



An analytical approach on the conundrum of the Transnordestina Railway in Brazil

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Abstract: This paper aims to provide an analytical understanding of the practical problem to implement public policy in transport infrastructure in Brazil: the unfinished construction of the Transnordestina Railway. The implementation of the work cannot be considered a standard public policy, but it is rather the concretization of crony capitalism, where state and private interests collude. We present the background of entrepreneurship from its origins until the impasses, which have resulted in delays and constant budget increases from the perspective of cognitive theories of public policies, political science and positive political economics. We also identify and describe the networks of conflicts, actors, interests, institutions and referentials involved in such policy. We claim that, on the viewpoint of public intervention, the Transnordestina is a great political failure with the inefficient use of scarce resources.

Keywords: Transport Infrastructure; Transnordestina Railway; New Institutional Economics; Crony Capitalism; Public Policy.

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1. Introduction

This article is an attempt to scrutinize the items that explain one big Brazilian government failure – regulation of the Transnordestina Railway that purports to promote regional economic development in the Brazilian northeast and to lower its high transaction costs constraining the country's potential for the international division of labor. More specifically, it draws on an approach that combines insights from Transaction Cost Economics, Cognitive Approaches on Public Policy, and to assess whether, why, and how exactly Transnordestina Railway is a predictable manifestation of crony capitalism in Brazil. Cognitive approaches to public policy and transaction cost economics are complementary in their analysis of the role of the institutions, interests, and ideas involved in implementing public policy. The first approach focuses on the dynamics of public policy implementation and the interaction of actors within institutional boundaries. The second focuses on the cost of transactions (such as property rights) involving public action.

Our main aim is to uncover how the contractual arrangements have changed over time and their unintended consequences in response to the public officials' knowledge problem, their shifting incentive structures, and actual decision-making procedures underlying the very design and implementation of the Transnordestina railway project (Holcombe 2012). Also, it is worthwhile to stress that the private shareholder of Transnordestina Logistics S.A (henceforth: TLSA) is Companhia Siderúrgica Nacional (CSN), a former state-owned National Steel Company privatized in the early 1990s.

More precisely, this article focuses on the distorted relationship between the private railroad operator (Transnordestina Logistics S.A) and the public agencies playing the role of regulating, managing, and funding transport infrastructure. We focus our attention on TLSA connections with BNDES (Brazilian National Bank of Economic and Social Development), VALEC Engenharia, Construções e Ferrovias S.A. (the public company responsible for planning the Brazilian railroad investments), BNB (Bank of Brazilian Northeast region), FINOR (Investment Fund for the Northeast of Brazil), SUDENE (Superintendence for the Economic Development of the Northeastern Brazil) and FDNE (Development Fund of the Brazilian Northeast).

We go on to argue for the idea that the systematic government failures surrounding the unfinished Transnordestina Railway project provide a case study for testing our hypothesis that most manifestations of crony capitalism in Brazil are (mal) adaptations of an unstable business environment with concentrated benefits and disperse costs, where government officials shift their roles to benefit named private investors and promote misallocation of scarce resources.

This paper is organized as follows. Section 1 describes the historical background of the Transnordestina railway project from its initial phase in the late 1960s until now. Based on a transaction cost economics approach, section 2 presents and analyzes the operation of the Transnordestina railway as part of CSN's verticalization strategy that results from its hierarchical governance structure to minimize transaction costs and seek efficiency. Section 3 focuses on how cognitive approaches of public policy analyze and discuss some troubling coordination strategies among bureaucrats from the Ministry of Transportation, the Ministry of Domestic Affairs, VALEC, SUDENE, BNB, and private actors coming from TLSA, CSN among other business associates. Section 4 wraps up the overall argument, briefly draws some implications and conclusions.

2. Digging deeper into the institutional background of Transnordestina Railway

This section presents and discusses the institutional background in which negotiations and institutional arrangements to build up the Transnordestina Railway have evolved. The railway investment project was part of the Economic Growth Acceleration Plan (PAC)⁵ designed under the second term of ex-president Luiz Inácio Lula da Silva (2007-2010). According to government rhetoric, PAC purported to be a Keynesian-oriented set of public policies to minimize the economic downturn following the 2008 financial crisis, promote Brazilian economic growth, and the country's increase social indicators. The official narrative relies on the premise that public incentives for investments in the Transnordestina railway would allow for regional integration and sustained socioeconomic improvements in the Northeast areas of Brazil.

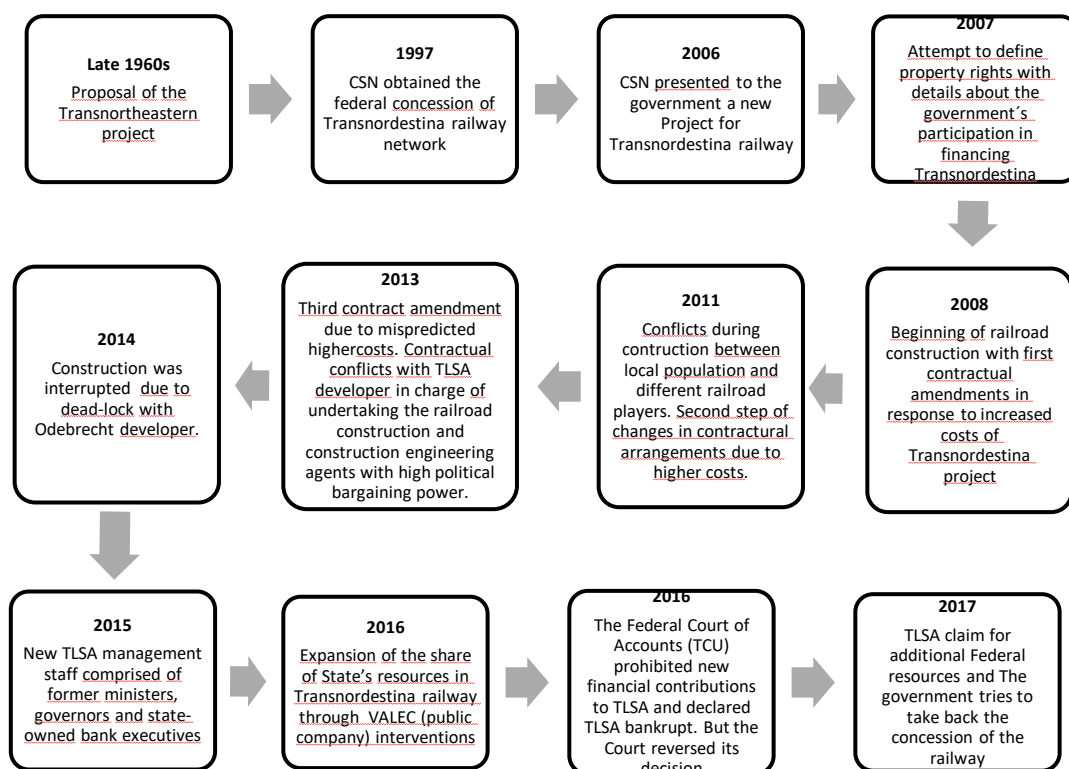
⁵ In this article, all the proper names of Brazilian and foreign entities, projects etc. were freely translated to English, followed by their abbreviations or acronyms as used in Portuguese.

Given the complexity of the issues at stake, we appeal to a complementary explanatory perspective to assess more critically the puzzles surrounding Transnordestina investment project delays, changes in its institutional arrangements, and increased non-credible budget requirements. Our main aim is to provide an analytical understanding of the institutional flaws underlying the ambitious project of the Transnordestina Railway, which remains unfinished.

The construction of the Transnortheastern Railway has gained much room in the Brazilian press and gave rise to several political arrangements and conflicts. To the best of our knowledge, making sense of the ongoing delays and the increasing budgetary requirements depends on a more precise account of how private and public actors with dispersing knowledge make choices in a weak institutional environment where crony relations do pay off highly to the detriment of economic efficiency and productivity gains.

The idea of constructing a railway to link the hinterland of the northeast Brazilian region with the coast and its main ports dates back to the 19th century. Given Brazil's continental dimension, integration had always been a hot topic in the political as well as economic agendas. In the late 1960s, the military government (1964-1985) started to build a railway similar to the current Transnordestina project, but it was soon put aside by public authorities and the works were interrupted soon afterward and were resumed only in the next century, as displayed in Figure 1.

