

Latin American Exceptionalism: The Politics and Economics of Unfulfilled Potential.

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Latin America: Physical



Recent Progress

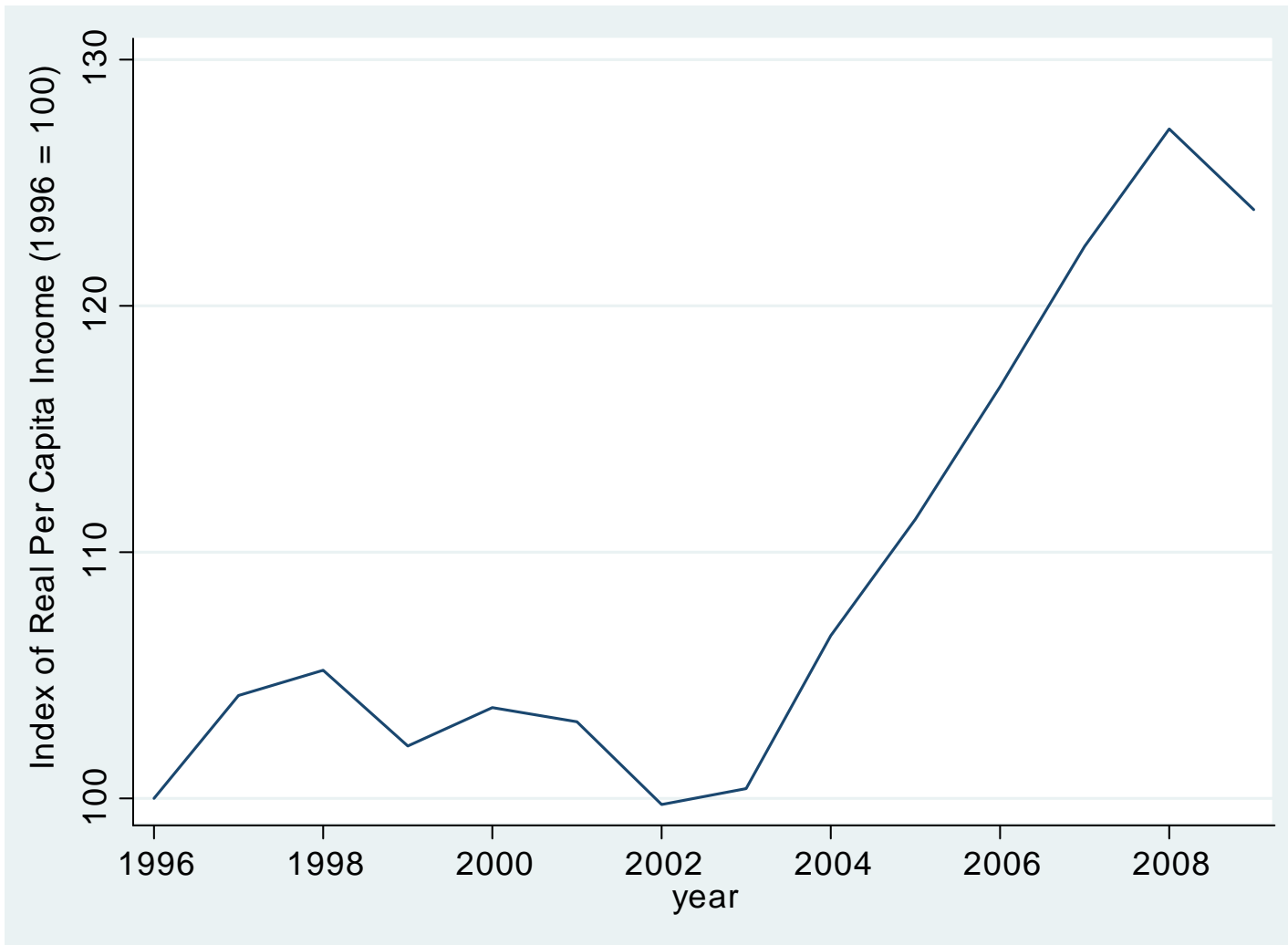
- Democratization
- Rule of Law
- Economic Growth
- Decreasing Inequality and Rising Middle Class

Latest Democratizations

Argentina	<i>1983</i>	Honduras	<i>1982</i>
Bolivia	<i>1982</i>	Mexico	<i>2000</i>
Brazil	<i>1985</i>	Nicaragua	<i>1984</i>
Chile	<i>1990</i>	Panama	<i>1989</i>
Ecuador	<i>1979</i>	Paraguay	<i>1989</i>
El Salvador	<i>1984</i>	Peru	<i>1980</i>
Guatemala	<i>1986</i>	Uruguay	<i>1985</i>

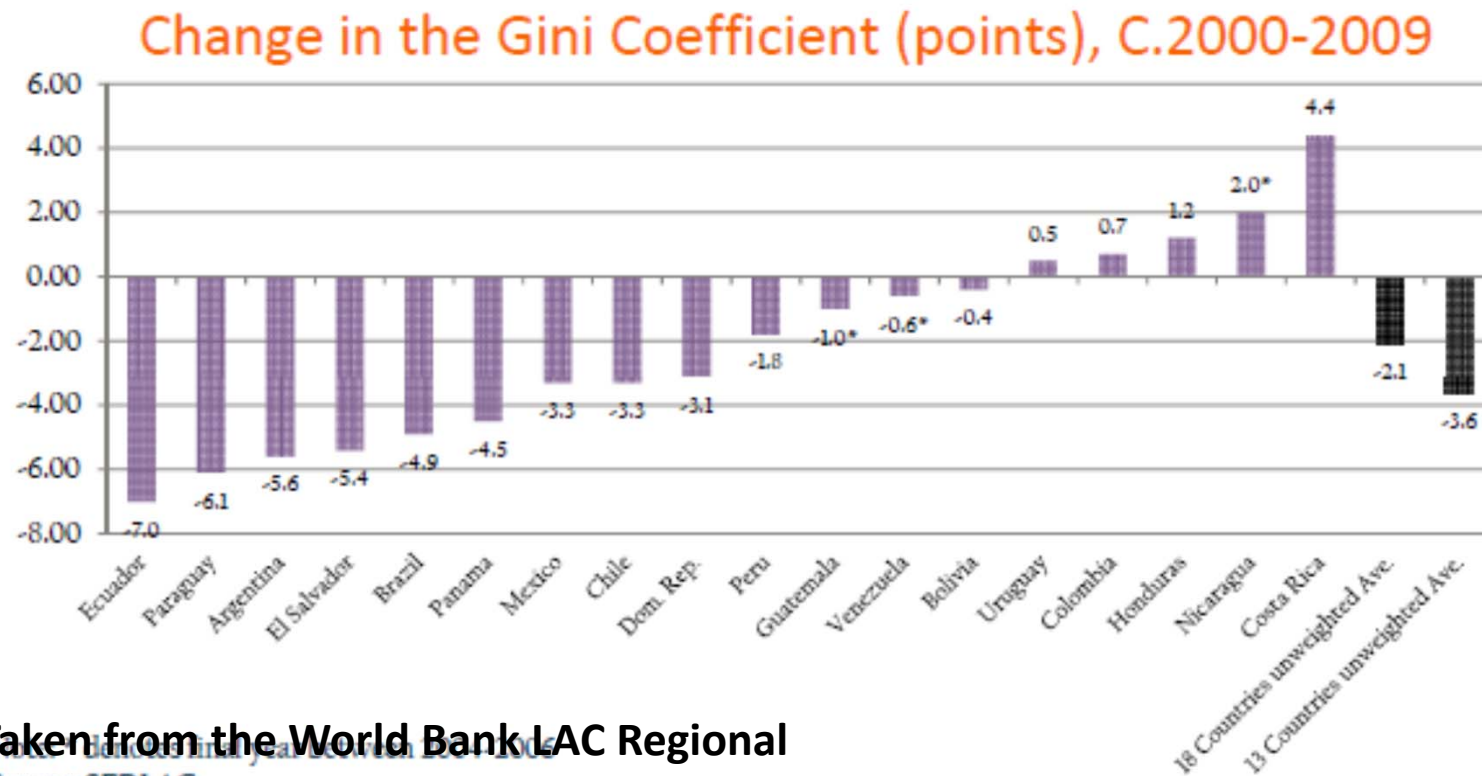
Note: Democracy coded as electoral democracy. Source: Cheibub, Gandhi & Vreeland (2009)

Steady Economic Growth



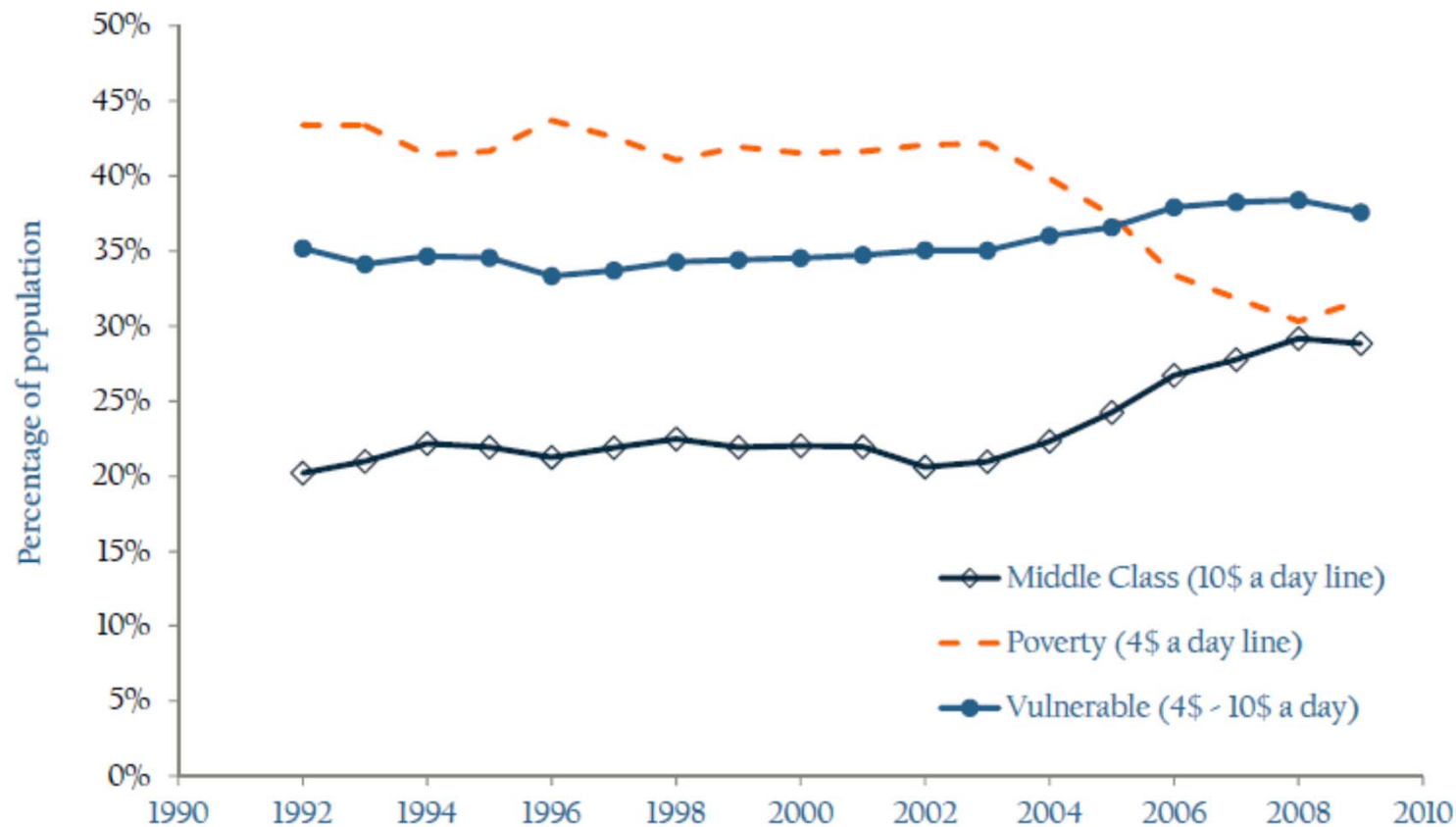
Note: Avg. Real Per Capita Income in 2005 dollars for Latin American countries excluding Central America
Source: USDA. Macrostatistics

Declining Inequality



Taken from the World Bank LAC Regional Flagship (2012). Original report written by Francisco H. G. Ferreira, Luis Felipe López-Calva, María Ana Lugo, Julián Messina, Jamele Rigolini, and Renos Vakis.

Rising Middle Class



Taken from World Bank LAC Regional Flagship (2012). Original report written by Francisco H. G. Ferreira, Luis Felipe López-Calva, María Ana Lugo, Julián Messina, Jamele Rigolini, and Renos Vakis.

Chile

- GDP per capita has doubled over past 18 years, fastest sustained expansion in country's history.
- Poverty rates have fallen precipitously.
- Chileans from humble families attending college.
- Chile has attained homeownership rate roughly equal to that of the United States, about 70%.

Peru

- Country has grown at 7% per year over past few years.
- Commodity boom has fed public investment & consumption boom
- FDI keeps pouring in & currency strong.

Mexico

Living standards—infant mortality rates, life expectancy and years of education—have improved greatly.

