POLITICAL RISK IN LATIN AMERICA

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Abstract

This article presents two political risks investors may consider when building portfolios in developing countries, i.e., presidential impeachments, and social democratic governments. As for the methodology, we developed four linear regression models to find the relationship between the stock market and impeachment processes and between the stock market and social democratic governments. Regarding our findings, we discovered that political color influences economic policy elections and that macroeconomic consequences come from those elections. In addition, we indicate the adverse effects of specific economic policies and impeachment processes on Latin American stock markets. In conclusion, this research contributes to the literature that intercepts political science and finance from a Latin American framework.

Resumen

Este artículo presenta dos tipos de riesgo político que los inversores deben tener en cuenta en la construcción de portafolios en países desarrollados, i.e., juicios políticos presidenciales, y algunas políticas de gobiernos socialdemócratas. El documento privilegia metodologías cuantitativas. Desarrollamos cuatro modelos estadísticos de regresión lineal para encontrar la relación entre el mercado de valores y los juicios políticos, y entre el mercado de valores y los gobiernos socialdemócratas. Con respecto a nuestros hallazgos, descubrimos que el color político influye en las elecciones de política económica y que existen consecuencias macroeconómicas provenientes de esas elecciones. Además, indicamos los efectos adversos de políticas económicas específicas y procesos de juicio político en los mercados bursátiles latinoamericanos. En conclusión, esta investigación contribuye a la literatura que intercepta la ciencia política y las finanzas desde un marco latinoamericano.

I. INTRODUCTION

The main idea of this work is that political phenomena affect the stock market.

We are concerned about presidential removals through impeachment and with the democratic Latin American Left. Both, we hypothesize, have a negative effect on the stock market. Our first hypothesis is that social democratic Latin American governments, from 2005 to 2020, were negative for their stock markets. For the second hypothesis, we state that presidential impeachments, which effectively end in a dismissal, are negative for the stock market.

II.

Scholars have argued that political events are more significant to market performance in developing countries than in developed ones (Diamonte et al., 1996; Bilson et al., 2002). Diamonte (1996), demonstrated, using analyst estimates of political risk, that average returns in emerging markets experiencing decreased political risk exceed those of emerging markets experiencing increased political risk by approximately 11% a quarter. In contrast, the difference is only 2.5 percent a quarter for developed markets.

On the other side, Faccio (2006) revealed that companies benefit when key businesspeople effectively enter politics (CEOs, Board Members). That is due to the government's ability to grant subsidies and other privileges. Thus, when winning a public election, they access public funds and influence, contributing to the organization’s benefit (Wisniewski, 2016). For example, Wisniewski (2016) found that companies linked to a prime minister

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ISSN 2248-7212 · ISSN-e 2322-9152

outperformed unconnected ones by 1.14% per month. Now, regarding the executive branch, benefits are more significant. Wisniewski (2016) tracked the evolution of stock prices after the 2001 Thai general elections and found that the returns on firms associated with cabinet members exceeded non-connected firms by one hundred and sixtieth (160) percent –during the three years following the elections. In summary, the literature indicates that companies benefit from being connected with a political figure, specifically, the ones with high-rank employees in important political positions.

Up to this moment, we have presented endogenous political factors related to economic performance. We have also established that share prices fall when the economy is not performing. However, economic performance in Latin America is also a result of exogenous factors. As Campello & Zucco (2015) pointed out, commodity prices and international interest rates decide economic performance in Latin America. According to them, countries in Latin America "do well" when global interest rates are low, and oil prices are high; when the opposite happens, their economies plunge.

The effect of commodity prices is straightforward. Countries in the region are mostly commodity exporters, which means that a significant part of their economy is based on primary exports. When prices are high in international trade markets, export revenues soar, boosting economic performance. For example, Juan Manuel Santos's government experienced favorable commodity prices that benefited the economy and the government. High commodity prices were vital to finance government activity.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

The international interest rate dynamic is not as simple as the dynamic for commodity prices. First, let us establish why interest rates are essential for emerging economies with low savings that crave foreign capital. In summary, simply because money could boost economic performance. Second, let us explain what determines capital movements, especially in developing countries. In essence, flows of capital to developing markets are determined by international rates –in Latin America, capital flows are determined by U.S interest rates. With those premises, the dynamic goes as follows: when interest rates are low, liquidity increases, and it is more likely that part of that liquidity ends up in Latin America; additionally, if rates in developing countries are higher compared to international rates, investors will see an opportunity –which increases the likelihood to receive capital. Conversely, higher international interest rates prompt an exit to safer havens (Campello & Zucco, 2015). To add more nuance, prices and global interest rates are not equally important to all Latin American countries. In other words, some countries are more exposed to changes in international interest rates and others to commodity prices. The economic performance of Panama, Mexico, and Honduras varies with international interest rates. On the other hand, Brazil, Chile, Peru, and Colombia's economic performance is more connected to commodity prices.