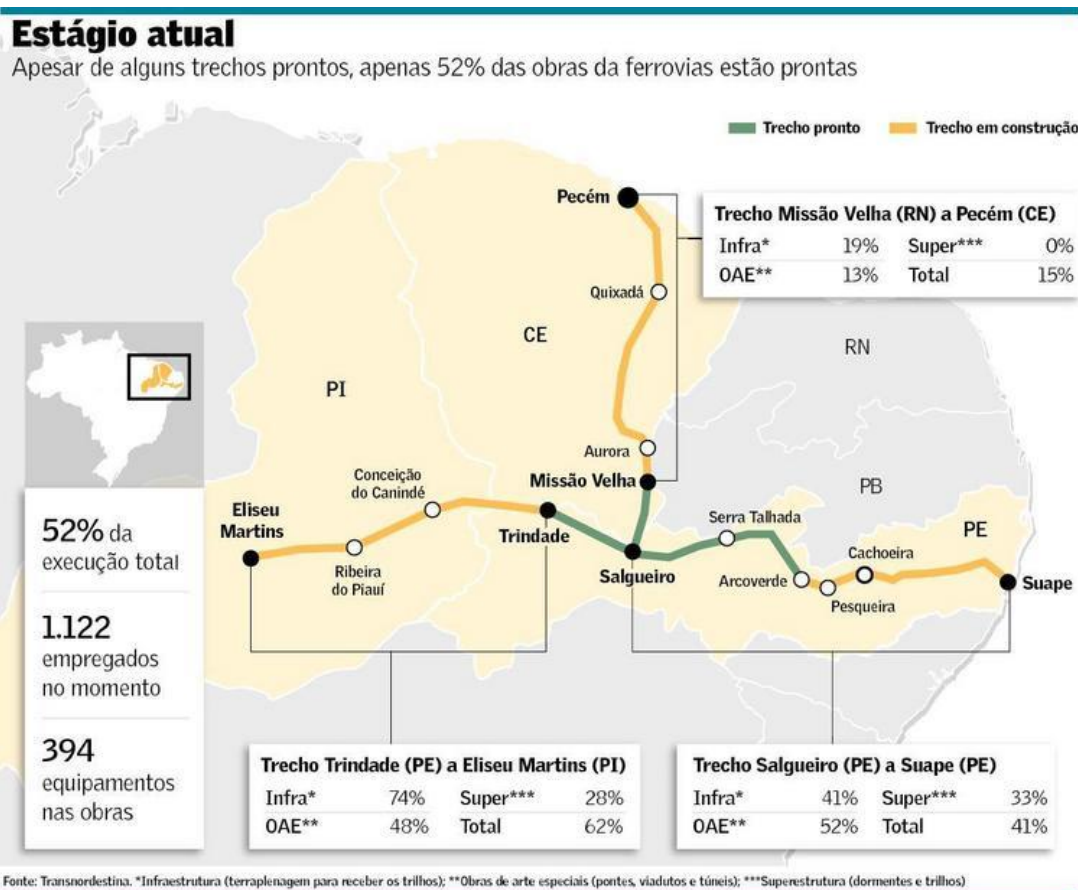
Figure 1 – Timeline of the relevant facts underlying the Transnordestina railway project



In 1997, under a political and economic context that rewarded privatizations, the bidding process of the northeast part of the Federal Railway Network ended with great market enthusiasm. At that time, the bidding process winning group was CSN (National Steel Company). The government ascribed to CSN the right to explore all activities related to freight car transportation with the Transnordestina railway (see Map 1).

Surprisingly enough, the government officials never requested any previous economic feasibility analysis of Transnordestina enterprise to help them deal with their knowledge problem and designing better agreements that would specify clauses regarding budget constraints, and investment schedules, construction deadlines and punishments in case there was an opportunistic move of the contracting parts. The only piece of information referred to the fact that the federal government would take responsibility for the Transnordestina railway using financial provisions.

Map 1 – Plan of the New Transnordestina Railway



Source: Brasil, Ministério dos Transportes (2013)

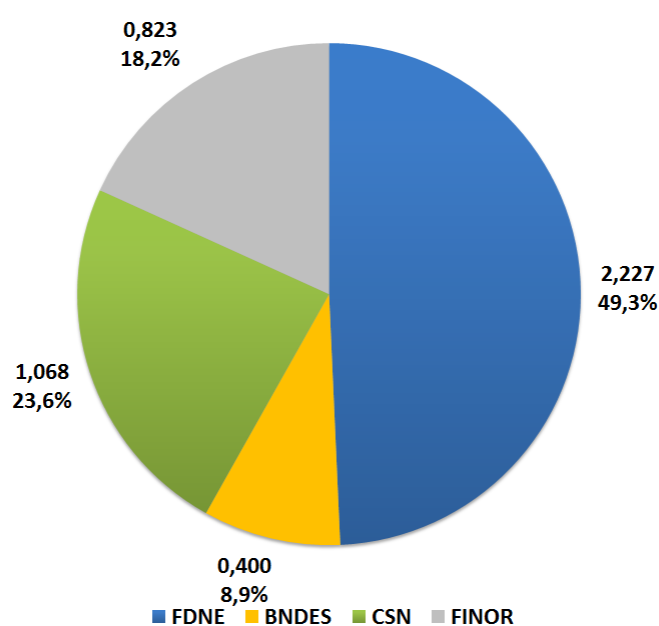
In 2006 (at the end of President Lula's first term), CSN submitted to the federal government an R\$8.0 billion worth project for the construction of 1,728 kilometers of the Transnordestina Railway. CSN also received alternative funding schemes for infrastructure projects through *project finance* with BNDES support (Ministry of Transport, 2005).⁶

After several rounds of negotiations, the Transnordestina project cost was revised and it lowered by R\$4.5 billion in response to government pressures. According to the new proposal, the new company Transnordestina Logistics (TLSA), controlled by CSN, would be in charge of the construction and future railway operation. According to the investment project, the railway would be completed in three years.

6 BNDES (National Bank of Economic Development) defines this kind of partnership as follows: "Project Finance is a form of financial engineering supported contractually by the cash flow of a project, having as guarantee the assets and receivables of this same project." Available at http://www.bndes.gov.br/SiteBNDES/bndes/bndes_pt/Institucional/Apoio_Financeiro/Produtos/Projeto_Financeiro/, retrieved on 20/06/14.

In 2007, the funding sources for the construction of the new railway were defined, as seen in Chart 1. TLSA would get loans of R\$2.3 billion with the Northeast Development Fund (FDNE), and R\$0.4 billion with the National Bank of Economic and Social Development (BNDES). The remaining sum would be invested in the form of TLSA capital increase by its controller CSN and the Investment Fund for the Northeast (FINOR). Therefore, the participation of the direct and indirect public administration of the Transnordestina Railway would total 76.4% of the scheduled investments.

Chart 1 – Sources of funding the Transnordestina project in 2007 (in R\$ billion and %total)



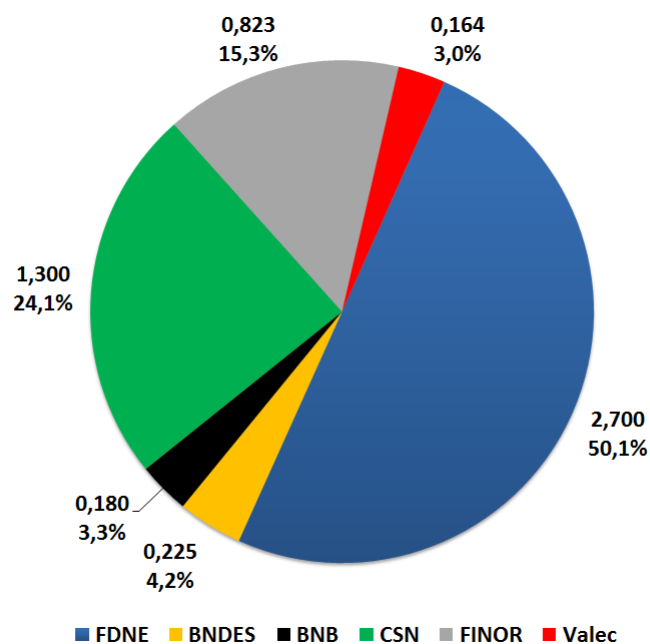
Source: Based on Valor (2013).

After the actual beginning of the construction work in 2008, there was pressure for TLSA to require budgetary adjustments to the Transnordestina project due to significant increases in labor and materials costs, such as concrete, steel and oil. The renegotiations with the federal government resulted in a new R\$5.4 bi budget, distributed as seen in Chart 2. The FNDE increased its financial participation through loans and CSN made further capital increase. Besides, two federal state-run companies provided additional resources for the railway: the Engineering, Constructions and Railways (VALEC), which became the TLSA shareholder, and the Northeastern Bank

(BNB). The latter promised to provide R\$180 million with funds for the Transnordestina railway.

Due to the changes in the financial arrangements, the new deadline for completing Transnordestina construction would be 2014, the last year of ex-President Dilma Rousseff's first term.

