Models of Capitalism and Latin American Development

Evelyne Huber

University of North Carolina and
Institute for Advanced Study, Princeton (1998-99)

Department of Political Science
CB#3265
University of North Carolina
Chapel Hill, NC 27599-3265

email: ehuber@unc.edu

Models of Capitalism and Latin American Development[*]

Actors, Institutions, and Policies

Latin American societies have undergone fundamental changes in the past two decades, moving from capitalist economies with very wide-ranging state intervention towards more market-driven systems. These changes have produced some successes in the area of economic growth, but also many problems, particularly in the area of poverty and inequality. Moreover, there are underlying problems like low saving and investment rates and sluggish export growth that are reason for concern regarding future economic growth (e.g. Fishlow 1995). As the perception of a need for continuing changes in economic and social policies is widely shared, the search for solutions to the challenge of growth with equity has intensified. In this period of globalization, the experiences of countries in different parts of the world are becoming more and more accessible for comparative study, and policy-makers increasingly look to a variety of experiences as potential reference points.

In comparative perspective, societies with market economies exhibit great diversity, at every level of economic development, in terms of their capacity to produce growth and equity, or growth and social integration. The obvious question is why some societies are more successful than others in achieving these central goals. During the 1980s, the dominant answer to this question in the debate in international financial institutions (IFIs), private banking circles, and a number of powerful member governments of the Organization for Economic Cooperation and Development (OECD) was that success varies positively with the extent to which economies are governed by markets and inversely with the extent of government intervention in the economy. Many economists studying the East Asian Newly Industrialized Countries (EANICs) and most social scientists studying social policy in a wide variety of countries challenged this view throughout, and by the 1990s the view that proper regulation, supervision, and - if necessary - correction of markets, along with public investment in human capital are pivotal for sustained economic growth and social integration, asserted itself even among the IFIs and the more conservative OECD governments.[1]

Here we shall approach the question of reasons for success in growth and equity from the policy angle, asking which types of economic and social policies governments in the more successful societies pursued. We attempt to identify different models of capitalism, understood as sets of core economic and social policies in the context of market economies . We are choosing this approach because we intend to draw lessons for political action, and policies are action relevant. Geography and resource endowments did have an impact on growth and distribution in different countries, both a direct one and an indirect one by making certain policies likely to be successful. Certainly, a large part of the

[*] This paper is a draft of the conclusion to a volume on Models of Capitalism and Latin American Development, edited by the author. The volume assembles papers presented at two conferences on this topic, organized under the auspices of the Social Science Research Council in May and November of 1997.

[1] Wade (199x) makes clear that not only dissenting economists but also the Japanese government disagreed with the World Bank's interpretation of the experience of the EANICs.

success story of the South East Asian Newly Industrialized Countries (SEANICs) is the investment from Japan, Korea, and Taiwan (Welsh's contribution to this volume; Stallings 1995). However, policymakers in charge of promoting growth and equity can neither rearrange geographic locations nor natural resource endowments, but they can use successful policy models as guides to designing policies for their own societies. Thus, we attempt to understand the policy models themselves, the institutional and political conditions under which they operated, and the extent to which the effectiveness of these models is bounded by time and space.

Comparisons with North East Asia and South East Asia are particularly relevant for Latin America because of the extraordinary developmental success of the former and the more moderate success but greater similarities to Latin America in terms of resource endowments and initial insertion into the world economy of the latter. Comparisons with advanced industrial democracies in the areas of labor market and social policies are relevant because there are wide contrasts among these countries in the degree of poverty elimination and reduction of inequality despite largely similar levels of affluence. These contrasts demonstrate the imperfect relationship between economic growth and poverty and inequality. Whereas there is evidence that very high inequality is a fetter on growth, there is no evidence that growth automatically translates into greater equality.[2] Rather, a variety of economic, labor market, and social policies affect the primary income distribution, and this distribution in turn can be heavily modified by tax and transfer systems.

Now, despite the analytical need to disaggregate national models of capitalism into their constituent parts, it is still important to explore the interrelationships among institutions, actors, and policies. Various policies can be mutually reinforcing or work at cross purposes; different institutions can make the pursuit of certain policies more or less difficult; and various actors can improve collective outcomes through cooperation or make everybody worse off through confrontation. One example of positive relationships among actors, institutions, and policies is offered by the coordinated market economies with social democratic labor market and welfare state regimes. Strong employer and labor organizations and an activist state work together to achieve high competitiveness of firms, high levels of employment, a high level of human capital, and a very generous social safety net. These actors work with medium and long term horizons and cooperate to maintain high levels of investment, technological upgrading, high quality production, labor training and retraining, wage setting to safeguard competitiveness of exports, job placement, etc. High quality production allows for both high market wages and a high social wage in the form of high earnings replacement rates in unemployment, sickness, and pension insurance, provision of extensive public social services, and generous transfers to groups with a tenuous relationship to the labor market, particularly children and youths. In contrast, at similar levels of economic development, in uncoordinated market economies with liberal labor market and welfare state regimes the lack of cooperation among employer and labor organizations and the state results in more skewed distributions of human capital, a more dualistic economy with high and low productivity sectors and a dual labor market, a more unequal distribution of market wages and a lower social wage,

[2] For an empirical analysis challenging the Kuznets curve, see Bowman (1997).

particularly in the area of transfers and services for the working age population and their children.

In North East Asia, there has been coordination, but between business and government only, under the exclusion of labor organizations. This coordination has been successful in achieving high investment rates, technological upgrading, high levels of human capital, and high levels of employment. Market and even more so social wages lagged behind for a long time, as labor did not have the organizational strength to push for improvements. That distributional outcomes were nevertheless comparatively egalitarian is largely due to the redistribution of assets through the land reform, the high level and relatively equal distribution of human capital, the low levels of unemployment, and the welfare functions of the extended family.

In Latin America, there has never been any general coordination between the government, employer and labor organizations. Employer organizations have typically been weak, and individual businessmen sought direct and personalistic relations with government agencies. Relations between individual employers and labor organizations have generally been highly antagonistic. Governments, through the Ministry of Labor, were intimately involved in labor relations, but in mediating and adjudicating specific conflicts, not in seeking general cooperation at levels above the firm. Relations between governments and labor organizations were overwhelmingly antagonistic as well. Where they were not, they tended to be paternalistic; organized labor received material benefits but had to accept governmental controls over its activities, particularly political and strike behavior. The absence of coordination and trust among government, business, and labor contributed to the comparatively low investment levels, slow and limited technological upgrading, low levels of human capital, and high levels of un- and underemployment. The resulting dual labor markets and low market and social wages, along with the historically very highly unequal distribution of assets, maintained poverty and inequality at comparatively very high levels.

Of course, institutional factors shape the degree of coordination between government, labor and employer organizations to a significant extent. A Weberian bureaucracy, with hiring and promotion based on merit, with salaries adequate to attract highly qualified officials, and with an esprit de corps is a crucial asset for establishing continuity and credibility of government policies and eliciting cooperation from business and labor. Business and labor on their part need to have organizations that can speak and negotiate authoritatively for their members. The fewer these organizations are in number, that is, the more centralized the organizations of both labor and employers are, the easier it is to achieve cooperation and compliance on broad economic, labor market, and social policies. Finally, particularly in democracies, the structure of political institutions proper which can concentrate or disperse political power, is important for the achievement of comprehensive legislation. Institutions like federalism, presidentialism, and bicameralism disperse political power and offer many veto points through which particularistic interests can obstruct reforms of a wide-ranging character. This applies both to reforms that enlarge governmental functions and those that reduce these functions. The strength and discipline of political parties can to some extent compensate for this dispersion of power, but in federal systems parties tend to be more fragmented and thus to aggravate it.

However, within the context of broad similarities regarding the extent of coordination between government, business, and labor, as facilitated or obstructed by institutional factors, there are important differences in levels of poverty and inequality, attributable to different political coalitions and their policy choices. Among Latin American countries, Uruguay and Costa Rica have consistently done better than other countries. Similarly, within the category of coordinated market economies there are important differences between social democratic and christian democratic welfare state regimes in terms of distributive outcomes, as there are in the category of uncoordinated market economies with liberal labor market and welfare state regimes. Across these different systems, generous minimum benefits in transfer programs; pensions, child allowances, unemployment insurance, or even means tested social assistance; are effective in keeping poverty rates low. In the area of social services, public funding and delivery of health care provides more equal access and is cheaper than private alternatives. The existence of these differences points to room for meaningful choice in policy designs. Or, to look at it in another way, even if a country cannot achieve the benefits of cooperation in all or even in many of the policy areas because of the nature of the actors and institutions, governments have the option of choosing policy instruments that will deliver some of the desired outcomes.