III. THE LEFTS AND THE STOCK MARKET

We are about to cover the institutional framework under which the left Latin American governments executed their decisions as well as outlined their economic policy.

a. Institutional framework

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

The election of the Left in Brazil (Lula) and Chile (Bachelet) were signs of consolidation of the democratic framework as left governments had clearly strong conservative opposition to their candidates, but they were able to compete, which signal openness and pluralism within the system –democratic values themselves.

Table 1. Political orientations

Country	Government (party)	Orientation toward democracy
Chile	Michelle Bachelet	Liberal democratic
Brazil	Lula	Liberal democratic
Venezuela	Hugo Chavez	Plebiscitary
Peru	Alan Garcia	Liberal democratic

Source: Levitsky (2011)

According to Levitsky (2011), in Chile, Michelle Bachelet ran a vigorous opposition campaign that included a strong critique of neoliberalism, but its discourse was by no means anti-systemic, meaning it tacitly accepted the rules of democracy.

b. The economic agenda, communism as a starting point

Communist regimes do not go well with businesses because they do not respect private property. Also, in a communist state, the government plays a major role in the economy, meaning significantly expand state ownership of the economy.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Furthermore, they argue the economy would work better if the market-free economy is replaced by a centralized planned economy with state-run enterprises. In Latin America, only Cuba and Venezuela have been statist regimes.

The economic policy of the far-left **is different** from social democratic economic policy. First, countries governed by social democratic policies **do not commonly** confiscate assets as a way of operating and financing their programs. On the other hand, moderate left-wing politicians have a more diverse toolbox to intervene in the economy, including high public spending, and subsidized capital. In a nutshell, we see moderation as a defining characteristic of social democratic economic policy.

Table 2. Socioeconomic orientations

Country	Government	Social and economic policies
Chile	Michelle Bachelet	Social liberal
Brazil	Lula	Social liberal
Peru	Alan Garcia	Orthodox

Source: Levitsky (2011)

According to Levitsky (2011), Brazil and Chile are examples of the policy orientation that he called social liberalism –he explicitly says he coined the term to characterize the efforts of the Latin American left to mix market liberalism with social policies. In his

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

words, these governments retained relatively orthodox fiscal and monetary policies, yet all three governments combined macroeconomic orthodoxy with substantial investment in society aimed at reducing inequalities, enhancing the living standards of low-income groups, and expanding social citizenship rights. Therefore, elevating public spending substantially.

On the contrary, the García government in Peru, which Levitsky characterizes as not a left government, kept social and economic policies predominantly orthodox. In his words, the García government maintained the export-led model and strict macroeconomic orthodoxy. Furthermore, the García government invested relatively little in social policies.

After establishing the differences between the radical and moderate left, we would like to mention what the literature has stated about the left-stocks relationship. Let us begin with the *Partisan Business Cycle* (PBC) theory claim that left parties tolerate higher inflation levels in exchange for low unemployment (Alesina, 1995) –essentially, the nature of its constituency controls its policy preferences. Labor and Liberal parties often develop their campaigns considering blue-collar and informal workers' interests, as they are most of its voters. As we will present later in the following sections, inflation has various consequences that have negative effects for stocks. The result is higher interest rates –higher interest rates deplete the liquidity of stock markets because it increases the appetite for high-yield, financially secure vehicles. The model described above presumes that wages are rigid due to contract constraints, and prices move freely. On the contrary, the right-oriented parties tend to favor less government intervention to avoid inflation surges. When considered a continuum where parties take turns in power, the right-wing

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

parties will have low Gross Domestic Product (GDP) growth at the begging of their presidencies. Two years if we refer to a 4-year presidency. Afterward, Alesina's theory predicts a "natural" growth rate at the end of the presidential term. We have explained a chain of reactions resulting from political choices. Also, we have associated specific policy choices with ideologies. Furthermore, those policy elections have economic consequences that, in turn, have market repercussions.

