soldatos, which happened to prevail in the specialized literature⁹. Duchacek established differences among transborder paradiplomacy (relations between neighboring substates separated only by the international frontier of their own countries), the transregional paradiplomacy (relations between substates of different countries but not necessarily contiguously located) and global paradiplomacy (including substate relations with counterparts in the world as a whole).

However, as highlighted by Leal Farias (2000), the word paradiplomacy won a more different use than the one proposed by Soldatos and Duchacek. James Der Derian (1987), by using a "neoclassical" approach and considering the nation-state as the only actor to have diplomacy, puts paradiplomacy as a form of non-governmental diplomacy, no matter if it is central or not central. For Der Derian paradiplomacy would be any kind of activity of non-governmental non-state actors. It would include transnational corporations, international labor organizations, religious communities, non-governmental organizations (NGOs), international lobbying, scientific associations, among other possible "categories" of actors. By its lack of specificity, such "post-modern concept" of the paradiplomacy will not be used in this article.¹⁰

Moreover, the British theorist Brian Hocking suggests the idea of "multilayered diplomacy", i.e. multiple layers of diplomacy. What Hocking criticizes in the term coined by Soldatos, and also taken forward by Duchacek, is that it incorporates the idea of permanent competition and conflict between the central government (CGs) and non-central or subnational governments (NCGs). Hocking suggests that there is an interaction between these two spheres of authority, since subnational governments are themselves governments after all, showing that there are issues pertaining to both spheres of governance.¹¹ In the same vein, it is noteworthy to cite Iñaki Aguirre (1999), as summarized by Leal Farias (2000:18):

"As Aguirre puts (1999:201)," the analytical approach proposed by Hocking takes seriously into account the political nature of NCGs [non-central governments]. In fact, this "multilevel" and theoretically more comprehensive approach, operates a Copernican revolution in relation to approaches to NCG behaviour in foreign activities, since these activities are no longer studied from a purely 'state-centric' point of view, from outside and from the top, as they previously were, but from their own position". Aguirre reaches an important conclusion in his article (1999:205): "the highly relevant international activity of NCGs is definitively not an "abnormal", not even a parallel form of diplomacy". For himself, "the international involvement of NCGs could much more properly be labeled "post-diplomatic", because it is a process that moves beyond the nation-state, that is, "beyond diplomacy."

The notion of "diplomacy of multiple layers" by Hocking is adopted in this article, which considers that there are major points of convergence between the interests

⁹ See, incidentally, SOLDATOS, Panayotis. "An Explanatory Framework for the Study of Federated States as Foreign-policy Actors", as well as DUCHACEK, Ivo. "Perforated Sovereignities: Towards a Typology of New Actors in International Relations", both articles in: *Federalism and International Relations: the role of subnational units*/Eds: Hans MICHELMANN and Panayotis SOLDATOS. Oxford: Clarendon Press, 1990.

¹⁰ For more details, see, DER DERIAN, James. *On Diplomacy: A Genealogy Of Western Estrangement*. Oxford: Basil Blackwell, 1987

¹¹. For more, see, HOCKING, Brian. "Patrolling the "frontier": Globalization, Localization and the "actorness" of non-central Governments". In: Francisco Aldecoa e Michael Keating (eds.) *Paradiplomacy in Action: the Foreign Relations of Subnational Governments*", London: Frank Cass Publishers, 1999.

of central governments and subnational governments. Among these points, there is willingness to expand the economic relations of the country as a whole with the rest of the world. But given the wide dissemination of the term "paradiplomacy" in the academic, governmental and international organizations means, it will be the one used in this article:

"... paradiplomacy can then be defined as non-central governments' involvement in international relations through the establishment of permanent or ad hoc contacts with foreign public or private entities, with the aim to promote socio-economic outcomes or cultural issues (e.g., export promotion, investment attraction, international tourism marketing, funds raising and technical cooperation agreements) as well as any other foreign dimension of their constitutional competences".¹²

Soldatos and Duchacek and were pioneers in identifying a theoretical framework to analyze and interpret the growing international activity of subnational or non-central governments (NCGs). In this case, the framework chosen was the "transnational global approach" and the notion of "complex interdependence" put forward in the theoretical essays by Robert Keohane & Joseph Nye (1977). Given the major changes underway in the world in the mid-1970s, both authors argued that the new agenda of international relations would be characterized by an increasing number of complex issues, without a clear hierarchy or easy solutions, to involve all levels of governance. Therefore, any possible solution to international problems would require higher levels of intergovernmental cooperation. Inadequate coordination of policies on such issues would entail significant costs while several issues could raise different coalitions and different degrees of conflict.¹³