Policies to Promote Economic Growth

There is a long-standing consensus in the debate about the determinants of economic growth that high levels of investment in physical capital have a positive impact; more recently, a consensus has developed that investment in human capital has a positive impact as well (Schmidt-Hebbel, Servén and Solimano 1996).[3] [economist colleagues: what are the other "must" cites on these positions?] The next question to ask is what factors account for differences in investment levels. Several factors have been proposed, such as high savings rates, stable macroeconomic conditions, political stability, favorable exchange rates, and access to foreign savings. The logical conclusion would be that governments should concentrate on policies that increase domestic savings, maintain macroeconomic and political stability, adapt the exchange rate to the economy's changing position in international markets, and attract foreign savings. Yet, caveats have been raised in several of these policy areas.

There is disagreement about the direction of the causal relationship between domestic savings and growth (see e.g. Fishlow 1995; Page 1997 vs. Gavin, Hausmann and Talvi 1997; Schmidt-Hebbel, Servén and Solimano 1996), and about the level of inflation defining macroeconomic stability and being conducive to growth. There is also a recognition that an inflow of too much and unregulated foreign savings can have detrimental effects on growth (Ffrench-Davis and Reisen forthcoming). Whereas no attempt can be made here to take a position in these disputes at a general theoretical level, what we can do is to look comparatively at the experiences of North East Asian, South

[3] Central among other factors that have been emphasized as determinants of growth are technological innovation and expansion of exports. Several of the essays in Birdsall and Jaspersen (1997) review these debates.

East Asian, and Latin American countries and identify systematic patterns of variation in their performance on indicators accepted by the literature as related to economic growth. As an additional step, we can identify the policies that were pursued with the intent of improving the performance in these areas.

There is no doubt that both domestic savings and investment rates were significantly and consistently higher in East Asia than in Latin America for the past three decades. As of 1965, investment and savings rates were roughly similar in the two regions, around 20% of GDP, but in the period 1970-80 investment grew faster in East Asia than in Latin America, and in 1980-91 it continued to grow at 7% a year whereas it declined by 1.2% per year in Latin America. In 1991, the average investment rate for Latin America was 18% of GDP, for East Asia 35%; average savings rates stood at 22% and 32%, respectively (Jaspersen 1997: p.83).[4] In East Asia, both private and public savings rates have been high; in Latin America, both of them have been lower. A strong banking system, stable interest rates, and private savings for retirement are often credited with keeping private savings rates high in East Asia. Chang (this volume) offers an additional explanation, restrictions on luxury consumption through high tariffs, taxes, and outright bans; Fishlow (1995: 18) adds to this the emphasis on exporting industrial consumer goods that were not made readily available in the internal market. Most of these restrictions would be obviously extremely difficult to use in contemporary Latin America, both for political reasons and because of the Uruguay Round of GATT. However, the imposition of high taxes on luxury consumption - while politically difficult to implement - would not violate any international economic agreements. Such taxes then could contribute to an increase in public savings and a slow recuperation of public investments which fell to exceedingly low levels - with detrimental consequences for growth - during the period of structural adjustment.

An additional problem in Latin America has been the channeling of savings into productive investments; this is true for both domestic and foreign savings. The traditional explanation for this problem is the weakness of financial markets, and the prescription has been financial liberalization. However, at least so far financial liberalization has not resulted in significant increases in savings and investment rates in Latin America.[5] On the contrary, financial liberalization has made capital flight, a historic problem for most Latin American countries, even easier, and it has introduced serious new vulnerabilities. In particular, the unregulated inflow of foreign capital into Latin America in the 1990s, mostly in the form of portfolio investment and therefore short term funds, has led to an expansion of internal credit, much of it going to consumption and real estate booms, an appreciation of the exchange rate, and the danger of abrupt and massive capital outflows requiring severe adjustment measures, as in the Mexican peso crisis of December 1994 (Ffrench-Davis and Reisen, forthcoming). It is important to note that Chile, the supposed

[4] The Latin American countries included in this calculation are Argentina, Brazil, Chile, Colombia, Mexico, Uruguay, Venezuela, and Costa Rica; the East Asian countries are Japan, Korea, Singapore, Hong Kong, Thailand, Malaysia, Indonesia.

[5] Edwards (1997: 135) argues that it is too early to tell how recent financial reforms will eventually affect aggregate savings, but he adds that recent evidence suggests that the results may not be as favorable as expected by early supporters of financial liberalization.

model of neoliberal reforms, reimposed some controls after the financial crash of the early 1980s and has had controls in effect on short-term capital flows. Thus, unlike Argentina for instance, Chile managed to escape the ramifications of the Mexican crisis, known as the "Tequila Effect."

In fact, the experience of East Asia in the 1990s should caution against any uncritical advocacy of financial liberalization. As Radelet and Sachs (1998) have convincingly argued, the East Asian crisis is essentially a financial crisis, in large part caused by a boom of international lending followed by a sudden withdrawal of funds, as a result of rapidly escalating panic on the part of foreign investors. The repercussions of this sudden withdrawal of funds on the collapse of domestic financial institutions then imposed huge financial burdens on public budgets to bail out the failed institutions. Chang et al. (1998) agree that the panic in international financial markets was an essential ingredient of the financial crisis in Korea, and they argue that it was precisely the speed and mode of financial liberalization and the abandonment of traditional policies to coordinate investments that made Korea so vulnerable and contributed to the bankruptcies of some major firms.

There is general agreement that DFI has more favorable effects on economic growth than portfolio investment; it increases productive capacity, brings access to technology and markets, and has a weaker effect on the appreciation of exchange rates (Stallings 1995: 11). Nevertheless, the neoliberal arguments for unregulated inflows of DFI, or even more so for undifferentiated use of incentives to attract DFI, can be challenged on the grounds of both the Latin American (Evans 1979) and the East Asian experiences (Chang 1998). Evans demonstrated some two decades ago that DFI in Brazil had the most beneficial effects on local production of inputs, technology transfers, and local R&D where the Brazilian state had bargaining leverage and put pressure on foreign corporations. In fact, the most successful examples occurred in industries where joint ventures were formed between foreign corporations and Brazilian state-owned enterprises (1979: 276-7). Chang points out that both Korea and Taiwan maintained strict regulation on entry and ownership of transnational corporations. In Korea in the early 1980s around 50% of all industries were still closed to foreign investment, and only in about 13% of manufacturing industries was foreign ownership above 50% allowed. The Korean government encouraged joint ventures and carefully monitored technology transfers and imposed local contents requirements and standards of export performance. Of course, not all Latin American governments will have the same bargaining leverage, and this leverage will also vary by industry. However, it would be a grave mistake of omission for these governments to rely on the market alone to induce foreign capital to make contributions to local productive capacity, and to fail to exploit bargaining leverage stemming, for instance, from the size of local markets, location in relationship to other markets, the quality of the labor force, resource endowments, and prospects for economic growth.

For foreign and domestic investors alike, predictability of future economic conditions is a key consideration in committing major investments to productive projects. Predictability rests on stability - stability of the rules of the game and of major economic parameters such as inflation, growth, and exchange rates. There is no question that political instability is a major disincentive to private investment, as are severe macroeconomic fluctuations. It is less clear what constitutes favorable levels (as opposed to changes) in inflation and exchange rates. Chang (this volume) argues that inflation in East Asia was actually moderate, not low, by comparative standards during the periods of high growth. The implication is that excessive emphasis on low inflation might have costs in terms of investment and growth. From a Latin American perspective, with the recent experience of hyperinflation in several major countries, the issue looks very different. A return to even moderate inflation would be seen as a dangerous step on the slippery slope towards loss of control over inflation. Since inflationary behavior is so heavily determined by expectations, such a development might even become a self-fulfilling prophecy. In other words, what may be levels of inflation that are tolerable and supportive of high levels of investment in one historical context may not be in another. Or, at the very least, the move from one level to another may not be tolerable under certain historical conditions.

None of the papers in this volume, nor in a recent IDB volume (Birdsall and Jaspersen 1997) explicitly problematizes the issue of exchange rates. In peripheral comments, the stability of East Asian compared to the volatility of Latin American exchange rates is pointed out, along with the "realistic" level of the former which favored export growth (e.g. Pack 1997: 245). There is an intellectual vacuum here which is interesting considering that there is a political perception that North East Asian exchange rates were (unfairly) undervalued for years, which led to their revaluation under American pressure through the Plaza Accords of 1985. Undervalued exchange rates should stimulate investment in production for exports, as long as input prices are not a major factor in the calculation - or they are subsidized. The effect on investment in production for the domestic market would depend very heavily on the degree of protection of that market. In the new international economic environment where subsidies are largely illegal and protection greatly limited, undervalued exchange rates should benefit countries with an already established productive structure that has a low dependence on imported inputs. Countries producing at lower levels of commodity chains, particularly those dependent on raw material exports where local labor costs constitute a relatively small percentage of production costs, should benefit less from undervalued exchange rates.

