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## Latin America's Struggling Institutions Is Democracy Threatened?

Norman Gall

Latin America is one of the world's privileged regions, with abundant resources in proportion to population. It has plentiful energy supplies; few ethnic, religious or linguistic conflicts, and is far from the main areas of international tension. Democracy in Latin America was supported by a favorable international climate fostered since the 1970s, yet the advantages of democracy are reduced by the weakness of institutions. But electoral systems in Latin America have expanded and shown resilience after ending chronic inflation in recent decades, despite the weakening of political parties – a worldwide trend – and the mediocrity of political leadership.

I have been engaged in reporting and research on Latin America for the past 43 years, with lots of field work in remote regions.

There is much talk of *retrocesso* (going backwards), but the real *retrocesso* lies in the denial of progress, a denial that has become a common feature of political and economic discourse that undermines the legitimacy of evolving institutions. Societies have been modernizing much faster than public institutions. For this reason, I will suggest three priorities in public policy:

- Increase the capacity of people to manage complex societies by creating centers of excellence in education.
- Make political processes more representative and accountable.
- Expand tax revenues to sustain modern government and finance public investment.

This essay, prepared for an international conference on democracy commemorating the 16th anniversary of the Fernand Braudel Institute of World Economics, will argue that the quality of human organization to be achieved from investments in human capital and the strengthening of institutions will go far toward shaping the future of democracy in Latin America. (For our conference program, see [www.braudel.org.br](http://www.braudel.org.br)).

### 1. The Challenge of Progress

The challenge faced by these democracies today lies in the mediocrity of their economic and institutional performance. The main obstacles to further advance lie in (1) low levels of taxation (except in Brazil, which spends wastefully) that prevent them from financing the operations of modern government without resorting to heavy borrowing and chronic inflation, and (2) the maturing of their economies as a result of urbanization, imposing burdensome maintenance costs with little chance for improving productivity at present levels of organization and public



To Market, El Alto Airport, La Paz, Bolivia, 1985.

education. A new economic model is emerging, which demands a new political strategy. The future of democracy will be influenced by the quality of purpose and creativity with which these difficulties are faced in striving to sustain economic stability and broadened opportunity.

#### Weak Public Institutions

Is democracy threatened? Not immediately, but weak public institutions could undermine the broad gains of modernization. The future is promising if democratic institutions can be strengthened in coming decades to overcome failings in systems of justice, public security, infrastructure and economic regulation. These are long-term undertakings to meet needs that are widely recognized. While not overlooking these needs, this essay seeks to outline ways to improve the political mechanisms and provide the skills needed to sustain these long-term efforts. The main uncertainties facing these efforts involve novelty and persistence. As Thomas Mann argued in *The Coming Victory of Democracy* (1938): "The advantage, or the apparent advantage, of the tendencies that are hostile to democracy is, above all, the charm of novelty – a charm to which humanity shows itself highly susceptible."

The United Nations expects Latin America to enjoy moderate demographic increase over the next half-century, suffering neither from the rapid aging and population losses foreseen for Europe nor the worst ravages of the AIDS pandemic and civil wars that already are causing dramatic mortality surges in Africa. Meanwhile, the bulge in Latin

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America's young adult population (ages 15-29) is moving up the demographic pyramid, having peaked in the 1980s. In coming decades, the share of young adults in total population will fall from 28% in the 1980s to 19.7% by 2050, reducing the pressing demand for jobs seen almost everywhere today. A critical test for Latin American democracies will lie in their capacity to make successful investments in human capital that will enable them to reduce inequality and to benefit from their strategic advantages in physical resources and population dynamics. The dangers and deficiencies exposed so far by the democratic process cannot cloud its benefits. They are: (1) greater freedom, (2) more opportunities for human development and (3) more leverage by most citizens in choosing political leadership and in deciding government policy. Throughout Latin America today, there are few places where rulers are not chosen by free elections, where political debate is suppressed and where citizens fear arbitrary actions by the security forces. But problems of scale and credibility in the democratic process have not been overcome, although the organization of national states has broadened horizons as never before in human experience, thanks to technological advances that have penetrated widely.

#### Where Has All the Progress Gone?

Denials of progress often appear in studies of contemporary inequalities, either between nations or within the same society, that disregard the progress made by poor people over a time line of several decades. More and more, this denial is incorporated into the culture of international agencies under pressures from NGOs that have spawned an industry of denunciation. "Catastrofismo pays in the economics profession," says a World Bank veteran of many years of work on Latin America. "No Latin American economist will say that things have improved vastly, even where they have. Nobody will listen to them. Being a prophet of gloom and doom, on the other hand, pays off handsomely. This is vicious, as it fans the flames of populism." A target of all this scolding is the grotesquely misnamed "Washington Consensus," which was no more or less than advocacy of a return to economic fundamentals to provide a more solid base for progress by overcoming chronic inflation and restructuring the deficit-ridden public sector. Most staff members of international agencies lack the field experience that would enable them to recognize and validate this progress.

Over the past half-century the progress has been enormous. Since 1950 the population of Latin America and the Caribbean has more than tripled, while life-expectancy at birth rose from 51 to 69 years and infant mortality fell by more than 70%, from 126 per 1,000 live births. Literacy and school enrollments have expanded hugely, although the poor quality of instruction wastes a large part of public investment in education. Improved transportation enables poor people to migrate, visit and trade over long distances. Near-universal access to radio and television provides them with entertainment and information never available to previous generations. Expansion of electricity grids enabled millions of families to buy refrigerators and other domestic appliances that improved food preservation and preparation, enhancing nutrition and reducing household drudgery. The spread of cheap cell phones over the past decade developed the logistical capacity and productivity of low-income populations, especially in big cities. All these improvements have strengthened the vocation for democracy. Nevertheless, there persist classic problems of distributing power and benefits between the One, the Few and the Many that have bred tensions in civilized communities since ancient times. (See article on page 5.)

In a climate of slower growth in the world economy, Latin American democracies must address their institutional problems more purposefully to provide broader opportunities for the undeveloped talent that abides in their populations. These institutional advances would strengthen democratic practice and open new possibilities for creation of wealth. Research on institutional development recently has become a growth industry at universities and international agencies such as the IMF and World Bank, with many platitudes but few practical results. Modern research has failed to advance beyond the simple truths stated by Adam Smith in *The Wealth of Nations* (1776):

*Commerce and manufactures can seldom flourish long in any state which does not enjoy a regular administration of justice, in which people do not feel themselves secure in the possession of their property, in which the faith of contracts is not supported by law, and in which the authority of the state is not supposed to be regularly employed in enforcing the payment of debts from all those who are able to pay. Commerce and manufactures, in short, can seldom flourish in any state in which there is not a certain degree of confidence in the justice of government.*

#### "Reform Fatigue"

Latin American republics soon may be afflicted by "reform fatigue" if they fail to establish clear priorities in seeking justice and stability. Backward institutions often are entrenched in perverse incentives. We define perverse incentives as the devices of law and custom rewarding behavior that undermines the stated purpose of institutions. The crowded agenda of the 1990s put forward "first generation" and "second generation" reforms. The "first generation" reforms got rid of chronic inflation by strengthening public finances and monetary policy, opening economies to international trade and privatizing state enterprises, many of whose losses were diverting government resources from productive public investment. Huge budget deficits and hyperinflation may be a thing of the past (one hopes), but low investment and dismal public services are not.

Several "second generation reforms" have been proposed and widely discussed, creating a congested legislative agenda in the fields of economic regulation and reorganization of government services in public security, education, health, the judiciary, taxation and pensions. These "second generation reforms" are very broad in scope, involve detailed political negotiations and remain controversial in their approaches and final goals. With benign aims, they tend to overload the political system and threaten entrenched interests while lacking the urgent public support that drove the struggle against inflation over the past two decades. We need to narrow the agenda. This is why policy proposals outlined later in this essay will focus on education, political organization and taxation in order to stress the issues that are most urgent and neglected.