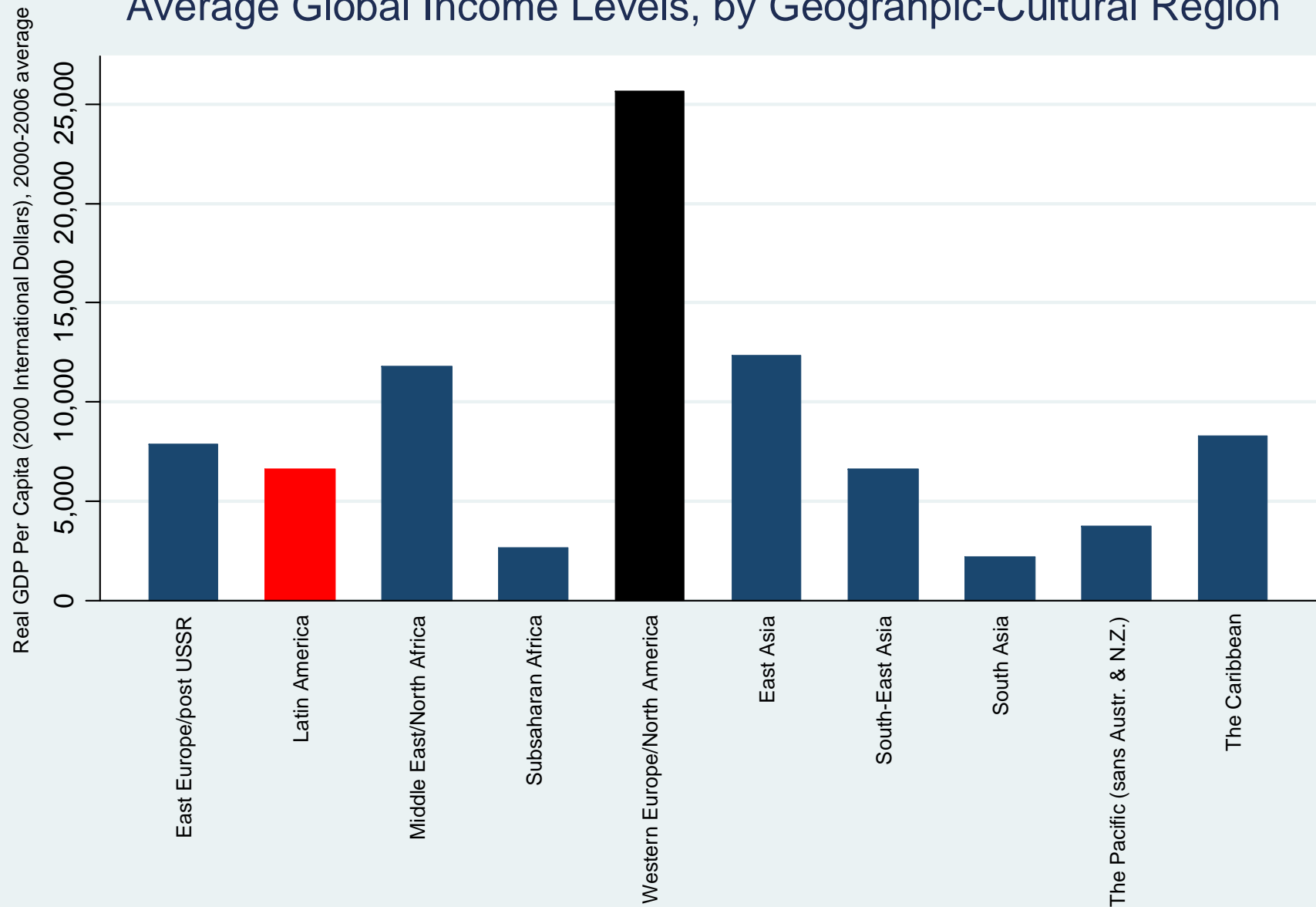
Country is growing again; giving China run for its money with *skilled* labor.

Immigration to USA has been drastically reduced.

LATAM exceptionalism:
unfulfilled promise

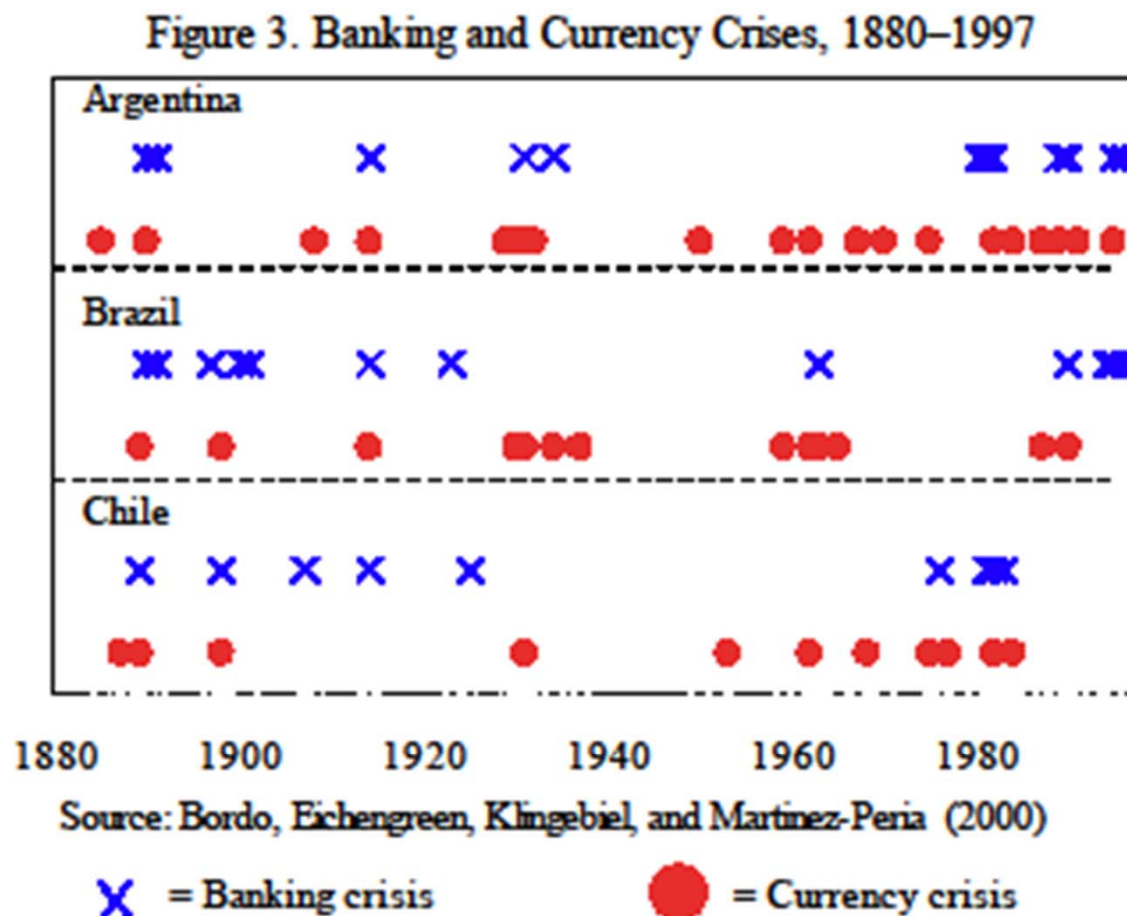
- Lower economic development than expected given these countries' age, resources & proximity to foreign markets.
- Serious corruption and challenges to rule of law.
- Spending on education, health, social insurance & infrastructure less than expected, given the vast needs.
- Lower & more regressive taxes than rest developing world.
- Still highest inequality in the world

Average Global Income Levels, by Geographpic-Cultural Region



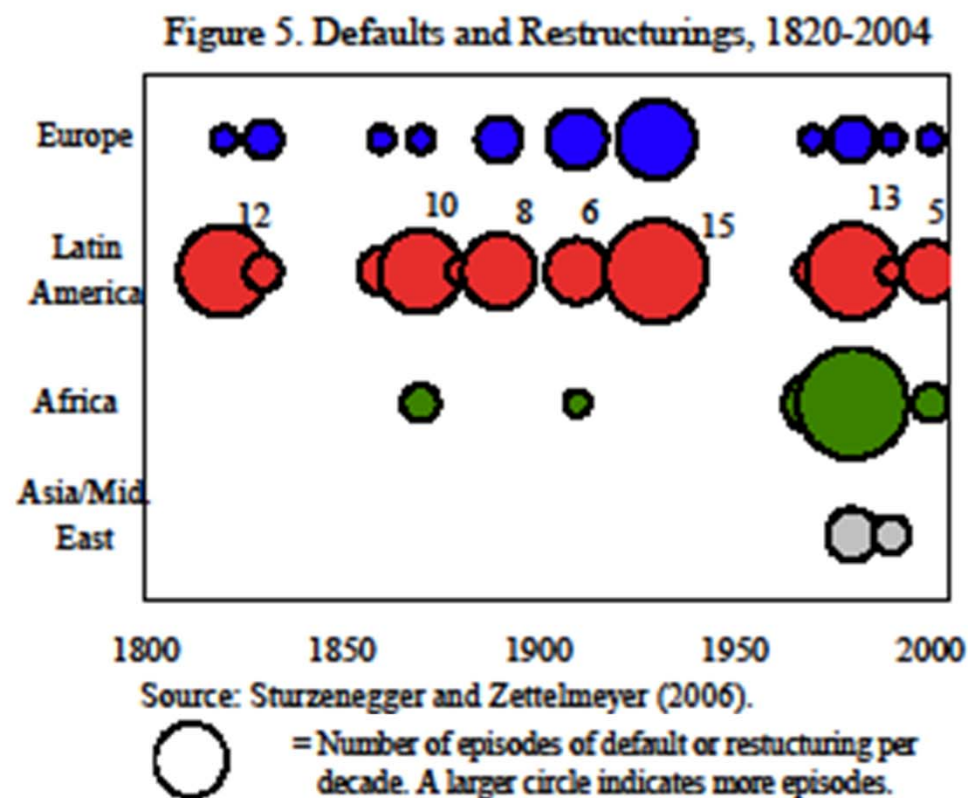
Source: Haber and Menaldo (2010). Notes: regions defined by Hadenius and Teorell (2005); Latin America includes Cuba and Dominican Rep.; Cyprus included in Western Europe/North America; Mongolia included in East Europe/post USSR

What if 2008 Financial Crisis was the norm?



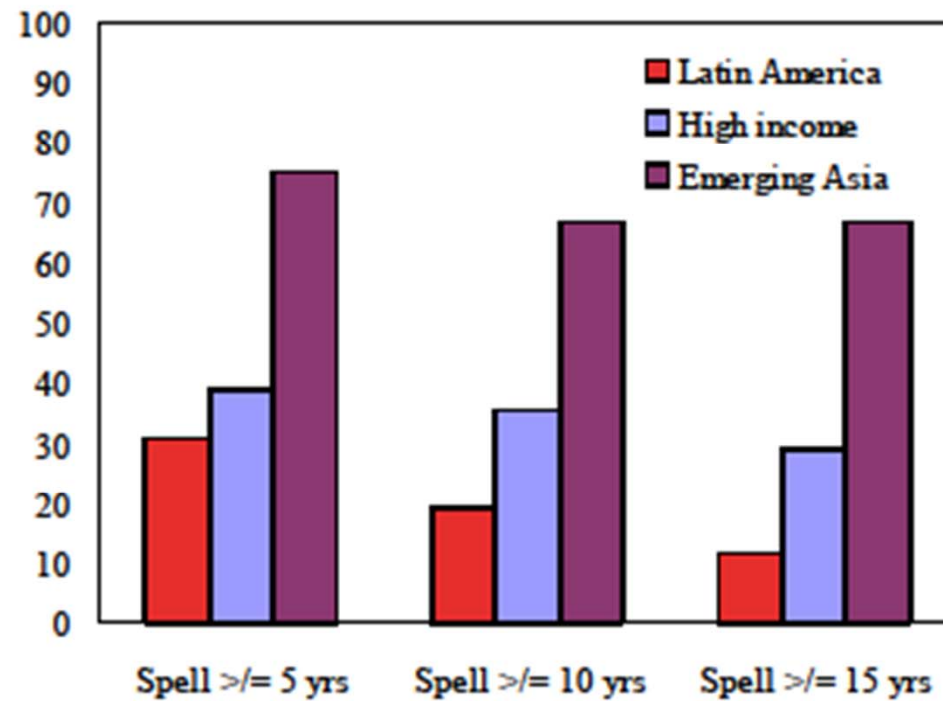
This chart is taken from Bordo et al. (2000)

We think Greece has it bad today?