Trade Policy

Trade liberalization in Latin America has been rapid and of great magnitude, but it has hardly fulfilled the promises made by its most ardent advocates. Trade has increased, but, as Baumann (this volume) makes clear, import penetration more so than export growth. Moreover, diversification and upgrading of exports has been limited; natural resource based exports remain crucial. The argument that competition from imports along with lower prices for inputs would force companies to become more efficient and enable them to break into international markets turned out to be based more on ideology than on empirically grounded understanding. There are at least two major flaws in this argument. First, many companies were simply too weak financially, managerially, and technologically to make this adaptation rapidly and on their own; they went bankrupt and their installed production capacity was lost with them. Second, comprehensive trade liberalization, while obviously not a sufficient condition for export growth, is not even a necessary one. Rather, liberalization could be selective, aimed specifically at inputs for export production.

Thus, if the goal is export promotion, particularly a move toward higher value-added exports, selective protection may be an appropriate policy, along with a number of other policies, as will be discussed in the next section. The danger is, of course, that protective measures become permanent and do allow for inefficient production, as happened in many cases under the ISI policies in Latin America. Korea and Taiwan demonstrate that this is not a necessary feature of protectionist policies. As Chang (this volume) shows, Korea used a combination of protection of infant industries with industrial policies, such as managed competition and technology policy and export promotion, and gradually increased the exposure of these industries to international competition.

Given the presence of excessive protection, there is no doubt that trade liberalization was necessary in Latin America. The problems lie in the speed and scope and erratic nature of liberalization and even more so in the neglect of complementary policies that should have preceded or accompanied trade liberalization. Gradual and predictable phasing out of protection, along with support for technological upgrading, investments in human capital, improvements in industrial relations systems, and provision of information about international market opportunities are all essential ingredients of a policy regime supportive of adaptation of companies to an open market environment. Of course, they require a more interventionist state than the neoliberal vision of the 1980s allowed. Though some of the costs incurred in terms of destroyed production capacity are irreversible, a resolute pursuit of such supportive policies could still be highly beneficial for expanding and upgrading export production.

In Latin America regional integration has clearly been important for the growth in trade. It has also been associated with an increase in foreign capital inflows, both from within and outside the region. Mercosur is the most dynamic area and has attracted most of the DFI going into Latin America. Yet, critics point out that regional trade expansion does not expose Latin American industries to the same competitive pressures for technological upgrading as export expansion to extra-regional markets.

In any discussion of trade policy, the projected impact of the Uruguay Round of GATT and the WTO is crucial. It makes open trade barriers illegal, except in situations of impending balance of payments crises. There is more room for action in the promotion of industries, particularly at the local level. The use of tax breaks and direct subsidies is limited, with some exceptions in the case of regional development programs. However, it is by no means clear how consistently the rules can and will be enforced, particularly vis-à-vis the actions of local governments. However, support for technological upgrading is crucial and can take many forms; the same is true for the provision of market information. This makes close cooperation between governments, business associations, and individual firms in designing appropriate policies and strategies for export promotion essential.

Industrial Policies

In Latin America in the 1980s the view predominated that the state should do little more than protect private property and provide infrastructure. By the 1990s the realization set in that the state's role in promoting accumulation as well as providing social services and income transfers - at least enough thereof to ensure political stability - remains essential. This of course raised the question as to the appropriate policies for the promotion of industry. Since the official view of pre-1980 policies is one of undifferentiated failure, the initial answer to this question was "not the industrial policies of the past," but rather new horizontal, or neutral policies supportive of industrial development in general, not specific sectors. However, as Chang (this volume) argues convincingly, the notion of horizontal industrial policies is misleading in a context of scarcity. Even support for R&D or skills upgrading of the labor force requires decisions about the types of research and the types of skills most likely to contribute to technological upgrading of production in growth sectors. Research and skills developed for the biochemical industry cannot easily be shifted to the information technology industry and vice versa.

Selective industrial policy has not only a sectoral dimension but also a local one. Restructuring of industries that are the main support of local economies makes targeted industrial policy necessary to dampen social disruption as well as upgrade productivity. Tokman (this volume) emphasizes the importance of targeted sectoral and local industrial policy as an essential complement to labor market policy to promote high employment levels in medium to high productivity activities.

The traditional total package of industrial policies as pursued in Korea comprised import protection for infant industries plus managed competition to deal with the problem of economies of scale plus technology policies plus export promotion. The successful implementation of these policies required cooperation among enterprises, banks, and the government to assure long-term finance, a high quality training system, and an industrial relations system that avoided disruptions. The achievement of such cooperation has become more difficult in Korea as large enterprises have gained more independence from the government, for instance due to direct access to foreign financial markets. It has also become more difficult as trade unions have gained strength and autonomy in the course of political liberalization. It is even more difficult to establish in a context where enterprises developed without strong ties to the government as over the past 10-15 years in Latin America, and where labor relations have traditionally been highly antagonistic.

Industrial policy, particularly government support for technology upgrading also becomes more difficult as industries are approaching the technology frontier. Technological learning is easier where an economy is attempting to catch up with more developed economies, but the closer the most advanced sectors come to the technology frontier, the more difficult technology transfer becomes and the tougher the competition and pressures from advanced firms and countries. This means that there should be sectoral differences in industrial policy. Traditional technology transfer policies may work well in more established mass production industries whereas in the most advanced sectors new forms of industrial policy need to be developed, arguably with greater concentration on support for R&D in cooperation with the private sector. Still, such policies should be tied to export promotion policies for these most advanced sectors, such as arrangements for financing and the provision of market information.[6]

As Peres argues (this volume), Latin American policy makers are highly skeptical vis-à-vis the idea of "picking winners" and developing new industries, preferring instead to strengthen already existing industries. To some extent, this is certainly reasonable; nobody would expect Paraguay to develop major production of personal computers or components. On the other hand, it becomes a matter of fine distinction what constitutes "already existing industries." Brazil for instance has a well developed production of some components for the informatics industry, and several countries have firms that produce petrochemical and biochemical products and consumer electronics. How much production makes "an established industry" that deserves support, and how much weight should be given to the goal of upgrading export production and thus supporting branches that have still a small volume of production?

Recognizing these issues and devising strategies to deal with them is certainly preferable to pretending that they can be avoided by pursuing non-selective industrial policies. Still other problems have to be overcome in order to develop effective industrial policies in Latin America. As with any other policy, a well structured bureaucracy with highly qualified and motivated members is a crucial prerequisite. Peres points out that implementation of industrial policy often falters because of overlapping and poorly defined areas of responsibility. Moreover, the extent of political appointments in the bureaucracy means that there is little continuity and industrial policies are typically designed and implemented with a time horizon of one period in office - hardly a basis for building the kind of long-term cooperation needed for success in this area.

Labor Market Policies

The main tasks for labor market policies are promotion of high employment levels and low unemployment and underemployment levels; protection of labor rights; organization of wage setting; and promotion of cooperation for improvements of productivity. The actual creation of jobs cannot be assigned to labor market policy, or only to a very small extent in a contributory role. Rather, private investment decisions shaped by public investment policies and industrial policies are crucial for job growth. Labor market policies can make a contribution in the form of rules facilitating flexible working hours, job sharing, etc., and in providing a qualified labor force that can make investments more attractive.

The main problems in Latin America are not only open unemployment but also underemployment, that is, employment in low productivity sectors and low wage jobs, mostly in the informal sector and thus without legal protection. The main focus of policy in the past 15 years, though, has been on open unemployment, as the destruction of large numbers of jobs in manufacturing and the public sector was not accompanied by an

[6] Many analysts argue that it was precisely the failure to upgrade their export structure that made South East Asian countries, particularly Thailand, so vulnerable to the repercussions from the externally induced financial shocks.

adequate rate of job creation in the new growth sectors, even once economic growth resumed. Rather than being understood as structurally rooted in the new economic model, the lack of significant employment growth has been blamed heavily on labor market rigidities in wage setting and job protection. Accordingly, IFIs and many governments have called for more flexibility in wage setting and in hiring and firing, at the same time as the governments withdrew from an active pursuit of investment promotion and industrial policies. The IFIs and many neoliberal economists have pointed to the United States as a model of labor market policies worthy of emulation because of its presumed outstanding record in employment creation.

Robertson's chapter takes a closer look at the supposed model quality of American labor market policy and points to the falling minimum wage, the high number of people who are working two jobs, and the less than stellar performance in unemployment once the huge prison population is taken into account. He suggests that other factors are responsible for the high rate of job creation, including the deficit spending of the 1980s. Moreover, despite the high rate of job creation, the expansion of the dual labor market has led to growing poverty and inequality in the primary income distribution. Robertson argues convincingly that American federalism is an important factor keeping labor rights and strength restricted by fragmenting authority and creating veto points against protective legislation, as well as by setting states up in competition for investment through providing a favorable business climate.