Chart 2 – Composition of the resources of the project in 2008 (in R\$ billion)

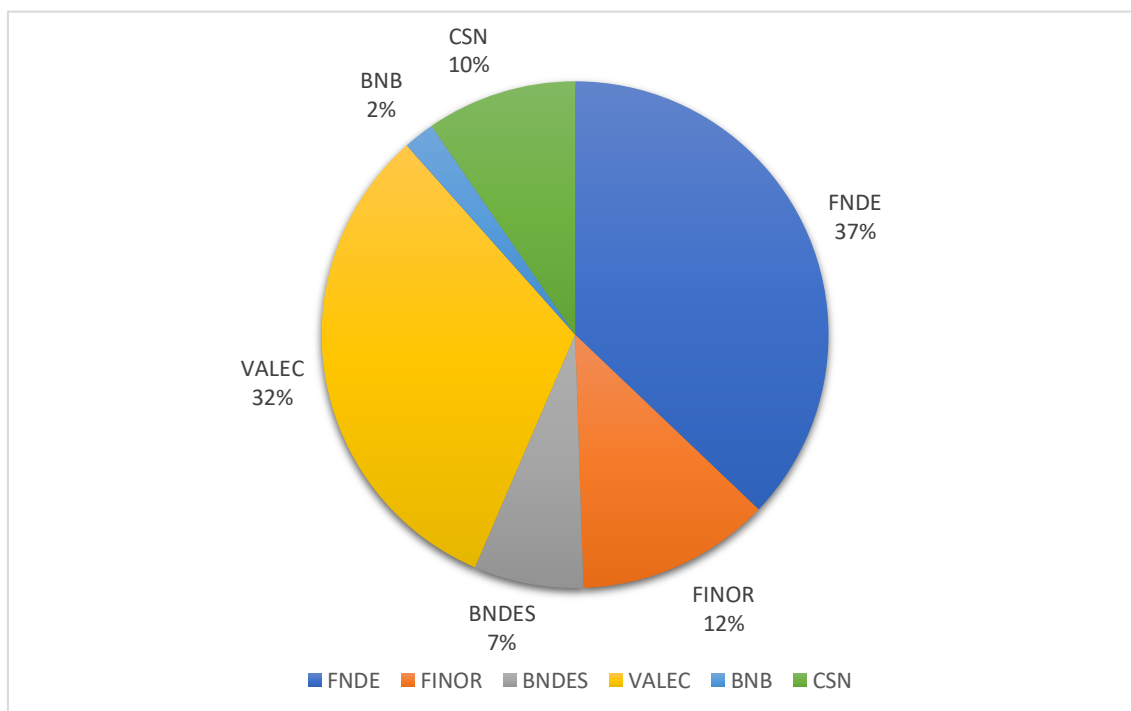


Source: Based on Valor (2013).

At the end of 2011, there was a demand for a new budget adjustment to the Transnordestina railway project. TLSA submitted the request to the federal government. After a few months of negotiation, TLSA players and government officials agreed on a R\$1.3 bi increase in its budget schedule, which implied a total budget R\$6.7 billion for the Transnordestina project in 2012. The construction deadline was postponed for December 2015.

Interestingly enough, the last stages of negotiations made all the contracting parties - public funding sources and CSN, to increase its expenses in the Transnordestina Railway project, as shown in Chart 3.

Chart 3 – Composition of the resources of the project in 2015



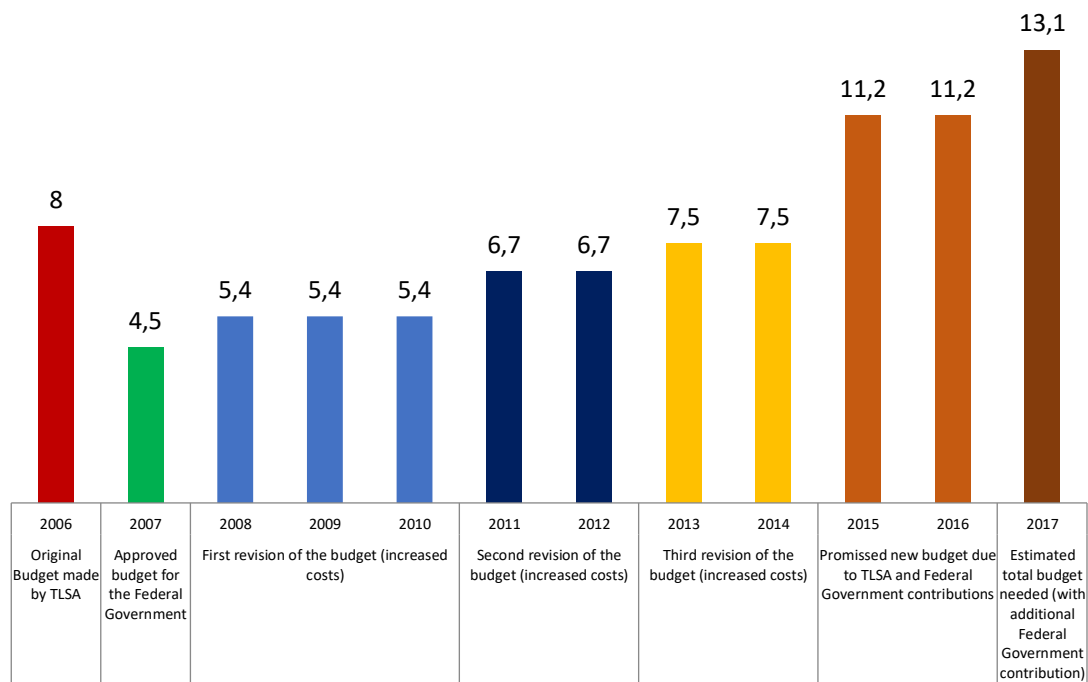
Source: Based on Valor (2015)

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In 2013, the Transnordestina Logistics (TLSA) again submitted to the Ministry of Transport a new proposal of budget revision with a new deadline for completing the Transnordestina railway. After many rounds of negotiations, the Federal government accepted a new agreement. The latter allowed for increased investments in Transnordestina by R\$7.5 billion. Furthermore, the new agreed deadline would be September 2006 (see budget evolution in Chart 4).

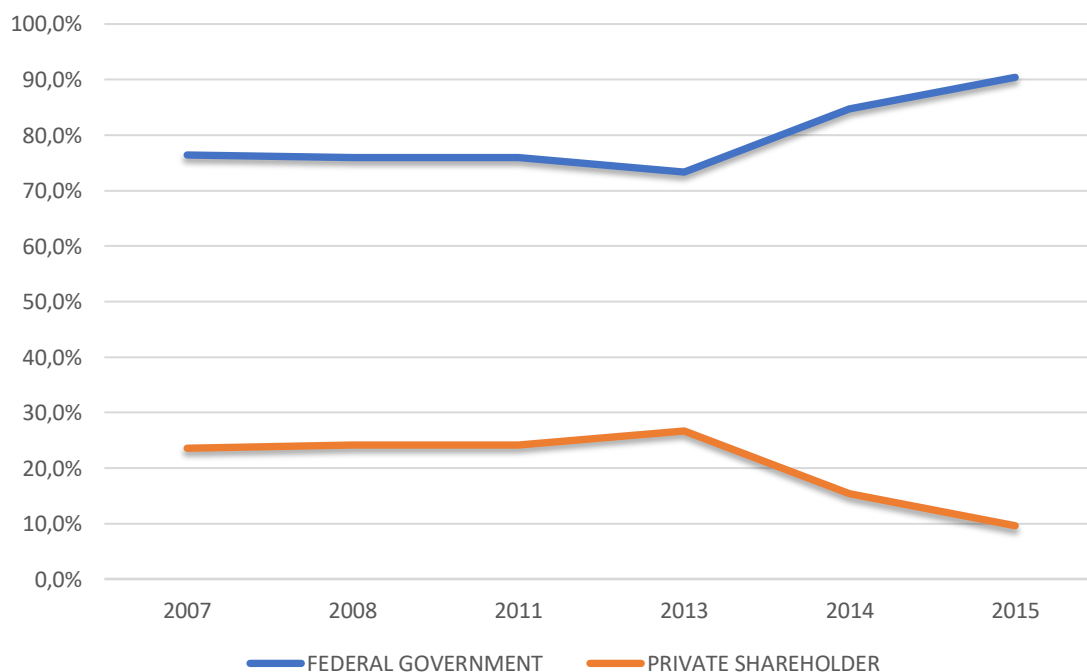
Under the new terms of the new agreement, it is expected a R\$400 million increase due to VALEC participation in the TLSA capital. According to recent CSN briefs, R\$4.1 billion were invested in the project until 2013, around 53% of the total initial money investment schedule (Valor, 2014).

Chart 4 – Evolution of the New Transnortheastern Railway budgets from its conception until the last contract revision (in R\$ billion)



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Chart 5 – Public and Private resources in Transnordestina budget



The status of the Transnordestina project implementation and construction, displayed in Table 1, suggests that only three out of the 29 lots were fully completed during the 2007-2013 period. This means that 216km out of 1.728km of the Transnordestina railway was ended, which corresponds to only 12.5% of the total project. It seems that there will still a long way to go before the Transnordestina railway becomes a reality.

Table 1 – Indexes of the Transnordestina Railway execution in late 2013

Lots and extension	Total investment	Completed extension	Total evolution
29 lots and 1.728 km	R\$ 7.5 billion	216 km	40%
Pernambuco: 743 km (10 lots)		Salgueiro – Missão Velha (96 km)	Infrastructure: 48% Works of Art
Piauí: 392 km (7 lots)		02 lots in Salgueiro – Suape	Special: 41%
Ceará: 593 km (12 lots)		(120km)	Superstructure: 24%

Source: Brasil, Ministério dos Transportes (2013).

In 2015 the updated amount of the total investment was approximately R\$9 billion, with expectations of increased by R\$11 billion. According to TLSA president, Ciro Gomes, the Transnordestina railway might be ready in 2018.