#### Freedom and Wider Horizons

The gains of poor people became clearer to me earlier in a recent trip to Bolivia and Peru, revisiting places where I did field research in the past. In 1970 and again in 1973, I conducted research on Peru's land reform and education reform at the remote Hacienda Lauramarca, along the dirt road that crosses the barren mountains of the Department of Cuzco and slowly descends to the jungle outpost of Puerto Maldonado, two days' journey beyond. I saw "a gray-green feudal domain stretching over 200,000 acres of rolling, windy puna of grass and stubble and glacial stone [with] a primeval and intricate confusion of stone fences, each defining the Indians' subsistence plots." The peasants had managed to build seven schools, irregularly served by government

teachers. The schoolhouse at Mallma, at the eastern edge of Lauramarca, was “a sagging, whitewashed adobe structure with two tiny windows and a thatched roof, dark and damp and windy for most of the year,” near “the white slopes of Mount Ausangate, 21,000 feet high, which holds all Lauramarca in its spiritual and ecological dominion. According to the Indians, the white mountain is a god who has abandoned its people. This feeling of abandonment haunts the people of Lauramarca, as they emerge from their traditional ways into an incipient, perhaps stillborn modernization.”

Returning to this region 30 years later, in 2003, I found big changes, mainly in terms of freedom and wider horizons. The main regional roads were paved, halving travel times between La Paz and Cuzco. Most towns now are served by direct-dial telephones and public internet booths. Telephone and internet service also now reaches Ocongate, the *municipio* to which Lauramarca belongs. With agrarian reform came land rights and freedom from feudal obligations such as labor for the landlord without pay. Electricity arrived in 1993, followed by television, inducing families to move from isolated huts to nuclear villages on the expanding network of local roads. More money circulates now in peasant communities, enlarging the national market. Primary and secondary schools proliferated in these communities, giving more people access to the printed word. “In the old days, they walked long distances along mountain paths before dawn to spread out their wares in the light of kerosene lamps at the Sunday market,” said Padre Antonio Sánchez Guardamino, a Spanish Jesuit who has been Lauramarca’s parish priest for two decades. “But now many of them have second – or third-hand Japanese cars and mini-trucks. They come to the market as late as 8:30 a.m.” In a remarkable political development, 25 peasants last August organized a hunger strike to force a judicial decision on a corruption case against the mayor of Ocongate. “They had a town meeting in 1995 because a lot of money was missing,” Padre Sánchez said. “The court case dragged on for five years, with documents going back and forth between Cuzco and Lima. Finally the *campesinos*, having spent eight days and bitter cold nights without food inside the church, got a judge in Cuzco to sentence the mayor to five years in prison.” Part of this political activity is due to the spread of secondary education in the Andes over the past three decades. While much of this schooling may be of poor quality, it was able to equip a new generation of rural leaders to exercise more influence than they could in the past. Many are elected mayors of *municipios*

formerly dominated by mestizo merchants and landlords. Meanwhile, Protestant sects spread among peasant communities, reducing drunkenness and relieving *comuneros* of obligations to spend heavily in support of traditional Catholic fiestas. Throughout Latin America, these evangelical cults have proliferated, along with religious radio and TV stations producing an incessant stream of fervent preaching. Religious fervor replaces politics in the hopes of believers.

### Rising Consumption

The expansion of institutions (however weak they still may be), improved links with the outside world and increases in consumption are even more impressive in urban areas throughout Latin America. Rising consumption by low-income people has been spectacular, accelerating

and extend credit, as information technology facilitated transactions. A survey showed how big Brazil’s low-income market had become:

- Brazil is one of the world’s fastest-growing credit card markets, with 42 million cards issued after a 19% increase in 2003. The share of low-income customers rose from 5% in 1998 to 21% by 2003, with double the rate of use of upper-income groups. Between 1994 and 2003, the use of cards in retail transactions rose by 423%, while payment with checks fell by 45%.

- The boom in consumer durables extended coverage of refrigerators (85% of all homes) and TVs (89%), largely restricting sales to a replacement market. With the world’s seventh-largest automobile output, 70% of purchases are for “popular cars,” costing about US\$7,000. In São Paulo alone, 1.5 million used cars are sold yearly, some of them for as little as US\$150.

Roughly 60% of the cars registered in the City of São Paulo are in its poor Eastern Zone.

- Brazil is the world’s second-largest market for cell phones, 60% of them on prepaid plans for low-income users, multiplying four-fold since 1999 to reach 40 million units, roughly one for every three adults, exceeding the number of fixed lines.

The Fernand Braudel Institute of World Economics is conducting field research on low-income consumption in Greater São Paulo, whose population increased from only 31,000 in 1870 to 18 million today, the fastest long-term urban growth in human experience. We see an important process of adaptation in a migrant population to a new regime of low fertility, declining chances for formal employment and rapid expansion of consumption, despite endemic violence in the metropolis, with some 12,000 armed robberies on city buses and 10,000 homicides each year. Our young researcher Maurício Santos, who lives in the peripheral region of Cidade Tiradentes, observes: “Clearly the low-income class is consuming more. The paradox



Marajó Island, Amazon River Delta, 1979.

lies in the fact that it’s easier to acquire possessions, but people don’t feel that life is easier, mainly because of the lack of jobs.” With all these difficulties, our interviews reveal attitudes very different from political discourse focused on the idea of social exclusion often identified with poor people of the periphery. Our interviews tell us of a strong trend toward adaptation and an openness to innovation.

the long-term cheapening and diversifying of consumer goods that go back to 16th Century Europe. Because of the scale of its economy, Brazil has led the way in recent consumption increases. The rich make Brazil the world’s second-market for helicopters and executive jets and the fourth producer of private planes. For the middle class and poor, it ranks third in sales of motorcycles, video rentals and the number of TV sets installed in homes. The biggest increases in consumption have been among the poor, known in marketing jargon as classes C, D and E, embracing 110 million individuals, or 69% of Brazil’s population, 77% of urban households and 40% of consumer spending. After the Real Plan stopped chronic inflation in 1994-95, economic stability consolidated real incomes and enabled manufacturers and retailers to reduce their costs

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### Urbanization and Democracy

Since first appearing in the Greek city-states 2,500 years ago, democracy always has been rooted in urban life. It spread fastest as urbanization transformed human society in the late 20th Century, along with gains in wealth, literacy and public health. Along with other less developed regions, Latin America is struggling to cope with the effects of the spectacular



*Buying and Selling, El Alto, La Paz, Bolivia, 1985.*

urbanization of world population in the late 20th Century, a one-time event in human experience that contributed to economic growth and the spread of democracy but poses daunting political and financial challenges for the coming decades. By 2000 Latin America had become more urbanized than Europe, with three-fourths of its people living in towns and cities after its urban population grew more than five-fold since 1950.

Between 1950 and 2000, world population reached six billion, multiplying 2.4 times, while the number of people living in towns and cities grew nearly four-fold to 2.9 billion, increasing the share of urban population from 30% to 48%. The number of big cities, with at least five million people, rose from eight in 1950, all in rich countries, to 39 in 2000, with nearly all the increase taking place in poorer nations. In these decades, cities like Lima, Bogotá, Cali, Guayaquil, Santo Domingo, Managua, Ciudad Juárez and Guadalajara multiplied roughly ten-fold in population. By 2000 sprawling megacities such as São Paulo, Shanghai, Cairo and Delhi each contained more people than the entire world did when agriculture was first invented, and about as many as Great Britain counted at the time of the Industrial Revolution. An extreme projection is for Dhaka, in Bangladesh, whose population grew from only 417,000 in 1950 to 13 million by 2001 and is expected by the United Nations to become the world's second-largest metropolis, with 23 million people, by 2015.

In Latin America, systems of secondary cities are developing in the larger republics to share political and economic power with the capital. For example, the number of Brazilian cities with at least one million people grew from two in 1950 (Rio de Janeiro and São Paulo) to 14 in 2001 and, according to United Nations projections, should embrace 20 cities by 2015. In the late 20th Century, giant cities surged like comets on the horizons of mankind, only for most of them to recede quickly into slower growth or stagnation. Big cities are hard to manage. They are under taxed and under funded. Like many complex systems, most cities develop spontaneously but then need management as well as investment in infrastructure and human capital to avoid degeneracy and disintegration. This is a basic problem of Latin American democracy.