This chart is taken from Bordo et al. (2000)

Figure 6. Duration of Growth Spells, 1950–2003
(percent of countries achieving the indicated duration)



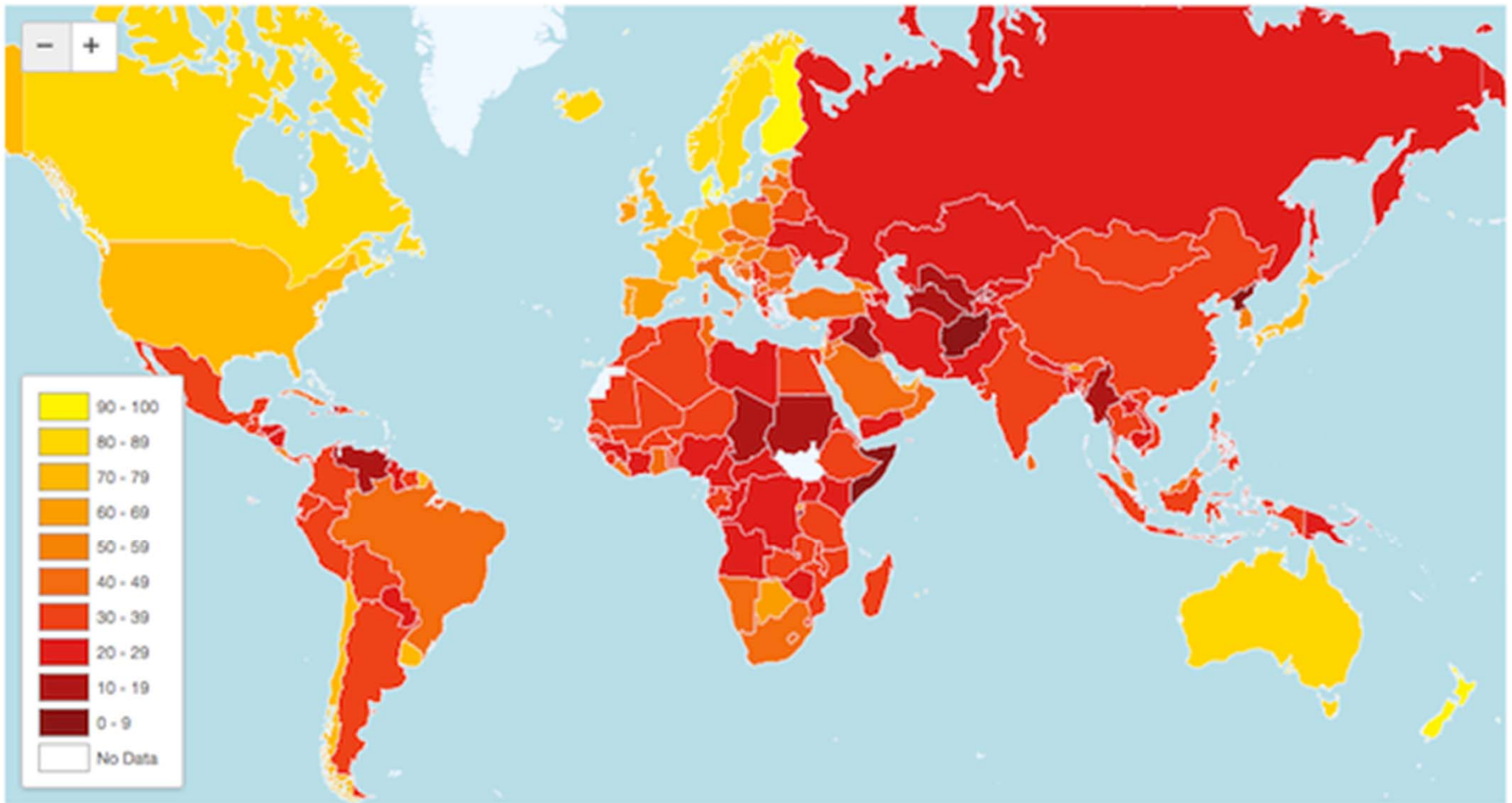
Source: Berg, Ostry, Leite, and Zettelmeyer (2006).

This chart is taken from Bordo et al. (2000)

In 1899, Argentina was wealthier than the USA!

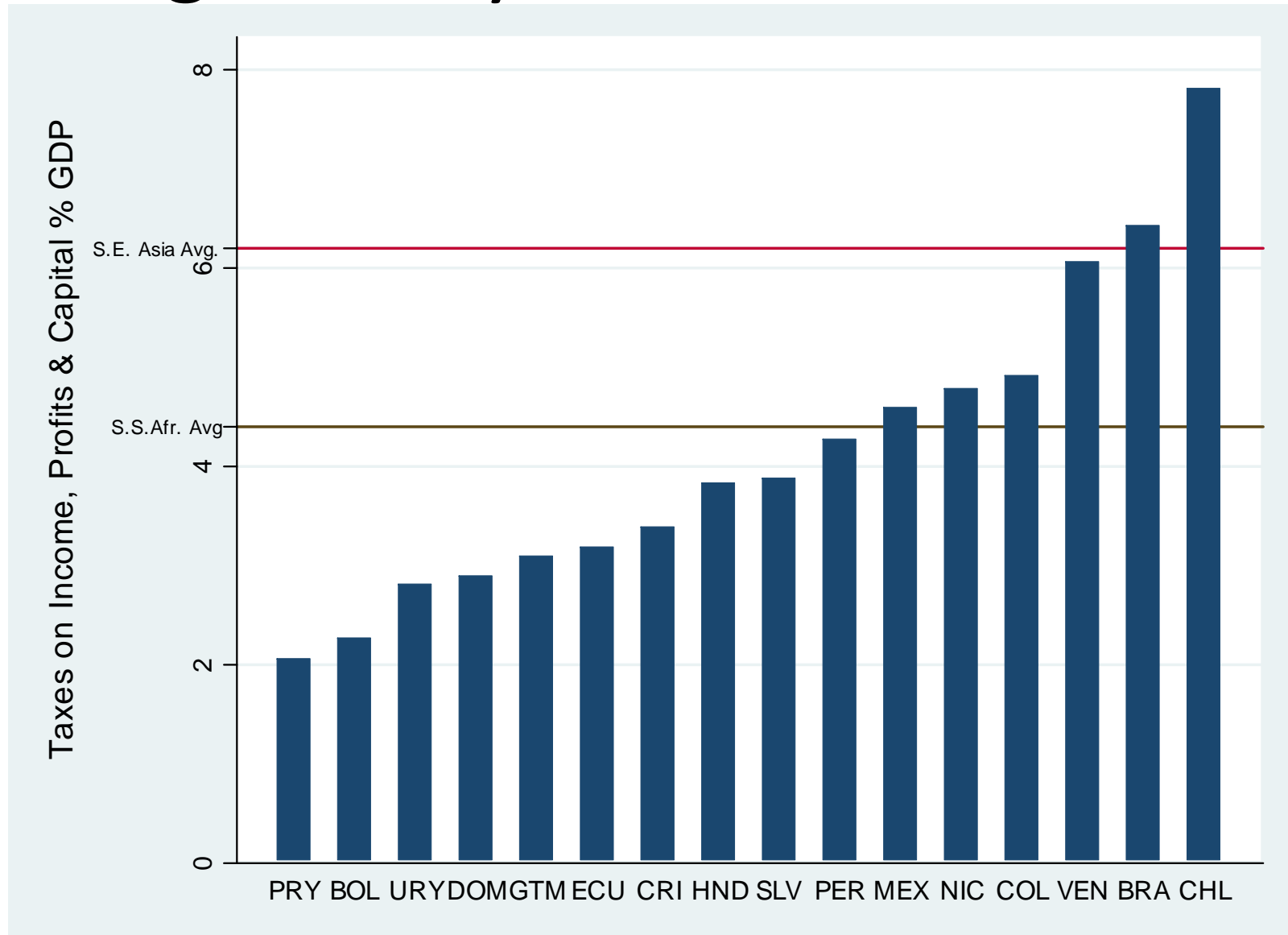


A big challenge is corruption



Notes: Transparency International's 2012 Corruption Perceptions Index. Source: Screenshot taken by Julia Knight: <http://foreignpolicyblogs.com/2012/12/08/in-case-you-missed-it-transparency-international-corruption-perceptions-index/>

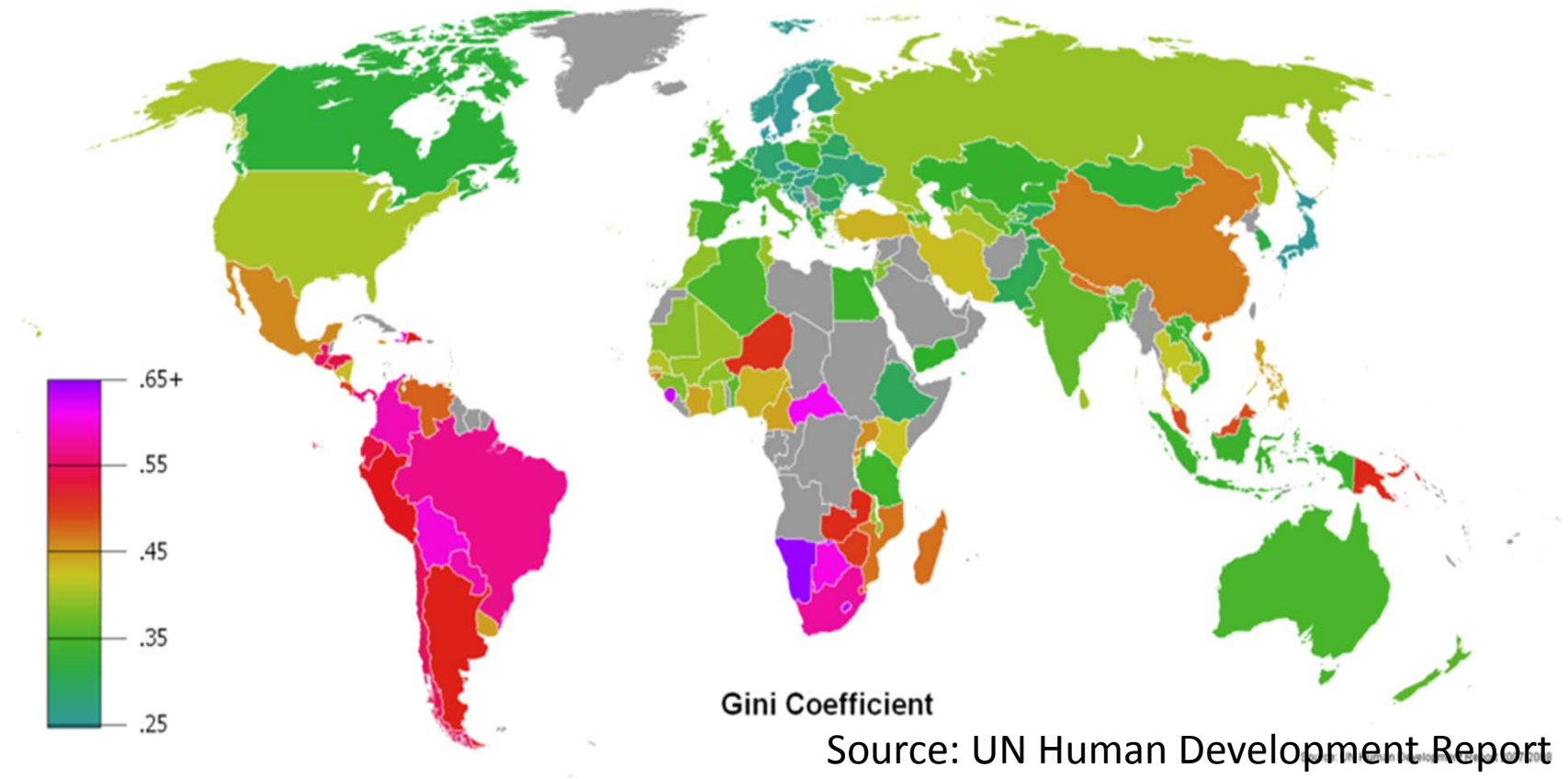
Progressivity of Taxation in 2005



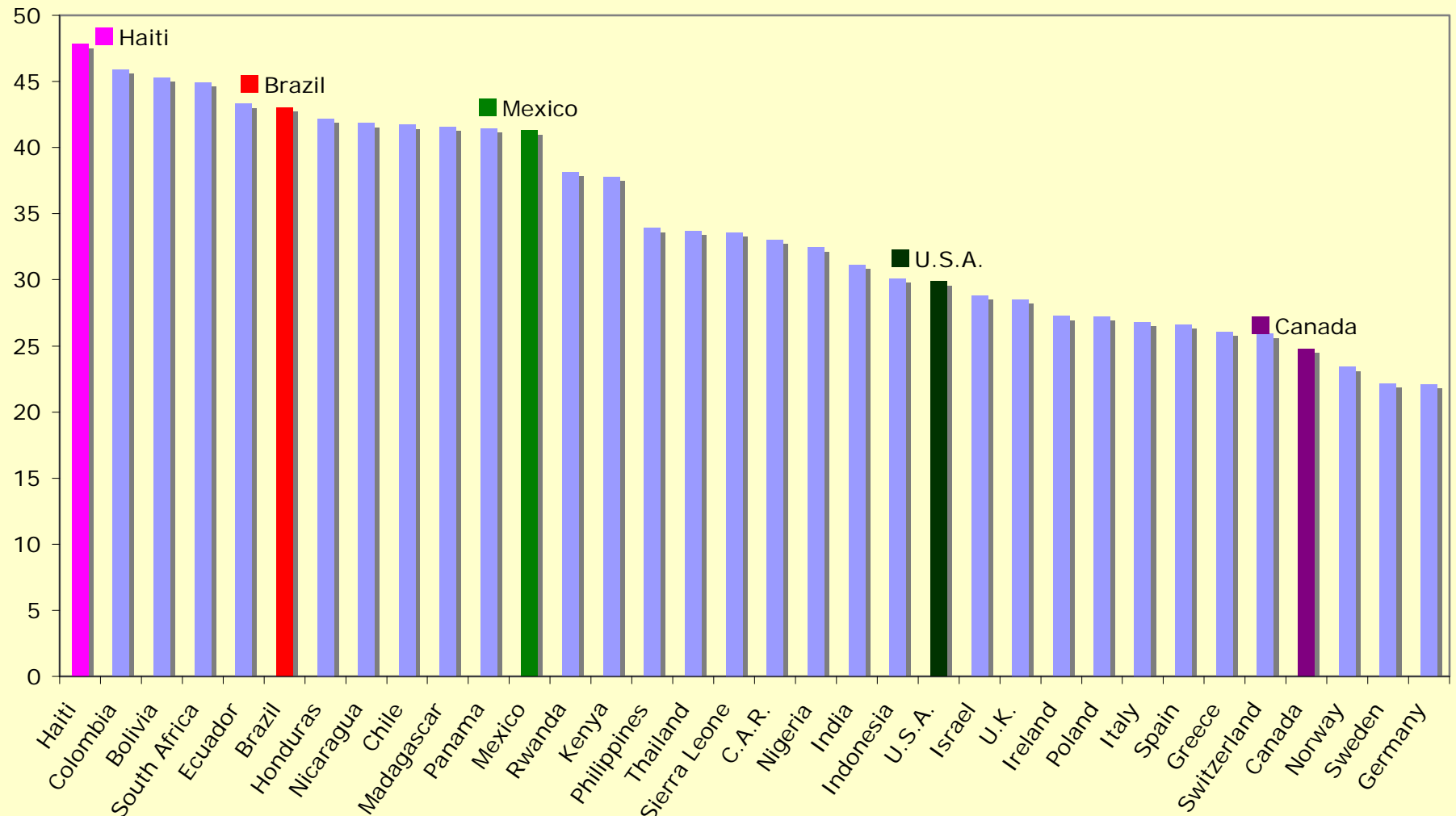
Notes: Income, Profits & Capital as defined by IMF GFSY.