Keohane and Nye were perhaps the first theorists to question the realist model of unitary state-centric actor in international politics, recognizing that world politics is developed in a more complex world of interdependent relations, formal and informal, which happen not only between nation-states but also among private corporations, international organizations and other actors. However, Nye and Keohane focus only interstate, transnational and transgovernmental relations, which is clearly insufficient to take the subnational governments into account. Even if they can be fit into the category of transgovernmental relations (which associate actors of different structures of governance that maintain direct relations with similar structures in other countries, with international organizations and non-governmental actors). This category also covers combinations of different nature, as those which do not pass through the screening of the ministries of foreign affairs or other bureaucratic agencies of central governments.

¹² This theoretical and pragmatic definition of paradiplomacy was made by CORNAGO PRIETO, Noé: "Diplomacy and Paradiplomacy in the Redefinition of International Security: Dimension of Conflict and Co-operation". In ALDECOA, Francisco and KEATING, Michael (eds.). *Paradiplomacy in Action: the foreign relations of subnational governments*. London: Frank Cass Publishers, 1999. pp.201-205.

¹³ Robert Keohane and Joseph Nye in *Power and Interdependence. World Politics in Transition*. Boston, Little, Brown, 1977, by analyzing the various and complex international connections, speak on a complex interdependence between states and societies, noting that the economic links have increased while the military links have been reduced, despite remaining to be important. In a certain way, both authors throw the international relations into the area of international political economy (IPE), but still keeping some of the legacies of the realism school. They also put the international organizations at the forefront of international relations. Thus the authors unleash subsequent contributions of globalists and transnationalists, for whom the economic well-being on the international politics stage becomes as much important as are security issues.

Thus, the analytical category of Keohane and Nye becomes too wide, losing its explanatory power.

James Rosenau (1990), in his turn, distinguished actors in the international arena as "sovereignty-bound actors" and "sovereignty-free actors". This distinction emphasizes what the constraints and responsibilities of sovereignty can imply for the external action of international actors. Thus, the sovereignty-bound actors (basically central governments) would be obliged by their sovereign responsibilities to rely on various issues in the global agenda and allocate their resources between them, while the sovereignty-free actors, with less dispersed responsibilities, would be free to pursue more limited and specific objectives. Among the diverse range of sovereignty-free actors (transnational corporations, ethnic groups, bureaucratic agencies, political parties etc), Rosenau also included the subnational governments.¹⁴

In a more recent article, referring to the dilution of national and international spaces, James Rosenau (1997) examines the formation of what he called a new "political border" involved in multiple contradictions and changes regarding the distinction between foreign and internal affairs and with regard to state sovereignty as well. The formation of a new border is related to the ability of states to absorb and adapt to changes considering the formation of a new phenomenon. Understanding the international reality would be therefore directly related to this new border, which would mean a new and wider political space, a space where the international world is revealed. As the author himself expresses:¹⁵

(...) The worldview should recast the relevance of territoriality, highlight the porosity of boundaries, treat the temporal dimensions of governance in the less significant than the spatial dimensions, recognize that networking organizations have become important to the hierarchical ones, and posit shifts of authority to subnational, transnational, and nongovernmental levels to normal. "

From similarities and differences between central and subnational governments, and what they cause in terms of international relations, scholars like Hocking (2004) and Paquin (2005) classify the latter as mixed actors, half way to what Rosenau did. In other words, they prefer to consider the subnational governments in a mixed category, which combine characteristics of sovereignty-bound actors and sovereignty-free actors. Hocking (2004) even goes further as he highlights the greater freedom of choice with which the subnational governments can rely on in comparison with the central governments, which are tied to the commitments of foreign policy. For lacking foreign policy powers, the subnational entities need not either assume the responsibilities inherent to the nation-state condition and thus they can act more flexibly.¹⁶

¹⁴ For more, see ROSENAU, James. *Turbulence in World Politics: A Theory of Change and Continuity*. Princeton, N.J.: Princeton University Press, 1990.

¹⁵ For more see ROSENAU, James. *Along the domestic-foreign Frontier: "exploring governance in a turbulent world"*. *Cambridge Studies in International Relations*, 1997. pp. 29.

