Latin American Liberalism

A Mirage?

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It is said that Latin America's misfortune is instability. I believe the opposite. "Next to instability," Germán Arciniegas wrote in 1958, "there at times occurs something worse: stability" (all translations from Spanish-language material are mine). A word with a double meaning, *stability* signifies continuity yet also denotes a static or immutable quality. In the two centuries of Latin America's existence as independent republics, a permanent institutional and political order has followed a path of continuity under the constant swings of the present and the mirages of turbulent change. At the same time, we Latin Americans have not known how to be unstable where we should be. For this reason, Latin America's standard of living is one-tenth that of the United States and Canada; one-half of our population is poor, and one-quarter lives in misery (Sol M. Linowitz Forum 1997). A decade after the poorly named "liberal" reforms south of the Rio Grande, dismay is spreading from one end of Latin America to another. The developed countries are stable in essential matters and unstable in the rest—perfectly inverse to our own realities. In the United States at the beginning of the twentieth century, railroad stocks, the symbol of heavy industry, were the only stocks that a conservative investor took into account in the so-called blue chips. At the close of the century, with a recorded increase of 26,130 percent in the Dow Jones index, the stars of the American stock market were companies with no profits, examples being such dissimilar endeavors as Amazon and the Internet Capital Group (Norris 2000). Can there be any greater instability? Yet, thanks to fundamental stability, this transition, a revolution that has changed the symbols of the modern economy, has taken place, transferring

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the locus of universal progress from industrial goods to the world of the mind and the imagination. In Latin America, however, our sense of what must be changeable and what must be constant in a society has determined that the only progress recorded during the past century was that forced by the progress of the developed countries. Whereas some countries of the world rode on the back of the universal technological Pegasus, we clutched its hooves and were dragged along. Ours was a passive progress.

Auth is the word I would use to describe the basic characteristic of our institutional organization and, by extension, of our societies. Caudillismo, the overwhelming influence of the strongman in government that emerged from our battles for independence, is still the mark of our political life, even in democracy. Together with the strong positivist influence inherited from the nineteenth century, caudillismo has placed the will over legislation and legislation over law to the point that we have been governed by a teleocracy (a government of objectives) instead of by a nomocracy (a government of laws)—to apply the formula used by Bertrand de Jouvenel. Heliocentric like the Inca society, which revolved around a Sun god incarnated by the emperor, our societies have circled the orbit of political and military power. For us, order has not been that "balance generated from inside" a society, but rather the "pressure exerted from outside it," according to Ortega y Gasset's conception ([1927] 1974). Therefore, the distinguishing Latin American figures at the end of the twentieth century were authoritarian caudillos—from Fidel Castro to Augusto Pinochet and from Alberto Fujimori to Hugo Chávez—a strange cocktail of populism, nationalism, theatricality, and antiliberalism arising in the homeland of Francisco Miranda and Andrés Bello (also the homeland, to be sure, of the military caudillos Simón Bolivar and Antonio José de Sucre).

In our countries' collectivism—or disdain for the individual—has been another constant, the offspring of an ancient tradition. The Greeks gave personal, individual characteristics to abstractions of the mind. At some point, human intelligence began to do the opposite: to give an abstract, later collective, meaning to the individual and to the human. Perhaps Roman law, a great achievement in many ways, later contributed through legal abstractions to the birth of collectivist concepts such as *race, nation,* and *people*. In any case, the collectivist rationalism of the eighteenth and nineteenth centuries took deeper root in us than did ideas of freedom. Since then, collectivism has been a political seal, a product and extension of our authoritarianism.

Is it strange, then, that in this context during the 1990s the rule of law and the market economy were magically separated? Not at all. The magic consisted of making it appear that they are different. When it was no longer possible to deny the failure of collectivism, we Latin Americans in the 1990s embarked on a supposedly great reform in the name of a market economy, viewing it separately from a government of laws, which is in truth the other name for a free economy. The result has been not just a partial and frustrated reform, but an ideological confusion whose denouncement and rectification are perhaps the greatest of all the tasks engaging Latin American liberals today. Many people had a notion of what a market economy is and how it works, but few understood the transition from a closed to an open society. Consequently, we

have had many surprises during this transition. It is one thing to design a free society from scratch, another to journey toward it from a closed society, in the here and now. This journey is what has failed, not the free society (which we still do not have).

Nothing provides greater evidence of our disdain for the rule of law than the continuous changes to our constitutions or, worse, the perpetuation of ourselves in power or the attempt to create the world from nothing with each new government, but without truly altering anything essential, so that our constitutions today are—as they were in the nineteenth century, after independence—a dead letter at best, mere legal cover-ups for the murder of the individual at worst. "I have been told that you are good at drawing up constitutions," Napoleon said to Father Siéyes. "For the new order I need you to write a short, obscure constitution for me" (qtd. in Fernández 1999). Likewise, our leaders draw up custom-made constitutions. Even worse, they make them not short and obscure but interminable and detailed, like a military plan.