Human progress in the 20th Century was bred by the complementary forces of capitalism, democracy and education. Better organization and technological advances raised productivity and enabled governments to spend more to expand webs of cooperation and dependence. Rapid urbanization since 1950 was driven by the fastest economic growth that the world ever has seen. Angus Maddison, a member of our Institute, divides the late 20th Century into two periods: a "Golden Age" (1950-73), when the world economy grew at the unprecedented annual rate of 4.9%, and a "neoliberal order" (1974-2000), when real growth slowed to 3%, which still was double the pace of expansion in the century before 1950. Meanwhile, Latin America's economy grew by 5.3% yearly in the "Golden Age" but then slowed to 3% since 1973, with annual increases in per capita gross domestic product (GDP) falling from 2.5% to 1%, a much lower rate than in any long period since 1870.

#### **Democracy and Economic Growth**

During these years of "neoliberal order," Latin America suffered through the surge of world oil prices, which slowed international economic activity, leading to heavy foreign borrowing and the debt insolvency of the "lost decade" of the 1980s. Despite great frustration, mortality continued to decline and big cities kept expanding, though at a slower rate. Governments were forced to clean up their finances to halt chronic inflation, which had surged into hyperinflation in Argentina, Brazil, Bolivia, Peru and Nicaragua. Inflation in those years provoked widespread public indignation, which undermined military regimes and hastened the spread of democracy. While there were spurts of growth in the 1990s, tensions grew with a large residue of unemployment in the cities and a shift into informal economic activity.

Despite a spurt of activity in 2003, there is little promise of faster long-term growth in the world economy. All economies have matured with the effects of aging, lower fertility, massive entry of women into labor markets, establishment of big welfare programs and nearly complete urbanization felt more strongly. Setting aside short-term risks, the maturing of economies lowers the horizons for growth in Latin America.

Many economists argue that high long-term economic growth, of at least 5% yearly, is needed to stabilize Latin American societies. My view is that high growth rates over a long period, while welcome, may not be achievable, since the high growth rates of the "Golden Age" were due to one-time events in human experience, such as urbanization and the surge of population growth due to rapid declines in mortality in the initial phase of the demographic transition. Nor are these very high economic growth rates necessary, since current rates of Latin America's population increase are barely half those of the "Golden Age" and are expected by the United Nations to fall by 2050 to roughly one-sixth of the surge levels of the decades following World War II. Major gains in per capita income can be achieved with much lower rates of GDP growth. What is needed, at any rate of economic growth, is a strengthening of institutions for more productive investment of capital and better distribution of justice, security and opportunity.

This brings into focus the vague notion of total factor productivity (TFP), used by economists as a residual to account for growth that cannot be attributed to physical inputs such as labor and capital. The TFP concept can be useful in giving weight to, if not accurately measuring, the efficiency gains in economies and societies that come with the strengthening of democratic institutions – of justice, education and security – that create conditions for more productive use of labor and capital. According to recent calculations by Samuel Pessoa of the Fundação Getúlio Vargas, the major countries of Latin America in the 1990s reversed their annual TFP losses of 1.4% of the 1980s in what may be an upward regional trend with striking national variations. Brazil, Mexico and Peru improved their TFP by roughly 3% yearly, while Venezuela and Colombia went into a downward spiral because of political turbulence.

The difficulties faced by democracies in reproducing the high rates of economic growth to which many countries became accustomed in the second half of the 20th Century poses important political questions. All answers point to a growing need for strengthening of institutions to increase capacity for management of democratic stability.

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# The One, the Few and the Many

## Republics and Democracies

Since the earliest appearance of republican and democratic forms of government, in Athens some 2,500 years ago, the unstable relationship between the One, the Few and the Many – that is, between the ruler, the privileged and common citizens – has been the focus of continuing tension and experiment. Dispute and dialogue over the One, the Few and the Many pervaded development of republican institutions in the West and today continue in Latin America. Nearly all Latin American republics recently overcame the historic problem of dictatorship (the One) by establishing orderly succession of elected Presidents, so that attention is focused now on the Few and the Many.

In modern democracies, we return continually to the dilemmas and opportunities faced by earlier republics. “It was in the Aristotelian and civic humanist channel that the stream of republican tradition was to flow,” John Pocock argued in *The Machiavellian Moment: Florentine Political Thought and the Atlantic Republican Tradition*. “The classical republicanism to which John Adams [in the American Revolution] still adhered was basically a Renaissance rephrasing of the political science set forth in Aristotle’s Politics, and it had a high degree of capacity for dealing with the social phenomena of the 17th and 18th centuries.”

The model for the city-states of the Italian Renaissance was the wealthy, imperial and aristocratic republic of Venice, which maintained political stability for six centuries under a complex formula of power-sharing under which the One, an elected Doge, ruled for life under the influence of the Few, following “the principle that that the doge should never act contrary to the advice of his councilors,” according to the historian Frederick Lane. “The throng of nobles around the doge when he took office were men accustomed to acting as judges and as his councilors. The growth of population and traffic made it necessary for every doge to have such a group to assist in the government.”

But “the little people” (*popolo minuto*) demanded more power. The *popolo minuto* were the shopkeepers and artisans that established themselves in Venice and other prospering cities, forming guilds as specialists in printing, glassmaking, jewelry, pharmacy, carpentry, shipbuilding, armaments, music, painting and other crafts and seeking a role in government, achieving political victories with parallels in the rising cities of Flanders and Germany. People rising from poverty are the engines of human progress, more so than those inheriting wealth and knowledge, who seldom are driven to discovery.

This story is repeated many times, with many variations, in the development of political institutions. Venice was a magnet for migrants that enlarged the *popolo minuto*, just as other prospering cities drew newcomers who demanded rights and powers at other times and places: Florence and other Italian Renaissance

cities; Amsterdam in the 17th Century; London in the 18th and 19th Centuries and New York and São Paulo in the 20th Century.

The “civic humanism” that emerged from the violent politics of the Italian city-states of the 15th Century revived Aristotle’s argument that “the best political community is formed by citizens of the middle class, and that those states are likely to be well-administered, in which the middle class is large, and stronger if possible than both the other classes [which] prevents either of the extremes from being dominant.”

Throughout history, these emerging classes played a critical role in shaping forms of government and the divisions of power that led to the consolidation of democracy. In contrast to modern democracies, it was hard for townsmen in the Italian city-states to avoid performing public duties. Siena in 1257 recorded 860 paid employees, excluding military, out of a male population of roughly 5,000, doing jobs ranging from night watchmen to tax assessors to keeping donkeys, pigs and lepers off the streets. Everyone paid taxes. “The fact that the numerous poor paid their small sums in

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**People rising from poverty are engines of progress, more than those inheriting wealth and knowledge.**

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direct taxes and also endured hunger and squalid surroundings is not surprising,” Daniel Waley wrote. “Taxation was for all. What seems to require more explanation is the very substantial sums paid by the powerful. To some extent this must have been due to pressure from those who ranked immediately below them in power and wealth.”

Struggles over taxation formed the crucible shaping new political institutions in the West. States nearly always seek to live beyond their means. Pressures for more and more taxes arose mainly from the cost of wars, including the interest on loans to pay for them. Each new advance in military technology, making warfare more expensive, brought innovations in public finance. The creation in 1265 of the first funded public debt, the Monte Vecchio, mostly an accumulation of forced loans, roughly coincided with advances in ship construction, navigation and naval armaments that enabled Venice to expand and protect its trade empire. These financial devices spread quickly to other Italian cities. Several of them, at war with each other, desperately sold offices, taxed heavily and raised forced loans to avoid being sacked by their mercenary troops who had not been paid.

According to William McNeill, “efficient tax collection, debt-funding and skilled, profes-

sional military management” made the difference in Europe. “States that lagged in developing an efficient internal administration of armed force, like Florence and Genoa, continued to experience sporadic outbreaks of civil violence. Venice, the most successful innovator in the management of armed force, entirely escaped domestic upheavals, through it barely survived external attack provoked by the Republic’s long series of diplomatic and military successes on Italian soil.”

The warlike monarchs of France and Spain, drawing upon the resources of larger states, taxed and borrowed even more as their growing armies, using more advanced cannon in what became known as the Gunpowder Revolution, ended the sovereignty of Italy’s city-states. Over 200 years the size of armies deployed in battle grew tenfold. In the 18th Century, Britain was almost continuously at war. To pay for these wars, annual tax revenues more than tripled and public debt grew 15-fold. In *The Sines of Power: War, Money and the English State, 1688-1783*, John Brewer explains how Britain laid the foundations of modern public finance with administrative reforms that increased transparency and gradually reduced corruption thanks to “undisputed powers of national taxation; the presence of a commercialized economy whose structure made it comparatively simple to tax, and the deployment of fiscal expertise that made borrowing against tax income an easy task.... Public creditors invested in public securities precisely because they were secure.”