¹⁶ See, by the way, the following articles: HOCKING, Brian. *Regionalismo: "uma perspectiva das relações internacionais"*. In: VIGEVANI, Tullo; WANDERLEY, Luiz Eduardo; BARRETO, Maria Inês & MARIANO, Marcelo Passini (orgs.). *A Dimensão Subnacional e as Relações Internacionais*. São Paulo, Editora da PUC/Editora da Unesp/Cedec/Fapesp, 2004, e PAQUIN, Stephane. *"Les Actions Extérieures des Entités Subétatiques: Quelle Signification pour la Politique Comparée et les Relations Internationales?"* *Revue Internationale de Politique Comparée*, Vol. 12, n° 2, 2005.

From the foregoing, one may infer that despite the phenomenon of paradiplomacy is a reality in today's domestic and foreign policy of many and major countries, its theoretical framework is still underdeveloped, requiring an additional effort of theory building so as to allow the appropriate insertion of the subject into the analytical categories and current research agenda in International Relations. Because of inherent complexities involved in domestic and foreign public policy-making and the governance management at subnational entities, the subject of paradiplomacy is not restricted to the International Relations field but also because it has to do with both International Political Economy (IPE) and Federalism Analysis or Economics of Public Sector (EPS), requiring thereby the simultaneous pursuit of several multidisciplinary skills and adoption of analytical and empirical verification methods which are quite different among themselves.

It is expected, however, that the challenge to gather the academic disciplines mentioned above in the treatment of the subject of paradiplomacy in the international relations in Brazil will offer an important contribution to better understanding of this issue and provide useful subsidy for eventual improvement of the mechanisms of foreign insertion of the country as a whole as well as the articulation of the Brazilian nation-state foreign policy with the foreign proactivity of its constituent subnational entities.¹⁷

The experience of Fiscal Reform, Economic Modernization and Paradiplomacy in the State of Ceará

Known as one of the most backward areas of Brazil for long, *Ceará* state began to change its condition in the late 1970s, when the incipient industrialization, encouraged by federal tax incentives, generated a value-added of the manufacturing industry greater than the product of agriculture and cattle-raising combined. This growth instigated awareness of a group of "young" local entrepreneurs, dissatisfied with the attitude of traditional oligarchs, the so-called "politics colonels". Gathered in an old business association (the Industrial Center of Ceará-CIC, founded in 1919), these new leaders began to discuss alternatives to break with the backwardness and modernize the local public administration and the economy.

This regenerative movement started in 1978 by converting the CIC in a forum of discussion which led to political repercussions. In the elections for governorship of the state in 1986, the former chairman of the CIC, Mr. *Tasso Jereissati*, an entrepreneur (then 36 years old), now an incumbent senator of the Republic, was chosen to run for governor against the proxies of the old oligarchy. The mobilization of civil society led by CIC managed to gain support enough to defeat the so-called "colonels".¹⁸

¹⁷ Incidentally, there is a research project for doctor's degree in progress at the Institute of International Relations (IREL) of the University of Brasília (UnB), trying to combine the simultaneous pursuit of several multidisciplinary skills to prove empirically the existence of financial paradiplomacy in Brazil and examining its impact on a set of economic variables relevant to both the country and the subnational levels.

¹⁸ For a detailed reconstitution of the pathway of the Ceará Industrial Center (CIC) from its renewal until the arrival of business reformers to power at the state level, see. MARTIN, Isabela. *Os Empresários no Poder: o Projeto Político do CIC (1978-1986)*. Fortaleza: Secretaria da Cultura e Desporto do Estado do Ceará, 1993.

The fiscal responsibility as a basic requirement of modernization

The paradiplomacy, as an ingredient of the strategy of modernization in *Ceará*, began almost at the same time it implemented a major fiscal reform in 1987, when the local state machine was in complete bankruptcy. The situation of managerial chaos was then addressed by means of strict fiscal adjustment measures to curtail expenditures, recover revenues and renegotiating debt. The measures had immediate effects: the management reform excluded hundreds of "ghost servants", the accumulation of positions by the same persons in the civil service payroll as well as undue wage perks. Around 40,000 paychecks were eliminated. The corruption was been tackled successfully and computerization of the systems for collecting taxes and rationalization of expenditure were adopted to ensure greater efficiency and control in government management.¹⁹

The pioneering fiscal adjustment and reform of the state machinery in *Ceará* had faced strong resistance inside the corporatist groups previously privileged by the old pork barrel style of administration. Without political support for measures requiring legislative change, the collective demands for better public services had to be met through new and innovative practices for improving projects management. The state government of *Ceará* came to encourage direct participation of communities to identify demands and monitor the management of services. The success of public projects with initiatives of participatory approach in *Ceará* aroused interest in Brazil and abroad, attracting international organizations consultants, academics and journalists all curious to understand the success achieved in one of the most traditionally backward areas of northeastern Brazil.²⁰