Source: Albertus and Menaldo (2013).

Income Inequality



Income Share of the Top Ten Percent



Source: World Bank, World Development Indicators (data refer to most recent year available)









Imagestate





Paul Conklin/West Stock







LATAM Exceptionalism is Very Puzzling!

Consider a natural experiment

- Areas conquered by Spaniards populated by more sophisticated, wealthier civilizations.
- LATAM colonies wealthier & more important than North American ones.
- LATAM countries just as old as USA.

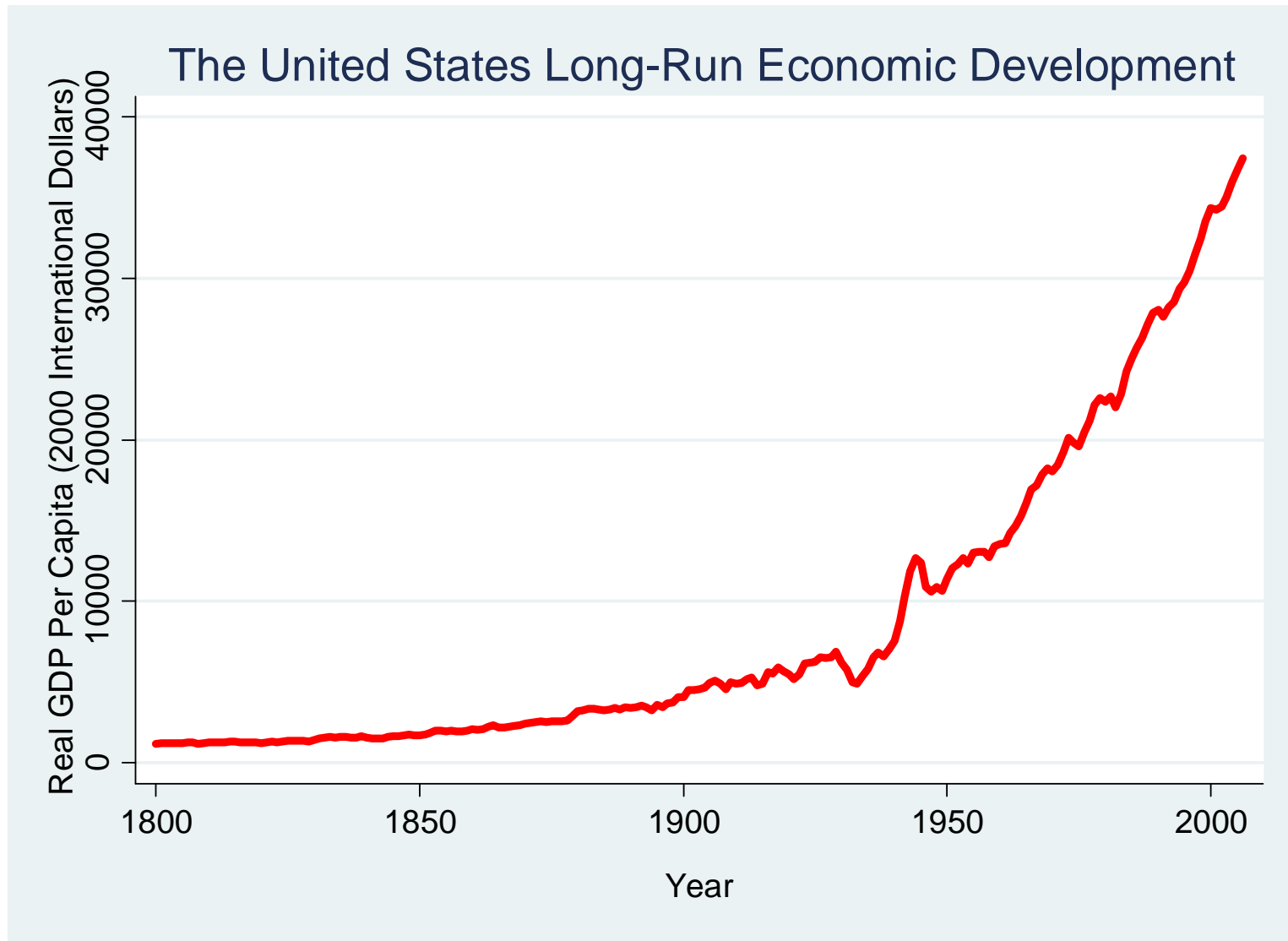
YET THERE WAS A NOTABLE REVERSAL OF FORTUNE

After colonialism, North America surpassed LATAM and became much wealthier and influential.

Much of LATAM got stuck in neutral.

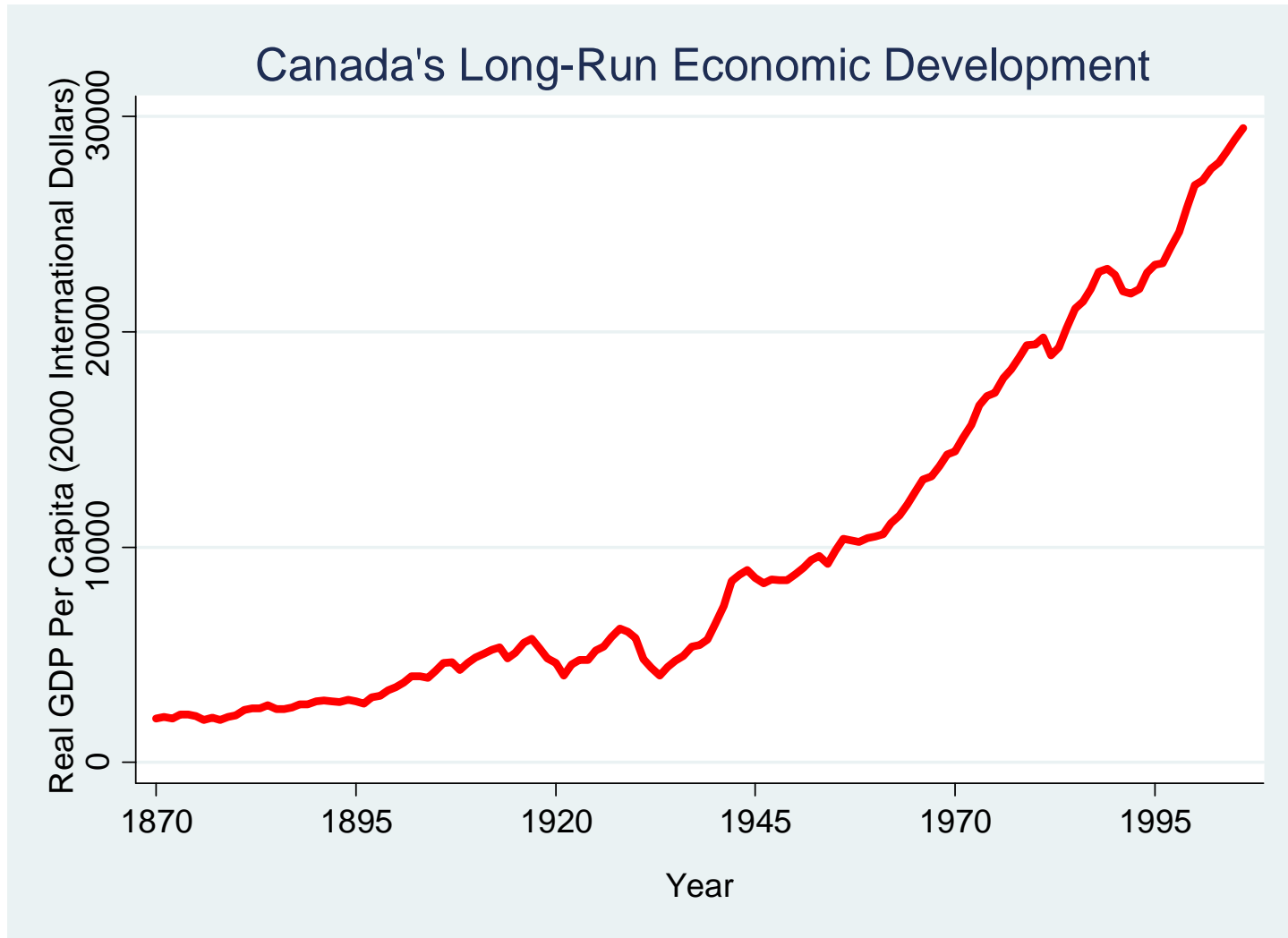
Some LATAM countries went in reverse.

We became rich, steadily and then explosively!



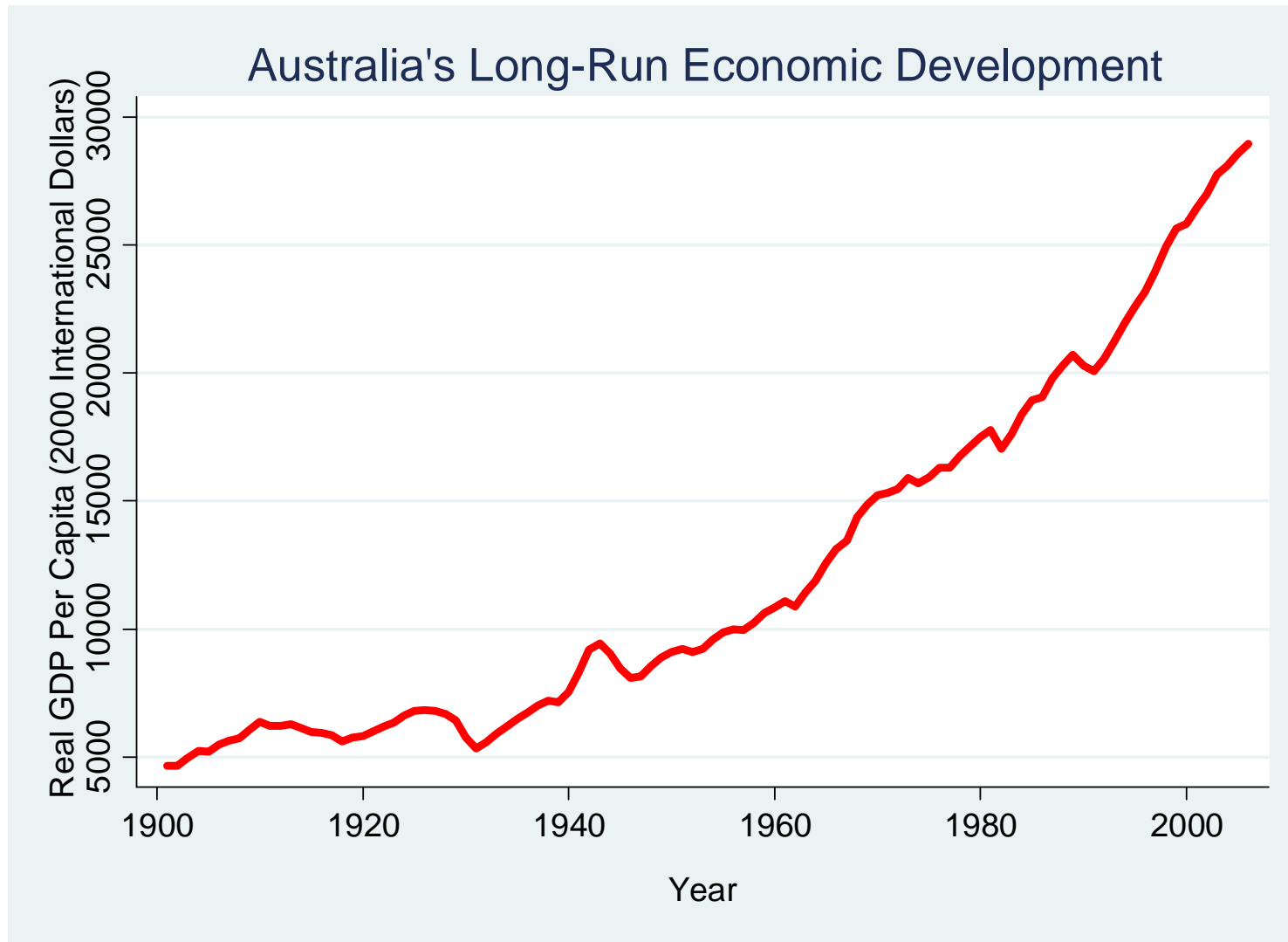
Source: Haber and Menaldo (2010)