To pay these debts, a highly-trained corps of tax collectors was organized: “The work performed by these excise officers was technical, complex and time-consuming. Entrants to the service were required to pass both a written and practical test and to complete a period of pupillage.... Carrying their books, seven instruments, pen and special inkpot attached to their lapels, officers often worked long hours. Their supervisors worked for even longer.” Institutional developments like these, driven by pressures of warfare on an ever-larger scale, enabled western governments to harvest increasing shares of national income as taxation, first to pay for wars and more recently to finance democratic welfare states.

As societies became more complex, absolute monarchs had to share power with emerging interests, hastening evolution toward national democracies. Eventually, universal public education, health care and pensions became basic rights. As a share of GDP, general government spending rose in the rich countries from roughly 13% in 1913, on the eve of World War I, to 46% by 1996. While Latin American republics tried to keep pace with the rich countries in assuming the responsibilities of modern government, they have not been able to mobilize the resources needed to perform these functions by the standards of the western democracies that they emulate.

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Siglo XX tin mine, Catavi, Bolivia, 1966.

## 2. Democracy in Latin America

The strength of Latin American peoples' vocation for democracy has been proven by recent experience. Brazil since 1989 conducted several orderly and clean elections for President as well as for state and local offices, becoming a worldwide pioneer in electronic voting. Argentina provides a tragic lesson of how populism and chronic inflation can destroy the social and economic fabric of a prosperous country. Populism in Argentina has been promoted by the Right and the Left, by civilian and military regimes, producing spiraling disorder. However, over the past two decades, Argentina persisted in seeking democratic solutions despite hyperinflation, collapse of dollar convertibility and the failures of the Radical and Peronist parties. Chile restored and consolidated democratic practice, with skillful economic management during three Presidential administrations since 1989, after the inflationary disorder of the Allende years and then 16 years of military dictatorship.

Peru may have made a low-level adjustment, with acute dissatisfaction, in its struggle for stability. But mortality rates continue to decline. Recorded levels of personal violence are low. The big urban problem, of course, is jobs, but this problem remains unsolved by all but a very few rich or poor countries. Meanwhile, after living through the convulsions of hyperinflation, a guerrilla insurrection, the *El Niño* and Fujimori's *autogolpe* and flight into exile, Peru's people have chosen a return to democracy with low inflation and a stable currency. Guatemala's fragile democracy was threatened by the menacing tactics of a former dictator, General Efraín Ríos Montt (1982-83), who presided over one of the bloodiest massacres in Latin America's history, in seeking election despite a constitutional prohibition excluding former dictators from public office. Ríos Montt's bid for a political comeback was rejected decisively

by voters in the first round of an election that awarded the presidency to Oscar Berger, a conservative former mayor of Guatemala City. In Venezuela, a struggle continues over efforts by opponents of leftist President Hugo Chávez, a friend of Fidel Castro and Colombia's guerrillas, to oust Chávez by either constitutional referendum or violent means to end economic disorder and decline. A deal brokered by foreign mediators, under the aegis of the Organization of American States (OAS), provides for a recall referendum under a clause inserted in Venezuela's newest constitution by Chávez's followers.

According to Joseph Schumpeter, "the democratic method is that institutional arrangement for arriving at political decisions in which individuals acquire the power to decide by means of a competitive struggle for the people's vote." In Latin America, this democratic method has been applied widely over the past two decades in the decentralization of governmental powers, with direct election of governors and mayors and increased transfer of revenues to states and municipalities. Since 1980, the number of republics providing for direct election of mayors rose from three to 17.

Participation in politics has increased by creating thousands of elected positions in provinces, states and municipalities. However, governmental decentralization also has meant a power shift that has weakened national parties and led to proliferation of local movements, that in many cases expanded and strengthened civil society. The 163 seats in Colombia's Chamber of Deputies are spread among 39 parties, mostly representing regional and specific policy interests and ending the traditional hegemony of the Liberals and Conservatives. In Bolivia, the Popular Participation Law of 1994 provided for direct election of 310 mayors and councils and for transfer of 20% of central government revenues to these municipalities. Five local and indigenous parties won 64 of the 130 seats in Bolivia's Chamber of Deputies in

the 2002 elections. In Venezuela as in Colombia and Bolivia, much of this governmental decentralization was enacted as a defensive measure by traditional parties to strengthen the legitimacy of the political system, producing unexpected results that still are being assimilated. However, broad public support for these innovations has been sustained despite recent political turbulence.

The modern history of democracy embraces periods of expansion and retrenchment. A decade ago, in *The Third Wave: Democratization in the Late Twentieth Century*, Samuel Huntington identified three phases in the spread of democracy since the French Revolution and Napoleonic Wars. By 1926, democratic forms of government were established in 33 countries, followed by a period of relapse into authoritarian rule in 22 countries during the two decades that ended in World War II. The Great Depression interrupted democratic government in 11 Latin American countries. A second wave of democratization (1945-62) added or restored 41 countries to the roll of democracies in the world, after which another relapse, lasting until 1975, again truncated democratic government in 22 nations. Since then, democracy has flourished as never before.

The "third wave" of democratization began in the mid-1970s with a leftist military revolt against the old Portuguese dictatorship's handling of its colonial wars in Africa; with peaceful transitions from dictatorship to democracy in Spain and Greece, and with adoption by Brazil's military regime (1964-85) of a new policy of "slow and secure" *distensão* (decompression) that led to a return to civilian rule. Many of these transitions to democracy, in Latin America and Eastern Europe as well as in Spain, Turkey and South Korea, mobilized conservative leadership. In Brazil, civilian politicians supporting the military regime continued in key roles after 1985 in a revitalized Congress and as ministers, exploiting institutional weaknesses to shift allegiances and

develop new opportunities with each change of government. According to the 2002 United Nations Human Development Report, 81 countries took “significant” steps toward democracy since 1980, with civilian governments replacing 33 military regimes.

Much of this progress was engendered by benign changes in the international climate. The spread of democracy was reinforced by globalization and increased access to information. In Latin America, much has been made of the pivotal role of the United States, which in the past has been criticized for failing to promote democracy. However, in recent decades this has changed. In 1974, the U.S. Congress began to show increasing concern about human rights violations, a theme quickly adopted by President Jimmy Carter as a key foreign policy issue. In 1984 the Reagan Administration created the National Endowment for Democracy. Later that year Julio Maria Sanguinetti, following his inauguration as the first elected President of Uruguay since 1971, said: “The vigorous policies of the Carter Administration were the most important outside influence on Uruguay’s democratization process.” U.S. diplomats intervened to warn against military coups in Peru, El Salvador, Honduras and Bolivia, as well as in Korea and the Philippines, and were active in promoting and restoring democracy in the Dominican Republic, Portugal, Chile and Poland, among other countries. More recently, neighboring countries banded together to stop a military coup in Paraguay. On September 11, 2001, the General Assembly of the Organization of American States, meeting in Lima, Peru, adopted an Inter-American Democratic Charter that provides for diplomatic machinery and procedures to restore democracy “in the event of an unconstitutional alteration of the constitutional regime that seriously impairs the democratic order in a

member state.”

Under these improved conditions, the Third Wave since 1974 has spread democracy more prolifically than earlier ones, helped in many ways by the United States. In Latin America, democracy has continued to expand, without reversals, in contrast to the experiences of Turkey, Pakistan, Thailand, Nigeria and other African countries. Democracies in Latin America have dealt more effectively with chronic inflation than military regimes and have gained support as a result.

#### Support for Democracy

A survey of 17 countries by Latinobarómetro, a Chilean polling organization, was summarized by *The Economist* (August 17, 2002), finding some hopeful signs: “Despite the economic turmoil gripping many of their countries, Latin Americans are becoming somewhat more supportive of democracy, but they have little trust in political parties and believe that corruption is widespread and worsening. They have lost faith in privatization, and want the state to take a more active role in regulating the economy, but in most countries they have not moved more generally to the left.” People remain largely centrist, shifting to the right since 1996 only in the most turbulent countries (Colombia, Guatemala, Honduras, El Salvador, Nicaragua, Venezuela). Only in Paraguay did more than 30% prefer authoritarian rule.