The fiscal shock of 1987 and regime change for 20 full years running towards fiscal responsibility led *Ceará* to become a sort of management model for subnational entities in Brazil and in other developing countries. As the Table I below shows, curtailment in the state personnel expenditure from the unthinkable mark of 92.3% of net current revenues in the period 1979-85 to less than 50% in the 2001-2006 time span, released resources to invest 10% of total expenditure (capital expenses) and allocate

¹⁹ For more in depth analysis on the fiscal adjustment process in the state of *Ceará*, see the following articles: de BESSA MAIA, José Nelson. "O Bem-sucedido Ajuste Fiscal do Ceará". Rio de Janeiro: FGV, *Revista Conjuntura Econômica*, dezembro de 1993, e de BESSA MAIA, José Nelson e BOTELHO, Demartone. "Estabilidade e Crescimento: o Caso do Ceará", Rio de Janeiro: FGV, *Revista Conjuntura Econômica*, outubro de 2000. For aspects dealing with political analysis of the state reform in *Ceará*, it is advisable to see a series of articles contained in PARENTE, Josênio e ARRUDA, José Maria (orgs.) *A Era Jereissati: Modernidade e Mito*. Fortaleza: Edições Demócrito Rocha, 2002.

²⁰ For more, see, i) TENDLER, Judith. *Good Government in the Tropics*. The Johns Hopkins University Press. Baltimore: 1997; ii) The World Bank. *Poverty Reduction, Growth, and Fiscal Stability in the State of Ceará*. State Economic Memorandum. Policy Report no 19217-BR, Washington, D.C., August 2000; iii) The World Bank. *Brazil, Strategies for Poverty Reduction in Ceará: The Challenge of Inclusive Modernization*, Report No. 24500-BR (In Two Volumes) Volume II: Technical Paper, Washington, D.C., April, 2003; iv) The Interamerican Development Bank (IADB). *Estado do Ceará: Análise das Finanças Públicas e Tendências Sócio-Econômicas*. Relatório, 1994; v). The Economist, *Hope from the Northeast*, 335, December, 1991, and vi) The Economist, *Leading by example: Paraná and Ceará*, Survey of Brazil, April, 1995.

12% more of the total expenditures with timely payment of debt service, which is the only way to assure new internal and external fund raising. By the way, fund raising accounted for 5.6% of total revenue in the period 2001-2006, even so just half of what it was during the previous stage of chronic fiscal imbalance.

| State of Ceará: Fiscal Performance, 1979-2006 | | | | | |
|---|---------------------------|----------------------|-----------------------|-----------|-----------|
| Discrimination | Periods | | | | |
| | Chronic Unbalance 1979-85 | Fiscal Shock 1987(*) | Fiscal Responsibility | | |
| | | | 1988-94 | 1995-2001 | 2001-2006 |
| 1. Tax Revenues | | | | | |
| Real Growth (**) | 4.6 | (11.2) | 9.2 | 3.7 | 1.4 |
| 2. Payroll Expenditure/ | | | | | |
| Net Current Revenue | 92.3 | 86.3 | 54.7 | 52.9 | 49.7 |
| 3. Investments/ | | | | | |
| Total Expenditures | 2.9 | 1.7 | 9.7 | 9.5 | 9.8 |
| 4. Debt Service/ | | | | | |
| Total Expenditures | 10.1 | 44.3 | 11.8 | 11.0 | 12.4 |
| 5. Credit Operations/ | | | | | |
| Total Revenues | 11.2 | 23.0 | 7.4 | 8.3 | 5.6 |
| 6. Gov't Current Account Savings/ | | | | | |
| Net Current Revenue | 6.5 | (37.5) | 37.7 | 11.4 | 12.0 |
| Source: Ceará State Treasury Department; elaboration: the author | | | | | |
| (*) the year the fiscal shock happened giving way to radical change in the State management | | | | | |
| Current account savings=current revenues - current expenditure | | | | | |
| (**) At constant prices (deflated by IGP-DI/FGV). | | | | | |

As a result of reforms conducted in *Ceará*, from 1987 until 2006, the state government, over five consecutive terms of governorship with the same political view, started to generate net savings in the budget current account at stable levels, enabling it to leverage resources from internal sources, and especially from external lenders (multilateral and bilateral financial organizations). At the same time, pro-business orientation of the state government and its balanced fiscal position enabled the state to put in place an active industrial policy for attracting private investment via tax breaks and financial support. These two factors resulted in continued increase in gross fixed capital formation and removal of location competitive disadvantages. This gave way, in turn, to a virtuous process of local industrialization and sustainable growth, driven by increases in public and private investment.