So did our neighbors to the north



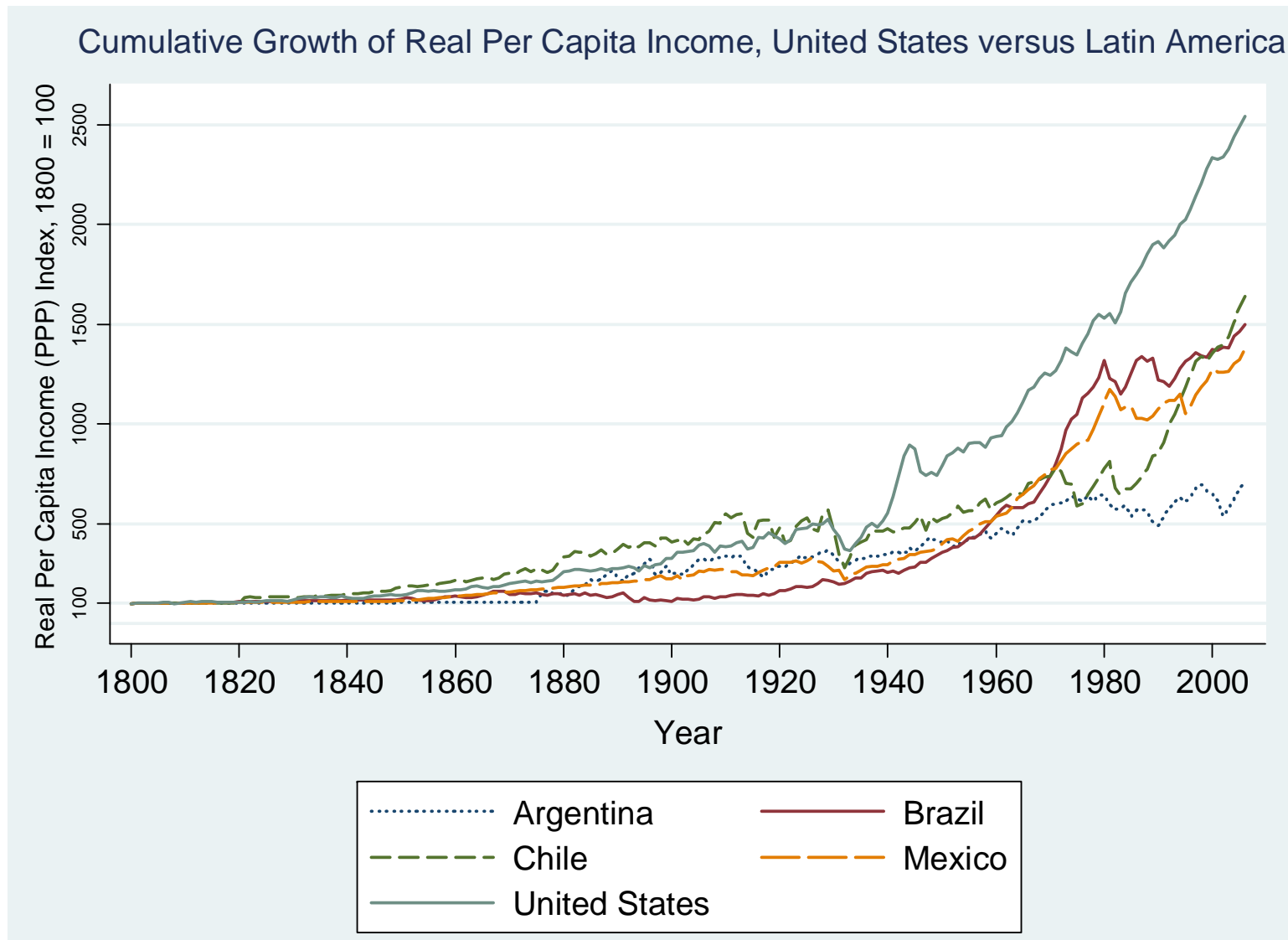
Source: Haber and Menaldo (2010)

As did other “settler colonies”



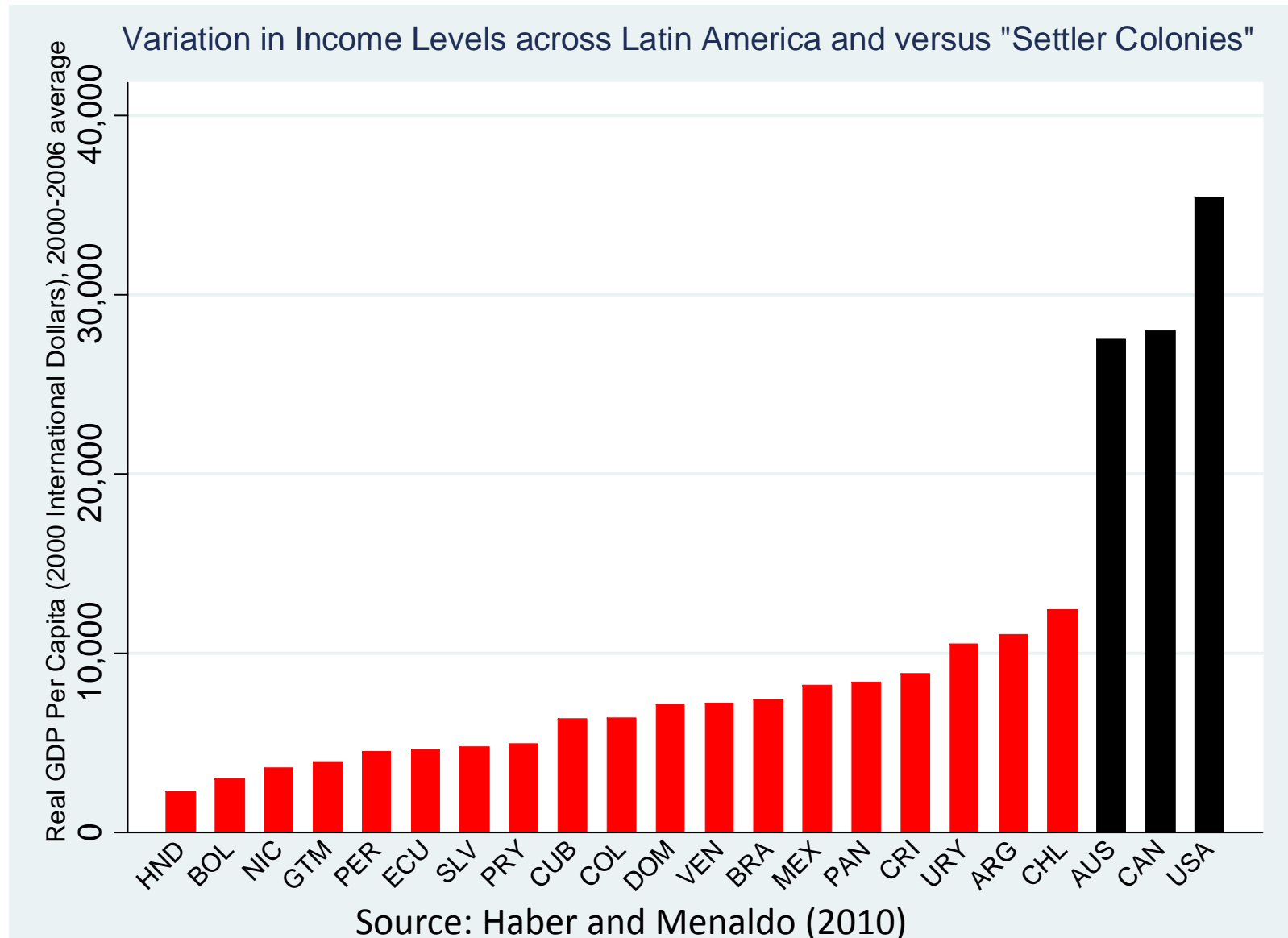
Source: Haber and Menaldo (2010)

Comparing growth records



Source: Haber and Menaldo (2010) and Coatsworth (1998). Notes: linear interpolation used for Latin American countries to fill in missing values during the nineteenth century.

Steady growth culminated in pronounced income differences



What explains Latin American
Exceptionalism?

Some popular explanations

1. LATAM countries cursed by abundant natural resources
2. LATAM dependency on the vagaries of international capitalism
3. Protestant Work Ethic versus Catholicism
4. British Cultural Legacy versus Spanish Legacy
5. NA had brilliant founding fathers while LATAM suffered from inept, myopic leaders

These explanations are all wrong!

1. United States, Canada, and Australia have greater resource wealth than LATAM
2. LATAM countries have been historically more protectionist and isolated than North America
3. British colonies in Africa have not fared better than French or Portuguese colonies
4. I don't disagree that we had brilliant founding fathers, but they had Simon Bolivar, Miguel Hidalgo and O'Higgins.

What explains differences between North America and Latin America?

- Differences in soils, climates & native pop. densities
- Differences in political & economic institutions
- Differences in distribution of wealth/income/knowledge
- Differences in policies that reinforced these institutions & distribution of wealth, income & knowledge

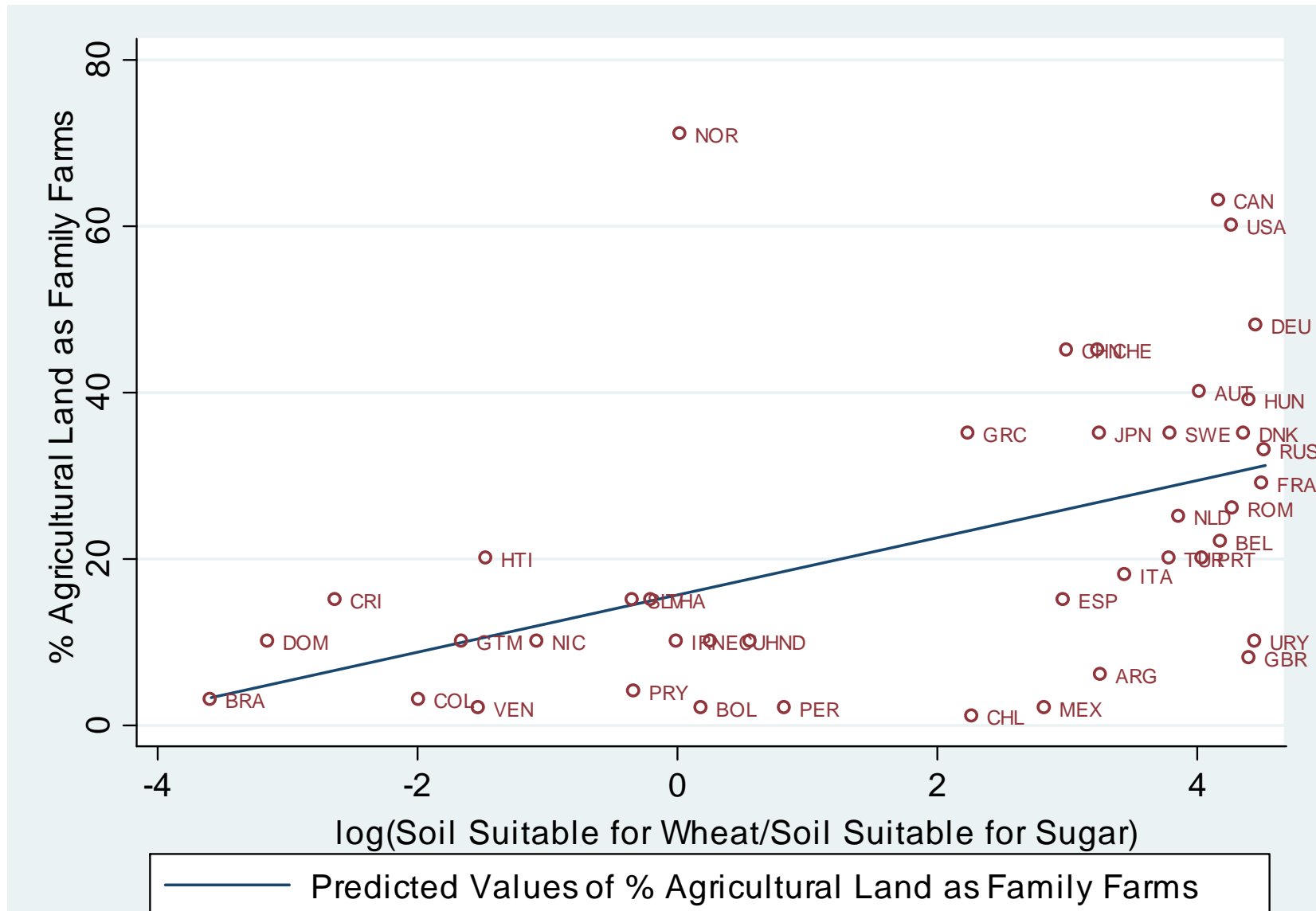
The North American Model

1. Temperate climate & fertile soils + diffuse & small native populations →
2. Colonial strategy based on European settlements and economy based on grains at small scale →
3. Colonial institutions favored equality & middle class →
4. Postcolonial institutions centered on democracy & federalism →
5. Public policies reinforced equality & democracy