When the Latinobarómetro poll was repeated in 2003, it showed substantial year-to-year volatility and a decline since 1996 in those endorsing the proposition that “democracy is preferable to any other form of government.” But nearly two-thirds still said that democracy is the best form of government and the only path toward development, with 57% saying that development can only be achieved through a market economy. Indeed, 44% said that large companies are performing well in building a

better society and 51% found that executives of these companies could provide better leadership than the present political class. But there also was much ambivalence. In Brazil and Peru, 69% and 60% saw democracy as best, but nearly as many said that they would accept authoritarian rule if it would solve economic problems. Throughout Latin America there is great fear of unemployment, with 23% saying they have difficulty making ends meet. Of those in economic hardship, 47% supported democracy, against 57% of those who can save from their earnings.

Although scholars have produced a vast literature on the nature and prospects of democracy, Kurt Weyland of the University of Texas notes: “Political science has not advanced a unified, coherent theory of democratic stability.” The expansion of Latin American electorates came with long-term urbanization. In Peru, the number of votes grew from only 324,000 (5.5%) in a population of six million in 1931 to 12 million (46%) out of 26 million in 2001. In 1931, illiterates were excluded. Voters were mainly *mestizos* with little schooling. In rural Amerindian regions, few voted: only 14,000 in Cuzco (surging to 458,000 in 2001) and only 10,000 in Puno (reaching 522,000 in 2001). Since voting started in 1850, electoral fraud was common.

Violence and vote-buying were organized by candidates hiring mobs from among the urban poor to take balloting places by force. Rural landlords, doubling as political bosses in many countries, herded peons and other dependents into polling stations. In Brazil, control of judges and police chiefs decided elections. In 1872, only one million of nine million Brazilians were eligible to vote and only 20,000 did so. According to Richard Graham, “elections and violence often went together. While the result of elections often could be easily predicted at the national level, local struggles for certain men were of



To School, Collique, Lima, Peru, 1973.



Entering the mine, Siglo XX, Catavi, Bolivia, 1966.

desperate importance.” Losers often were persecuted and winners gained patronage and influence above and below their station in the hierarchy. The total of federal, state and local jobs in 1920 was about 200,000, which equaled the votes needed to win the 1919 presidential election.

Given this history, it is extraordinary that Latin American electorates grew so fast over the past two decades with so few incidents of fraud and coercion. Since 1945 Brazil’s electorate grew 19-fold, from 5.9 million to 119 million. Fiscal parasitism expanded with growth of the political system. The numbers of the Few multiplied, under bizarre election rules that leave them unaccountable to the Many for long periods. Between elections, politics tended to be reduced to exotic and arcane machinations within what became known as “the political class.” The costs of competition and the quantity of insiders increased as parties in Congress proliferated, with individual politicians flying flags of convenience. After Brazil’s 2002 elections, one-fifth of the members of the Chamber of Deputies switched parties to align themselves with the winning side. From the mid-1970s until 1994, deformities in the political system were financed by foreign borrowing and chronic inflation. Under the Real Plan (1994-99), efforts to correct these deformities were funded by increased taxation as well as by foreign money. This mix is still unstable.

#### Reversals and Frustrations

Reversals in the democratic process can be expected. In its first 150 years as a republic, Bolivia suffered 170 military coups. Along with the rest of Latin America, Bolivia recently achieved government by consent of the governed, a precious heritage of western civilization, in contrast to the military rule that prevailed in most of the region in the 1960s and 1970s. Bolivia enjoyed two decades of constitutional democracy since 1982, embracing six orderly successions by freely-elected Presidents. It overcame hyperinflation to gain

stability of its currency and prices. Over the past two decades, infant mortality was halved, school enrollments grew fast and networks of transportation, communications, electricity and basic sanitation expanded dramatically to raise living standards in a very poor country. However, President Gonzalo Sánchez de Lozada, who headed the effort to end hyperinflation in the 1980s and carried out major political reforms in the 1990s, was forced to resign in October 2003, after a bloody popular revolt marked by street battles and road blockades ended his efforts to reduce a huge public deficit (8.5% of GDP) while seeking to negotiate the claims of coca farmers, landless peasants and unemployed workers from the collapsed state mining industry. None of these claims have been satisfied. The Bolivian sociologist Roberto Laserna calls this “a populist trap.” The political banner of the revolt was protest against exporting natural gas through a port on the desert coast of

Chile, which wrested the territory from Bolivia in the War of the Pacific (1879-84), leaving Bolivia with no access to the sea. The October revolt deprived Bolivia of its chance to become a major hub of energy supplies in the Americas, providing its government with a secure, long-term flow of badly needed hard currency.

The climax of the revolt was the blockade of La Paz at the entrance to the capital at the suburban community of El Alto, cutting off food and other supplies. When I first visited La Paz in 1965, El Alto was little more than a cluster of adobe huts beside the airport, at the edge of the altiplano. By the time I did a detailed study in 1984-85 for the World Bank, *El Alto de La Paz: The Origins and Prospects of Poverty in Bolivia*, El Alto was becoming an independent municipality of 300,000 people. When I returned again in 2003, El Alto had become a major actor in national politics, with a population of 700,000. This fast growth was not simply the swelling of poverty.

This is not a city sinking into hopelessness and destitution. El Alto embraces impressive infrastructure development, commercial expansion and solid home construction. But its growth is based on an informal economy in which petty traders compete fiercely with each other and travel laboriously at low cost, in trucks and buses, far and wide in Bolivia and neighboring countries to exploit differences in local prices, free of regulation and taxation, a trade that flourished in recent decades with improved transportation. While few taxes are paid, demand for public services grows fast. El Alto’s brand of populism is embodied in the new Congress, roughly half of whose members are of indigenous Aymara and Quechua stock. Yet its revolt leaves Bolivia adrift economically and politically, again deeply wounded by the weakness of its institutions.

Over the past two decades, Mexico’s political regime evolved from an overpowering Presidency to a limited Presidency, now forced to share power with a Congress and state



Trikki Indian girl, Oaxaca, Mexico, 1967.



governors beyond its control; from a one-party system sustained by manipulated elections to a multi-party system with free elections. The three year-old Mexican government of President Vicente Fox ended 70 years of one-party rule by the Institutional Revolutionary Party (PRI). In Mexico as in Brazil, changes in both the political and financial systems were triggered by the debt crisis of the 1980s. When Mexico defaulted on its huge foreign debt in 1982, its public deficit had reached 16% of GDP and nobody knew how much the government was spending or how much it owed. According to Hector Aguilar Camín, “Mexico has a State that spends like a millionaire and collects taxes like a beggar, with many responsibilities and little income. The State is a specialist in not collecting what it should collect so as to avoid political problems with those who owe taxes.” As in Brazil, the reorganization of public finances and democratization of politics went together in a process that still continues. Fox and his National Action Party (PAN) suffered major losses in mid-term Congressional elections in July 2003, reflecting their failure to break a legislative deadlock in order to fulfill their campaign promises of freeing the economy and accelerating growth. They have maintained economic stability but are stalemated in tax reform and in establishing clear rules to attract private investment to overcome severe shortages in the electricity sector.

The revival of democracy in Peru came with the election in 2001 of President Alejandro Toledo, a Stanford-educated economist of Indian stock who succeeded Fujimori’s corrupt and authoritarian rule. Toledo’s support soon fell to 7% in opinion surveys. His discredit has been blamed on weakness of character, to raising his salary to \$18,000 monthly amid widespread poverty and to carrying on a well-publicized night life while refusing to recognize a teenage illegitimate daughter despite pleas for DNA tests. Toledo faces hard budget constraints, with tax receipts only 12% of GDP. The benefits of fiscal and monetary stability and recent economic growth are undermined by a stream of petty corruption scandals and by what some observers call an “explosion of democracy.” Fiscal austerity worsened frustrations associated with decentralization of governmental authority and aggressive mobilization of civic and interest groups, leading to road blockades and a one-month national teachers’ strike.