The Economic Dynamics as the Pillar of Modernization

Combining fiscal responsibility and paradiplomacy in conduct of government actions led *Ceará* to a more dynamic economy based on exploitation of its comparative advantages in agribusiness, textiles, clothing and footwear industries, exportable fruit growing and tourism.

Based on regional accounts data from the IBGE and the Institute of Economic Research and Strategy of *Ceará* (IPECE), one may observe, in the Table 2 below, that the state economy grew at the average real rate of 4% real per year, in the period 1985-94, above the national growth rate (2.25% per year), what increased the state's share in the national GDP. In the following period (1994-2001), featured by major changes (like the Real Plan, the inflation stabilization impact on subnational public finances and the 1997-98 Asian and Russian crises), *Ceará* grew almost as fast as the Brazilian average (2.25% per year). In the final period (2002-2006), *Ceará's* economy expanded even faster, at the average rate of 3.5% per year (compared to 3.27% for the country as a whole). According to IBGE figures, with such a performance, *Ceará's* economy came to account for more than 2% of the Brazilian GDP in 2006 compared to 1.7% in 1985.²¹

The role of Commercial Paradiplomacy in *Ceará's* foreign trade

The state of *Ceará* development strategy had a clear paradiplomatic component of export promotion, in particular for manufacturing industry production fostered by the local policy for attracting private national and foreign direct investments. In fact, three factors contributed to promote exports in the state: i) establishment of an external articulation apparatus in the state administration, operated by the Economic Development (SDE) and Irrigated Agriculture (SEAGRI) Departments and also by the Governor's International Affairs Secretariat (ASSINTER), all of which were established in the second half of the 1990s; ii) enhanced operational partnership among the state government departments, the Small Brazilian Service for Support of Micro and Small Companies (SEBRAE/CE) and *Ceará* Business Federation of Industries (FIEC), and iii) entry into operation of the modern port complex of *Pecém* facilities (in 2001). All these factors combined encouraged the local business community to expand export earnings.²²

²¹ Regional accounts (GDP data) for all subnational entities in Brazil are jointly computed by the federal statistics and geography institute (IBGE) and the state-owned statistics agencies using the standard methodology so as to allow comparisons among the different subnational units. The state statistic agency in *Ceará* is the Institute of Economic Research and Strategy of *Ceará* (IPECE). Both IBGE and IPECE have accessible and friendly web sites: www.ibge.gov.br and www.ipece.ce.gov.br.

²² According to the State of *Ceará* reports the commercial paradiplomatic action focused specially on the European Union (EU) countries (Spain, Italy and Portugal), Eastern Asia (China and South Korea), Africa (Angola, Cape Verde and Senegal) and Latin America (Argentina, Chile and French Guiana). For more details, see: *Ceará. Assessoria Internacional. As Relações Internacionais do Ceará: Relatório de Atividades 2005*. Fortaleza: Gabinete do Governador, 2006. The positive results of *Ceará* state commercial paradiplomacy, operated by the state agencies (such as SDE and the Governor's Office International Affairs Secretariat) were also highlighted by SARAIVA, José Flávio Sombra. "Federalismo e Relações Internacionais". In: *Relações Internacionais do Brasil: temas e agendas*, Volume 2/Henrique Altemani de Oliveira & Antônio Carlos Lessa (orgs.). São Paulo: Ed. Saraiva, 2006. pp. 443-450