More successful models in terms of poverty and inequality in primary income distribution are provided by the Northern Continental European and Scandinavian countries, even though employment growth there has been lower than in the United States over the past 20 years. The key there has been promotion of full employment and a reduction of inequality through a combination of supply side industrial policies, investment in human capital, active labor market policy, centralized wage setting, and high contract extension. The internationalization and deregulation of financial markets has made the pursuit of traditional investment promotion and thus job creation policies more difficult, but the other policies mentioned remain viable (Huber and Stephens 1998). Active labor market policy in the form of assistance for retraining and relocation and finding new jobs for people who have lost theirs has been a cornerstone of labor market policy in the Scandinavian countries. This type of policy is successful in the context of other employment promotion policies, but much less so as an isolated set of measures or even as a substitute for these other policies. At times active labor market policy has also been used as a substitute for passive labor market policies, that is, for the provision of adequate income maintenance in the context of cuts in unemployment benefits. White (this volume) points out that in the context of generally high unemployment levels, active labor market policies can still have beneficial effects on equity by keeping people in contact with the labor market and preventing long term unemployment. However, the costs of these policies tend to be higher than the gains in employment.

East Asian countries have not had extensive labor market policies outside of investment in human capital and labor training, but their investment promotion and industrial policies were most supportive of employment creation. The land reforms in Korea and Taiwan supported self- and family employment in the rural sector, and fast industrial growth helped the absorption of the labor force into the urban sector. Labor rights remained minimal until the 1960s in Japan and the 1980s in Korea and Taiwan. Even after that, as Pempel points out (this volume), only a minority fraction of the labor force, mostly middle-aged and older men, came to benefit from stable employment and company welfare in large firms. In Japan, this fraction amounts to roughly one quarter of the labor force. Women, younger people, and workers in small enterprises enjoy less stability and benefits. One of the reasons why inequality has remained relatively low despite this situation is the redistributive function of the extended family.

Wage restraint in the sense of keeping wages from rising faster than productivity is clearly an essential element of labor market policies. Even if unions in traded sectors realize the need to adjust their wage demands to the requirements of competitiveness in world markets, the problem remains how unions in non-traded sectors, particularly the public sector, can be prevented from driving up wages and exerting pressure on unions in the traded sector. Measures to ensure wage restraint can take very different forms. The polar opposites are labor repression combined with dictates of the Ministry of Finance in East Asia and highly centralized collective bargaining with voluntary wage restraint on the part of unions in exchange for commitments of investments and social policies in the coordinated market economies of Europe. In the United States and in Latin America since the 1980s wage restraint has largely been a result of restrictive labor legislation and significantly weakened unions.

Given these different experiences and the specifics of the Latin American situation, what would be desirable labor market policies for Latin America? Certainly in one area the diagnosis of rigidities and the call for greater flexibility in Latin American labor market policy was correct. Traditionally, labor legislation protected not the right to employment and income maintenance in general but the right to a specific job. Laying off employees was costly as employees were entitled to significant severance pay, which obviously was an obstacle to structural adaptation of enterprises to changing demand conditions. On the other hand, unemployment insurance has been virtually non-existent, which made loss of a job a near catastrophic event. However, changing the rules for layoffs caused by structural adaptation does not mean that protection against arbitrary firings should be relaxed. Employers in Latin America have traditionally fought unions, and firings of union organizers and supporters are potent weapons in that fight. In addition, a change in legislation to facilitate layoffs should be accompanied by a sustained effort to improve unemployment insurance protection.

Another generally recognized problem in Latin American labor markets is the low average skill level of the labor force. Investment both in general education and specific skills training is the obvious solution. Yet, despite general agreement on the diagnosis of the problem and the remedy, little has been done to advance in these areas. General education expenditures contracted in the 1980s and recovered only partially in the 1990s, and there is comparatively little being done by governments and the private sector to improve specific labor skills. One factor that works against private sector efforts is the extensive use of subcontracting and the unwillingness of small and medium subcontractors to invest in the upgrading of labor skills. In East Asia large contractors have often participated in the training of workers in those subcontracting enterprises with which they maintained long-standing relationships. In Latin America, governments could create a regulatory environment to make subcontracting relationships more stable and thus investment in training of the subcontractors' labor more attractive, and they could support labor training directly.

One of the major arguments against protective labor legislation in Latin America, of course, has been the size of the informal sector. The informal sector has grown, so the argument goes, precisely to avoid government regulation. While there is more than a grain of truth to this argument, the commonplace conclusion that a generalized reduction of government regulation and taxation is necessary and sufficient to reduce the size of the informal sector is unwarranted. Rather, intensified enforcement efforts could have the effect of drawing some of these enterprises into the formal sector. This raises the question of differences in the importance of various types of government regulations. Clearly, excessive red tape in getting permits to establish an enterprise, along with high payroll taxes can discourage entrepreneurial activity, and enforcement of these regulations may lead to business closures. On the other hand, enforcement of basic labor rights and basic tax collection should be expanded to small and medium enterprises, along with better access for these enterprises to credit. The direct and indirect (via a stronger tax base) benefits in terms of workers' welfare would arguably outweigh the loss of substandard employment that might occur.

A central question in the debate about labor market polices in OECD countries as well as in Latin America is the presumed trade-off between greater downward flexibility of wages and higher employment levels. Even in advanced industrial countries, it is highly questionable whether such a trade-off exists. Certainly the British example suggests that simply lowering wages and taking away rights from the lowest paid does not necessarily create more jobs. In Latin America, wages already are abysmally low in the informal sector, particularly in personal services, and the central problem is precisely the prevalence of low productivity, low paid employment that leaves workers and their families way below the poverty line. Lowering formal sector wages might bring some of these jobs into the formal sector, but it would not alleviate the key problem of poverty. On the contrary, it might aggravate the problem by lowering the wages of those already employed in the formal sector. In addition, it would weaken the incentive for employers to invest in upgrading productivity.

The Chilean example is a case in point for the negative effect of excessively flexible labor markets on poverty. Díaz (1993) argues that precarious waged employment was the single most important element of poverty in Chile at the beginning of the 1990s. Forty-one percent of the two lowest income quintiles in the 1990 household survey were associated with formal urban employment, but many of them without any contractual arrangement. The growing practice of large firms to use subcontractors has led to a proliferation of small and medium firms that employ workers at very low wages, for limited time periods, under poor working conditions, and with little access to training.

In Latin America a closely related debate is whether these economies can afford a meaningful minimum wage. One of the arguments against it holds that the enforcement of a minimum wage would destroy formal sector jobs and push more people into unemployment or the informal sector and into poverty. Others emphasize that it would be of extremely limited benefit because it would only cover formal sector workers and hurt others by swelling the ranks of those in the informal sector and thus depressing wages there. Lustig and McLeod (1997) review these debates and conclude that the theoretical discussion is inconclusive and the matter is essentially an empirical one. They show in a regression analysis of changes in poverty in 22 developing countries that the levels of the minimum wage and of poverty are negatively related; an increase in the real minimum wage is accompanied by a fall in poverty. However, they caution against using the minimum wage as a tool to combat poverty, arguing that this might increase unemployment in the longer run. The Inter-American Development Bank's 1996 Report finds that in country-level analyses "in general there is no evidence that raising minimum wages leads to greater unemployment" (IDB 1996: 203), presumably because those in charge of setting the minimum wage are taking the relevant conditions into account . So again, the issue of a tolerable level of the minimum wage in a given country is certainly an empirical one. Morley's (1995: 148-50) analysis of Costa Rica confirms the importance of the minimum wage as a tool to combat poverty. He shows that poverty could be reduced in Costa Rica in the 1980s despite very low economic growth in part because of the increases in the minimum wage, and that employment increased at the same time. The two general conclusions one can draw from these studies are that a lowering of the minimum wage in Latin America would most likely increase the level of poverty, and that gradual increases in the minimum wage are effective means to lower poverty.

A final question concerns the desirable strength and role of unions. Outside of a few sectors in a few countries, organized labor in Latin America is extremely weak. The combination of physical repression under the military regimes and loss of membership due to destruction of jobs in traditionally well organized sectors is largely responsible for this state of affairs, but restrictive labor legislation is keeping labor from regaining strength in several of the democracies (Drake 1996). Opponents of changes in these restrictions argue that the East Asian example demonstrates that weak unions are good for development whereas labor in Latin America has mostly had a negative impact on development by taking adversarial positions to capital and engaging in heavily politically motivated actions. There are several strong counterarguments to make. First of all, the Northern European experience demonstrates that strong labor movements can be good for development, or at the very least compatible with the development of highly competitive economies and very important for the equitable distribution of the benefits from economic growth. Second, given that labor in Latin America was either fought by employers and governments or met with paternalism and attempts at co-optation, but was rarely ever accepted as an autonomous partner, it is not surprising that unions sought help from sympathetic political forces and used strikes to demonstrate their strength and gain concessions where they failed to gain them in negotiations. Third, in East Asia there was a strong drive for development, a sense of national purpose rooted in the pursuit of national security, which resulted in sustained high investment levels and a relentless search for technological progress, even in the absence of union pressure for higher wages. Where this drive and national purpose are missing, as in contemporary Latin America, union pressure can be an important factor forcing employers to invest in technological upgrading and move production up the commodity chain. In contrast, in the absence of union pressure the incentive to compete on the basis of cheap labor and neglect technological upgrading is much stronger.