The Weight of Our History

Throughout the 1990s, a more critical view of our political, economic, and cultural tradition advanced, although its practical expression left much to be desired. This is no small matter because the politically authoritarian and economically mercantilist tradition has long standing. Our theocratic pre-Columbian states, despite their differences (the city-states of the Mayan civilization were more scientific, and the Aztec and Inca Empires were better organized socially) were centralist and vertical, collectivist and despotic. Superimposed on this sociopolitical structure were the Spanish colonies, which were (as was the Portuguese colony in Brazil) quite different from the ones established by the Anglo-Saxon settlers in the North American colonies. The peninsular vision that arrived on our coasts was well summarized by Claudio Véliz in defining baroque art, the symbol of Counter-Reformation Spain: "The Baroque is a reminder of imperial greatness, an obstacle to dissolution, a technique for the preservation of unity, an alibi for the central control of diversity, a justification for the pursuit of glory, a noble excuse for the recurrence of defeat. . . . An assertion of stability, a refusal to give way, a glorification of obstinacy, an affirmation of belief, an indictment of change as an illusion. The Baroque is the mode of the hedgehog" (1994). In the North, in contrast, the "Ruskin gothic" vision prevailed, a world of asymmetry, eccentricity, and diversity, common law instead of civil codes, romanticism rather than canonical classicism (Véliz 1994).

Through a monopoly of commodity exchanges, the Spanish Empire controlled the trafficking of goods, capital, and human beings between the mother country and the colonies through the ports of Porto Bello, Panama, and Veracruz, Mexico (Pendle 1976). The Crown also controlled religion through the Patronato de Indias (Council of Indias), and the Roman Catholic Church introduced the Inquisition (in cases such as the Jesuit settlements in Paraguay, it established quasi-totalitarian systems). Even language was part of the political power, as demonstrated by Antonio de

Nebrija, who upon completing the first grammar of the Castilian language, offered it to the Crown, stating "language is the companion to the empire" (Véliz 1994). The result was smuggling, which in the seventeenth century represented two-thirds of commerce, along with the buying and selling of public offices and the disregard for law and authority. "I obey, but I do not comply," said officials of the colony. The Bourbon reforms of the eighteenth century, which promoted local administration, perhaps helped to accelerate the independence movements carried out by the Creoles, who distrusted the Peninsular authorities, but although some mestizos, such as the Mexican priests Morelos and Hildalgo, were among the rebels, independence was not a movement primarily from the bottom up, but rather a rebellion of one privileged caste against another. One report illustrates the enormous difference between what occurred in 1776 in England's North American colonies and what happened in the Spanish colonies of Latin America in 1820: in the revolutionary North, there were three thousand newspapers; in revolutionary Mexico, there were only three (Harrison 1997).

The colonial experience seems especially futile if we consider the fascinating intellectual phenomenon that had previously taken place in imperial Spain: a group of Scholastics writing about economics had anticipated the Austrian school by almost three centuries. The influence of Christian humanism and the Thomist idea of natural law are also apparent in the thinking of these writers, several of them belonging to the School of Salamanca, to which Jesús Huerta de Soto (1999) has recently directed appreciative attention. Diego de Covarrubias y Leyva formulated the subjectivist theory of value; Luis Saravia de la Calle demolished the medieval superstition of a "just price"; Jerónio Castillo de Bovadilla praised free competition; Francisco de Vitoria challenged slavery in the name of natural law; and Juan de Mariana defended "tyrannicide" in the name of justice (Huerta de Soto 1999). These scholastics also anticipated the Chicago school in subjects such as inflation.

Despite its great achievements, this tremendously rich tradition of thought from our Mengers and Böhm-Bawerks *avant la lettre* continued to be disregarded. During the nineteenth century, great rational constructions and Comtian positivism bewitched our thinkers' minds and infected our leaders, turning their thinking about the state into a sort of "geometry" (Ortega y Gasset [1927] 1974). I am not speaking of liberal rationality as defended by Ayn Rand (1961) in opposing Kant and his rejection of all possible rationality, certainty, or exact science, but of constructivist rationality of the sort that emerged from the Age of Enlightenment, which is the antithesis of Hume's school of philosophy and which conceived of government as an entity morally responsible for the fate of its subjects through social engineering. Legal and legislative positivism helped to turn our governments into factories for producing rules and laws intended to do good, and our governments steadily reduced the citizens' private room to maneuver. Intellectuals played a preeminent roll in this development.

During the nineteenth century, there was no shortage of spokesmen—from Francisco Bilbao in Chile to Faustino Sarmiento and Juan Bautista Alberdi in

Argentina—to attack the colonial tradition of the Counter-Reformation, but except in Argentina, thanks to Alberdi's masterpiece *Bases y puntos de partida para la constitución política de la República Argentina* (Bases and Points of Departure for the Political Constitution of the Argentine Republic, [1852] 1996), this thought did not result in practical action. For us, the nineteenth century turned out to be what Francisco Miranda famously called "chaos, nothing but chaos." Our liberal caudillos, the most famous of which was perhaps Benito Juárez in Mexico, fought ecclesiastical privileges and did much by secularizing our societies, but at the same time they strengthened military authority and oligarchic privileges.

Around the turn of the twentieth century, when the United States was emerging as a great power, Latin American intellectuals assumed ontological distrust of the North in the name of supposedly "spiritual" values as against "material" ones. Paul Groussac and especially José Enrique Rodó ([1900] 1999) occupied themselves in carrying out the task of promoting these spiritual values. In Uruguay, the first Latin American welfare state was established, thanks to the tenacity of José Pedro Varela, the arch defender of "free" education, and later to the action of José Batlle y Ordoñez's government. Following the Mexican Revolution, nationalism, anti-imperialism, socialism, and agrarianism captivated political thought. Two Peruvians, José Carlos Mariátegui on the communist side and Victor Raúl Haya de la Torre on the nationalistic and socialist side persistently exerted influence. Joseph A. Schumpeter (1942) famously predicted that the success of capitalism would generate an intellectual class opposing it; he might as well have predicted that such opposition would spread to countries in which capitalism had not yet taken root. Not until the 1970s did an intellectual—Venezuelan Carlos Rangel—emerge ready to fight a solitary battle against that ideological body united under the curious and contradictory banner of "the left." Our political tradition, joined with ideological confusion and our institutional inheritance, amounted to a mixture of corporatism, mercantilism, socialism, and populism that exalted oligarchies and privileges while it isolated large alienated masses.