| Table 2. State of Ceará: Economy and External Sector Performance, 1985-2006 | | | |
|---|---------------------------|---------------------------|---------------------------|
| Discrimination | Yearly Change 1985/1994 % | Yearly Change 1994/2001 % | Yearly Change 2001/2006 % |
| I - Gross Domestic Product | | | |
| Brazil | 2.2 | 2.25 | 3.27 |
| Ceará | 4.00 | 2.24 | 3.5 |
| Share % CE/BR | 1.72(1985) | 1.99 (2001) | 2.02 (2006) |
| II- Setor Externo | | | |
| 2.1.Exports (US\$ million)** | | | |
| Brazil | 6.1 | 4.25 | 18.75 |
| Ceará | 4.99 | 6.71 | 12.75 |
| 2.1.1.Manufactured goods | | | |
| Brazil | 6.6 | 4.02 | 17.8 |
| Ceará | 10.8 | 12.83 | 14.12 |
| 2.2. Imports (US\$ million)** | | | |
| Brazil | 10.8 | 7.7 | 10.5 |
| Ceará | 21.3 | 7.6 | 12.0 |
| Yearly Average Value | | | |
| 2.3. International Tourists (1000 persons) | | | |
| Brazil | 1,625,072 | 4,254,425** | 4,643,241 |
| Ceará | na | 93,302 | 222,239 |
| Share % CE/BR | - | 2.19 | 4.79 |
| Loan Agreement signed in the period | | | |
| 2.4. External Financing contracted by Ceará State (US\$ million)*** | | | |
| Number of Projects | 4 | 10 | 5 |
| Sources: IPECE;IBGE; MDIC/SECEX; EMBRATUR Elaboration: the author | | | |
| (*) change rates on current dollar value | | | |
| (**) average value from 1996-2001 | | | |
| (***) international organizations' credits, not included external funds raised by the Federal Government and allocated in the State | | | |
| na - not available | | | |

According to Table 2 above, based on figures released by the Brazilian Ministry of Development, Industry and Foreign Trade (MDIC), *Ceará's* exports jumped from the modest mark of \$ 216 million, in 1985, to \$ 527.6 million in 2001, until to reach U.S. \$ 961.8 million in 2006, having grown 6.7% annually between 1994-2001, against only 4.2% for Brazil as a whole, after having expanded at an average rate of almost 5% in the 1985-1994 period. In the following time span, *Ceará's* exports continued to grow vigorously (12.75% per year) but at lower pace than in Brazil as a whole (18.75% per year). The export earnings reached the record mark of \$ 1.27 billion in 2008.²³

Such an export performance was also a result of increase in capital and intermediate goods imports which helped to modernize the local manufacturing industry and enhance its capacity to compete in foreign markets. During the three periods under review, *Ceará's* imports grew strongly from 1985-1994 (around 21.3% per year compared to just 10.8% per year for Brazil as a whole) and from 2001-2006 (12% per year compared to 10.5% p.a. to the all country combined), meanwhile the import bill almost reached the national pace during 1994-2001 (7,6% against 7.7% p.a.).

Access to imported machinery and inputs seemed to have really increased competitiveness of *Ceará's* industry until then remarked for small exposition to external markets. In fact, from 1994-2001, exports of manufactured goods made in Ceará rose three times more than the Brazilian manufactured goods (12.8% p.a. against 4.0% p.a.). In the final period of 2001-2006, *Ceará's* imports kept growing (14,1% p.a.) but stood

²³ The MDIC provides regular and detailed statistic series of foreign trade for the Brazilian states and major municipalities in a monthly basis. For more, see <http://aliceweb.desenvolvimento.gov.br>.

behind the Nation (17.8% p.a.). Despite this, *Ceará's* manufactured goods exports continued to expand very fast, reaching the record mark of \$ 490 million in 2006.

The role of the Commercial Paradiplomacy in *Ceará's* international tourism

Another important paradiplomatic factor in the developmental strategy of *Ceará* was fostering a dynamic tourism sector with high multiplier effects in income and employment. As a matter of fact, establishment of a Tourism Department (SETUR) by the state administration in 1995 gave way to a long-term planning for the sector with focus on international visitors and investors. With the state government efforts to open air connections straightway to and from Europe (via TAP Air Portugal), Africa (via TACV Cape Verde Airlines) and Latin America (via TAF airlines), attract foreign investments into the sector of hotels and resorts, train the local workforce and promote *Ceará* destination inside the major emissive tourism markets (by participating regularly in fairs and conventions in Europe and Latin America), *Ceará* local tourism authorities managed to greatly expand entry of foreign tourists, thereby transforming the state in one of the gateways for international tourism towards Brazil.²⁴

As a result of this strategy to develop and promote a competitive tourism sector in the state, *Ceará* has really taken off as an important tourist destination in Brazil. According to data from the Brazilian Institute for Tourism (EMBRATUR), a Federal government agency (see Table II above), the number of foreign tourists in *Ceará* rose from an annual average of only 93,300 people in the period 1996-2001, to the mark of 222,000 people per year during 2001-2006, more than doubling its share in total entry of foreign tourists in Brazil (from 2.19% to 4.79% between these two periods). This result is no doubt impressive for a place which was rather isolated from the outside world and the routes of international tourism 20 years ago. Development of tourism activities in *Ceará* was so much pronounced that its share in the state economy more than doubled in ten years as it came to account for 13.6% of the local GDP in 2005.²⁵