The European experience, particularly the contrast between Scandinavia or Germany on the one hand and Britain on the other, also demonstrates that high degrees of centralization are conducive to coordination of union action and cooperation with governments and employer organizations in the interest of maintaining national competitiveness. A fragmented union movement is in a much more difficult position to restrain wages when needed and seek compensation in other ways. Thus, whereas the restrictions on higher level union organization in contemporary Latin America are certainly contributing to keeping labor weak, as their advocates desire, they are failing to lay the groundwork for the eventual emergence of a labor movement that could play a productivity, growth, and equity enhancing role.

Social Policy

The goals of social policy, of course, are contested terrain. A minimalist conception of social policy sees its role as promoting social order and political stability, a maximalist conception sees it as building a welfare state regime that provides every citizen or resident with an adequate share in economic and social resources as appropriate for the standards of a given society, so that every individual is able to participate in the life of this society and fully develop her or his capacities. If one adopts the maximalist conception, one needs to develop operationalizations to assess progress towards this goal. I would suggest that in the context of all the societies considered here, social policies that effectively reduce poverty, redistribute income, and improve the provision of free public services, particularly health care and education, can be considered as working in this direction, as long as they are being promoted in a deliberate, coherent and comprehensive manner. According to this operationalization, the deliberately technocratic solutions that are being promoted by the IFIs as complements to structural adjustment programs do not qualify as efforts to move towards a maximalist conception, because they take the form of targeted programs to alleviate the symptoms of poverty under exclusion of more comprehensive and coherent approaches to combat its causes, and they divorce these programs from the issue of redistribution.

The historic problems that are at the root of the widespread poverty in Latin America are high inequality in the distribution of wealth, income, and human capital; high population growth; low labor force participation, including female labor force participation; and a high proportion of the labor force in low productivity sectors. The extent of these problems requires a broad attack on poverty from different angles. Comprehensive social policy, including both cash transfers and social services is obviously central, but it needs to be complemented by labor market policies and the provision of infrastructure in both urban and rural areas. Moreover, as the East Asian experience demonstrates, redistribution of land is a crucial factor for the reduction of poverty and inequality. As Filgueira and Filgueira (this volume) point out, however, this is not how the problem was traditionally or is currently being defined and attacked in Latin America. Rather, with few exceptions, land reforms have remained very limited or were even rolled back. Traditional social policy has mostly focused on formal sector wage and salary earners, and the approach to transfer payments and social services has largely been based on the social insurance model. Social insurance schemes developed in a highly fragmented manner, and by the early 1980s the older ones among them were beset by financial problems already (Mesa Lago 1989). These problems then were severely aggravated by the economic crisis of the 1980s and opened the way for profound reforms. In line with the neoliberal thrust of economic reforms, the dominant approach to social policy reform has been privatization, targeting and decentralization (Huber 1996). However, there have been very important exceptions both in traditional forms of social policy and in contemporary approaches to reforms, such as in Costa Rica and Uruguay, which make it clear that social policy designs are a profoundly political question, shaped by power and interests, not a technical question of finding the most efficient design to achieve generally shared goals.[7]

In Latin America as a whole, the 1980s saw a severe deterioration of living standards, with rising unemployment, falling real wages, and cuts in social expenditures. The wage share in gross national income declined, and inequality increased except in Costa Rica, Colombia, Uruguay, and Paraguay (Morley 1995: 28). In general, the different governments' approaches to social policy reform corresponded closely to their vision of an appropriate model of the relationship between state and market, and state and civil society, and to the interests of their power base. Those who fully embraced economic neoliberalism also went furthest away from universalistic approaches to social policy and towards residualism, that is, towards a growing role of private insurance and private providers of services and a restriction of the role of the state to taking care of the poorest of the poor only. Chile under Pinochet went furthest in this direction, with a preferred role for the private sector in both pensions and health care and a residual role for the state in taking care of those with lower incomes and the very poor. Uruguay in contrast has retained a universalistic approach with heavy reliance on the state, particularly in the pension system. Several countries introduced mixed public/ private schemes, often with competition between public and private components and incentives structured to the detriment of the public components.

Most of the reforms are of recent origin and their effects have not been thoroughly evaluated yet. However, a few statements can be made. The oldest reform is the Chilean pension reform, and it has failed to solve two crucial problems; the extent of coverage, which stands at about 60% of the labor force (Raczynski 1997), and the administrative costs which are high, particularly for low income earners, mostly because of the high expenses for marketing. Moreover, we know from studies of welfare states in advanced industrial societies that public pension schemes are more egalitarian than private ones, even if the public ones have a strong earnings-related component (Korpi and Palme 1997).

---

[7] The liberature on social policy reform in Latin America has been growing rapidly. For interesting collections of essays see Barreto de Oliveira (1994) and Raczynski (1995). The Kellogg Institute at Notre Dame published a number of very interesting working papers by Faira (1994); Draibe, Guimarães de Castro, and Azeredo (1995); C. Filgueira (1994); F. Filgueira (1995); Lo Vuolo (1995); Raczynski (1994); Hippolito (forthcoming) contains a number of papers presented at a conference on Social Policies for the Urban Poor at the Kellogg Institute at Notre Dame.

We also know that countries with private insurance and delivery of health care spend more of their GDP on health care and have more unequal access than countries with public insurance and delivery. In Chile, the private health system covered 30% of the population in 1995, the public one 70%; expenditures in the private system amounted to US$ 310 per person, compared to US$ 197 in the public system (Larrañaga 1997).

If we assume that effective large-scale poverty reduction is a desired goal, what can we learn from countries where this goal has been achieved about the most effective policies? First, we have to recognize that large-scale poverty reduction is not possible without a redistribution of income through the tax and transfer system. As Stephens shows (Table 4; this volume), the advanced industrial countries with the lowest poverty rates also have the lowest post-tax/ post-transfer inequality, partly due to comparatively low inequality in primary income distribution achieved through labor market policies, and partly due to highly redistributive tax and transfer systems. The need for redistribution is much greater in Latin America, of course, given the much more unequal primary income distribution. Thus, the first and most important policy lesson is the need to establish an effective and progressive tax system. It is very clear that Latin America is significantly undertaxed compared to other regions. In 1991-95, the average tax burden in Latin American countries was 14.1% of GDP, compared to 16.8% among East Asian countries. That it is not impossible to collect higher taxes at the level of development of Latin American and Caribbean countries is demonstrated by the considerable variation among them, with Guyana, Barbados, Jamaica, and Trinidad and Tobago all having tax burdens of 24% and above (IDB 1996: 128). Tax reform has been on the agenda of most Latin American countries as part of their structural adjustment programs, but progress has been rather limited. Where there was progress, it was mostly in aggregate tax collection based heavily on value added taxes; collection of income taxes from individuals remains very spotty (e.g. Berensztein 1998). This is a problem not only because of lost tax revenue but also because the income tax system can serve as a very effective and non-stigmatizing channel for income-tested transfers payments, as Myles' discussion of the Canadian example demonstrates (this volume).

Going back to the European experience, the countries with the lowest poverty rates have income transfer systems composed of (1) universalistic basic flat rate benefits financed from general tax revenue, (2) public earnings-related benefits financed by employer and employee contributions, and (3) social assistance supplements financed from general tax revenue for those still in need. Universalistic basic pension benefits and child allowances are particularly effective in keeping vulnerable groups, the elderly, families with many children, and single mothers out of poverty. Universalistic flat rate pension benefits were introduced at comparatively early stages of welfare state development, largely as a political compromise between the labor movement that pushed for social security programs and small farmers who opposed earnings-related benefits. Child allowances along with other family support programs were introduced later (Wennemo 1994). Universal flat rate pensions and child allowances would be an appropriate approach in the Latin American context as well, where a large proportion of the population are not formal sector wage and salary earners. They have the additional advantage of being simple and cheap to administer. The most frequent argument against them is that they waste scarce resources on middle and upper income earners who do not need them. However, this argument loses any validity in the context of an efficient and progressive tax system through which the benefits can simply be reclaimed. Universalistic programs have two more advantages. First, they acquire much larger political support bases than programs targeted at specific groups only. Second, they provide policy legacies that are more favorable for the maintenance of a redistributive and solidaristic thrust than particularistic and targeted schemes, as Myles' comparison between welfare state retrenchment in the United States and Canada makes clear.