The public ended up attributing its own condition to capitalism despite the absence of that system in Latin America and putting its hope in the state, which had replaced the Catholic Church of the nineteenth century and the preceding colonial centuries. Our political action was deeply influence by the developmentalist ideas of Raúl Prebisch, who favored import substitution and the determined action of the state, and later by the theory of dependency advanced by Fernando Henrique Cardoso, who attributed our marginalization to our location on the world's trading periphery and to local oligarchies who served as imperialism's accomplices. First, the Vargases, the Perons, the Lázaro Cardinals, and the Paz Estenssoros, then later the Velascos and the Castros emerged in all their variants as the product of that tradition of statism. In the 1960s and 1970s, statism reached new heights, bringing a massive wave of nationalizations prompted by an anti-imperialism content to ignore simple statistics showing that—even today in the era of globalization—U.S. investments in Latin America represent only 6 percent of worldwide U.S. investments (Harrison

1997). So strong was the superstition that even the black-economy workers, when voting or voicing their opinions, chose a socialist option. In the 1980s, with the Siles Suazos, the Alan Garcias, the Raúl Alfonsins, and the Daniel Ortegas—precisely when we were making the transition from dictatorship to democracy (or, in the case of Nicaragua, from one dictatorship to another)—the economic chaos, which until then had been ticking away, finally exploded, providing a rationale for the great changes in the 1990s.

Achievements and Failures

Great changes? In some senses yes, in others no. The dynamism of certain reforms in those years cannot be denied. Many governments privatized public companies; reduced tariffs; liberalized various aspects of trade, finance, and agriculture; and adjusted the belts in fiscal and monetary matters. The average inflation rate in the region was 17.7 percent in 1996, which is not bad when compared to the 200 percent in 1991, and income per capita grew each year for almost the entire decade of the 1990s, whereas it had fallen 10 percent in the 1980s. In 1996, foreign investment totaled some $50 billion, a sign of confidence and opening markets. In 1997, of the 500 main companies, 148 were foreign, 285 local, and only 67 state owned; five years earlier, 92 had been state-owned. That only 8 of the 20 largest companies were directly related to natural resources points to a more diversified economy ("500, las mayores empresas" 1996–97). Mexico, Chile, and Argentina have lightened the burden of their governments in more than one sense. In 1982, there were 1,155 public companies in Mexico, and half of all production was by the government. By 1993, $24 billion of public assets had been sold, and the maximum income tax rate had been lowered to 35 percent, which is reasonable by international standards. In Chile, where privatization began much earlier, this process has touched "the untouchables": pensions and health care. Almost $25 billion invested in pension funds has boosted savings, expanded the capital market, and benefited the workers, who have seen their savings books record annual interest rates of as much as 14 percent. More than a third of the workers have acquired private health insurance thanks to the government's introducing the option to leave the public health system. Even in Peru, some 100 government companies have been sold, half of which during the nationalization era belonged to Velasco's military regime (Roberts and Lafollette Araujo 1997). Although all these reforms have promoted economic growth during certain periods of the 1990s, they are far from decisive.

Observers tend to judge the quality of the reforms in terms of macroeconomic concepts and statistics. If rates of growth and of inflation, the flow of foreign investment, and the reduced number of government enterprises were the yardsticks by which to measure our progress, Latin America would already be a prosperous continent because since the 1940s its average annual rate of economic growth has been 5 percent, which is greater than the corresponding rate for Europe. Hyperinflation is a

relatively recent phenomenon in our history, as are nationalizations. Between 1900 and 1987, the real gross domestic product (GDP) of Argentina, Brazil, Mexico, Columbia, Chile, and Peru grew an average annual rate of 3.8 percent, more than the corresponding rates for the United States (3.2 percent), for the developed democracies in general (2.9 percent), and for nine Asian economies (3.2 percent). In that period, Brazil had the second highest rate of growth in the world. Factoring in the increase of population, we find that in that period Latin America's average annual rate of growth of GDP per capita was 1.7 percent, almost as great as the corresponding rate for the United States, 1.8 percent (Harrison 1997). It is obvious, however, from Latin America's lagging position and the enormous disparities within its population—in other words, from the quality and the nature of past growth—that we will continue to be underdeveloped. Reliance on macroeconomic indicators gives rise to fallacious conclusions about the development process.

In the past, we Latin Americans were important exporters, but our export activities failed to lay the foundations of genuine development. In the 1950s, 83 percent of the oil bought by the United States came from Venezuela; 95 percent of the coffee, 53 percent of the tin, and 87 percent of the sugar imported by the United States came from Latin America. The world depended on wheat from Argentina, copper from Chile, oil from Venezuela, and tropical products from Brazil (Arciniegas 1958). If exports guaranteed development, Brazil would be a superpower. That country went from exporting goods valued at $136 million in 1965 to exporting goods valued at $136 billion in 1992, of which almost 60 percent consisted of manufactured goods, not raw materials—a direct refutation of the dependency thesis.