As we argued, social-democratic policies could cause inflation. For example, they could try to reduce unemployment and execute their agenda through public spending increasing the amount of money in circulation. Furthermore, academic literature has established that inflation is a monetary phenomenon, i.e., if capital in circulation rises, inflation rises. The association (between inflation and capital increases) is positive and well-documented in the long run (Gómez-Pineda, 2010b). In the worst scenario, if the rise in circulating money is disproportionate, the currency rapidly loses value, affecting companies' profits. Markets will tank consequently. For investors, a company's ability to maintain earnings over time is positively related to its stock price, which means that if political maneuvers hinder profits, they are considered a source of political risk.

There is another undesirable effect of inflation on businesses. When raw material prices "inflate," companies often "eat the cost" by keeping prices steady; it allows them to stay in business. However, they cannot sustain this practice for an unlimited amount of time; eventually, they will have to raise prices. In any case, companies see their cash flow reduced, either because they try to protect the status quo or due to the decrease in sales caused by high prices. If the phenomenon described is consistent

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

across multiple sectors, the stock market will experience a reduction in value.

Under the frame presented, we will argue that a left-wing administration's negative market effect depends on the inflation rate the administration exhibits. In other words, being a leftist government is insufficient to watch inflation get out of control and its derived negative effects that affect the stock market. Thus, the political risk is not that the candidate or the elected president belongs to a leftist party but the ability to keep inflation under control. If there is a responsible way in which left-wing administrations can correct the most common free market imperfections while maintaining inflation and public spending in check, we will see functioning stock markets and good economic performance in such administrations.

Hypothesis: In leftists' Latin American governments, with high inflation rates, we expect to find a negative effect on the stock market.

IV. PRESIDENTIAL REMOVALS AND THE STOCK MARKET

In 2012, Dr. Mohamed Morsi was elected president of Egypt, the first democratically elected president in the country's history. However, the new democratic institutional framework did not last long: a military coup quickly interrupted the presidency and brought financial and social discomfort. On the financial side, the presidential removal disturbed the stock market. Egypt's aggregate market index (the EGX100) experienced a statistically significant negative response of 3.87% on the removal or event day (Ahmed, 2017). Ahmed (2017) also found a similar adverse reaction

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

after analyzing eleven days post-event. In that period, the EGX100 dropped 5.47%. Furthermore, if we consider economic sectors individually, some were more affected than others, but all were affected. For instance, banks showed abnormal negative returns of -10%, financial services excluding banks dropped by 13.13%, and foods and beverages fell by 10.50% (Ahmed, 2017).

In Latin America, presidents have also been removed from office, some by force, some by institutional processes. According to Perez-Liñan (2009), citing Kathryn Hochstetler, between 1978 and 2003, 40% of Latin American presidents were removed by civil actors. Impeachment trials were responsible for the rest. Pérez-Liñan goes even further, stating that impeachment trials are a new distinctive feature in Latin American Politics. With that in mind, we will analyze institutional removals to determine whether they would have the same effect on the stock market as in Egypt. We begin the analysis by presenting investors' reactions to the political instability that an impeachment involves.

"It will take a lot more than some drama in Washington to tank this market," wrote Yahoo! Finance about the stock market performance during the Clinton impeachment (1998). The peak years of the dot-com bubble were going by –economic conditions were promising, and investors were highly indifferent to political turmoil. Although the impeachment process failed in Clinton's case, the main point is to remark effects of the impeachment on the markets are mediated by the economic conditions of the moment. Conversely, The Watergate scandal, which led to a presidential impeachment and later resignation of Richard Nixon, occurred along with a sharp stock market decline, demonstrating that economic conditions were already worrying enough for investors; the political scandal just added the cherry on the cake.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Economic conditions were already worrying sufficient in Nixon's case –they were not in Clinton's case; the political scandal only added the cherry on the cake; it deepened the effects of the dire economic situation.

We theorize that impeachments create an appetite for safer assets among investors if in dire economic conditions. If the removal is violent, financial agents will respond quickly to protect their capital, guided by the disappointing economic performance due to social unrest. On the other hand, when the impeachment is expected to succeed, investors will also try to minimize political risk by moving the capital from stocks to safer assets – if there are bad economic conditions. In conclusion, nervousness is evident in both cases, causing a chain of reactions in the financial field that affect the stock market. In Wang (2009), political uncertainty would generate a risk premium whose magnitude may vary according to economic conditions; they stressed that the impact would be more significant in poor conditions and vice-versa.