My general argument in favor of universalistic and against targeted schemes should obviously not be misinterpreted as an argument for the immediate abandonment of all targeted schemes in Latin America, particularly those nutritional and other health schemes targeted at poor neighborhoods and poor schools. Targeting individual families through household means tests has many problems; it is cumbersome and expensive administratively; it has a stigma attached to it; it gives much room for administrative discretion and thus clientelism and political manipulation; and it is divisive by setting the poor up in competition with one another for benefits. The collectively targeted schemes, based on aggregate social indicators, can be very effective in alleviating some of the symptoms of poverty, even though they are also subject to the dangers of political manipulation. If they are channeled through schools in poor areas, they can also be useful to improve school attendance and thus human capital. What I am arguing against is governments concentrating on such targeted schemes as the essence of social policy and keeping off the agenda universalistic alternatives aimed at a comprehensive attack on the roots of poverty.

In addition to a universalistic income transfer system, the second major pillar of a comprehensive approach to improving the life chances of the majority of the population is the provision of high quality and universally accessible education and health care. That the state has an obligation to provide free public education, and even enforce school attendance, has long been a widely accepted premise in advanced industrial countries. Even in Latin America most governments rhetorically accepted this obligation, pleading resource constraints and lack of parental cooperation to explain the obvious gap between rhetoric and reality. In health care this obligation has been much more disputed, and the role of private delivery and financing of health care much more extensive, both in advanced industrial and in developing countries. The experiences of European and North American countries clearly show that public financing and provision of health care are vastly more egalitarian and also cheaper than private insurance and provision. The Costa Rican example demonstrates how successful an integrated approach to preventive and curative health care in a public health system can be in improving basic health indicators in the context of a developing country. The contrast with Brazil, for instance, which has a higher GDP per capita, is impressive. Brazil, of course, has made major efforts to strengthen the preventive and public parts of its health care system, but private hospitals, doctors, and drug companies have been formidable opponents in this struggle (Weyland 1996).

The reform thrust in many Latin American countries encompassed not only efforts to privatize parts of the pension and health systems and move towards public provision of services for the poorest groups only, but also a decentralization of the responsibility for the provision of social services to subnational governments. Theoretically, decentralization should make the providers of social services more responsive to the needs of the local population. In practice, the key issue remains financing. As long as the decentralization of responsibilities is accompanied by an adequate redistribution of resources from the central government, the outcome may well be better delivery of social services. Where decentralization is mostly a means for the central government to reduce expenditures and to break the power of public sector unions, and therefore redistribution of responsibilities for service delivery also means redistribution of responsibilities for raising the funds to pay for them, the outcome is growing disparity in the quality of the services between poorer and more affluent local communities.

Decentralization bears additional dangers. In Brazil, for instance, some state governors used resources from the federal government designated for the improvement of public health services for other purposes (Weyland 1996: 174). Political manipulation of social services to strengthen the support base of local power holders is every bit as likely as at the national level. The degree of responsiveness to local needs depends very heavily on the organizational capacity of the local population, which implies that responsiveness is not likely to be greatest towards the neediest because of their lack of organizational capacity.

Change from one system to another, in transfer systems as well as social services, is always difficult. People who have paid into an earnings-related social insurance scheme are obviously extremely reluctant to accept a transition to a universalistic flat-rate benefits scheme. Private providers of health services sternly resist an expansion of government regulation of their compensation. Nevertheless, some of the changes in Latin America over the past 15 years have been dramatic, and there is no a priori reason other than the interests and power of neoliberal and other opponents of universalistic and redistributive measures why these changes could not have gone into a different direction. If the earnings-related pension scheme is in such a financial crisis that it cannot pay adequate benefits and according to the government needs to be privatized, why would citizens naturally be more inclined to accept the promise that the government will provide some compensation for previously made contributions than the promise that the government will provide a basic tax-financed subsistence pension for all, to be supplemented by earnings-related benefits from a new scheme? In the case of health care reform, given the opposition from private providers and insurers to an expansion of public supervision, it is crucial that any new initiatives be directed towards strengthening public provision and financing of health services so as to gradually push private providers and insurers into a minority position.

Traditionally, financing of social security schemes in Latin America rested on employer and employee contributions, with employer contributions reaching very high levels. In protected economies this was acceptable to employers as they could pass the costs on to their customers; in the new open economic environment, employers are opposing contributions to social security schemes as a problem for competitiveness. There is no doubt that such obligations are one factor affecting labor costs and that they need to be kept at internationally comparable levels. However, this does not mean at all that they need to be abolished, as they were in Chile. The vast majority of industrialized and industrializing countries do impose such obligations on their employers. Still, financing of income transfers and social services in Latin America needs to be shifted more towards general taxes. This is particularly appropriate to finance universalistic flat rate pensions and child allowances and health care services. Employer contributions assessed as a percentage of remunerations paid can be considered one form of corporate taxation and be channeled into the general fund for transfers and social services rather than into one or more funds to finance specific entitlements of employees, thus strengthening the solidaristic aspects of social policy.

Transferability of Policies

As Filgueira and Filgueira, Pempel, Robertson, and Stephen argue forcefully, if we want to understand the possibilities for transferring growth and equity- promoting policies from one geographical-historical setting to another, we need to look primarily at institutions and actors, and at the distribution of interests and power among these actors. There are good reasons to discount cultural arguments as determinants of the feasibility of given policies. The argument about Confucianism and its promotion of discipline and harmony as a precondition for the success of East Asian industrialization is not at all convincing in the light of the harsh labor conflicts in Japan in the 1950s and 1960s and Korea in the 1980s. In the Latin American case, the argument about the catholic and corporatist tradition and its impact on the acceptance of hierarchy and fatalism and thus the lack of entrepreneurial motivation is equally unconvincing in the light of the long tradition of popular protest and revolt and the flourishing of informal entrepreneurial activities. Rather, to understand the roles of the state, capital, and labor in the shaping of policies, we have to look at their relationship to each other and to other major social actors, as well as at domestic institutions and the international context in which they operate.

To begin with an examination of domestic institutions, the first precondition for making coherent policies is a considerable degree of centralization of political institutions, or in other words, the absence of numerous veto points. Centralization should by no means be equated with authoritarianism, however. Certainly, there was very high centralization of power under the authoritarian governments in Korea and Taiwan, but the example of the Scandinavian countries shows that democracies can act in a comprehensive and coherent manner as well. Federalism and presidentialism disperse political power and provide numerous veto points which make comprehensive approaches difficult. The effects are very visible, for instance, in welfare state policies in the United States and also in austerity and adjustment policies in Brazil.[8] In addition to providing veto points, federalism also bears the danger of setting subnational units up in competition with each other for investment, thus giving capital great leverage against both governments and

[8] Maioni (1998) demonstrates this point very clearly in her comparison of health care policy in Canada and the United States. Huber, Ragin and Stephens (1993) demonstrate the impact of power dispersion on social policy in a pooled cross-sections and time series analysis for advanced industrial countries.

labor to keep labor rights and the social wage restricted. This dynamic is made very clear by Robertson in his discussion of the United States.

Policy legacies constitute another aspect of institutional structure, whose importance is demonstrated by Myles in his comparison of social policy in Canada and the United States. Path dependency is clearly important in that it shapes conditions within which later changes have to be made; on the other hand, these conditions can gradually be modified through additional policies. Radical departures from established policy patterns are rare, but they are possible in perceived crisis situations. The radical departure from traditional economic and social policies in many Latin American countries under the impact of the debt crisis is a clear example. Under normal conditions, changes are easier where old structures are not firmly entrenched, that is, where they have not been in existence very long or where they are not affecting powerful actors or large sectors of the population. One key lesson to take into account for social policy in the stage of setting up programs is the danger inherent in relying on private providers of services and insurance. Private providers will always work according to a market logic and thus introduce more inequalities into transfers and services than public providers who - under the direction of progressive governments - are more likely to be working according to a political logic of universalistic access and uniform quality.

There is little disagreement that a key requirement for effective policy transfer in any area is an effective bureaucracy capable of implementing policies as designed. Emphasizing the Weberian characteristics of an efficient bureaucracy and its autonomy from particularistic interests does not entail ignoring the importance of the power distribution in society that shapes the overall design of policies; it does direct attention to the capacity of the state apparatus to pursue policy goals in a consistent manner. Similarly, Evans' (1995) notion of the need for autonomy to be counterbalanced by embeddedness, that is, effectively functioning channels for ongoing interaction between the bureaucracy and the private sector, has been widely accepted as a precondition for the successful pursuit of developmental policies. This notion can be extended to the need for such channels between the government, business, and labor for the pursuit of labor market and social policies that are generous, comprehensive, and compatible with improvements in productivity and international competitiveness. In terms of specific state capacities, an efficient tax administration system is of primary importance both for mustering the resources needed for growth and equity-enhancing policies and for administering income transfer programs.