Even judging Latin America's reforms of the 1990s from a macroeconomic viewpoint, however, we are left with poor results. In that decade, our economies grew an average annual rate of 3 percent a year, three times faster than in the 1980s but only half as fast as they grew in the 1970s and much slower than East Asia's 8 percent. Only Chile and El Salvador surpassed that average. In most countries, wages are below the level of the 1980s, and since 1991 unemployment has grown in Mexico, Argentina, and Peru, and the number of people who live on less than a dollar day has increased from 23 percent to 25 percent, whereas in East Asia unemployment has fallen from 17 percent to 13 percent (Sol Linowitz Forum 1997). Peru, whose reforms were praised, has not grown since 1998, and one of every four jobs in the capital has vanished without the market's being able to replace it (Arroyo 2000). Foreign investment in Latin America has reached 20 percent of GDP, which is almost half the ratio for East Asia, but direct investments have been few because investors have preferred highly liquid instruments. Nowadays, receiving investment from abroad is not unusual; even Africa—Nigeria, Ghana, Angola, and of course South Africa—is benefiting from large foreign investments. Yet Latin American exports, even Chile's, still heavily depend on raw materials. It is true that our finances are improving in some cases, but we have acquired more debt than advisable for a healthy economy. The debt of the seven main economies exceeds $600 billion, which is equivalent to almost two

and a half times the average of all their exports, even though those exports rose almost 80 percent between 1993 and 1996 (Sol M. Linowitz Forum 1997). Thus, even in macroeconomic terms, our performance has been poor.

Flawed Reforms

The Latin American reforms have suffered from a philosophically fundamental flaw, possibly because they have not been governed by an overall view but by immediate monetary or fiscal needs—in other words, by expediency in the circumstances. This error relates to the confusion between a private economy and a free economy or, better yet, to the divorce between the economy and a government of laws. We have gone from statist economies to private economies, but the state has not ceased to be the determining factor in economic outcomes or in the material fate of the people, often to the detriment of individual rights. We can learn many lessons from this experience. Most important, the *transition* to an open society is quite different from the *creation* of an open society. We liberals who demanded reforms in the 1980s did not anticipate this reality in its full dimensions. When we championed liberalism, we frequently started from a mistaken viewpoint, advocating a free society as if it could be created from emptiness, on virgin territory, like an architectural design. On discovering the quicksand beneath the transition—that is, on discovering that the space is neither empty nor virgin and that within it the existing elements undermine, exhaust, or devour the new—we realized that almost as important as the free society we sought to reach was the route by which we reached it. The transition—the process wherein government yields to the private sector by forsaking mercantilism, privileges, and state enterprises—might easily give way to a subtle, more hypocritical, and almost as injurious state presence dictated by regulationism and the constraints that political power can still attach to private life, despite the state's apparent withdrawal or shrinkage.

Roger Douglas, one of the heroes of New Zealand's transition, has made two points that we Latin American liberals should have considered. First, for him, "the essence of structural reform is the abolishment of privileges," something that is very difficult to achieve because the cost of privileges, being widely dispersed and sometimes invisible to a society, is great in total but small per person and per item (1997). Therefore, the pressure from interest groups seeking to avoid the abolition of their privileges always exceeds the pressure from society as a whole, the overall beneficiary of these reforms. George Reisman (1996) has made a similar point by noting that because a subsidy is much greater per beneficiary than the cost of that subsidy for each taxpayer, lobbyists push hard, whereas the taxpayers do not. Douglas's second observation on transition pertains to the simultaneity of the various reforms, for him an essential condition for success. The economy consists of a network of connections; there is no point in eliminating export subsidies if transport tariffs and regulations are not eliminated, and shipping ports and services are not privatized. What good is it to have fiscal gains as a result of privatization if, instead of reducing taxes or the debt, the

government dedicates these gains to exorbitant social expenditures? This very outcome occurred in Argentina during Carlos Menem's administration. By increasing federal and provincial expenses 100 percent, a $6 billion deficit was generated despite the substantial revenue from privatizations. What good is it to relieve the government of its employees if anticapitalist labor legislation prevents the market from reabsorbing those workers, again as happened in Argentina, where Menem's administration bequeathed his successor 15 percent unemployment after having received an unemployment rate of 6 percent from the hands of the unsuccessful Raul Alfonsin? Moreover, if the reforms stop, then the foreign investments, falsely taken to be eternal, will also stop, as recently seen in Peru.

Failing to abolish privileges and failing to effect simultaneous reforms are the two serious flaws in Latin America's reforms. Because of them, we have journeyed toward economies that are more private than before but in many cases not any freer. Where the barriers to the entry of new participants have been insurmountable, the benefits have not been extended to consumers but rather to the government, and numerous visible and invisible regulations have interfered with what Israel Kirzner calls the process of the "discovery of wealth." As Kirzner aptly notes, "the provisions of regulators do not reflect the incentives in the entrepreneurial search for profits" (1995).

The divorce between the economy and the rule of law stems from not understanding that freedom is a political concept before being an economic one and ethical even before political. To suppose that economic reform can be carried out without political reform is to divide the indivisible, to delay indefinitely the emergence of fully free societies. We forget that capitalism in Flanders, Venice, and England was created by means of political processes, by the efforts of merchants to open up their towns for commerce by gaining political concessions from feudal lords and monarchs. Once created, those freer political frameworks generated natural economic consequences. This linkage does not mean that the creation of wealth is a political process. On the contrary, as Franz Oppenheimer (1975) observed, there are only two ways to amass wealth, the economic and the political; the first is the free and rational way, by means of production, and the second is the authoritarian way, by means of violence and expropriation. Still, the economy arises from free human action in a predetermined framework and under specific institutional rules. The attempt to liberalize parts of the economy within an authoritarian political context just as intervening and suffocating as it was previously, with no system of administering impartial justice (a crucial institution for every capitalist process), has resulted in the failure of many of the reforms. Our politicians do not understand economics (Miranda was astonished at the end of the eighteenth century to find in the Massachusetts Assembly so many merchants and blacksmiths), and our businessmen do not understand the advantages of doing less politics and more business—although it must be said, to be fair, that their inability is owing in part to the system in which they have had to operate.