However, further complications and delays are expected to the currently turbulent political and economic environments, although some federal government announces public incentives for the Brazilian infrastructure sectors just like Dilma Rousseff's II PIL (Second Program of Investment and Logistics) in 2015.

In February 2015, reports coming from TCU (Federal Court of Accounts) encountered many irregularities in contractual relationships involving the Transnordestina railway construction process. Some of the mistakes could imply the cancellation of the railway concession contract and severe punishments for CSN. That sheds extra light on the fact that bureaucrats cannot overcome their severe knowledge problem and come to grips with government capture and crony relations (Valor, 29.02.2016).

The Federal Court of Accounts (TCU, 2014) reported irregularities in government managing contractual arrangements and monitoring entrepreneurial goals. Besides, there is no coordination between budgetary issues and investment schedules. Also, many terms and conditions underlying the Transnordestina concession contract failed to be followed with ANTT consent (Ground Transportation Regulatory Agency), which suggests some room for another government failures named regulatory capture. TCU reports go on concluding that TLSA has not complied with the deadlines. It has not respected budget constraints over time, either.

Stigler (1971), in his Economic Theory of Regulation, allows the possibility of capturing public agents, especially government representatives, with influence over regulatory bodies, by which to defend the deregulation of markets, considering the regulatory process ineffective. This disadvantage stems from the rapprochement between the political class and the regulated companies, in which the first resources obtained for their electoral campaigns, and once elected, carry out the regulatory process in favor of the financiers.

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Therefore, the presence of regulatory action may lead regulated companies to capture governments through their regulatory bodies or allow the establishment of this relationship, increasing the possibility of seeking an economic income, which evidences a habitual situation seeking rent (Posner, 1975).

In this context, it is noted that at the beginning of 2016, VALEC, a run-state company, attempted to promote Transnordestina railway construction of the railway by providing additional funding of R\$ 420 million. In response to the puzzles, the government decided to increase its share in the total capital of the Transnordestina railway project. It began with a percentage of 8.2% and some politicians want the public agency VALEC to acquire 49% of TLSA. (VALUE, 02.03.2016)

In the first half of 2016, two events involving TLSA seem to put the railway project under significant threat. First, the TLSA was declared bankrupt (VALUE, 03.30.2016). Second, The Federal Court of Accounts prohibited the federal government from making any public money transfer to Transnordestina (VALUE, 05.19.2016).

With all this in mind, there seem to be no significant prospects for resolving such anomaly. Transnordestina Railway may remain an unfinished infrastructure project due to government failures and an institutional environment of crony capitalism.

3. Making sense of Transnordestina Railway through Williamson's economic lenses of transaction costs

In this section, we briefly present and scrutinize Williamson's (1979, 1985, 1988, and 2005) and North's (1990) transaction cost economics (TCE) to understand the institutional arrangements and organizational forms underlying Transnordestina Railway.

It is important to stress that TCE is one of the various strands of New Institutional Economics (NIE) that draws on Ronald Coase's (1937) view of economic organizations and their arrangements as initiatives to respond to actual transaction costs and achieve efficiency. According to Peter Klein's TCE portrait,

TCE represents another approach to studying institutional arrangements. Here the emphasis is on governing transactions. TCE holds that all but the simplest transactions require some mechanism – what Williamson (1985) calls a governance structure to protect transacting parties from various hazards associated with an exchange (Klein, 1998, p. 13).

More precisely, TCE regards organizations as a complex network of contractual relationships that purport to align incentives for cooperation. In Williamson's perspective, the real choice over a governance structure – market, hybrid, and hierarchy – depends on behavioral parameters (opportunism and bounded rationality) as well as specific features of business transaction (frequency, uncertainty, and asset specificity).

From the perspective of North (1992), there is a concern to understand how institutions can favor economic growth in a context in which property rights are the central point of guaranteeing the proper functioning of institutions, which, in turn, are conditioned by specificities of each country. North regards them as an incentive system in barter relationships and it is in this role that they relate to property rights. In

this sense: “It is the cost of measuring the valuable attributes of the goods and services or the performance of agents in exchange that is the fundamental key to the cost of transacting” (North, 1992, p. 7).

Marketed goods and services have multiple attributes and characteristics, which makes it difficult to measure the transaction costs associated with them. Thus: “insofar as these costs are high or uncertain, property rights end up being imperfectly or incompletely specified” (Fiani, 2003). North (1989, 1990) sees the state as the basis of the impersonal and complex exchange relations in modern societies. Since state dominance (or influence in its decisions (Weber, 1970)) is the subject of a political dispute between interest groups and social classes, its actions are the result of this dispute, which does not imply actions that necessarily lead to economic efficiency. For the author, agents present distinct and competing ideologies as a consequence of modernity. In this view, ideology is an individual and subjective way of understanding reality (positive aspect) and how it should function (normative dimension). However, if we look at ideology through the sociological lens, we can define it as a worldview and a set of values and principles shared by a group, social class or political party. At this point, the theories of institutional economics and cognitive approaches to public policy converge, as will be explained in the next section. The government's decision to build the railroad is based on the state's view as an inducer of economic activities. This developmentalist view is both the referential of this public action (by the approach of the political sociology of public action or the theory of the referential) and the ideas that influence the interests and the functioning of the institutions (in the theory of the three Is).

The TCE framework stresses that agents are boundedly rational, i.e., they have constrained computational capabilities to anticipate all the contingencies that the future will bring. As a result, contracts have inevitably incomplete clauses that, in turn, bring additional risk to transacting parties. This is partly so because adaptation costs tend to be positive. The holdup problem is one empirically grounded example of maladaptation. Businesses learn that their relationship-dependent investments cannot be free from the risk of changing circumstances in the future that might motivate one of the trading parts to be willing to behave opportunistically.

In this paper, we argue that the holdup problem seems to be a pervasive issue of distorted Transnordestina railway arrangements. Following Klein, Crawford and Alchian (1978), specialized assets or investments that are not deployable motivate business partners to try to expropriate quasi-rents and make strategic use of their personal relations with government officials and agencies to achieve their goals.

It is important to stress that the Transnordestina railway institutional arrangement is closer to a hierarchical governance mode than a market structure. To the best of our knowledge, the choice over building up a railway in the northeast of Brazil reveals an effort to economize on transaction costs associated with transportation and regional integration, which put severe constraints on the country's productivity and competitiveness. This is the effort to show the converging interests of the statistical and private actors that, in turn, conditions the institutional design of the work and the ideas that support it, as will be explained in the theory of the three.

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3.1. History matters for understanding the logic of Transnordestina governance structure and its contractual practices

In 1997, Companhia Siderúrgica Nacional (CSN, National Steel Company) deliberately joined the former Northeast Railway Network bidding process and turned out to be the winner of this specific railway concession. Buying valuable "logistic assets" seems to be part of CSN's verticalization strategy to lower its high transaction costs and become less dependent on Companhia Vale do Rio Doce (CVRD, currently named VALE), the most prominent Brazilian mining company with the most productive railway concessions. This is partly so because CSN deals with very high asset specificities or relationship-specific negotiations and investments that are indispensable for the very operation of its production line, which in turn depends crucially on an ongoing supply of iron ore.

CSN's iron purchases require contractually defined prices and must respect their strategic plans and production schedules. It comes as no surprise that such requirements may call for a long-term relationship that creates incentives for cooperation and accommodating specific investments and its related sunk costs (Klein, Crawford and Alchian 1978).

In tune with Williamson's (1985) line of reasoning, any contract is imperfect and would be too risky for CSN to entirely depend on CVRD/ VALE, which controls most of the iron ore production and presents itself as the leading supplier for the Brazilian steel industry (Vale has more than 80% of the iron production).⁷ This leads us to suggest that CSN's organizational form can be regarded as an attempt to overcome high transaction costs and to respond to specificities of the institutional environment. To put it differently, CSN chose to pursue efficiency by internal (vertical) production, coordinating, under the same corporation, activities that would involve some contractual hazards if operated by several independent organizations in the market.

In other words, CSN has verticalized its operations and started to extract its iron ore since the 1990s through acquisition of *Casa de Pedra*, *Engenho*, and *Fernandinho* mines in the State of Minas Gerais. It also engaged in transportation and logistics by becoming an essential shareholder of the MRS Logistics S.A. The latter is entitled to operate important railways to transport the iron ore production in Minas Gerais state. MRS has administrative control over two terminals in Itaguaí Port in Rio de Janeiro state.⁸ The prior institutional arrangement made CSN the second largest Brazilian iron ore producer, responsible for 4.59% of the total production in 2010.⁹

It is important to stress that CSN is aware of the fact that the Brazil's state of Piauí has the fourth-largest iron ore reserve, which remains unexplored. The economic prospects of mining activities in Piauí, where the final stretch of the Transnordestina railway purports to connect partly explains CSN's participation in the Rede Ferroviária do Nordeste (Northeast Railway Network) bidding process in 1997.