Hypothesis: the stock market experiences a negative effect when a president is removed.

V. RESEARCH DESIGN

This section presents the data, the countries, and the statistical tests we ran to evaluate our hypotheses. We included four Latin American countries, from 2005 to 2020. They are Brazil, Mexico, Peru, and Chile. Peru has interesting presidencies due to a few inconsistencies in campaign promises and government style (Alan García y Ollanta Humala).

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

We have also constructed four ordinary “least squares models” —one for Latin America, one for Chile, one for Peru, and one for Brazil. The dependent variable is the stock market performance. The independent variables are the impeachment process and the leftist government. As we established before the left in Latin America is very diverse but for the methodology, we will treat them as similar governments.

a. Stock market data

The stock market data for each country was gathered from the Morgan Stanley Capital website. The data included a significant number of Large and Mid-Cap Stocks populations for each country. The index constructed for Brazil includes 48 constituencies and covers 85% of the Brazilian market. Peru’s index consists of 3 constituents, approximately 85% of the Peruvian equity universe. Mexico’s index includes 22 components that cover about 85% of the market. Chile`s index comprises 12 members, covering about 85% of the Chilean equity universe.

b. Inflation

Inflation data (yearly and monthly) was taken from different sources depending on the country. Chiles’s data came from Chile’s Ministry of Finance and the National Institute of Statistics (INE) personnel. Peru's monthly inflation data came from the National Institute of Statistics and Informatics (INEI). Mexico and Brazil’s information was grabbed from the World Bank Website. From Figure 2, we can conclusively state that Brazil and Chile have on average, the highest inflation in the region (from 2005 to 2020).

c. Ideological Stance

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Regarding the ideological classification of the different presidents, we have come up with the idea of creating a dummy variable. With a tremendous amount of help from academic experts, our variable will classify leftist governments as one (1) and "right" administrations as zero (0). We understand that grouping all the left into a single bag could be considered a methodological error, despite their shared characteristics, not all are the same. Therefore, this analysis must be taken only as preliminary.

We made a similar effort to form a variable for presidential removals. We developed a dummy variable in which one (1) signals a particular time frame –the six months before the impeachment starts, during the impeachment and six months after. The periods before and after the process are justified to the extent that they reflect the investors' sentiments both before the institutional process and after. Furthermore, uncertainty occurs before the day of the dismissal date while the process is being carried out; On the day of the dismissal, the investors know if the process will end with the politician's departure, making it a merely institutional event. The six months after the dismissal are essential to analyze insofar as it is a moment of political readjustment. Lastly, there are not enough cases of presidential removals during the studied period; as a result, we will only evaluate Dilma Rousseff's removal and Peru's case.

VI. RESULTS

Table 3. Regression results.

	Model 1	Model 2	Model 3	Model 4
Variable	Latin America (Peru, Brazil, Chile, Mexico)	Chile	Brasil	Peru

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Goverment	-1,116363**	-190.784**		-13.350
	(423.133)	(89.999)		(77.254)
Removed			-973.787**	
			*	
			(150.506)	
Constant	3,162.769***	1,797.657**	2,407.578**	1,365.224**
	(284.830)	(54.271)	(60031)	(23.293)
Constant				
ns	64	132	132	132
R2	0.138	0.056	0.244	0.0002

Note: *p<0.1; **p<0.05; ***p<0.01; standard errors in parentheses.

Model 1 reports the effect of the variable Government over the dependent variable Market. The variable Government does have a statistically significant negative effect –for each unit of Government, "Market" is negatively affected by 1,368.246 USD. Based on the results, we reject the null hypothesis. However, based on the R2 results, our model only explains less than 15% of the variations of our dependent variable.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Model 2 shows the results for Chile. Regarding Model 2, we found a significant negative effect when evaluating the stock market's performance during a social democratic administration in Chile –a discussion exogenous factors is presented in the next section.

Model 3 presents more exciting results. The model comprises the effect of the impeachment of Dilma Rousseff on the Brazilian stock market. In the period studied (2015-2016), a presidential removal negatively and significantly affected the stock market. As the results are statistically significant, we reject the null hypothesis that impeachment processes do not affect stocks. However, this applies only to Brazil, indicating more cases should be studied to expand the scope of the hypothesis.

Model 4 shows a linear model for Peru; the period studied goes from 2011 and 2021 –the dataset collects the monthly inflation, government, and stock market data. Two presidencies were elected on social democratic platforms in Peru: Ollanta Humala and Alan Garcia, yet they governed with orthodox policies –i.e., a more liberal approach. A broader discussion on this topic will be presented in the next section.