Labyrinths of Privilege

One might go on indefinitely enumerating the privileges that have been enthroned or preserved in Latin America's recent reforms. These privileges affect all areas of transaction, from state contracts (in Peru, one of the ministers of the economy has also been one of the government's main contractors) to privatization, commerce, state property, the currency, and pensions.

In privatizing state enterprises, we have with few exceptions granted state-protected monopolies, as in the case of the telephone systems in Mexico, Argentina, and Peru. The quality of service sometimes improved and sometimes did not. The result? The users saw their rates soar and watched with distrust the rapid recovery of investments by the buyers. Cases such as those of Telmex in Mexico or Telefónica in Peru have aroused resentment toward the very idea of privatization and have planted in the public's mind the idea that privatization is not a way to benefit the consumer or to encourage new producers to participate in a market, but the way to grant privileges to a fortunate few and to turn the customers into hostages of a company. The privatization of a Mexican bank through oligopoly—with the government guaranteeing the deposits, limiting foreign participation, and providing protection for last-resort moneylenders—encouraged major corruption. A $68 billion bank rescue of Fobaproa aimed to save some dozen banks, and in Mexico some bankers went so far as to flee from justice. In Peru, as elsewhere, the telephone system was privatized not to benefit the consumer by means of increased competition but rather to allow the state to reap maximum profits—it received $1.8 billion. Instead of distributing property ownership widely, as happened in England and in certain central European countries, privatization in Latin America served to close the tight circle of wealth.

In the arena of trade, the liberalization of recent years has been fraudulent in areas where privileges reign. We saw, for example, how in Guatemala the chicken producers succeeded in getting the government to impose tariffs on the Tyson Company of Arkansas, while at the same time setting import quotas to satisfy peak demand. In Mexico, a series of "compensatory quotas" were set in 1992 by which a tariff of 1,175 percent was levied on goods such as Chinese footwear, and in 1997 apple growers obtained barriers against American Starking from the government. In Brazil, a curious strategy placed extremely high tariffs on computers but extremely low tariffs on dog food. In Columbia, Federcafé, the union of coffee growers and sellers, has had a seat in the executive office, passing regulations that affect its own business.

Similarly discriminating interventionism has affected taxation. Duty-free zones and arbitrary exonerations, such as the maquiladoras or assembly plants, have interfered with the allocation of resources in Mexico, whereas in Argentina the value-added tax was applied selectively so that certain business activities—such as cable, medical insurance, and advertising—escaped the 21 percent tax although it was levied on others. At the end of Menem's term, an interest tax of 15 percent was created to

be paid by debt issuers only because the government judged it unfair for them to deduct this interest from their tax statements.

In other areas, even more direct state interference has continued, inasmuch as public companies have continued to operate. In Mexico, Venezuela, and Brazil (in this last country, some 150 companies remained in the state's hands at the end of the 1990s), oil continues to be controlled by the state; and in the "liberal miracle" of Chile, Codelco continues to belong to the government, and the military enjoys a rent from this enterprise protected by the Constitution. What good has it been to Venezuela to generate $250 billion from its oil in the 1980s and 1990s? The absence of a free society and of a market economy has meant that enormous wealth has been wasted.

In currency matters, the examples of privilege are equally numerous. When Venezuela liberalized its exchange rate, producing the inevitable devaluation, oil sales abroad generated more income in Venezuelan currency, and the upshot was increased public spending and inflation. The government could think of nothing better to mitigate the impact of this cash flow than to subsidize private banks that could not invest their excess liquidity because there was no productive activity in which such investment made economic sense.

Even in the area of pensions, where courageous measures have been taken in almost all Latin American countries to move from a distribution system to a capitalization system, one can point to distortions caused by governments that guarantee the existence of clients by requiring them to subscribe to a fund—a privilege unavailable to true entrepreneurs in the free (risky) market.

The Necessary Political Foundations of Genuine Economic Reform

The result of this labyrinthine network of privileges on the South American continent has been a concentration of wealth, which in part explains—with the exception of Chile—why the high rates of economic growth realized in the past have not diminished poverty or advanced the countries as a whole. Sixty percent of the income flows to the top 20 percent of the recipients, and in some cases, such as Peru's, 10 percent of the population controls 70 percent of the wealth, whereas several years ago that top group controlled just 50 percent. Our states thus continue to exemplify, in Bastiat's famous phrase, that "great fiction by which everyone tries to live at everyone else's expense" (qtd. in Leoni 1995)—the rich to gain privileges, the poor to attain what private life has yet to provide them.