Shifting our focus from institutions to the distribution of power and interests among actors, it is useful to discuss those in relationship to specific policy areas. The type of policies for promotion of investment and competitiveness that a government might successfully adapt depends to some extent on the leverage of the government vis-à-vis private investors based on the share of crucial resources controlled by the government. At one extreme is the situation in Korea and Taiwan in the 1950s and 1960s where the state controlled all external capital flows, much of it coming in the form of grants from the United States, and virtually the entire formal domestic credit system (e.g. Woo 1991); at the other extreme is the situation in Mexico in the 1990s where capital markets had been largely deregulated and private investors, domestic and foreign, could plunge the country into a financial crisis. In all countries, including Western European ones, government intervention in financial markets in order to stimulate productive investment has become much more difficult today than before the mid-1980s, because financial deregulation has shifted control over funds away from governments to private investors.

In the area of industrial policies, the more dependent companies are on public support for R&D, technology licensing, and protection from competition, the larger is the government's room for action. As domestic corporations advance in competitiveness and size, and in capacity to deal with foreign corporations and enter foreign markets independently, they will become much more likely to challenge government's development plans and policies and pursue their own particularistic interests. As Evans (1995) points out for the Korean case, the very success of the developmental state tends to undermine its power basis and thus its capacity to continue in the same role.

In Latin America we are dealing with a fundamentally different trajectory. Even in the heyday of the developmentalist state, the state never had the same amount of control over resources as did the North East Asian states. Though the state did take control over the foreign exchange system, it was never the recipient of grants to nearly the same extent as Korea and Taiwan; it remained dependent on private capital to generate the huge majority of foreign exchange inflows. Thus, private capital, both large domestic and foreign capital, enjoyed greater autonomy from the state and was capable of exerting more pressure for the protection of its interests. One policy area where this power distribution has remained important is in the use of industrial policies to move up the commodity chain in exports and thus get away from dependence on primary exports. The pursuit of such policies is very difficult where agribusiness and large landholders are powerful economic and political actors. In this situation, the forging of a countervailing political support coalition for industrial policies among export-oriented manufacturing and business service enterprises is an essential first step in the successful transfer of any kind of industrial policies.

Turning to the transfer of labor market and social policies, the question becomes who could be the carriers, the political support base for comprehensive and solidaristic social policy reform in Latin America? In Europe labor movements were the main social force advancing the cause of solidaristic social policy, and the key political role was played by social democratic and christian democratic parties. Labor movements, of course, needed different allies at different times, principally small farmers and white collar workers. Different alliances, and in particular differential strength of social democratic and christian democratic parties resulted in social policy regimes with different distributive outcomes, as Stephens demonstrates. It was the alliance between labor, small farmers, and social democratic parties, for instance, that produced the basic flat rate, tax-financed citizenship pensions. Christian democratic parties tended to respond to labor pressure more with employment-based, earnings-related social insurance schemes.

In Latin America both labor and reformist parties are much weaker, and dependence on allies is more pivotal. The large informal sector and the rural population are clearly potential allies in the struggle for basic flat rate pensions and child allowances and universal public health care, as they would greatly benefit from such schemes. However, they are very poorly organized and thus difficult to forge into partners in powerful alliances. This is another reason why unions need to be strengthened in Latin America at the enterprise and at higher levels. The leading role in forging alliances among different social actors falls by default onto democratic left or reformist parties. This presents another set of difficult prospects given the weakness of parties and party systems in general and of reformist parties in particular. Nevertheless, the experience of the Workers' Party (PT) in Brazil and recent advances of democratic left parties in Uruguay, Argentina, and Mexico suggest that there is hope for political organizing efforts on the part of reformist forces to result in greater influence on policy. There are some additional signs of hope for the construction of alliances. Growing concern among the middle classes about the deterioration of social services could generate pressures for a resumption of greater state responsibility for these services. Finally, there is a growing recognition on the part of some entrepreneurs that the quality of human capital is too low and that increased investment in education alone is not the answer, as this human capital deficit is at least in part a result of the widespread poverty and lack of medical attention. This suggests the possibility of an alliance between labor, business, and reformist parties to improve transfer schemes and social services while shifting more of the burden of financing from contributions to other forms of taxation. Tax-financed programs, in turn, open greater room of maneuver for redistribution and for an extension of the schemes to the population outside the formal sector.

One question regarding possible sources of progressive forms of social policies that is being raised in Latin America is whether innovation could come from local governments that may be controlled by progressive forces, and then be adopted at the national level. Though decentralization of responsibility for social policies has gone quite far in various countries, such a scenario seems unlikely for at least two reasons. First, local governments typically do not have sufficient resources to experiment successfully with comprehensive social policies. Second, even if they did, the power constellation at the national level would still have to be favorable to shape national policy following the local example. In other words, progressive forces need to be able to extend their control over policy-making to the national level.

Pempel and Welsh (this volume) emphasize the importance of the international context for the successful pursuit of growth-oriented policies in the East Asian economies, Pempel the Cold War and the consequent favorable treatment of Korea and Taiwan by the United States, and Welsh the integration of South East Asian economies into production networks of Japanese, Korean, and Taiwanese firms. Clearly, both global and regional influences shape the effects of economic policies (see Stallings 1995). Since the 1980s, the global context has made a variety of policy instruments more difficult to wield for governments everywhere. In Latin America, this difficulty has been aggravated by the regional hegemony of the United States. American influence for a century has been working against progressive reform in Latin America at various levels directly and indirectly (see e.g. LaFeber 1984; Schoultz 1998). Most recently, the U.S. government and the IFIs under U.S. influence, like the IMF, the World Bank, and the Inter-American Development Bank have been pushing for neoliberal economic and social reforms, amounting to a general retrenchment of state involvement in the implementation of market-correcting policies, be they aimed at growth or equity. Social policy has been promoted mainly in the form of compensatory measures to smooth the economic adjustment policies, not as a coherent strategy to attack the problems of poverty and inequality. In addition, U.S. corporations are making the formation of influential reformist coalitions more difficult by opposing a strengthening of unions. The only bright spot for Latin American reformist forces in the regional context is the possibility of mustering some support from regional branches of international organizations like the ILO or branches of the UN, such as the United Nations Research Institute for Social Development or the United Nations Development Program.

The process of regional integration may stimulate growth, but it will not offer any support for equity-enhancing policies, as it is a process of pure market integration. There are even fewer efforts being made than by the European Union to coordinate social and labor market policy, since freedom of movement for labor is not on the agenda. On the contrary, regional integration can be expected to exert downward pressure on taxation and social protection as a result of greater competition among states for investment and firms forging strategies to take advantage of this competition.

The essays in this volume have highlighted in various explicit and implicit ways the importance of cooperation between the state, capital, and labor for both growth and equity. In North East Asia public-private sector cooperation was highly successful in the pursuit of competitiveness policy and in the designing of infrastructure provided by state. In contrast, the approach toward labor consisted in a combination of repression and enterprise-level co-optation, not coordination like in Western Europe with inclusion of organized labor at the enterprise and higher levels. This approach not only created a situation of stress that exploded in significant labor militancy in Korea once political liberalization had set in, but it also provided less transparency of government - private sector interaction and thus less of a check on corruption. Of course, union corruption is also a well-known phenomenon, just to mention the Peronist unions in Argentina, the unions linked to the hegemonic Institutional Revolutionary Party (PRI) in Mexico, or the Teamsters in the United States, and inclusion of labor is not a panacea against the pursuit of particularistic interests over national policy goals. The point is simply that industry-wide or national-level tripartite bodies are less likely to leave corruption unexposed.

The example of Western European coordinated market economies demonstrates that cooperation at the national or sectoral level between government, business, and labor in training and wage setting can be beneficial to all parties in facilitating growth with high levels of productivity and employment and a generous social safety net. Cooperation between business and labor at the enterprise level is supportive of productivity increases. Tripartite cooperation makes it possible to sustain a labor market regime with an emphasis on active labor market policy, an adequate minimum wage, and health and safety protection, linked to other policies designed to stimulate investment and employment and to improve educational levels of the entire labor force, which in turn is most likely to be supportive of productivity increases and workers' welfare. Such cooperation also entails the acceptance of a well-functioning tax system, which in turn makes it possible to sustain a universalistic social policy regime, with adequate flat rate minimum benefits and free health care, and thus effectively to combat poverty and inequality without damaging fiscal discipline and economic growth.