Table 4. Regression results.

	Model 1	Model 2	Model 3
Variable	Latin America (Peru, Brazil, Chile, Mexico)	Peru	Chile
Goverment	1.233***	0.276**	-0.036
		*	
	(0.418)	(0.087)	(0.055)

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Constant	3.314***	0.236** *	0.299** *
	(0.282)	(0.026)	(0.033)
Observations	64	132	132
R2	0.123	0.071	0.003

Note: *p<0.1; **p<0.05; ***p<0.01; standard errors in parentheses.

Table 2 plays a supportive role. It reports the effects del of the government on inflation (dependent variable). The Latin American model showed a significant positive contribution of governments to inflation. The Peruvian model shows that their "left" governments had a positive relationship with inflation, meaning that the administrations, governed with orthodox policies, also had trouble controlling inflation. Chile's model did not report statistically significant results.

VII. EXOGENOUS AND ENDOGENOUS FACTORS. PROBLEMATIZING OUR RESULTS

According to Campello & Zucco (2005), the state of the economy determines elections. If economic conditions are good, a president will likely reelect or elect a successor. If the contrary, the opposition will have a greater chance of being elected.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

Additionally, they argue that economic performance in Latin American countries is determined by changes in international interest rates and commodity prices – which are out of presidential control. Therefore, they argue that there are exogenous factors affecting political outcomes. For our analysis, the idea that external factors highly influence economic performance in Latin America is critical because this section will investigate if exogenous or endogenous factors determine the economic performance of left-wing countries. If exogenous factors are behind the economic and stock market performance, our hypothesis will have to be checked; conversely, if we find that external factors are not a thing, we can suggest policy revisions to solve the economic performance issue. We will be analyzing Brazil and Chile.

d. Chile and Brazil. International interest rates and commodity prices.

The Federal Reserve is one of the most influential central banks in the world. They not only buy and sell assets internationally but also set policies to maintain and secure acceptable inflation rates for the United States. According to their website, policymakers generally believe that an adequate annual inflation rate is around two (2) percent or a bit below (FRB, 2011), which means that countries are responsible for keeping inflation close to that number. This points out that 2% inflation is a widely accepted inflation rate globally.

Why is inflation significant in this context? Inflation pushes monetary authorities to raise interest rates, and high rates reduce liquidity, affecting investors' buying power. We did point out that left administrations are more prone to economic policies linked with inflation.

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

We have calculated the average inflation rate from left presidencies in Brazil. From 2005 to 2017, the inflation rate was 4%. Also, lets us say that low rates are not attractive for Brazilian investors –specifically for bond investors or high-yield hunters; therefore, they keep their capital in the local currency, and no devaluation could explain the inflation Brazil experienced – it only applies to the period studied. Chile's case is similar. The average international interest rate from 2006-2010 & 2014-2018 is close to the average we calculated for Brazil; however, the inflation rate in Michelle Bachelet's presidencies was substantially higher, meaning that economic policy decisions could be dictating market movements and economic performance, not exogenous factors. However, Chile is more dependent on commodity prices (according to Campello and Zucco's analysis); therefore, a parallel between commodity prices, inflation, and market performance is needed to give more conclusive evidence –Chile is also a strong coal exporter.

This analysis can be replicated with coal and oil prices to strengthen our argument –particularly in Brazil's case. In other words, discounting commodities' effects on market performance will support the idea that economic policy is also a decisive factor affecting stocks. This can help design economic policy that controls inflation and evaluate if the mechanism comes from monetary policy, labor policy, or fiscal policy. In summary, we can suggest changes to better market and economic conditions. Additionally, in 2006 and 2007, US interest rates were high following the housing crisis; it would be interesting to analyze if they are either linked to bad stock market performance in the region or linked to high inflation.

e. Discussing the literature

Trans-pasando Fronteras, Núm.20, 2023. Cali-Colombia
ISSN 2248-7212 · ISSN-e 2322-9152

We started this work with an introduction that includes a literature review, now we would like to discuss the coincidences and tensions considering the results of the statistical model.