The poor deserve praise from liberals for having created the black economy, the popular capitalism that is now usually applauded. This is no minor accomplishment. In countries such as Peru, it represents 38 percent of the GDP and 60 percent of the hours worked, although these same figures reveal the lower productivity that results precisely from an economy's operating on the fringes of the law and behind the state's

back. It is true, as Ghersi says in applying Douglass North's analysis of transaction costs to Peru's informal economy, that this lower productivity springs not from cultural factors but from the inefficiency of the legal institutions: for example, to register a tailor's workshop in Peru takes 289 days and $1,200, as well as several bribes, whereas in Tampa, Florida, the same task can be accomplished in three to four hours and by mail (Ghersi 1997). Excessive regulations and the confusion surrounding the regulations have devalued the very idea of law. As Alberto Benegas-Lynch notes, quoting Planiol, "'the inflation of laws translates into a depreciation of the law'" (1999). Each law, each regulation, is a blow to freedom as long as it exalts privileges and discrimination, as happens in Peru, for example, with the conferring of the power of public law on the assembly of university presidents, making them capable of blocking almost completely the entry of new competitors into that market. Most legal regulations, however, take place beyond the premises of the legislature, arising from the administrative bureaucracy, a body that, as indicated by the Public Choice school, is in itself an interest group competing in the mercantilist marketplace. And Latin America's transition has been especially mercantilist in character. We liberals did not anticipate the full significance of the infinite opportunities that the transition from a state economy to a private economy would present for political power and oligarchies, foreign and domestic. We did not foresee very well that after the head of the state economy had been cut off, new ones would sprout, as from the Hydra.

Douglass C. North and Robert Paul Thomas (1973) have demonstrated the impact that secure property rights, contracts, civil responsibility, and the administration of justice had in bringing about economic growth in Europe. Latin America has in many ways still not created the institutions that form the basis of a free society and therefore of a market economy. If "the true objective and design of a government" is "security," as Thomas Paine declared in 1776 (1986), our governments are still not fulfilling their basic mission. The system of administering justice, corrupt and politically servile, continues to be what it was a decade ago: entelechy without content in the best scenario, an active instrument of abuse against citizens in the worst. There have been many studies on the nature of the judicial process in developed capitalist societies. Bruno Leoni has accurately demonstrated that whereas in ancient Greece the law was based on legislation, in Rome it was based on the autonomy of legal advisors, customs, and judicial law. Later Justinian assembled the known laws into codes but incorporated precedents and abundant opinions from legal advisors. "The judicial process," wrote Leoni, "always goes back to individual claims," and "individuals create the law insofar and as soon as they put forward claims that prosper" (1995). The Romans, like the English, believed that law is "discovered" rather than promulgated and that no one in society should be so powerful as to be able to identify his own will with the law of the country. Viewed in this light, law and justice in Latin America are seen to be just the opposite of what they should be. Our justice is not the reflection of the society, but of the power. Instead of inspiring the process of justice, the law and the citizens are its victims, as the daily operation of our legislation demonstrates by ignoring real life—with the black

economy being the most flagrant although not the only example. In our justice, politicians and rich businessmen (that is, the powerful) set the standard. This condition explains why the citizens generally distrust the administration of justice, and they have extended that distrust to the whole body of public institutions, creating propitious conditions for militarism or adventurism.

The rule of law is, of course, not the same as democracy. Our democracies can allow alternation in office without protecting individual rights or ceasing to be authoritarian. The Dominican Republic and Venezuela have had more consecutive years of democracy than many other countries in the region without having real protection of economic or even political rights. Costa Rica is without doubt an admirable example of democracy (independence did not come by way of a news item); a symbol of this spirit is José Figueres, who converted the Bella Vista barracks into a museum of fine arts right after the revolution ended in 1948. But Costa Rica's inability to develop substantially during all these years has to do with the absence of truly free and solid institutions. Our leaders can still forever harm the life of the people by decisions made overnight without any consultations. In the name of supposed human rights, all rights are violated. In the name of "diffuse rights"—those that "belong to everyone, in other words to no one," as Benegas-Lynch (1999) puts it—individuals are deprived of true property rights. Rights can only be concrete, and as Murray Rothbard has maintained, only "human rights that are translated into property rights are valid" (1995) because other rights often run counter to property rights. In the 1980s, Peruvian farmers, rebelling against the collectivist agrarian reform of the previous decade, parceled out 60 percent of the land; in other words, they privatized it. Approximately four million small landholders, however, still had not received property titles in the 1990s. In 1992, Carlos Salinas's administration in Mexico amended the Constitution to allow for private property in the countryside, but a limit of 2,500 hectares was imposed on companies, and the government continued to own the land under Article 27 of the Constitution, according to which "the nation" is the proprietor of land and water. Although more property rights have recently been granted in Mexico than in the past, Article 25 of the constitutional text establishes that the state is the one who "plans, leads, directs, and manages" the economy. No one should be surprised, then, when a large percentage of the investments that arrive in the country take the form of short-term speculations. Moreover, the cacique structure, important in Latin America provinces, has still not been directly attacked in Mexico, which explains, according to economist Oscar Vera, why only 14 percent of all the money CONASUPO distributed for agriculture arrived at its destination (Roberts and Lafollette Araujo 1997). I do not believe that subsidies are a good method for developing the countryside, but this figure reveals how property is controlled by a cacique bureaucracy in the Mexican province and not by citizens with full rights. The absence of true reform in the Mexican political structure allowed the $24 billion allotted by the National Bank of Rural Credit for agricultural subsidies to be used to feed rather than to subdue the guerrilla sedition in the country's southern region.