For Latin America, the achievement of such cooperation would require no less than a major institutional and behavioral transformation. After the wave of neoliberal reforms Latin America is in a way further from cooperation than it was in the 1970s. The state apparatus has been stripped of legitimacy and partly of capacity to intervene in economic development with investment promotion and industrial policies; unions have been greatly weakened; and the successful businesses have adapted to a largely unregulated market environment. The hegemony of U.S. capital and the IFIs in the region have taken tripartite cooperation and comprehensive approaches to industrial policies, labor market policies, and social policies off the agenda. Reversing this trend does not mean returning to the old patterns of cooperation and policy-making which were often very particularistic and paternalistic and had many negative effects on growth and distribution; it does mean recovering the best of the developmentalist tradition in Latin America, widening cooperation and policy coverage to make it transparent and universalistic, and learning from policies that have proven successful in other countries. If this volume can make a small contribution to this learning process, it will have achieved its purpose.

Bibliography

Barreto de Oliveira, Francisco (ed.) (1994) Social Security Systems in Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press.

Berensztein, Sergio (1998) "The Politics of Tax Reform in Argentina and Mexico." Ph.D. Dissertation, Department of Political Science, University of North Carolina, Chapel Hill.

Birdsall, Nancy and Frederick Jaspersen (1997) "Lessons from East Asia's Success." In Nancy Birdsall and Frederick Jaspersen (eds.) Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp. 1-12.

Bowman, Kirk (1991) "Should the Kuznets Effect be Relied on to Induce Equalizing Growth: Evidence from Post-1950 Development." World Development, Vol. 25, No. 1. pp 127-43.

Chang, Ha-Joon (1998) "Globalisation, Transnational Corporations, and Economic Development." In D. Baker, G. Epstein and R. Pollin (eds.) Globalisation and Progressive Economic Policy: What are the Real Constraints and Opportunities? Cambridge: Cambridge University Press.

Chang, Ha-Joon, Jae Park Hong and Chul Gyue Yoo (1998) "Interpreting the Korean Crisis: Financial Liberalisation, Industrial Policy, and Corporate Governance." Draft Manuscript.

Díaz, Alvaro (1993) "Restructuring and the New Working Classes in Chile: Trends in Waged Employment, Informality and Poverty, 1973-1990." Discussion Paper #47. Geneva: United Nations Research Institute for Social Development.

Draibe, Sônia Miriam, Maria Helena Guimarães de Castro and Beatriz Azeredo (1995) "The System of Social Protection in Brazil." Working Paper #3, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

Drake, Paul (1996) Labor Movements and Dictatorships: The Southern Cone in Comparative Perspective. Baltimore MD: Johns Hopkins University Press.

Edwards, Sebastian (1997) "Why are Latin America's Saving Rates So Low?" In Nancy Birdsall and Frederick Jaspersen (eds.) 1997. Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp. 131-58.

Evans, Peter (1979) Dependent Development: The Alliance of Multinational, State, and Local Capital in Brazil. Princeton NJ: Princeton University Press.

__________ (1995) Embedded Autonomy: States and Industrial Transformation. Princeton NJ: Princeton University Press.

Faria, Vilmar E. (1994) "The Current Social Situation in Brazil: Dilemmas and Perspectives." Working Paper #1, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

Ffrench-Davis, Ricardo and Helmut Reisen (forthcoming) "Capital Flows and Investment Performance: An Overview." In Ricardo Ffrench-Davis and Helmut Reisen (eds.) Capital Flows and Investment Performance: Lessons from Latin America. Paris: OECD Development Centre.

Filgueira, Carlos (1994) "Heterogeneity and Urban Poverty in Uruguay." Working Paper #9, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

Filgueira, Fernando (1995) "A Century of Social Welfare in Uruguay: Growth to the Limit of the Batllista Social State." Working Paper #5, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

Fishlow, Albert (1995) "Future Sustainable Latin American Growth: A Need for Savings." The Review of Black Political Economy (Summer) pp. 7-21.

Gavin, Michael, Ricardo Hausmann and Ernesto Talvi (1997) "Saving, Growth and Macroeconomic Vulnerability." In Nancy Birdsall and Frederick Jaspersen (eds.) 1997. Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp. 161-84.

Hippolito, Gabriela (forthcoming) Social Policies for the Urban Poor in Latin America.

Huber, Evelyne (1996) "Options for Social Policy in Latin America: Neoliberal versus Social Democratic Models." In Gøsta Esping-Andersen (ed.) Welfare States in Transition: National Adaptations in Global Economies. London: Sage/ United Nations Research Institute for Social Development. pp. 141-91.

Huber, Evelyne, Charles Ragin and John D. Stephens (1993) "Democracy, Constitutional Structure, and the Welfare State." American Journal of Sociology, Vol. 99, No. 3 (November) pp. 711-49.

Huber, Evelyne and John D. Stephens (1998) "Internationalization and the Social Democratic Model: Crisis and Future Prospects." Comparative Political Studies, Vol. 31, No. 3 (June) pp. 353-97.

Inter-American Development Bank (1996) Economic and Social Progress in Latin America: 1996 Report. Washington DC: Johns Hopkins University Press.

Jaspersen, Frederick (1997) "Growth of the Latin American and East Asian Economies." In Nancy Birdsall and Frederick Jaspersen (eds.) 1997. Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp.57-91.

Korpi, Walter and Joakim Palme (1997) "The Paradox of Redistribution and the Strategy of Equality: On the Role of Welfare State Institutions for Inequality and Poverty in the Western Countries." Paper prepared for the Conference on The Welfare State at the Crossroads, Sigtuna, Sweden, January 9-12.

LaFeber, Walter (1984) Inevitable Revolutions: The United States in Central America. New York: W.W. Norton & Co.

Larrañaga, Osvaldo (1997) "Eficiencia y Equidad en el Sistema de Salud Chileno." Serie Financiamiento del Desarrollo. Santiago: Comisión Económica para América Latina y el Caribe.

LoVuolo, Rubén (1995) "The Welfare State in Contemporary Argentina: An Overview." Working Paper #2, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

Lustig, Nora and Darryl McLeod (1997) "Minimum Wages and Poverty in Developing Countries: Some Empirical Evidence." In Sebastian Edwards and Nora Lustig (eds.) Labor Markets in Latin America: Combining Social Protection with Market Flexibility. Washington DC: Brookings Institution Press. pp. 62-103.

Maioni, Antonia (1998) The Emergence of Health Insurance in the United States and Canada. Princeton NJ: Princeton University Press.

Carmelo Mesa-Lago (1989) Ascent to Bankruptcy: Financing Social Security in Latin America. Pittsburgh University Press.
_________________ (1994) Changing Social Security in Latin America: Toward Alleviating the Social Costs of Economic Reform. Boulder, CO: Lynne Rienner Publishers.

Morley, Samuel A. (1995) Poverty and Inequality in Latin America: The Impact of Adjustment and Recovery in the 1980s. Baltimore MD: Johns Hopkins University Press.

Pack, Howard (1997) "The Role of Exports in Asian Development." In Nancy Birdsall and Frederick Jaspersen (eds.) 1997. Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp.227-61.

Page, John (1997) " The East Asian Miracle and the Latin American Consensus: Can the Twain Ever Meet?" In Nancy Birdsall and Frederick Jaspersen (eds.) 1997. Pathways to Growth: Comparing East Asia and Latin America. Washington, DC: Inter-American Development Bank/ Johns Hopkins University Press. pp.13-49.

Raczynski, Dagmar (1994) "Social Policies in Chile: Origin, Transformations, and Perspectives." Working Paper #4, Democracy and Social Policy Series. Notre Dame IN: Kellogg Institute, University of Notre Dame.

______________ (1995) (ed.) Strategies to Combat Poverty in Latin America. Washington DC: Inter-American Development Bank/ Johns Hopkins University.

______________ (1997) "Social Policies in Chile: Origin and Transformations." Paper prepared for the Conference on Social Policies for the Urban Poor in Latin America. Welfare Reform in a Democratic Context. Kellogg Institute, University of Notre Dame, September 12-14, 1997.

Radelet, Steven and Jeffrey Sachs (1998) "The Onset of the East Asian Financial Crisis." Draft manuscript.

Schmidt-Hebbel, Klaus, Luis Servén and Andrés Solimano (1996) "Ahorro, Inversión y Crecimiento Económico: Una Revisión de la Literatura." Pensamiento Iberoamericano 29 (Enero-Junio) pp. 107-54.

Schoultz, Lars (1998) Beneath the United States: A History of U.S. Policy Toward Latin America. Cambridge MA: Harvard University Press.

Stallings, Barbara (1995) Global Change, Regional Response: The New International Context of Development. Cambridge University Press.

Wade, Robert (199x) "Japan, the World Bank, and the Art of Paradigm Maintenance: The East Asian Miracle in Political Perspective. New Left Review. pp. 3-36.

Wennemo, Irene (1994) Sharing the Costs of Children: Studies on the Development of Family Support in the OECD Countries. Stockholm: Swedish Institute for Social Research.

Weyland, Kurt. 1996. Democracy Without Equity: Failures of Reform in Brazil. Pittsburgh, PA: University of Pittsburgh Press.

Woo, Jung-en (1991) Race to the Swift: State and Finance in Korean Industrialization. New York: Columbia University Press.