Let us begin with the affirmation that stock markets perform better in developed countries than in emerging markets when political turmoil occurs (Diamonte et al., 1996; Bilson et al., 2002). Although we have not conducted a comparative study, we ask if the political drama was equally irrelevant for stock in Latin America and the United States – as it proved to be in the impeachment case we mentioned. Impeachment processes are examples of political turmoil – by all means. To answer the question, we examined Brazil's case. Despite Brazil's results (that show that political turmoil is negative for profits), we recognized the limitation of one case example that can look like anecdotal evidence. However, it allows comparing scenarios. We argued that impeachment processes in developed countries were negative only if the economic conditions were the "right ones," unlike Latin American cases where regardless of internal economic conditions, Brazil showed a negative effect of political events. In summary, our results are in line with the anticipated from the literature, meaning that the stock market performance in developing countries is highly affected by political movements.

Second, we pointed out some cases in which economic performance was not determined by exogenous factors, as Campello and Zucco's argued, but rather by endogenous factors –Brazil and Chiles's cases can be taken to raise a reasonable doubt rather than mere anecdotal situations. However, more than a criticism, we think that our ideas can enrich an abstract of economic performance (EC) as follows: rather than looking for a unidimensional answer to economic performance, we believe

exogenous and endogenous factors influence EC at the same time though depending on the time and the cases, one of the factors could be heavily weighted compared with the other. In simpler words, it may be that in some cases, exogenous factors could be dictating the outcomes, like in a sudden and fast interest rate hike from the federal reserve, and there are other cases where endogenous factors will determine the "outcome." In summary, this contentious point respectfully invites sophistication and detailing rather than flat-out criticism.

Third, we included Alesina's theory about parties' policy preferences to show financial and political interactions. Although we added a broad discussion of each policy preference. Our results hold basic ideas PBC. First, inflation was negative for Chilean stocks as reported in model 2; meanwhile, the Chilean left was difficult for the markets in the same model. Indicating the left has a higher tolerance for inflation. Both being negative also supports our discussion on inflation being the path, after policy, that leads to market poor market performance. Model 1 and 2 supports our initial idea that the left does not "go" well with stocks. However, we could not establish if the time the left was in the government were times of high inflation, neither inflation was significant in the models constructed. Furthermore, recent literature has established the importance of political constraints, coinciding with our idea that investors not only react negatively to a left candidate being elected but they consider the context in which the election unfolds. According to Sattler (2013), if investors establish that there are sufficient institutional constraints (the new president does not have the necessary majority to carry out his reforms, for example) no matter how extreme is the newly elected candidate, the reaction is not the same as if the constraints were low. Per our analysis, this could be an interesting point to discuss with the

literature we outlined before.

Finally, we would like to draw attention to the fact that democratic structures not only provide stability for markets to function and a framework for profits (Ahmed, 2017; Tuncay, 2018), but they are also excellent sources of information helping investors to forecast when it is about to be a stock market disruption. In Dilma´s impeachment case, for example, institutions and their processes allowed investors to anticipate or prepare for what was coming. How do we explain it? Simple: by knowing the political climate and the balance of forces inside the legislative chamber, we can foresee the most probable scenario and act accordingly –in the case of Dilma, a removal was expected. In summary, without the structures and processes, it would not have been possible to make democratic frameworks a valuable source of information about the future that reveals through pattern regularity.

VIII. FINAL REMARKS AND IMPLICATIONS

We can fairly say that our **exploratory-preliminary** analysis found a negative relationship between specific economic policies and stock market performance. Model 1, for example, showed the negative consequences of policy elections. The model also revealed that Peru and Mexico's policy elections were neutral for stock market performance.

Second, this work found that institutional changes have negative effects on stocks. In Latin American countries, we found impeachments harmful for shares. The Brazilian removal process of Dilma Rousseff from office was negative for markets. We evaluated six months after and before the removal day to come to that conclusion. Furthermore, our model could explain 20% of the

variation of the dependent variable in the period studied, which is significant. To expand on this, more cases should be studied.

This work has also presented several comments on the economic management of social democratic governments. To begin, Social Democrats prefer to use progressive taxation and redistribution rather than nationalization. Their system is based on the idea that the higher the profits, the higher the taxes, applying this logic to individuals and corporations. Furthermore, we have covered scholars' criticism of the social democratic experience. Two comments stand out. First is the idea that deficit spending causes inflation affecting not only market profits but the ordinary citizen. Throughout the text, although you will notice the criticism we have talked about, you will also see we are interested in showing the danger of extremism –fascism included. We have **heavily** promoted the idea that democracy is keen for moderates, as Norberto Bobbio signaled in his work about extremism and moderated political ideologies.

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