It is important to stress that in the same period; iron ore reserves in Paulistânia city in Piauí started to be explored. Licenses for mining activities and exploration property rights were exchanged. Under the so-called Planato Piauí Project, Bemisa (Brazilian Mineral Exploration Group) took the lead to structure the iron ore mining business in the region. Yet the effective mining operation depends on

7 2010 Brazilian Mineral Yearbook published by the National Department of Mineral Production (DNPM), comprising the total amount of the production of Vale S.A. and its controlled company Brazil United Mining S.A. (MBR).

8 Available at <http://www.csn.com.br/iri/go/km/docs/csn_multimidia/csn/html/rel2011/a-empresa.html>.

9 2010 Brazilian Mineral Yearbook published by the National Department of Mineral Production (DNPM).

addressing the logistics bottleneck that could be somehow dealt with by investments in the Transnordestina railway.

One of the main investors of the *Planalto Piauí* Project is the Opportunity Group, mostly involved in several crony relations to be discussed later in this article.

3.2. Transnordestina Railway and its unfinished investment projects

To examine our conjecture, we begin by assessing: a) CSN's participation in the Northeast Railway Network bidding process, and b) features of the railway concession contract and agreements between CSN and government officials to build the Transnordestina railway.

Our hunch is that the presence of the CSN, an active player with several political relations and connections on all levels of government power, has influenced the way the institutional arrangement has evolved. This is also due to issues of path dependence since CSN was a run-state business until its privatization in 1993.

The Northeast Railway Network concession contract in 1997 granted the operation of the former São Luís-Teresina Railway and the Teresina-Fortaleza Railway to CSN. To foster the construction of new railway branch lines like Transnordestina, the federal government promised to give incentives for CSN that would be entitled to explore the potentially high gains from rail freight and cargo transport operations in the future.

In response to long delays and obstacles to advances in the Transnordestina project, the federal government negotiated changes in institutional arrangement with CSN. Unlike the prevailing contractual relationship of the late 1990s, a new company Transnordestina Logistics S.A (TLSA) was created and the cash flow of its future operations would be provided as a "loan guarantee." Such contractual change purported to be an extra incentive that the government gave to speed up the Transnordestina project. In this setting, property rights were restructured through two alternative options of legal channels orchestrated by the government. First, the federal government, probably through its state-run engineering company VALEC, would be responsible for the implementation of the Transnordestina railway. As soon as the project is completed, the Transnordestina railway would be granted to CSN (the

private operator). Second, the federal government proposed to renegotiate the contract with CSN by revoking the previously agreed concession clause and establishing a new bidding process. The latter would result either in a Public-Private Partnership (PPP), wherein a private company would be responsible for building, operating and managing the railway. The federal government would in its turn, guarantee a minimum profitability tax rate or grant the railway operation rights to a private company.

However, the federal government soon realized the negative consequences of its renegotiation moves with CSN that could imply reputational losses and decreases in government credibility resulting from the contractual breach. The solution public officials at the end proposed involved creation of a new company TLSA jointly run by CSN and the federal government under subtle financial engineer devices of project finance. Under this new setting, the government presented itself as the principal resource investor to accommodate potential conflicts and to satisfy CSN “friendly demands.” It does not seem surprising that the previous remarkable changes in institutional arrangements reveal the crony relations between CSN and political entrepreneurs within the government sector.

Provided that the federal government itself decided to assign to TLSA the construction (property) rights of the New Transnordestina Railway, it had submitted all the scheduled investments to government officials for their approval. The latter is the basis for defining financial parameters of the railway concession contract, such as the investment return rate. Also, the public government became the ultimate financial backer of such a risky endeavor, since private investors were somehow put aside due to the changes in the contract arrangement.

The encountered solution rewarded crony relations rather than the exchange of property rights via the market. This is mostly due to a traditional view of economic development tradition in Latin America that takes the government as playing a significant role in promoting investment and, therefore economic growth.

In the specific case of the Transnordestina railway, the federal and northeast state governments decided to present the investment project as a national priority to

achieve regional development that would require considerable public financial resources.

However, the final institutional arrangement between the government and CSN was very complicated and prevented a precise specification of property rights, on which economic efficiency depends. A private company was entitled to manage the construction of Transnordestina and its future cargo operation. Nonetheless, the Ministry of Transport would have to approve of any changes in budgetary issues, since different financial instruments could come from various types of public funds. Our hunch is that this setting sheds light on ill-defined property rights that, in turn, bring a “grey area” between the private and public rights and obligations related to accountability, compensation, assessment of socio-environmental impacts, and so forth. This is because, under the final contractual scheme, the conceding power and most of the capital is public, and the manager is private without precise details about how exactly all the various involved players would share the responsibility for credibly completing Transnordestina railway.

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With the above in mind, we claim that the recurrent long investment delays and changes in budget schedules that turn out to be the main features of the Transnordestina project as a government failure are unintended consequences of the fragile institutional arrangement between federal and three Brazilian northeast state government officials and CSN.

4. References on cognitive public policy theory: Actors, institutions, and interests

The construction of the Transnordestina Railway is regarded as a public policy of state decision making, implemented by public and private agents comprising a wide range of actors, interests, and social bonds. Besides the CSN and the federal government, through the Ministry of Transport, other important actors in the process include the Brazilian Institute of Environment and Renewable Natural Resources (IBAMA), which plays an essential role in the environmental regulatory mark; the participations of the Investment Fund of the Northeast (FINOR), the National Bank of Economic and Social Development (BNDES) the Northeastern Bank (BNB), the

Superintendent for the Development of the Northeast (SUDENE) and its Development Fund of the Northeast (FDNE), all of the relevant actors for the project finance.

Other public power spheres were also involved in the work development, with consequences for the social, political, and economic sectors, as displayed in Table 2. The Public Attorney and the Ministry of Labor acted to protect the workers and the population affected by the construction of the railway, and also representatives of the subnational governments – states and municipalities – which had their interests positively or negatively affected by the work. Moreover, the conflicting scenario of the actors' interaction in the search of solutions is essential because it expressed the action of the government political stance to redefine the action of the state as an instrument to promote economic activities, mainly through the implementation of the Growth Acceleration Program (PAC), started during the President Luiz Inácio Lula da Silva's term (2003-2010).

Table 2 – Actors and interests involved in the construction of the Transnordestina

Actors	Nature	Actions	Scope	Assumed interests
Presidency of the Republic	State	Execution and Political Articulation of the Public Policy	National	Integration and development policy
Ministry of Transport	State (linked to the executive power)	Coordination and Implementation	National	Integration and development policy
Brazilian Institute of Environment and Renewable Natural Resources- (IBAMA)	State - Autarchy	Environmental Regulation	Regional	Environmental regulation
National Bank of Economic and Social Development (BNDES)	State (Federal Public Enterprise) Empresa	Long term sources of finance for investments in all segments of the economy	National	Fostering development
Investment Fund for the Northeast (FINOR)	State	Investments jointly with the Superintendence for the Development of the Northeast (SUDENE)	Regional	Regional Development
Northeast Bank (BNB)	State	Bank for regional development	Regional	Regional Development

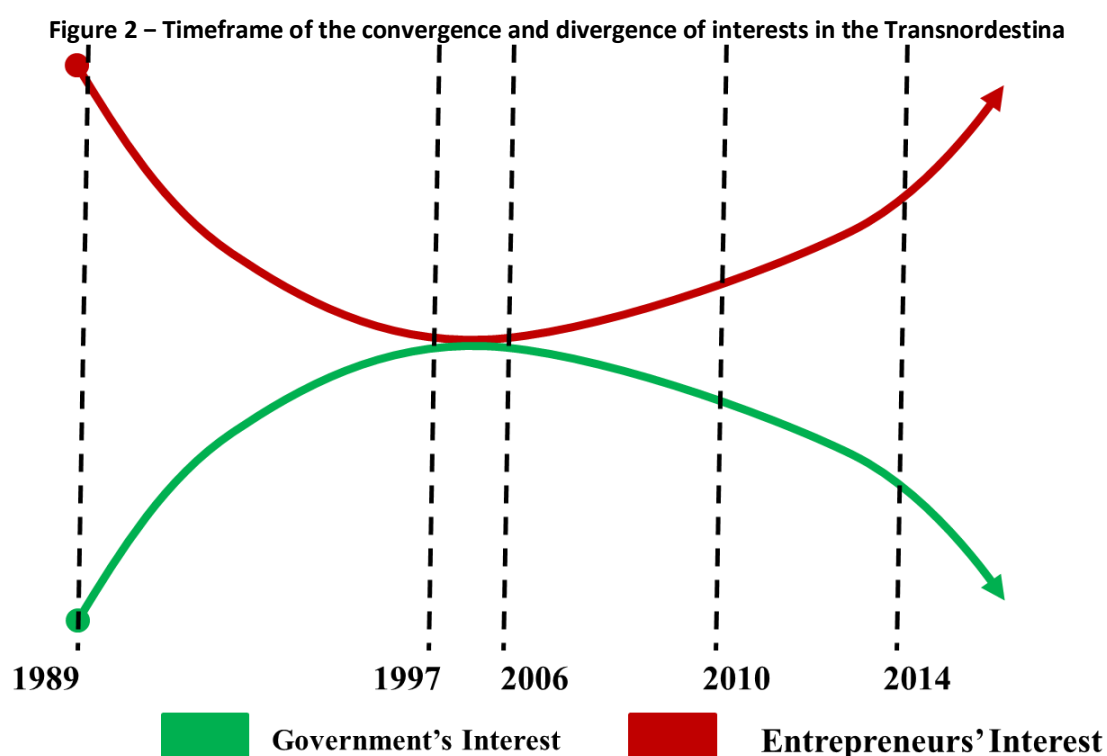
Superintendence for the Development of the Northeast (SUDENE)	State	Articulation of public policies for regional development	Regional	Regional Development
FDNE – Northeast Development Fund	State	Investments in the Northeast region	Regional	Regional Development
Engineering, Constructions and Railways S.A. (VALEC)	State enterprise	Investment, constructions, and maintenance	National	Railway network expansion
Transnordestina Logistics S.A. (TLSA)	Private	Construction and Operation of the Railway	Regional	Construction and Operation of the Railway
National Steel Company (CSN)	Private	TLSA's owner	National	Integration of the railway to its productive chain
Ministry of Labor (MT)	State	Regulation	National	Regulation of working relations
State governments	State-State executive	Implementation of regional public policies	Regional	Local interests
Municipal Governments	State–Municipal Executive	Implementation of local public policies	Local	Local interests
State Assemblies	State-Legislative	State legislation	Regional	Local interests
City Councils	State-Legislative	Local legislation	Local	Local interests