The Cuzco summit of Latin American Presidents issued this warning: “The increase and worsening of poverty, aggravated by a new period of prolonged economic stagnation, constitutes a fundamental threat to democratic governability, leading to deterioration of institutional stability and social peace.” But *Caretas* magazine commented: “The Peruvian case is different because it is not accompanied by an economic crisis as in other nations. On the contrary, inflation is minimal, the exchange rate of the currency is stable, the economy and hard currency reserves have grown and certain important investments in mining and gas are promising. Nevertheless, the popularity of President Toledo has fallen like a stone and the credibility of public authorities is declining. ... We face a contagion of frustrations, provoked not only by the secular misery of large swaths of the



Lázaro Cárdenas, President of Mexico (1934-40), Oaxaca, 1967.

population and by socioeconomic inequalities, but also by irritations planted by the government itself. Grandiloquent promises breed indignation when not fulfilled and hand battle flags to the opposition.”

#### Dissatisfaction and Citizenship

Can political dissatisfaction be seen as a sign of progress? “Disillusion with democratic rulers and nostalgia for authoritarian ones were an essential first step in the process of democratic consolidation,” Huntington wrote in *The Third Wave*. “Democracy does not mean that problems will be solved; it does mean that rulers can be removed. ... Disillusionment and the lowered expectations it produces are the foundations of democratic stability. Democracies become consolidated when people learn that democracy is a solution to the problem of tyranny, but not necessarily to anything else.”

The end of easy financing, from chronic inflation or foreign loans, places new burdens on the tortuous development of citizenship. Here we confront the evolving entanglements of the One, the Few and the Many that enlivened politics after the Independence Wars of the 1820s. Brooke Larson wrote in her magisterial essay on Andean peasants and nation-making in the 19th Century:

*Reforms gradually paved the way toward exclusivist political systems, fragile civil societies and incipient capitalist economies. Implicitly reforms were governed by a dual set of goals: to bring Indians into the economy as subsistence laborers, but to lock them out of the nation as citizens.*

In many Latin American countries, rule by one clique or another prevailed long after Independence and denunciations of “oligarchy” survived through the 1960s. However, Latin American oligarchies rarely were monolithic and often fought among themselves, as did the “magnate” families in the cities of the early Italian Renaissance, leading in most cases to endemic instability. In Colombia since the mid-19th Century, it has been common to speak of a “Liberal oligarchy” and a “Conservative

oligarchy,” but these labels were blurred by regional differences, family feuds and local rivalries that often turned violent.

Since Independence, the Spanish American republics proclaimed affinity with the political ideals of the French and American revolutions, but citizenship remained a problem. Brazil was the last nation in Latin America to abolish slavery (1888), but was no worse on issues of citizenship. Brazil’s monarchy was overthrown in 1889 by a military coup in a climate of public indifference. In 1891, the constitution of the First Republic (1889-1930) abolished the State’s obligation to provide primary education, an unfunded and unfulfilled legal mandate on the books as a dead letter since 1824. The historian José Murilo de Carvalho explained how political rights lagged behind social legislation, beclouding issues of citizenship: “The People had no place in the political system, neither under the monarchy nor the Republic. For them, Brazil was an abstract reality.”

Starting in 1930, social legislation leaped ahead of political rights under Getúlio Vargas, who dominated Brazilian politics for many years, in phases of revolutionary reform (1930-37), the *Estado Novo* dictatorship with fascist trappings (1937-45) and electoral democracy (1950-54). In *Father of the Poor? Vargas and his Era*, the late Robert Levine, a member of our Institute, posed in a masterful way the contradictions of populism and dictatorship, even as Vargas “personally shaped the modern Brazilian state” and became “the first politician to extend dignity to the Brazilian people.” As government grew at all levels, Levine wrote, “Vargas organized regional agencies to deal with drought, electric power and commodity production. Decrees prepared the way for civil service reform and a national minimum wage.... The government awarded pensions to selected workers, as well as job protection and workers’ compensation. A federal university system was started.... The country’s new roads led to jobs, leading to massive migrations of population, whereas decades earlier few ventured beyond their birthplace except when driven by famine.” Yet Vargas’s strongman rule distorted and truncated political institutions,

as did the two decades of military rule that followed the class struggles of the 1950s and early 1960s.

After military rule ended in 1985, the civilian political class enacted a new Constitution that enlarged, on an unsustainable scale, the social legislation pioneered under authoritarian governments to compensate for repression of political rights. After his election in 1994, President Fernando Henrique Cardoso announced that his administration would represent ‘the end of the Vargas era’ in Brazilian history. Cardoso meant that he hoped to curb the state domination of Brazil’s economy and the acquired rights of corporatist interest groups, both of which fed chronic inflation. Cardoso sought to erase the stigma of inflation that afflicted Vargas. According to Levine: “Pensions, a cornerstone of Vargas’s social program, were so eaten away by inflation that by the 1950s in many cases it was not worth the cost of a bus fare for pensioners to pick up their retirement checks.”

From 1960 to 1992, world prices multiplied 17 times, the worst global inflation ever recorded for a similar period. During those decades inflation in Latin America became such a chronic disease that its consumer prices multiplied not 17 times but 14 million times their 1960 level by 1992, while Brazil’s price level multiplied 22 billion times since 1960. In the annals of world inflation, no other country had lived so long (34 months) with monthly price increases above 20%, thanks to techniques of indexing wages, prices, taxes, debts and bank balances. Indexation worked until the infernal machine of inflation accelerated and threatened to race out of control again in 1994. Under the threat of hyperinflation, Cardoso gained his political triumph by launching the Real Plan, Brazil’s eighth try at stopping inflation since 1985, which ended indexation, reorganized public finances and cut annual price rises from 5,115% in mid-1994 to nearly zero in 1998. Other democratic governments, in Chile, Bolivia, Peru and Argentina, have subdued chronic inflation in the 1980s and 1990s, a historic achievement.

### 3. The myths of Lula

The new government of President Luiz Inácio Lula da Silva and his Workers’ Party, or Partido dos Trabalhadores (PT), will test the strength of democracy, as well as the competing appeals of populism and effective government. So far, its efforts have focused on a basic truth: The Brazilian people will not accept a return to the inflation and instability of the 1980s and early 1990s. A corollary of this truth is that people want better government, which the PT is finding hard to provide. However, its success so far in controlling inflation and restoring international credit, as well as the sympathy inspired by the new President, a man of the people preaching redemption from hunger and poverty, has muffled political opposition.

Lula has attracted more international attention than any Latin American leader since the rise of Fidel Castro in Cuba in 1958-59. He became a symbol of social mobility in a nation of 175 million people that is now one of the world’s most dynamic markets. A sensation was created by the election to the presidency of Brazil of a former lathe operator and union leader from São Paulo’s ABC industrial suburb, with only a fifth-grade education, born in extreme poverty in the back country of Brazil’s drought-prone Northeast.

Fifty years after migrating to São Paulo as a seven year-old boy in the back of a crowded truck called a *pau-de-arara* (parrot’s perch), Lula won a runoff election in October 2002 with a majority of nearly 20 million votes, in the biggest landslide in Brazil’s history, mastering the art of campaigning in his quest for the presidency after three previous defeats. With a big lead in the polls since the start of the campaign, Lula and the PT frightened financial markets in a program presented in April 2002 by his future Finance Minister, Antônio Palocci, promising a “necessary rupture of the present economic model, based on opening and radical deregulation of the national economy and its subordination to the interests and humors of

globalized financial capital.”

In June, Lula toned down this pledge of rupture in a Letter to the Brazilian People with promises of low inflation and fiscal prudence, mixed into an inspired media campaign that radiated indignation, confidence and, yes, happiness. But financial markets still feared the worst. The risk premium on Brazilian bonds rose from 700 to 2,400 basis points (24% above interest on U.S. Treasury bonds). The value of the real fell from R\$2.35 to nearly R\$4 to the dollar. But by the end of 2003, the new government clawed its way back to stability. Annual inflation fell to 9%, the real strengthened to \$2.90 and the risk premium fell to 468, its lowest level since 1998. The price of this consolidation was interest rates that peaked at 26.5% and government spending cuts that provoked a recession and rising unemployment. Despite his rejection of “*continismo*, open or disguised,” Lula so far has pursued the same fiscal and monetary policies as the previous government. His reward has been more trust by Brazil’s people and adulation on his many foreign journeys.