The Latin American Model

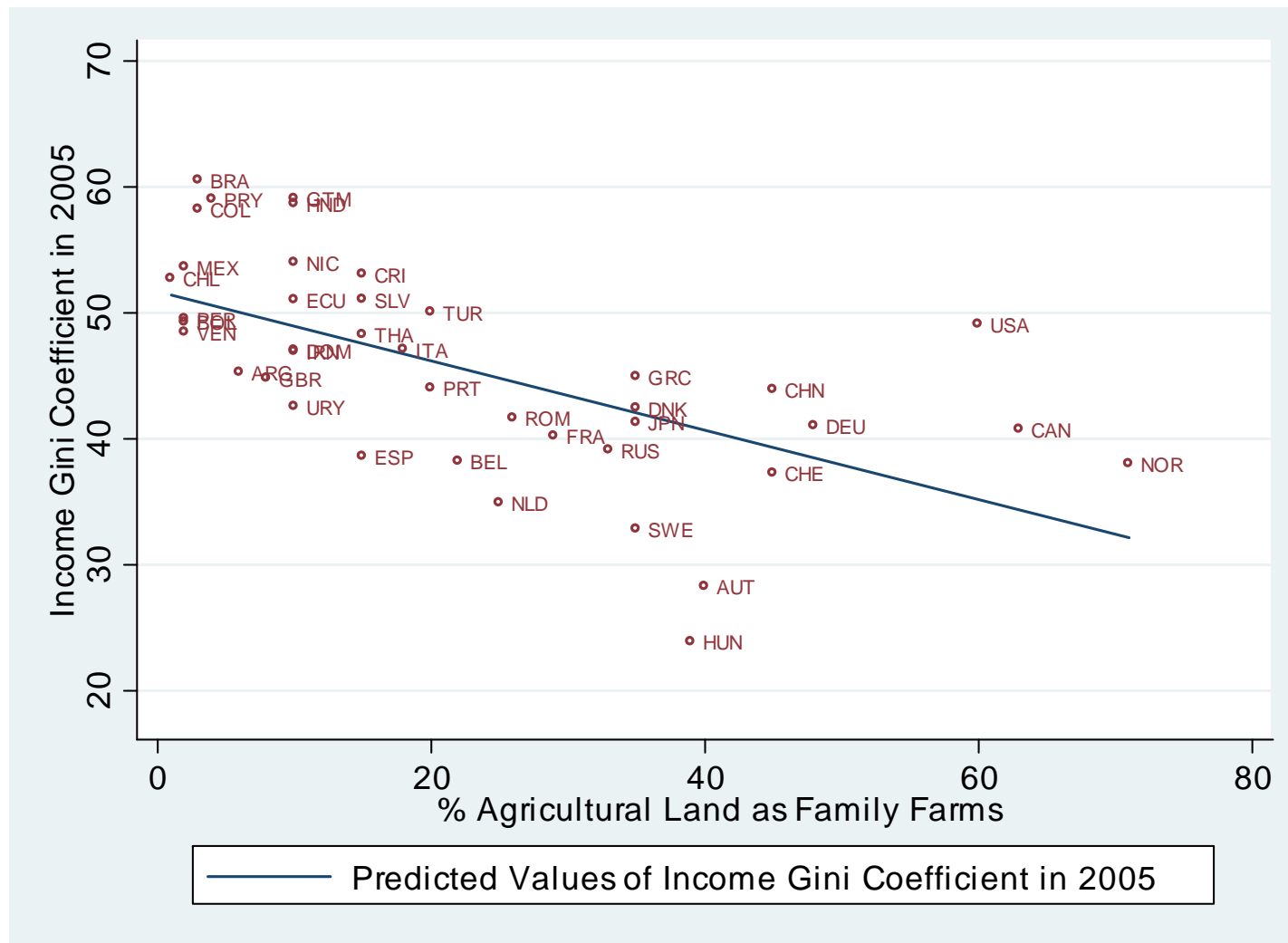
1. Tropical soils & climates or inheritance of mining centered economy + dense native populations/slave trade →
2. Colonial strategy based on plantation agriculture & mining. Mercenaries impressed servants/slaves →
3. Colonial institutions favored small elite of European heritage. Created vast differences in wealth/knowledge/opportunity →
4. Postcolonial institutions centered on oligarchy →
5. Policies reinforced inequality & oligarchy

Relationship btwn Land Suitable Wheat & Family Farms (1888)



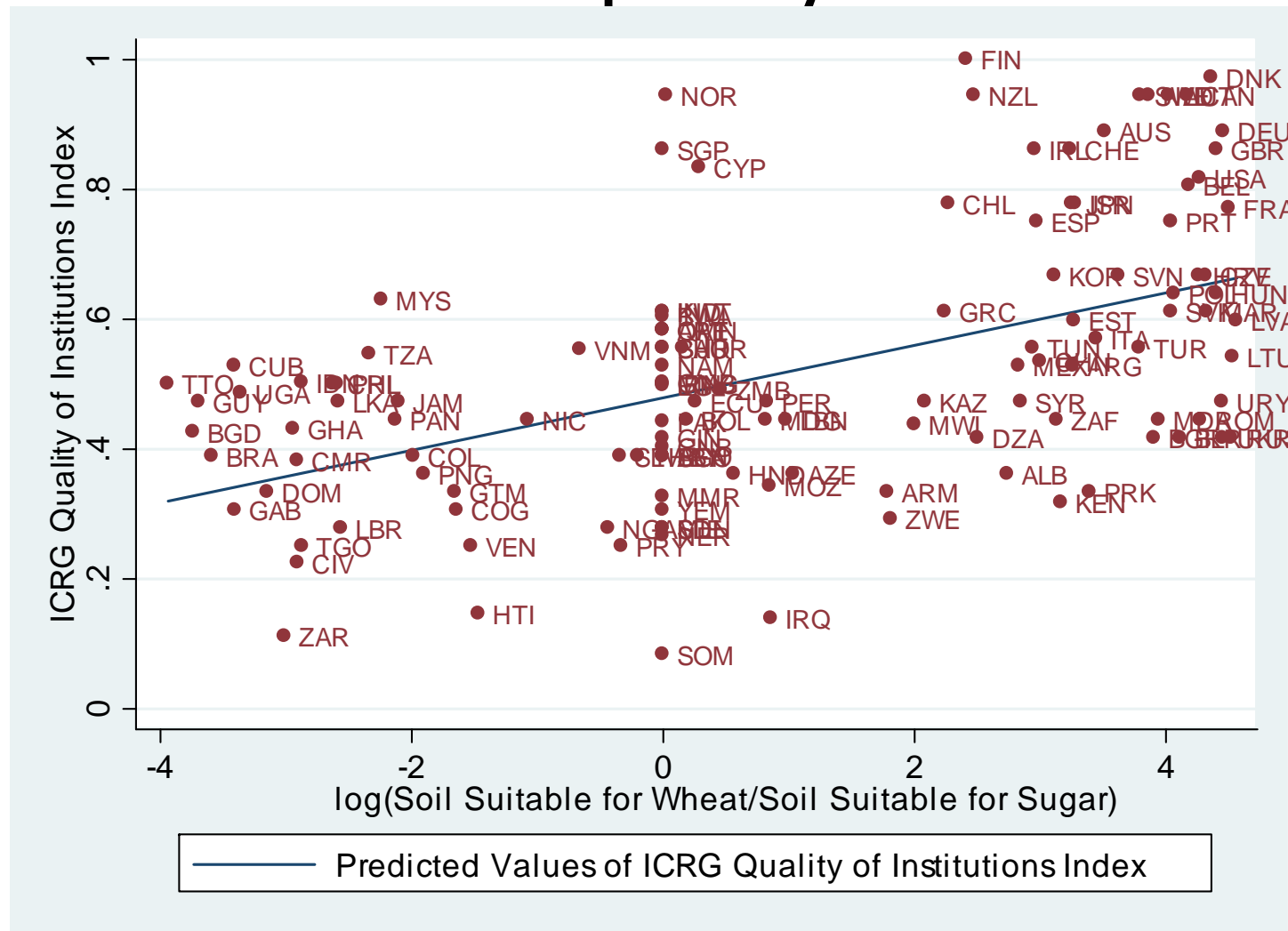
Sources: Family Farms is from Vanhanen (2003); Wheat to Soil Ratio (Menaldo 2013). See that paper for the methods and sources used.

Relationship btwn Family Farms in 1888 & Distribution Income Today



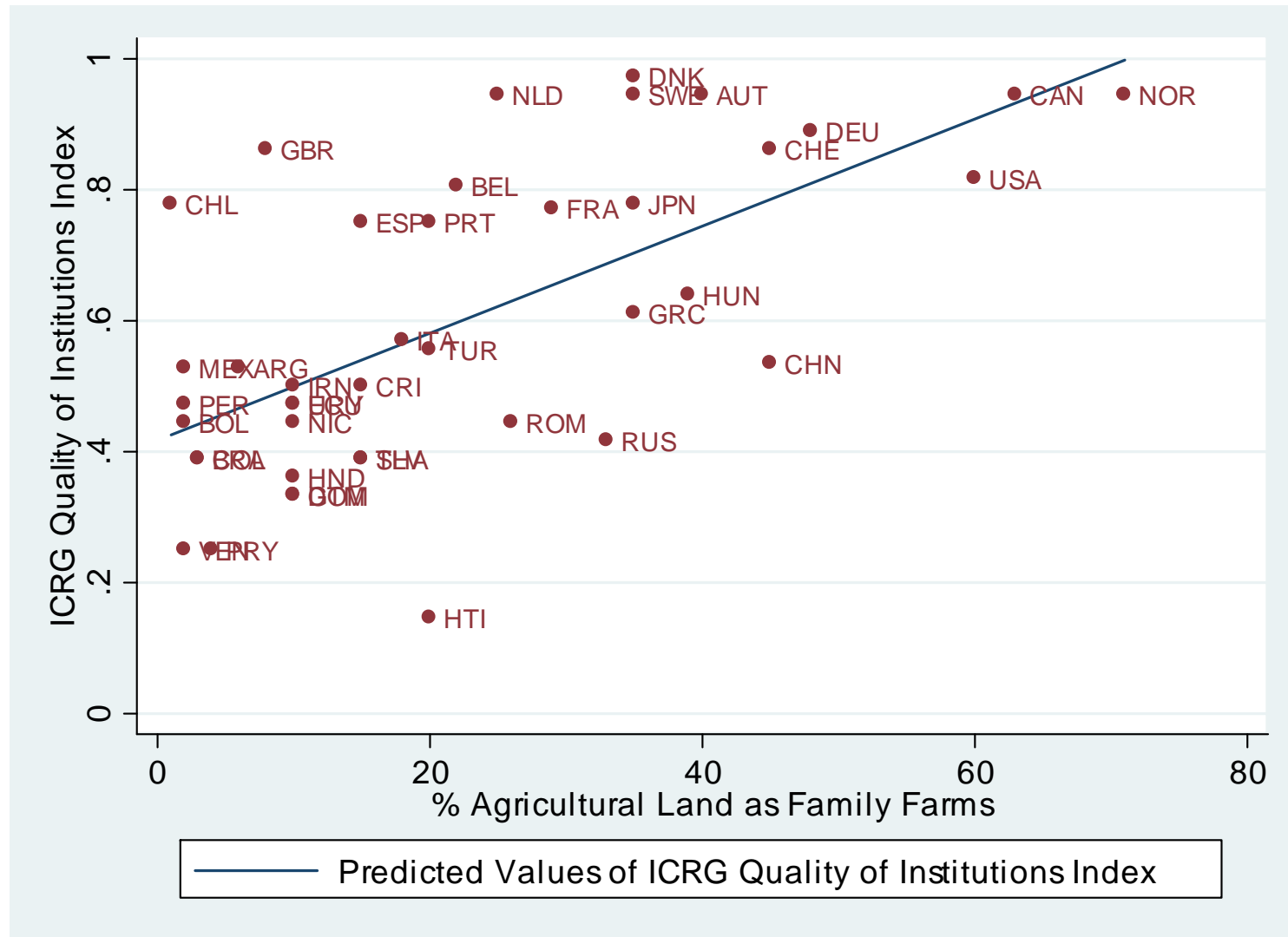
Sources: Income Gini is from the SIDD Dataset); Family Farms is from Vanhanen (2003).