For the Federal Government, the New Transnordestina Railway is part of a national project to insert the North and the Northeast in the Brazilian economy and the international market. The integration of the Ports of Suape and Pecém interlinking the Northeastern coast with the rest of Brazil, through the North-South Railway (see Map 2), opens a new route for the flow of primary goods – minerals, grains from the new frontiers of production, and industrial products, such as the industrial complex in Pernambuco (the backside area of the Industrial District of Suape) and Ceará (the backside area of the Port of Pecém).

It is thus a structuring investment to try to meet one of the central issues in Brazil at the beginning of the 21st century. As pointed out by Fronzaglia et al. (2013), the historical aim of reducing poverty and the secular regional inequality is recovered

through a process of industrialization of the Northeastern area and the structuring of a logistic and transport network integrating the Northeast to the other Brazilian regions and the international economy.

The Engineering clubs express the difficulties of its implementation in the Northeast, which, in a letter sent to former President Lula, recommended the recovery of the railway works by the state company VALEC and showed the obstacles to its execution. The TLSA is responsible for the implementation, the delays in the schedule, the shape of the railway and the exclusive management of its operation. We can say that the period between the concession of the Railway Network of the Northeast and the creation of the TLSA was marked by the convergence of the interests of the Federal Government and the CSN (a “honeymoon” which started to break up due to the conflicts resulting from the execution of the work, as depicted in Figure 2).



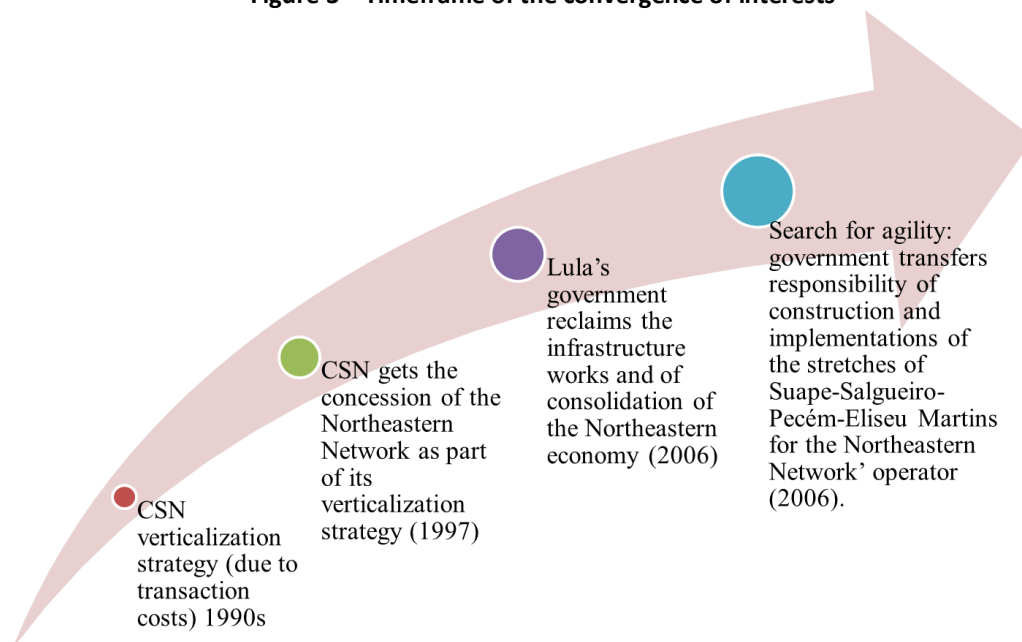
The project scheduled to begin in 2006 should have been completed in 2010, but it was then extended to 2014. The differences between the provisional and the practical costs, the alterations of the project, and land, environmental, and social

issues caused a series of delays. Even in 2019, the railway is not yet completely operational.

In fact, with the expansion of the production of grains from the North of Tocantins, Piauí and other states of the North and Northeast, the opening of new fronts of production of minerals and, on the other hand, the expansion projects of the Ports of Suape and Pecém and the industrial production of the region (shipyards, Abreu Lima Oil Refinery, industrial hubs in Ceará, Pernambuco, etc.), the interests are articulated to guarantee the effective implementation of this outflow route. The claim posed here is that the original arrangement made for the execution of the work is responsible for the current difficulties.

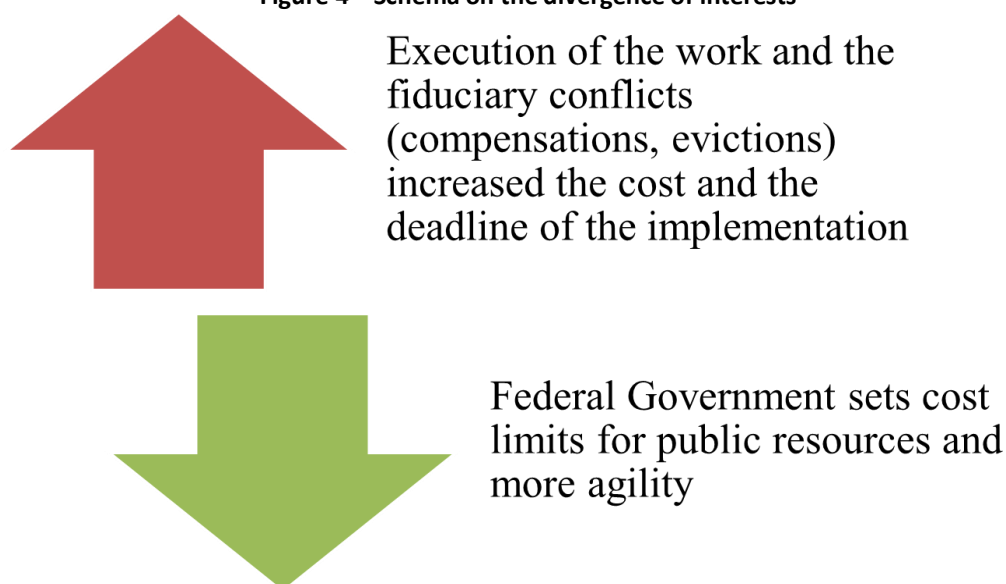
The search then was for the easiest theoretically way. It was a shortcut to overcome the time spent in the elaborate preparation and the procedures inherent to projects of such magnitude. The Project Finance set forth provisions for a capital increase of the CSN, the TLSA's controller, resources from the treasury and public financing, and established a partnership to reassign the responsibility of the construction to the beneficiary of the 1997 concession articulated with the governmental interests (see Figure 3).

Figure 3 – Timeframe of the convergence of interests



Obstacles due to expropriations, environmental issues, social, land, and political conflicts are important and inherent elements in any work of such magnitude but the model adopted and the disputes among the several actors involved were potentiated and proved difficult to be overcome. The conflicts embodied the divergence of interests, as displayed in Figure 4.

Figure 4 – Schema on the divergence of interests



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4.1. The referential theory

Jobert and Muller (1987) defined public policies as the “state in action.” Public policies occur within the limits of state regulation (political, economic, and social relations) and legitimation (Jobert, 2001). According to the authors, it is a mistake to consider the state as a homogeneous and coherent actor able to impose its consistent will on society for its well-being. The State machine often operates in an irrational and conflicting way and very rarely is shown as a unified actor. Public policies express these characteristics and contradictions in their actions. The rationality of the public action is an expression of diverse interests and actors, including the state ones, and the state institutional and legal structure limits it. Moreover, the work of the State as public policy is not an automatic answer to a specific problem, either social or private agents’ demands or even international issues.