Since he took office in January 2003, Lula has spent more and more time making speeches and traveling while leaving the management of government, and messy dealings with Congress on his reform program, to a nucleus of aides in the Finance Ministry and presidential palace. According to *La Razón*, a Bolivian newspaper, Lula is “the new Latin American political star.” His state visits have taken him to India and several Latin American republics; to the World Economic Forum in Davos, Switzerland; the G-8 summit in France; to the United Nations; four meetings with President Bush; five countries of sub-Saharan Africa and another five in the Middle East (Libya, Syria, Egypt, Lebanon and the Gulf). He was the main attraction at the meeting of Latin American Presidents in Cuzco, Peru. When he lectured in July at a conference on Progressive Governance at the London School of Economics, outshining the other participating presidents and prime ministers, the clamor for tickets was such that it was moved to from a 400-seat amphitheater to an auditorium for 1,000 people, while 500 more watched outside on closed-circuit TV outside. “Lula wants to change Brazil, but I seriously think that he can change the world,” rhapsodized Anthony Giddens, LSE’s president and a leading sociologist.

After his London triumph, *O Estado de S. Paulo* explained editorially that “Lula does well in the palaces of the world because his personal history fascinates the dignitaries with whom he comes into contact. An aura of curiosity and respect surrounds him, which no other leader of today seems to deserve. He also benefits from the stereotyped vision of Brazil that prevails abroad. Those who imagine that Brazilian society is rigidly stratified, offering poor people few opportunities to advance, have more cause to embrace with such good will a President with Lula’s biography, who speaks only Portuguese. Foreigners even are charmed by the blunders that his loquacity and love of improvisation tend to produce.” In October Lula was in Spain, receiving the Prince of Asturias prize for “his commitment to the needy that makes him a model for the world.” His message in



Traffic cop, Caracas, Venezuela, 1969.

speech after speech was: "Ethical development demands that the international community show solidarity with marginalized people. So I will keep fighting for a global fund to eradicate poverty." During his first year as President, Lula spent 185 days away from Brasília, 68 of them on foreign trips, making 236 speeches but giving no press conferences. His handlers aggressively isolate Lula from informal contacts with the media.

Lula seemed to enjoy all this traveling around, making speeches and receiving adulation. But now the fun is over. Lula knows that the novelty and charm of his electoral triumph will mean little if he fails to produce results for his people. A consensus across the political spectrum holds that, while economic stabilization has been successful, social policy has been failing. Recognizing these first-year failures, Lula and the PT carried out a cabinet reorganization in January 2004 to bring more experienced manager into the government and to consolidate their support in Congress. Meanwhile, the PT is struggling to deal with the effects of a sordid scandal involving the kidnap-murder in January 2002 of Celso Daniel, the PT mayor of the São Paulo suburb of Santo André, who was slated to be Lula's campaign manager. Daniel's murder has been linked to disputes over siphoning of campaign funds from Santo André to the PT, involving senior party leaders who now are key members of Lula's presidential staff in Brasília.

In his inaugural speech, Lula announced a food security program, *Fome Zero* (Zero Hunger): "We will end hunger in our country. We will transform the ending of hunger into a national cause.... We will give special emphasis to our *Primeiro Emprego* (First Job) project to create opportunities for young people who face such difficulty in entering the labor market." *Fome Zero* became the political banner of the new government's first months, but it was basically a recreation of existing programs that for many years have distributed food, cooking gas, school allowances and other resources to poor communities throughout Brazil. Promoted with aggressive marketing and worldwide publicity, *Fome Zero* sank into bureaucratic confusion and underwent a series of reorganizations that still continue. The federal government spends 66% more for lunch money (*auxílio-alimentação*) for 656,000 public employees than it spends for the millions of poor people supposedly benefiting from *Fome Zero*.

After a year in office, the government has been unable to announce a strategy for its First Job program. In the 2002 election campaign, Lula promised to create 10 million new jobs while his main opponent, José Serra, pledged to create eight million jobs, a kind of vow often made by politicians in Latin America and elsewhere. These populist promises are empty, since governments cannot create jobs for millions of people. They only can create better conditions for employment. Brazil lost 20% of its factory jobs since 1994 in a worldwide shrinkage of industrial employment, as firms produce more goods with fewer workers. Informal employment is growing throughout the world, especially in Latin America with its rigid labor laws, high payroll taxes and low levels of education. People are searching for new kinds of activity. Many show great ingenuity in this search. Government



Schoolgirl, Lima, Peru, 1973.

can support their adaptation to new conditions by providing better education, more flexible labor markets and economic stability, part of a broader program of institutional development.

Lula takes great pride in becoming President with only five years of schooling, and may feel that other poor people can do likewise, which has led him to neglect public education, the main instrument both for developing institutions and advancing social justice. Brazil's pupils ranked last among 15 year-olds in 32 countries tested for reading comprehension in 2000 by the Organization for Economic Cooperation and Development (OECD). The Education Ministry's National System for Evaluating Primary Education (SAEB) found no gains in pupil learning since 1991. Of every 100 Brazilian pupils who begin the eight years of primary school, only 41 finish, despite huge increases in enrollments over the past decade. Nearly one-fourth of Brazil's adult working population in 2000 had not finished the fourth grade. Three-fourths of those earning at or below the monthly minimum wage (US\$83) had not finished primary school. Lula likes to ridicule intellectuals, which may seem strange, since there are so many intellectuals in the PT. "I say that politics has no secrets," he said in Brasília a few days before his LSE speech. "If there's one thing that nobody needs to know about politics, it's a university degree."

Despite his educational handicap, Lula could become a great Education President by striving to improve Brazil's failing public schools. To achieve this, he would have to embark on the difficult political task of pressing the educational establishment to strengthen school management and supervision, improve teaching of reading in the primary grades and enrich the content of secondary education. To do this, the government would have to lead institutional change on a very large scale, involving many millions of students, teachers, administrators and parents. It also would have to overcome the traditional resistance to innovation in several key areas of public policy of entrenched interests in teachers' unions and universities, which have been

mainstays of PT support, along with other public sector workers.

If Lula were an educator, he would go on television to give the Brazilian people a simple arithmetic lesson in support of his ambitious pension reform, the effect of which was reduced by Congress, saying: "Brazil spends 12% of all its production of goods and services on pensions. The big deficits go to pay for public employees retiring early. This is a disgrace. It is roughly what European countries pay for pensions for much older and richer populations. If we can cut pension spending by only 1% of GDP, then we could increase spending per pupil in primary and secondary education by more than 25%. Today Brazil spends only \$150 per year for each pupil in the Northeast and \$400-\$500 in Rio de Janeiro and São Paulo. What can we achieve by spending such miserable sums on our children's education? Do we care so little about the future of our children and our country?"

Lula and the PT have been slow to recognize the problems of institutional development, as well as the progress achieved by previous governments. Most of these problems lie outside the electoral calendar and take time to solve. Failure to attack these problems tends to reduce public policy to denunciation and charity. Yet important electoral gains could be harvested by Lula and the PT if they made government more ecumenical by seeking consensus on key issues, like education and public security, and recruiting more capable people from different sectors and parties to devise and carry out long-term policies to be carried out by successive administrations. They already have done this in the effort to control inflation, with great political benefit.

#### 4. Institutional Development

For all his revolutionary rhetoric of the past, Lula is being assimilated by the metabolism of Brazilian politics. Yet he is making democracy more ecumenical in recognition of recent gains in social mobility. Lula saw what Brazilians wanted: stability with more social justice. The struggle is only beginning. It is too early to

predict the outcome. The tensions between populism and effective government in Brazil feed into broader issues faced by democracy in Latin America. The demands of stability, security and opportunity are frustrated by failure to develop institutional capabilities to deal with fiscal constraints, entrenched privileges and misallocation of resources. Here are some ideas on how to overcome obstacles to institutional development in the critical areas of public education, political organization and taxation.