The superficiality of the poorly named Latin American revolution confirms that political reform must provide the basis for economic reform. The political institutional framework is the environment in which the economy breathes or suffocates. Capitalism's historic roots are a controversial matter, but as a general rule the most successful capitalist countries are those in which a government of laws, often the product of political decentralization and the atomization of power, arose before substantial economic development occurred. It is equally clear that politics obstructs the development of capitalism in authoritarian countries or in those with populist environments. Witness East Asia, where the 1997 crisis can be read as a symptom of weak market economies operating in relatively closed societies. Latin America also presents good examples. The Chilean economy was never as robust and stable or generated as much confidence under Pinochet's regime as under the democracy of the 1990s. The evident corruption, abuse of power, and loss of confidence in Peru today show how a dictatorship, which by definition is the opposite of a rule of law, becomes capitalism's worst enemy. (In another example, the stock market fell five points the day President Fujimori withdrew businessman Baruch Ivcher's Peruvian citizenship in order to expropriate Ivcher's television channel.) When people can be exiled, jailed, tortured, or made to disappear by the state in a country where the law is a docile instrument of political will dedicated to perpetuating a leader, whether civilian or military, then property guarantees and private companies do not provide a body of institutions that can undergird a productive market economy. Instead docile businessmen bow before the government and enter into its corruption.

I blame certain "liberals" for having often been active or passive accomplices of regimes of this caliber, confusing public opinion and marvelously aiding the enemies of freedom. In the Mexico of reforms, President Salinas invited thirty leading businessmen to dinner to request contributions of as much as $25 million a plate for his party. Present were some of the main beneficiaries of monopolistic transfers of companies that were previously state property (A. Oppenheimer 1996). The absence of far-reaching political reforms in Mexico, as in other parts of Latin America, has meant that, despite a widening of the field of private companies and a decrease in state intervention in many areas, economic change has multiplied mercantilist practices and corruption. To some liberals, such as the admirable Murray Rothbard (1995), corruption is not bad because it is a "voluntary transaction," but I believe that this attitude is dangerously cynical. Corruption is an arbitrary reassignment of resources; it is almost always an illegal use of funds given to the state by taxpayers and generally implies discriminatory action from a position of political power that favors some and harms others. Borges used to say that the Argentines robbed the state without thinking it a crime because they believed the state was impersonal. Our societies have not yet learned that the state is not an impersonal entity. Neither state decisions nor state expenses are impersonal. In every case, there is a direct relation between these expenses and the citizens' property, whether that property take the form of their lives and freedom or their savings and wealth.

Culture versus Institutions

We liberals will never resolve all our debates. One of them pertains to culture: Does culture influence institutions or vice versa, and which of the two is the key factor in free development? The subject deserves consideration here, albeit tangentially. The first problem arises from the definition of *institutions.* Some observers contrast culture with institutions because they see a clear difference, but others, such as Douglass North, think institutions are "the rules of the game" and include legislation, cultural attitudes, and other forms of restraint on human interaction. "The path to institutional change determines the level of economic opportunity in a society," say North and Thomas (1973). However, North himself (1990) asserts that these formal restraints (regulations) and informal ones (culture) are determined by the market. Others take a completely different view. Lawrence Harrison, although acknowledging that "new policies and institutions are influenced by culture but culture is also influenced by new policies and institutions," maintains that the essential factor is cultural and that the definitive cultural changes that favor economic freedom have not taken place in Latin America (1997). Although Harrison is encouraged by the nearly thirty million Protestants in Brazil and the fifty million in all of Latin America and sees, for example, that the Basque immigration to Chile in the eighteenth century was a determining factor in the progress of that country in the last century as compared to the rest of the region (except for Argentina), his analysis focuses on a fundamental cultural deficit—attitude toward work, merit, frugality, education, ethics, justice, and so forth—that has not yet been remedied.

Rummaging through history, one finds examples of both sorts of influence. The Meiji Revolution in late-nineteenth-century Japan, which spurred the modernization and westernization of that country, was largely a decision made from above. A few decades ago, East Asian countries such as China and Korea exemplified an authoritarian Confucian culture incapable of attaining development; later the East Asian economic explosion, stimulated by the ruling classes, made those countries an example of cultural change generated by institutional decisions because they retained their cultural roots and continued to be partially closed societies. On the other side is the evolution of capitalism in Europe, where emerging merchants and other businessmen succeeded—from below—in gradually bringing the prevailing institutions to reflect their bourgeois culture.

I do not favor an exclusive formula; the process of economic development has been mixed, gradual, and sometimes so replete with shades that it is impossible to determine the proportion of each. Yet one thing is clear: culture alone, if it lacks an institutional correlative in the rule of law, is insufficient; likewise, institutions alone, in a world of anticapitalist culture, are insufficient. The black economy is a magnificent example of an emerging culture that breaks through exclusive and anticapitalist official institutions. This economic sector's development in Latin America began in the 1950s with migrations from the country to the city. After half a