The role of financial paradiplomacy in financing *Ceará's* public investment

The results achieved by the fiscal reform in the state of *Ceará* led to financial creditworthiness and continuous inflows of both bilateral technical cooperation projects with development aid agencies in countries like Germany (GTZ), Japan (JICA), United Kingdom (DFID) and Spain (AECID) as well as of foreign loans to support implementation of public investment projects from international financial organizations such as the World Bank (IBRD) and Inter-American Development Bank (IADB) and bilateral agencies of Germany (KfW) and Japan (JBIC) as well. Those loan agreements, all of which have to be given guarantee by the Federal government, were used to finance investment programs in areas as diverse as infrastructure (water resources,

²⁴ A detailed analysis of development of the tourism sector in *Ceará* and its attraction policy for foreign investors can be seen at: CABRAL, Alexandre and TELES, João Agostinho. *Mercado Turístico e Oportunidades de Investimento no Ceará*. Estudos Turísticos, SETUR nº 19, janeiro 2005. For statistical figures on tourism performance indicators at state-level in Brazil, see EMBRATUR, Anuário Estatístico, volumes 32-35 [http://www.braziltour.com/site/arquivos/anuario_2008___internet.pdf] access in March, 23, 2009.

²⁵ For estimates on the weight of tourism income in *Ceará's* GDP see: ABREU MOURA, Francisco Carlos: "A Economia do Turismo e o seu impacto no Produto Interno Bruto do Ceará". Master's dissertation, CAEN, Federal Universidade of Ceará, 2007. (unpublished)

roadways, energy, sanitation and urban development) and social services (rural poverty, social assistance, education and health).²⁶

From 1990 to 2006, according to the Department of International Affairs (SEAIN) of the Brazilian Ministry of Planning, Budget and Management (MPOG), the State of Ceará signed directly (with approval of the Federal Government) 19 loan agreements with international organizations reaching total value of almost US\$ 1.5 billion, apportioning at least an additional one-third of this amount as local counterpart funds and consolidating one of the largest portfolios of international loans among Brazilian states, behind only to the more developed and more populous Brazilian states like *São Paulo*, *Rio de Janeiro* and *Bahia*.²⁷

In addition to the direct contracting of external loans by the State, *Ceará* has received at the same time substantial external funds contracted by the Brazilian Federal Government for allocation in infrastructure projects in the State territory, such as the implementation of the *Ceará's* capital city (Fortaleza) Metrorail (so called Metrofor project), financed jointly by the Japanese Bank for International Cooperation (JBIC) (US\$ 285 million) and the World Bank (€ 98.6 million). Those external funds borrowed by the federal authorities and transferred freely to the State reveal how effective has been the local paradiplomacy efforts (federative diplomacy), given that the State has shown the ability to articulate their interests with those of the Federal Government and with the international financing organizations, in open competition against other Brazilian states.

This successful aspect of the financial paradiplomacy carried out by *Ceará* State demonstrates something like a virtuous circle of fiscal adjustment/international foreign proactivity/economic growth, serving as a lesson for other Brazilian states, including those more developed and populous, like *São Paulo* and *Minas Gerais*, which have just undertaken similar serious efforts of fiscal adjustment and management shock many years after *Ceará* made its own reforms. Such large states then acquired creditworthiness to raise long term and affordable funds from international organizations.²⁸ This pioneering initiative by *Ceará* State in fiscal adjustment and

²⁶ By Brazilian law and regulations, subnational governments are allowed to raise funds abroad by themselves but are subject to controls on indebtedness and repayment capacity levels for being liable for receiving the federal government formal guarantee required by the multilateral and bilateral lenders. Since subnational units are not sovereign entities, thus without international juridical personality, they are to be guaranteed by the Federal government, which is the sole voice for the sovereign nation-state in relations with international actors. For further details on technical cooperation and loan agreements contracted by the state government of *Ceará* with international organizations from 1990-2006, see MAIA, José Nelson Bessa and FARIAS, Deborah Barros Leal, op.cit., pp. 131-136.

²⁷ See, by the way, more detailed information on the credit operations of subnational governments for projects financed by international organizations of the site SEAIN/MPOG Internet: [http://www.planejamento.gov.br/secretarias/upload/Arquivos/seain/090123_projetos_estados_municipios.pdf]. Availability: 08/03/2009.