Relationship btwn Land Suitable Wheat & State Capacity 2007

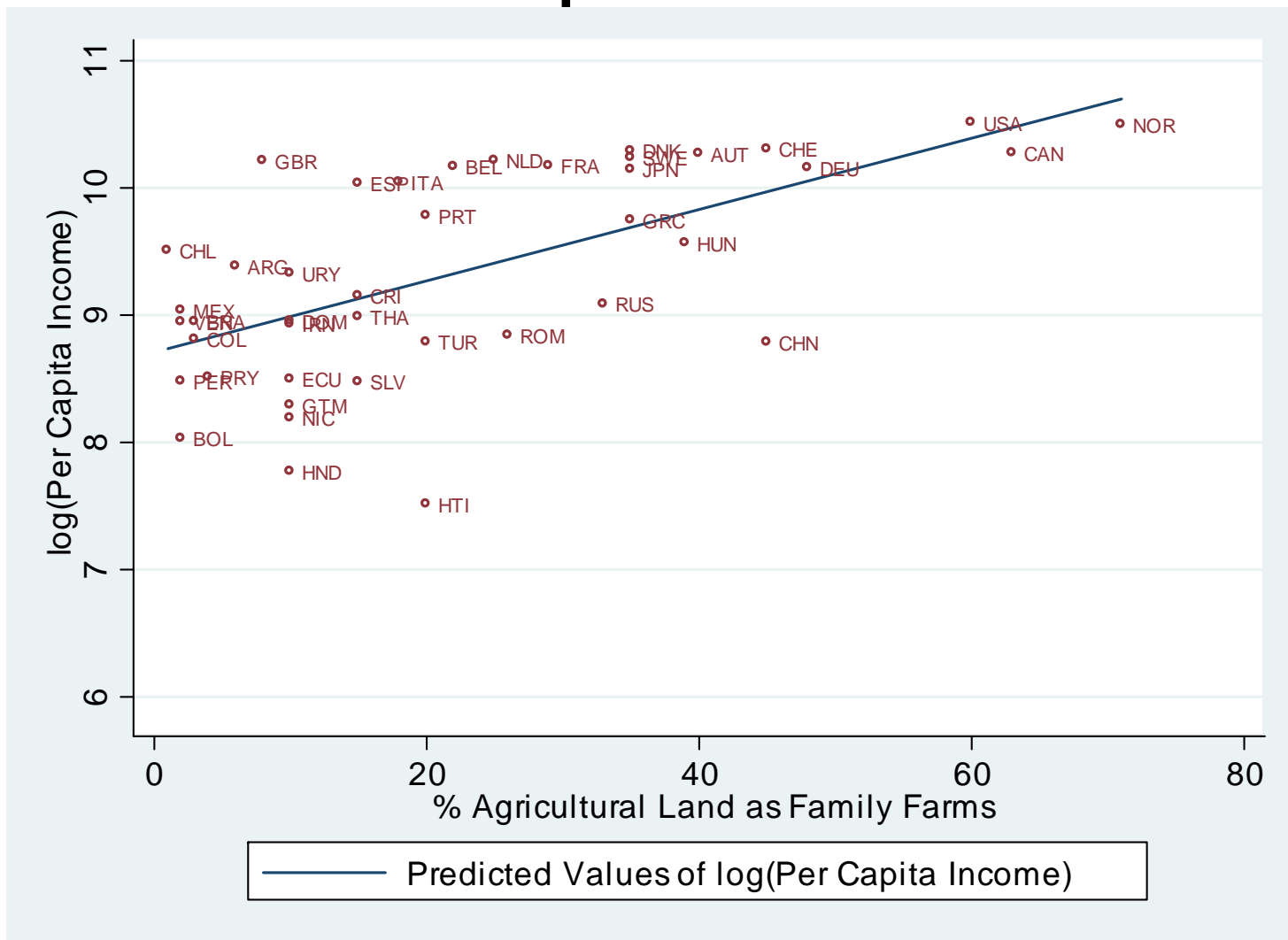


Sources: ICRG and Menaldo (2013).

Relationship btwn Family Farms 1888 & State Capacity 2007



Relationship btwn Family Farms in 1888 and Per Capita Income in 2005



Source for Per Capita Income: Haber & Menaldo (2011).

Postcolonial institutions & policies

North America

North America

- Extended the suffrage widely. Taxed and spent.
- Strengthened federalism & autonomy of local governments.
- Embraced market based development, promoted middle class & built safety net.

North America: Taxes & Education

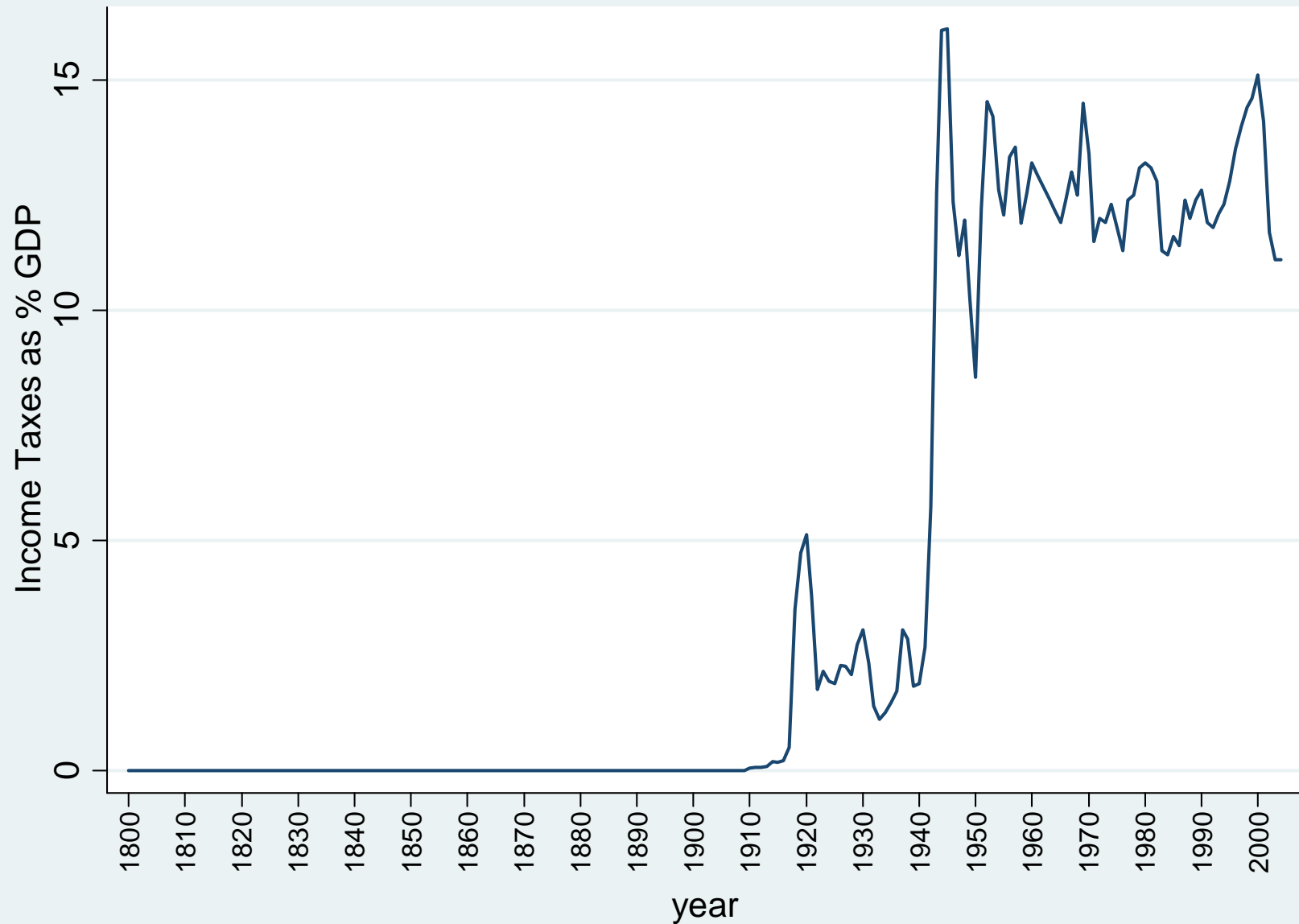
1) Progressive taxation at state and local level

Property and wealth taxes; income taxes.

2) Provision of public education

Tied to local property taxes; increasingly expanded and improved.; eventually included state universities

United States' FEDERAL income taxation



Source: NBER; OECD Fiscal Statistics

North America

1. Open immigration and generous land grants to small farmers with secure titles
2. Investment in Public Works
3. Low barriers to market entry & incentives for innovation: e.g., patent laws
4. Liberal bank charter policy with healthy competition between local level banks.

Costs to Transport One Ton in the United States (Cents per Mile)

	1815	Mode of Transportation	1860
Land	30 ¢	Road	15¢ or more
		Railroad	2¢ or more
Water	1/3¢ or more 6¢	River <ul style="list-style-type: none"> •River Raft downstream •Boat upstream •Steam boat 	1/3¢ or more
		Canal	1¢ or more
		Great Lakes	1/10¢
	1¢ or less	Ocean	1/2¢ or less

Source: George Rogers Taylor, The Transportation Revolution (New York: Holt, Rinehart, 1962) Appendix A, Table 2

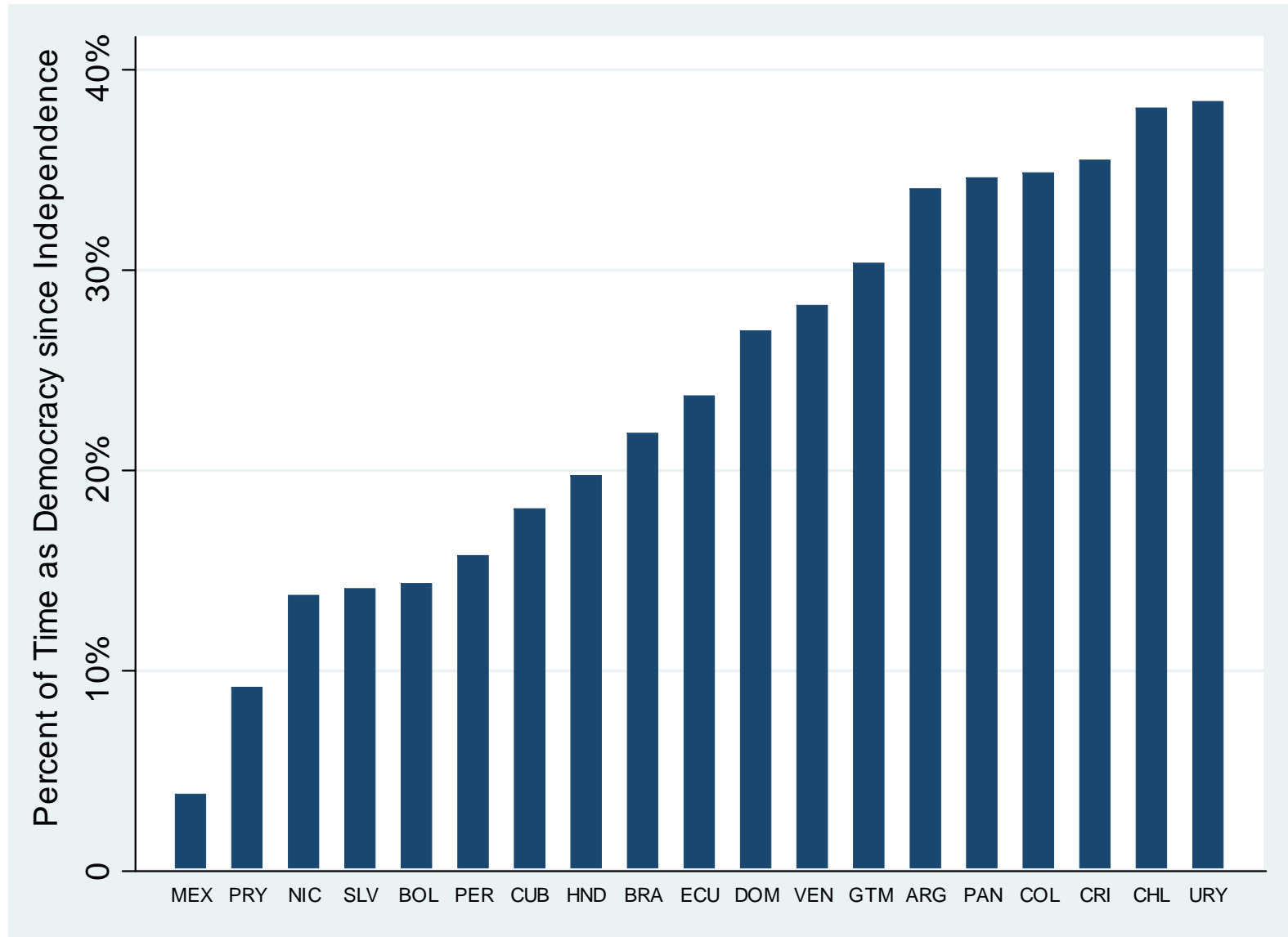
Postcolonial institutions & policies

Latin America

Latin America

- LATAM experienced authoritarianism, inequality & political instability
- LATAM became centralized
- LATAM countries embarked on crony capitalism to benefit politicians, bankers, and a small cadre of industrialists and unions.