century, however, our institutions have yet to reflect this phenomenon appropriately, with the consequences being those that I have already mentioned—the limitations of a black economy, which is an economy of survival more than of development. Similarly, all our formal institutions from the time of independence were dead letters because the beautiful words and desires did not have a cultural and practical counterpart. Isaiah Berlin has observed, "to each stage of social change there corresponds its own type of law, government, religion, art, myth, language, memory" (1976). This observation is manifest in Peru's black economy, which has generated a common law, spontaneous norms, various cultural manifestations such as *"chicha"* music, and even a distinctive politics—all rejected by the traditional political class. It is, therefore, a dual phenomenon, both cultural and institutional, but it still lacks a definite expression in what North (1990) would call the formal institutions. Paradoxically, the *"chicha"* culture, which in many ways embodies a choice for capitalism by the poor, also contains antiliberal atavisms, expressed in many ways, from its adherents' electoral votes to their scorn for the law even when it is "acceptable." Because of the inefficiency and the high cost of the law in this world, its inhabitants have decided to flee from the formal rules in sometimes irrational and paradoxical ways, attacking its own raison d'être—capitalism and the competitive society. Thus, authoritarianism and violence as well as cynicism and a certain degree of resentment are still visible in that culture. According to V. S. Naipaul, "the politics of a country can only be an extension of its view of human relations" (1981). Latin American society still harbors a view of human relations that is incompatible with a liberal civilization, a view apparent in its politics and in other institutions of formal life. Our error is twofold, cultural, and institutional, and therefore our adjustment must be twofold. Our formal world has not adapted to our changing social world with its increasingly pro-capitalistic attitudes, nor has our culture adopted the behaviors of a free and civilized society. The process of adjustment must necessarily have an institutional side so that a definitive adaptation also takes place in the culture.

If education is an expression and at the same time an ingredient of culture, our definitive cultural change is far from happening. In this area, with limited exceptions, nothing has been done in recent years in the interest of an open society. Indeed, education has been kidnapped by the state. This capture has nothing to do with money: public expenditure on education in Latin America represents 4.5 percent of the average GDP, higher than Europe's 3.9 percent. It has to do with the appropriateness and philosophy of education. It is believed that education is too valuable to be treated as a commodity and to be subject to market competition, an attitude that demonstrates the poor understanding of what individual freedom is and thereby confuses the matter. By condemning young people to apartheid—a rich minority can pay for private schools, while the rest vegetate in mediocre state education—the government, besides impoverishing education, is strengthening privileges and discrimination in the name of utopian equality and in the name of a false

"free" status, which forces those of lesser resources to redistribute income to those above. Timid reforms have been made in the Brazilian state of Minas Gerais, where meetings made up of parents to administer budgets have been allowed; in Columbia, where education vouchers have been granted as an experiment in one province; in Nicaragua, where education vouchers as well as decentralization have been successful; and in Chile, the country that has done the most with the education vouchers, although the state still controls the curriculum. In general, Latin Americans are given an education that, in addition to being of poor quality, is intensely collectivist and fraught with all the prejudices against the individual inherited from the egalitarian tradition. Instead of entering the marketplace knowing from life how important the value of one's own interests are, young people arrive with the notion that "concern for one's own interests is evil, which means to say that man's desire to live is evil" (Rand 1964). Our young people distrust the words *company, gains,* and *profit;* they feel guilty to "care about themselves"—the philosophy that, by the end of his days, even the collectivist Michel Foucault (1984), while studying the individualistic wisdom of the ancients, came to proclaim as a great tradition of Western freedom.

We Latin Americans have still not undertaken the greatest privatization of all, that of political language. We must privatize politics. "Words are signals for ideas, not ideas," according to Herbert Spencer ([1884] 1950). By taking control of political language, the state has been able not only to strip political communication of ideas but also to create a complex network of signals that have trapped the mind of its citizens in an intellectual and ideological spider web with no way of escape. Thus, our reforms have been insufficient also because they have lacked essential intellectual nourishment and an inoculation in the realm of ideas and political language that would immunize the citizens against the collectivists' sophistic viruses and against the hopelessness of that early stage in which the reforms seem only to involve a tremendous cost and no immediate benefit. Owing to this intellectual void, the adversaries of freedom have today turned "neoliberalism" into the great Satan of Latin America. Just as in the mysterious Japanese Kabuki, our political life has become filled with masks that disguise or hide the truth, and we have come to believe that those masks are real faces.

The Prospect

Can we be optimistic about the immediate future in Latin America? "Time wins more converts than Reason," sighed Thomas Paine (1776), and he was right, but we have already spent too much time without being converted to the truth. Yes, some things have been left behind for now. Nobody will propose the nationalization of companies in our countries for a long time, and anti-imperialism has been reduced to small circles because our societies admire and emulate the North American example. (An overwhelming reality—annual remittances from our relatives in the United States of

some $10 billion to their countries of origin [Harrison 1997]—works against traditional antiyanqui demagoguery.) Of course, the longer-term battle will be fought by the intellectuals, whose influence is enormous. The difference between an idea and a tangible product is that if the latter fails, it ruins its manufacturer or seller, whereas if an idea adopted in politics fails, it ruins the entire society (and the intellectual who created and disseminated it ends up with a professorship in a Yankee university). The "poor morals of the mediocre souls" (Ortega y Gasset [1927] 1974) of our intellectuals preclude great hopes for the members of those circles, but spectacular conversions have occurred in other parts of the world, and efforts should continue to educate our intellectuals. We have some important advantages, the greatest of which is that whereas the advanced societies are aging rapidly, ours are rejuvenating at the same rate. With the present process of capital accumulation, a period in which consumption should undoubtedly be moderate, it will be necessary to make sacrifices and to explain to our societies the usefulness of these sacrifices, but if anyone thinks that the new structures are already in place and that it is just a matter of time, he is mistaken. Many great reforms are still pending in order to ensure development, and in this process a new governing class will be required. Thanks to globalization, with trade growing twice as fast as industrial production, with direct foreign investment of more than $120 billion, and with the nation-state at its weakest point since the Treaty of Westphalia (1648), the thesis of "contagiousness" and "osmosis" has a promising outlook. Still, no one should believe that globalization magically changes countries: it only increases opportunities and determines that if one does not keep his foot in the stirrup, he will soon be thrown back to the Stone Age.

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