²⁸ As a matter of In fact, the process of fiscal adjustment and reform of public administration in *São Paulo* and *Minas Gerais* States occurred many years after the *Ceará* State fiscal adjustment experience of 1987. The State of *São Paulo*, for instance, just started his own reform in 1995 (governorship of Mr. Mário Covas), while *Minas Gerais* only started its own reform process in 2003 (governorship of Mr. Aécio Neves). For detailed descriptions of both processes of fiscal adjustment, see: i) Secretaria da Fazenda do Estado de São Paulo. "Ajuste Fiscal no Estado de São Paulo – histórico", published on [<http://www.fazenda.sp.gov.br/ajustes>]. Available on 08/03/2009; and ii) COSSIO, Fernando Blanco e

financial paradiplomacy was widely recognized abroad, but remains virtually unknown in Brazil, having been simply disregarded by many analysts of public finances and international relations.

Concluding Remarks

The State of *Ceará's* 20 years of fiscal responsibility and paradiplomacy is already part of the literature of development in research centers in the United States, like the SPURS Program of Massachusetts Institute of Technology (MIT), and in international organizations (like World Bank and IADB), but deserves to be better known in Brazil because of the similarity of its model with the specific cultural, institutional and political features of the country. The *Ceará* State case could even serve as an example and inspiration to other states in federations or provinces in unitary states, still on the same or on late stages of development, for taking off by taking into account the requirements of balanced fiscal accounts, exploiting their local comparative advantages and seeking out internationalization as a lever for economic growth.²⁹

However, after two decades of the successful strategy of modernization and material progress, the people of *Ceará*, under the impulse of civic fatigue with the political elite in power for 20 years and influenced by divergences between its main leaders, sought change in the elections of 2006, giving the opposition a chance to manage the destiny of the State. In spite of the positive outcomes brought about by the State paradiplomatic stance towards internationalization, the state agencies involved in trade promotion and international projection, including the International Affairs Secretariat (ASSINTER) were closed down in January 2007 by the new state government administration, whose extreme decision meant a break away from the previous governors' paradiplomatic model and towards the adoption of other governmental priorities focused on the rural sector to the detriment of international integration.

By looking over the reports often conveyed by the *Ceará's* press in the last couple of years, it is easy to realize that the lack of ideological and pragmatic commitment of the new local political elites with the pro-business and internationalist development seems to be leading to the resumption of old patrimonialist practices in addition to abdication by the State Government of its own development strategy and excessive dependence on Federal Government initiatives, a stance not appropriate for a federal and democratic system with self-ruled subnational entities prone to greater inclusion in an economically integrated and interdependent world.³⁰

VALADARES, Silvia Mourthé. "Ajuste fiscal com qualidade: o caso de Minas Gerais", Anais do XIII Congresso Internacional del CLAD sobre la Reforma del Estado y de la Administración Pública, Buenos Aires, Argentina, 4 – 7/11/2008, published on [<http://www.planejamento.gov.br/hotsites/seges/clad/documentos/COSSIobl.pdf>]. Available on 08/03/2009.

²⁹ The Special Program for Urban and Regional Studies (SPURS), in the Department of Urban Studies and Planning at MIT, is a graduated course destined for middle of career professionals from developing countries. In his faculty some brazilianist professors stand out like Mrs Judith Tendler and Mr. Richard Locke, who dedicated for a long time to study development in the Northeast of Brazil, including the case of the State of *Ceará*. For more information access the following web site: [<http://web.mit.edu/spurs/www/>.] Availability: 08/03/2009.

³⁰ In particular daily newspapers: *O POVO* (www.opovo.com.br) and the *Diário do Nordeste* (www.diariodonordeste.com.br).

Finally, one should stress that the paradiplomacy proactivity does not guarantee its sustainability over time by means only of the success of the initiatives in terms of economic and social outcomes. Therefore, the case of *Ceará* serves as an alert to highlight how relevant political factors are as propellants or regressive elements of the process of internationalization of a subnational entity. The defeat of the *Ceará* reformist elite in the elections of 2006, after two decades in power, in the face of a coalition of forces to the left and right of the political spectrum led to power another elite of agrarian nature and uncommitted to the ideals of capitalist modernization and averse to international integration, an elite more inclined to the traditional patronage in rural areas and to passive dependence to the Central Government, which is a position of a subnational government that is precisely the inverse of paradiplomacy.