Limited Experience with Democracy



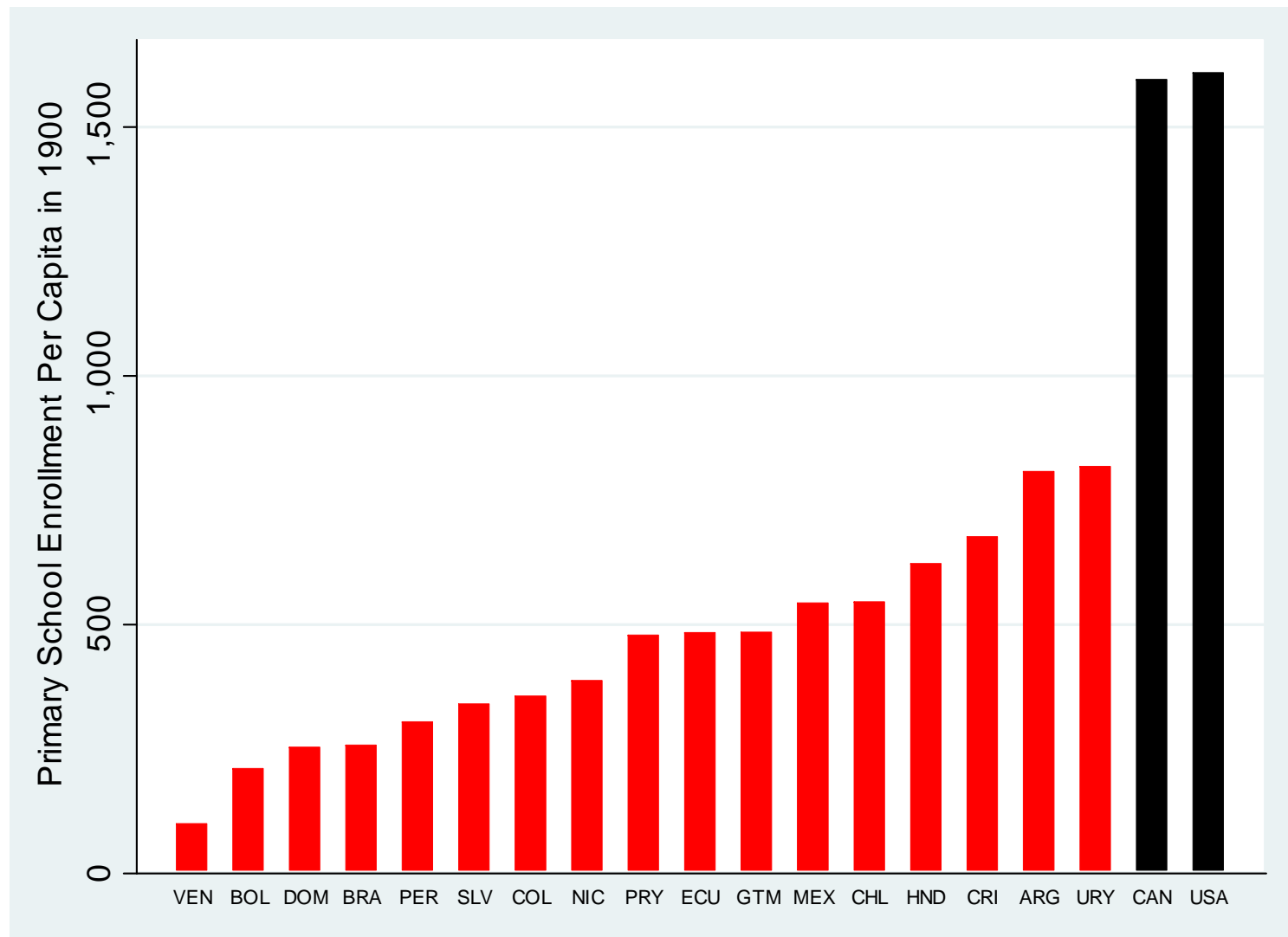
Note: Democracy coded as electoral democracy. Source: Cheibub, Gandhi & Vreeland (2009); Boix & Rosato (2001)

Latin America:

Regressive taxation and no taxes collected at state and local level: excise taxes on consumption goods & fiscal monopolies.

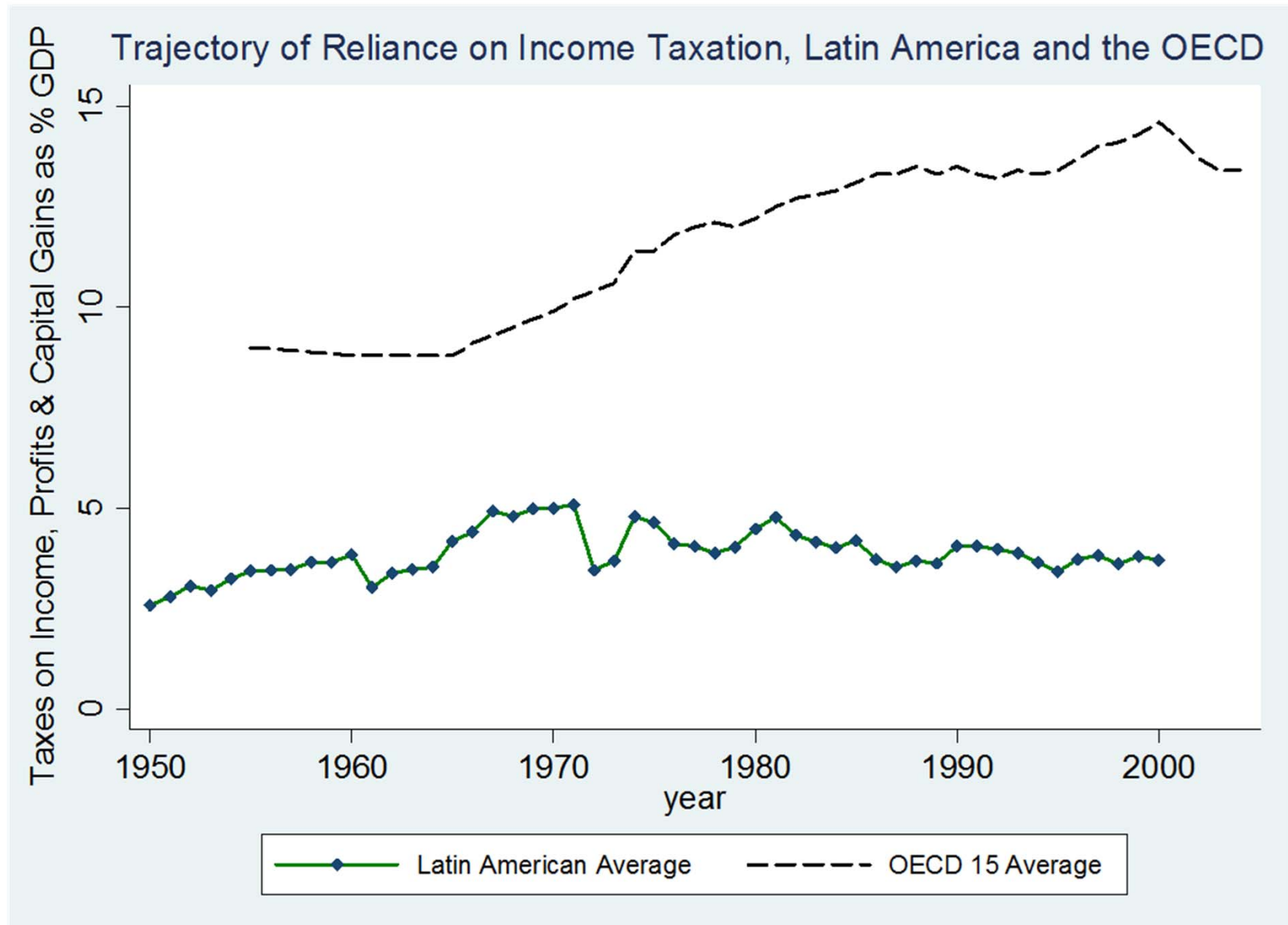
The wealthy provided private education to their own children and higher education was targeted to a narrow elite.

By 1900, LATAM had fallen way behind the education race



Source: Banks' Cross-National Time-Series Data Archive

Latin America Failed to Adopt Progressive Taxation or Provide Safety Net



Sources: Income Taxation data for Latin American countries from native treasury sources (Menaldo 2008), OXLAD Dataset (2008) & Government Finance Statistics Yearbook (various years). GDP data is from OXLAD 2008). Income Taxation as share of GDP data for the EU 15 is from OECD Factbook (2007).

Latin America

1. Constrained immigration and land grants only to very large landholders
2. Limited investment in public works
3. High market barriers to entry & low incentives for innovation
4. Restricted bank charter policy with credit allocated on political grounds.

LATAM transportation costs over 30 times greater than within USA!

Circa 1842, costs of moving a ton of goods from Latin American countries' major ports to their capitals (pounds sterling):

Lima, Peru: 1

Santiago, Chile: 2.4

New Granada: 45

Mexico City: 13.8

Quito, Ecuador: 15

Sucre, Bolivia: 19.3

Caracas, Venezuela: 4.3

Source: Brading (1969: 243-4).

Dictator Porfirio Diaz, 1876-1911



Percent of non-government loans made to banks' own boards of directors:

Banamex 1886 to 1901	100%
Mercantil de Veracruz 1898-1906	86%
Banco Coahuila, 1908	72%
Banco Durango, 1908	51%
Mercantil de Monterrey, 1908	31%
Banco Nuevo León, 1908	29%

Source: Haber (2012)

Explanation for LATAM Exceptionalism

1. Factor Endowments: wheat vs. sugar
2. Colonial Strategies: settlers vs. mercenaries
3. Political-economic institutions: democrats & federalists vs. oligarchs & centralists
4. Distribution of Wealth/Income: equality vs. inequality
5. Policies reinforced distribution of political-economic power: inclusive/efficiency vs. exclusive/distortive

Cause for Hope? Democracy

Argentina	<i>1983</i>	Honduras	<i>1982</i>
Bolivia	<i>1982</i>	Mexico	<i>2000</i>
Brazil	<i>1985</i>	Nicaragua	<i>1984</i>
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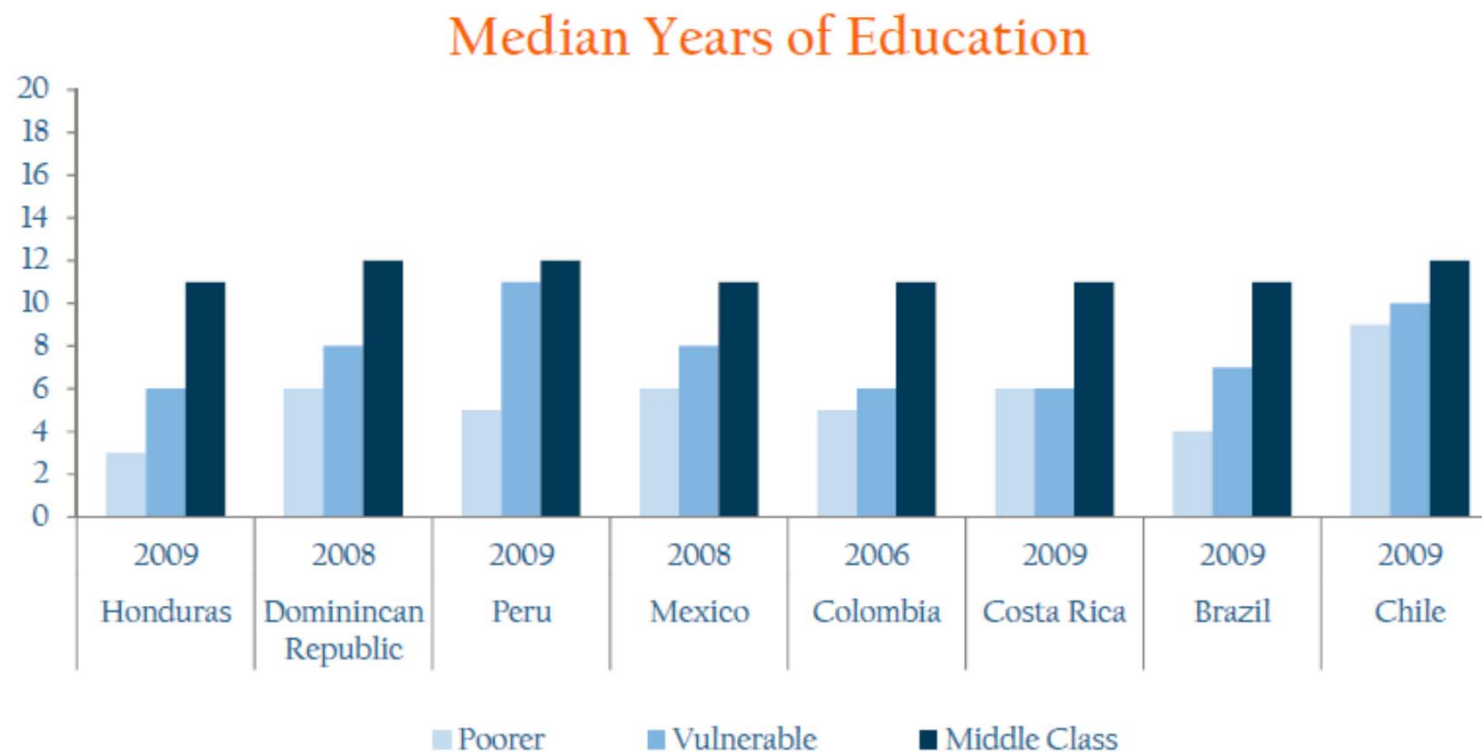
Reforms

- Rule of Law
- Decentralization
- Prudential banking regulation
- Clamp down on tax evasion
- Cut down on wasteful government spending and target spending towards poor & education

Accomplishments

- Political & civil liberties
- More secure property rights & access to credit
- Prudent fiscal & monetary policy
- Much lower debt & inflation
- Higher levels of trade & FDI
- Less sensitive to global business cycle
- Better education for more people

Increasingly decoupled from USA business cycle: skilled labor force



Taken from World Bank LAC Regional Flagship (2012). Original report written by Francisco H. G. Ferreira, Luis Felipe López-Calva, María Ana Lugo, Julián Messina, Jamele Rigolini, and Renos Vakis.

Sao Paulo: Financial Capital of South America