The construction on the Transnordestina does not configure itself as a response to a kind of mechanical input-output model but rather as a consequence, in the first place, of a decision of the federal government on its new view of development for the Northeast region in collusion with private agents with convergent interests. There was no republican rationality in the “agenda-setting” of the case studied here (Kingdon, 2002). At the time of its implementation, new actors take part in the social and learning construe for the elaboration of this public action. The solutions found over time have not been set a priori but were and (still, are) necessarily construed subsequently and continuously. Jobert and Muller (1987) divide public policies into three elements: the sectoral-global relation, the referential, and the actors who frame and take part in the power relations of this specific public policy.

Besides, public policies are mechanisms of the State’s self-reflexivity (Muller, 2015; Faure and Muller, 2013) and should reflect a specific conception of State. Therefore, Muller identified four public policy cycles of action: the liberal industry state, the welfare state, the enterprise state, and sustainable governance. The sequences are a process through which a global configuration is developed, stabilized and is then fragmented and disaggregated, defining the role of public policies in society (Muller, 2015). For each cycle of action, there are different regimes of economic activities, citizenship, and public policies that are developed and are the reflection (self-reflectivity) of the referential according to the State performance. It is worth noticing that the complexity involved in the society and the recent history of Brazil result, in several moments, in not so well-defined cycles. If at the time the privatizations and concessions during Fernando Henrique Cardoso’s term in office (as well as in 1997 in the concession of the Railway Network of the Northeast), the State seems to follow the liberal path, the process of reducing the size of the government were guided and supported by state banks and state enterprises’ pension funds to organize and finance the groups participants of the bids (which implication in the Referential, as we shall see in the next section). Even in President Lulas’s term in office, mainly in the first one (2003-2006), where it seemed to go through a cycle of sustainable management, the state took actions inspired by the sequence of enterprise

state. The ill-defined relation between public and private sectors in the case of Transnordestina reflects these overlapping cycles of state actions.

4.1.1. The sectoral-global relation

The sectoral-global relation is the attempt to adjust both levels, the sectoral which refers to the development areas of public policy (in this case, the infrastructure sector of transport and logistics) and the global, which refers to the state actions (legitimation, integration, regulation, and social cohesion) for social totality. This relation is not free from contradictions, and interim balances as the state itself hold in its dynamics antagonistic interests among the sectors which comprise or and influence it in decision-making. A global sectoral relationship also demonstrated an attempt to adjust the objectives and interests of the three levels of government in Brazil: federal, state, and municipal.

4.1.2. The referential

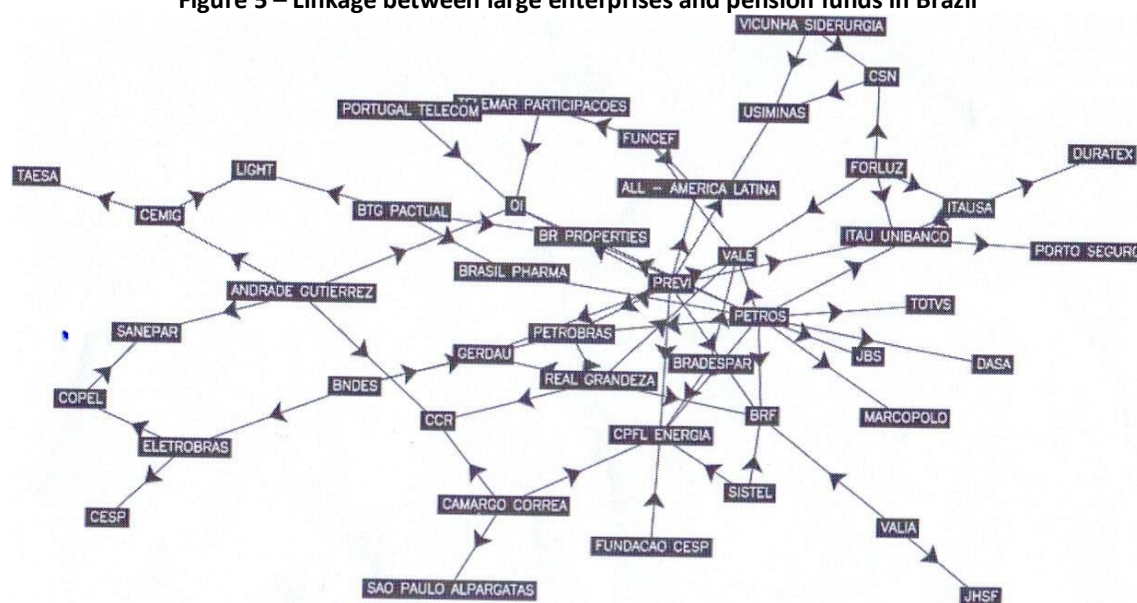
The referential element can be a set of norms and references which delimit the parameters of the state action, including legal rules. References also concern previous experiences in the same public policy. Previous public policy actions established a benchmark, or a paradigm, of public action. At this point, where the bonds are set, provided by the reproduced and followed new institutional economics (NIE) political culture, a concept closer to the referential is the so-called 'institutional environment' which encompasses legislation, property rights, ethical codes, customs and habits consolidated in the rules and informal institutions. Moreover, if the referential embodies aspects of a society's political culture, in the case of the Transnordestina we can note a new outfit for an old one: it is a new version of the old patrimonialism (Campelo, 2003; Faoro, 2005; Werneck Vianna, 1999), the so-called "capitalism of ties" (Lazzarini, 2011; Musacchio & Lazzarini, 2014). Patrimonialism is the set of existing relationships between the State and private actors to use public policies for private interests. Patrimonial relationships are long rooted in Brazilian history and politics. If patrimonialism exists everywhere, what would be the specificity of the Brazilian version? According to Souza Filho (2017), Brazilian patrimonialism is characterized by

the State's instrumentalization by the elites that subvert the public interest to their interests. This subversion is distinct from the forms thought by Weber (1970) because it is built in a context of dependent capitalism.

Modern capitalist organized its activities in property networks where the same actors play different roles in different settings but keeping the defense of the private interests intact. Lazzarini (2011) identifies a pattern in these connections (agglomerations) with the collusion of private capital and direct or indirect state resources. It is not rare to see executives and business people acting on several administrative boards. We can see then a vast network of intimate (and dangerous) relationships between state decision-makers on several levels and the ones who represent the interest of the high capital (the state enterprises pension funds play a crucial role here, as shown in Figure 5). The example of this logic is in the TLSA itself with its shareholders, CSN, VALEC, the Development Fund for the Northeast (FDNE), run by Superintendence for the Development of the Northeast (SUDENE).

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Figure 5 – Linkage between large enterprises and pension funds in Brazil

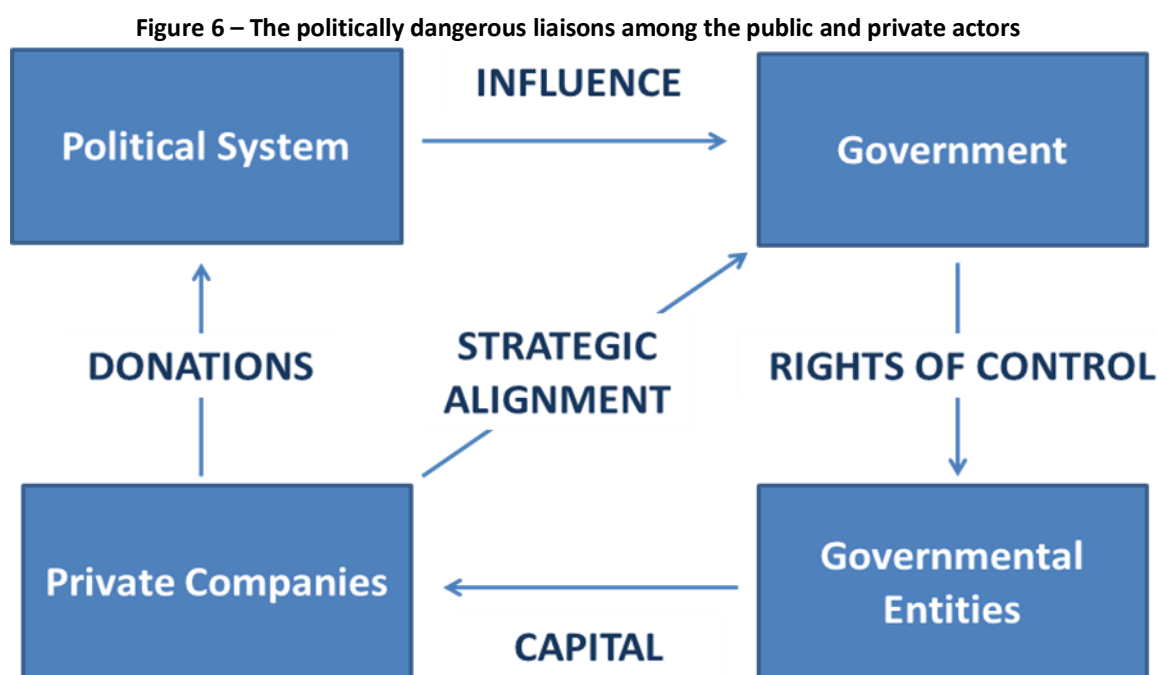


Source: Repórter Brasil.¹⁰

Lazzarini (2011) relates this event to campaign donations, evidencing that the enterprises which donated most to winning candidates were the ones that got most

¹⁰ Available at < www.reporterbrasil.org.br/elesmandam >, retrieved on 21 June 2014.

resources from state banks, including the BNDES. The CSN relations and later on the TLSA financial configurations are in this context. These elements form a politically dangerous liaison between public and private spheres and public and private interests, as shown in Figure 6.



Source: Lazzarini (2011, p. 55).

4.1.3. The construction of the referential

The third element refers to the construction of the referential, that is, the actors, their origins, characteristics, interests, and form of interaction. We can unveil power relations in public policies from action references to know the potential of each involved actor's action as well. The construction of the referential is not expressed by a sequential dynamic but rather by a net of dynamics wherein the actors are interlinked and act according to referentials mutually construed. The cycles of actions conditioned referential construction (Muller, 2015). There is a strong caveat to understand the public policy expressed in the construction of the Transnordestina Railway. In Brazil, the development of the cycles of action has followed a different way. Brazil had a late industrialization process; its constitutional rights developed in the opposite direction (Carvalho, 2001), and our path to the referential of the regulating

state (or entrepreneur state) occurred concurrently with the development of necessary welfare policies. The Transnordestina building during Lula's term expressed a developmentalism referential (some would call it neo-developmentalism) where the state is the driving agent of economic development. This reference dates back to the previous century, and its transposition for a scenario of change of cycles of public action reflected the deadlock and lack of action of the own execution of the Transnordestina Railway.

4.2. The theory of the three 'is'

The referential theory (a cognitive approach to public policy) provides us some analytical tools for understanding (Palier and Surel, 2005) the subtleties of the State action in the case of the Transnordestina Railway.

Surel (2000) defined public policy achievements as social interactions that result in the production of shared ideas, representations, and values. In their turn, ideas and values conditioned the way society sees public problems and provide answers to such issues. The shared values and representations do not exclude the conflictive dimension of public policy because the social groups with distinct interests construct and share conflicting values and actions in the political action.

The importance of the values and representations expressed here, the legal configurations, the fragmented state behavior and, in consequence, the conflict of interests leads us to a new cognitive approach to public policies: the theory of the three 'Is' – interests, institutions, and ideas – which complement the notion of referential, power relations and the sectoral-global relation.

According to Palier and Surel (2005), institutions concerned the state and all its structure of power and operation in several areas of action, its several and autonomous spheres of action and power division. Moreover, institutions play the 'rules of the game' and create a system of (often contradictory) incentives for the agents' decision-making. In the case of the Transnordestina Railway, there is direct participation of the federal government, through the Ministry of Transport, and the involvement of the Public Attorney's Office, the Brazilian Institute of Environment and Renewable Natural Resources (IBAMA). They are all public institutions that defend

conflicting interests. There are also issues related to the interests of the subnational governments, municipalities, and states affected by the progress of the work. That description of the role of institutions is very similar to the one of Douglas North and the new institutional economics approach.

Interests, inseparable from the institutions, involve the goals of each agent and actor involved in the process. At this point, the patrimonial arrangement between the public and the private spheres becomes clearer.

The ideas comprise the collective images and representations, and the values expressed in the actors' actions. They create the context and influence the actors' behavior and also the configurations wherein the referential is consistently embedded and elaborated. According to Surel and Palier (2005), the joint mobilization of the three 'Is' is based on the idea that the constituent and the explanatory variables of a public policy are not exclusive but are interwoven and associated with limiting the dynamics of the actors' action, something essential for understanding the State in action. At this point, we can see how the concepts of cognitive theories and the new institutional economics are related.

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Table 3: Cognitive Theories of Public Policy: a synthesis table

Referential Theory	The Three Is
The Sectoral - Global Relationship: The Relationship of the Public Policy Target sector and the other levels of government performance	Functioning of Institutions
Referential: norms, customs, and social learning of public policy.	Interaction of interests and ideas in state action
Actors: interaction of public and private actors in the construction of the referential	Interaction between institutions and the interests and ideals of the actors involved.

The identification of the three 'Is' and their effects in the case of the New Transnordestina Railway are depicted in Figure 7.

Figure 7 – The Analytical Scheme of the Three Is for the Transnordestina Case



5. Implications and final remarks

In this article, we attempted to provide analytical insights on the practical problem of the implementation of public policy in transport infrastructure in Brazil: the Transnordestina Railway. The project, part of the federal government Growth Acceleration Program (PAC), was approached in the light of different theories of political science and the positive political economics.

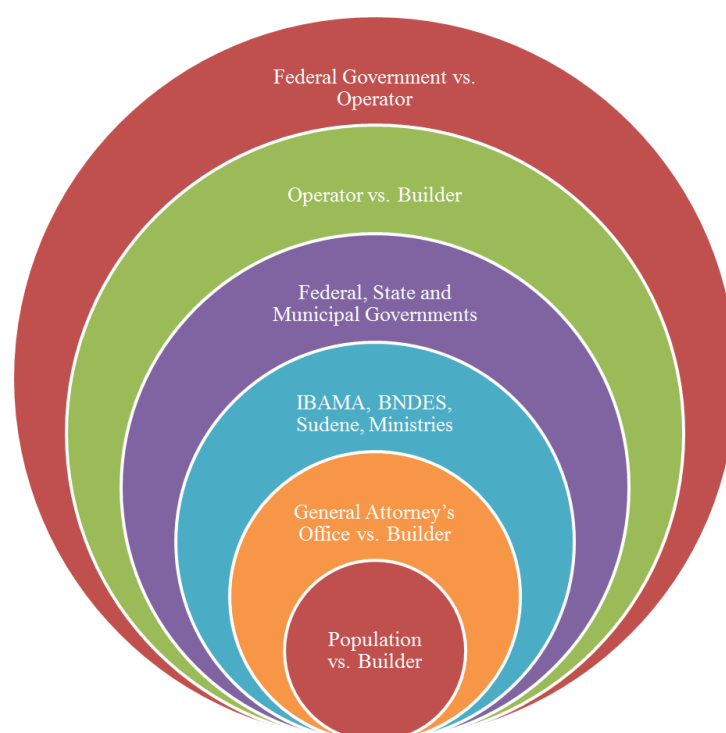
In Section 1, we described the background of the work from its origins until its current status, the work progress, and its costs and delays from the end of President Lula's first term in office. In Section 2, we provided an account of the conflicts and errors in the project involving actors, interests, and legal in the light of the new institutional economics (NIE), which resulted in constant delays and budgetary increases. In Section 3, we discuss the cognitive approaches on public policies, in particular, the referential theory and the theory of the three 'Is' and the concept of crony capitalism in search of explanations that consider the political and social variables to understand this complex public action.

The Transnordestina project is to be understood as a public policy which converges state interests on several governmental levels and distinct private interests, not completely separated from the political and partisan interests, that is, when politics and policy act together. In this scenario of arrangement between the public and the private sectors, and policy and politics, the public interest seems to be obliterated as the political balance involving institutions, interests, and ideas in a particular scenario which enables and is expressed in public policies is always temporary (Jobert and Muller, 1987), though not still brief, we need to analyze the

structural characteristics of the state's power, its institutional reference, its values, the dynamics of the actors' interactions and their explicit or implicit interests, and the legal configuration which limits and conditions its development.

The construction of the Transnordestina Railway can be described as a real expression of unsolved conflicts between actors and interests involved in a context marked by references of patrimonialism in collusion with the public and private spheres on several levels of the government and public power. The relations displayed in Figure 2 comprise a network of conflicts which are both interconnected and conditioned to it.

Figure 8 – Network of conflicts involving the Transnordestina Railway's work



Conflicts are inherent in significant infrastructure works. Their completion tends to take longer than scheduled and the resources initially provided to deal with compensations, and socio-environmental lawsuits proved quite often insufficient in the course of their execution. However, what we claim in this article is that such conflicts were inserted in a more significant dispute involving the federal government and the operator of the Northeast Railway Network. A good example is shown by

Fronzaglia et al. (2013) regarding the conflict in the municipalities of Gameleira and Escada, in Pernambuco which was due to the railway plan and the families' expropriation and compensation. This could be reasonably solved using the existing institutions, but, on the contrary, it involved the Public Attorney's Office, mayoralties, and the government of Pernambuco state, with impacts on the contractor, the operator and the federal government. Therefore, the usual conflicts were intensified resulting in more than a ten-year delay of the initial schedule and around 66% cost increase.

The analysis of the legal context, including the contract, legislation, interests, ideas, and institutions of the New Institutional Economics, led us to the origin of this public policy: it is neither the result of a grave diagnosis nor the precise and objective demand of the affected subnational governments or the several private actors and sectors of society. The origin is in the networks of interests developed between the government and specific private agents, between the Labor Party government and one of its main supporters, the CSN. All the analysis provided here is an attempt to explain how such a singular action (or such an institutional, legal deviation) is configured as public policy and has involved several actors, interests, values and references. It is where the public interest, in its clear republican meaning, fades out.

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