#### 4.1 Centers of Excellence in Education

Around 1960, in 14 Latin American countries, only 1.7% of children of school age finished primary school. Despite the idealism invested in rural education by the Mexican Revolution, four-fifths of Mexico's 20,000 rural schools had only three grades. In Guatemala, only 5.2% of rural children reached the third grade. Of the 12.7 million children in rural Brazil, only five million were in school. Of those in school, most dropped out in their first year. In *Ten Keys to Latin America* (1962), Frank Tannenbaum explained the tasks facing governments trying to meet modern educational needs:

*The central government must find, build, rent or appropriate schools for the 50% or more of the school population now without schools. It must find, educate and draft double the number of teachers it now has and place them on the national payroll. It must print twice as many books and notebooks, procure twice as many pencils and blackboards. It must double the number of school inspectors, bookkeepers, clerks, supervisors and normal schools for the training of teachers. It must do all this and a great deal more, and it must do it in a hurry....The means must be found to double the education budget, although in some countries it already is large.*

Four decades later, these gigantic tasks mostly have been accomplished, even if at dismal levels of quality. While schools, teachers and education bureaucracies have materialized, pupils still fail to learn. Was this enormous investment a wasted effort? Probably not, since public schools have provided socialization and access to learning that, while grossly deficient, would not otherwise been available in stressful urban environments swollen by migration from rural areas. But Latin American schools clearly are failing to produce the critical mass of educated people needed to manage complex societies and to start new enterprises that would create jobs and accelerate economic growth. The minds of its next generation of citizens are exposed to the incompetence of underpaid and untrained teachers.

In our Reading Circles in public schools of the periphery of Greater São Paulo, young educators from the Fernand Braudel Institute of World Economics discuss the classics of world literature with gifted adolescents who struggle to learn in an environment where laxity and disorganization flourish. In these schools we see the waste of talent, the opportunities lost and the contributions to society never made because of boring and empty lessons, chronic teacher absenteeism, abrupt and rapid staff turnover and violence, vandalism and deafening noise in the corridors. Supervisors rarely visit the schools and almost never enter a classroom. While São



Fishermen, Bahia, Brazil, 1978.

Paulo's schools may be among the most violent in Latin America, disorder and failure to learn are features of many other school systems plagued by perverse incentives. With official school days limited to four or five hours in most countries, real daily teaching time can average less than three hours over an academic year.

One of the main challenges facing democracy in Latin America is the notorious reluctance of politicians, with rare exceptions, to invest productively in public education. According to *Latinobarómetro*: "Education is one of the strongest factors explaining support for democracy." Among people with university education, 65% support democracy, against just 49% of those with only primary schooling. "Never before has access to education been so broad as it is today," the survey added. "More education and better incomes for more people produce more critical citizens. More education often is largely responsible for popular protests against corruption and poor government performance."

Clearly, Latin American governments lack the financial and human resources for massive improvement of public education on a national scale. However, most can upgrade selectively. To create the critical skills needed for future political and economic development, centers of excellence can be established in provincial or regional capitals. These centers of excellence would be endowed with enriched and challenging courses, special training for selected teachers and modern libraries, information technology and sports facilities. Standards could be crafted for entry by students and teachers to these centers on a competitive basis. To restructure perverse incentives, successful principals and teachers can be rewarded financially. Successful students can be rewarded with national scholarships. Degrees of success can be measured by competitive examinations and by competition between provincial and regional centers of excellence, which would create new standards for other public schools. These performance standards would be monitored at the national and regional levels by people from

outside the education bureaucracies, representing community organizations, legislatures, the private sector and international donors. Absolute equality in public education now is beyond the reach of governments of nearly all rich and poor countries. However, centers of excellence at least would educate more people to manage government and business more effectively. They also may help Latin America emerge from its marginal and insignificant role in the development of knowledge and technological advance.

#### 4.2 A Democratic Charter

We should not expect altruism in politics, so we need fair and coherent rules. But Latin America's party and election rules are an archipelago harboring a wide variety of habitats and species. Archaic political systems have failed to accompany the modernization of societies. The lack of clear rules breeds distortions that often misrepresent the will of electorates and weaken voters' belief in the legitimacy of government decisions. This has undermined the credibility of parties in Argentina, Brazil, Bolivia, Peru, Ecuador and Venezuela. *Latinobarómetro* notes "a large dose of political cynicism in the region. While 42% say they would vote for a political party, only 11% voice confidence in parties." In Peru, according to Julio Cotler, "there is widespread disillusionment with the political class for its noncompliance with the fundamental principle of accountability. Public disenchantment has accelerated the decomposition of political identities and contributed to the increased volatility of electoral preferences and to social disorganization.... Disenchantment with 'democracy' became so widespread that a majority of Peruvians openly rejoiced at President Fujimori's palace coup in April 1992."

The problem of representation is central to democratic rule of complex societies. In Latin America today, presidents tend to be democratically elected, while legislators still in effect may be chosen by oligarchies, who control local fiefdoms, aggravating tensions between

the Few and the Many. Recent research stresses the importance of fair electoral laws as a key to stability. Election of single representatives of standardized districts, uniform in population size, can correct distortions. To create more effective standards of representation, respecting the different conditions of individual republics, it may be helpful to organize a convention of experts and political practitioners from different countries, under the aegis of international bodies, to draft a Democratic Charter as a non-binding framework to serve as a useful reference in the modernization of democratic systems.

The weakness of parties is especially acute in Brazil, where party discipline never existed in what has become by far Latin America's most complex polity, thanks to the size of its population and territory, its decentralized federalism and its far-flung system of big cities. Election laws favor the proliferation of small parties and frequent switching of allegiances. Presidents cannot form stable majorities in Congress and must bargain individually with legislators to win their votes on critical issues. During the 1991-94 term of Congress, most of the 502 deputies switched parties.

Weakness of political institutions is compounded by malapportionment of seats in Congress. Brazil and Argentina present the worst injustices in apportioning legislative representation among states and provinces, giving the poorest and least populated regions enormous leverage in bargaining for special transfers of money from the central government. Solution of the fiscal problems of Brazil and Argentina has been blocked by this distorted representation in Congress. Malapportionment of seats in Congress in Argentina is worse than in Brazil, but Argentine parties are older and stronger. The loose and atomized structure of Brazil's political system permitted the emergence of new parties after military rule ended in 1985, not least Lula's PT. Argentine party loyalties are stronger because national and provincial bosses control access to the ballot. Radicals and Peronists, the traditional parties, reemerged virtually intact after successive waves of repression under military regimes, battling each other in a kind of non-ideological clan warfare.

Despite the difficulties, big political decisions were made recently by Latin American republics. The biggest of all made by new democratic regimes was to stop chronic inflation, which plagued several countries and led to hyperinflation in Argentina, Bolivia, Brazil and Peru. As a corollary to economic stabilization, these countries became more open to foreign trade and privatized money-losing state industries. Several republics have decentralized their structures of government. With local authorities granted more autonomy, the need for clear, uniform and balanced rules of federalism becomes clear. Brazil's Congress passed a Fiscal Responsibility Law in 2000 that limits spending, borrowing and hiring of employees by federal, state and municipal governments.

In 1990-94, nine republics reformed their election laws, but huge distortions remain. Election districts often are too big, increasing the cost of campaigns and freeing members of Congress of accountability to a local and identifiable constituency. In Brazil's legislative

elections, voting is state-wide and city-wide. In May 1985, two months after the return to civilian rule, Congress amended the constitution to enable its members to change parties at will and to allow the proliferation of parties by abolishing national threshold quotas for representation in Congress. Elections and political fund-raising are personalized, since candidates can run against several members of their own party as well as those of other parties in an open list system. In São Paulo, all 55 members of the City Council are elected in a single district of six million voters. They are entitled to hire 21 "advisers" each, but have no local allegiances and responsibilities. Neighborhoods of 200,000 or 500,000 people have no identifiable representative.

Academics have amassed a huge literature on problems of democracy in Latin America, but few suggestions appear on the improvement of practice. The classic questions are: How can weak political institutions be strengthened while the influence of parties is declining worldwide? How can political parties accurately meet and reflect the demands of voters? Given the weakness of parties, what are the bonds that mobilize political action? How universal should suffrage be? Should voting be compulsory? What are the consequences of universal compulsory voting? How can democracies provide enough legislative support for presidents to make government effective while guaranteeing minority rights? What are the causes and consequences of prolonged legislative gridlock? Why are some systems immobilized by too many parties? To what political actors do people turn in desperation? What constitutes an emergency? Under what conditions, if any, should a president govern by decree? What role should Congress have in the budget process? How can unfair apportionment of legislative seats be corrected? How can parochial amendments to major legislation be limited? Under what conditions should voters be consulted in referendums? How can state and local governments be empowered as agents of democracy without becoming free riders, adding

burdens to public finance? How can taxation and budget transfers to needy regions be shared fairly without generating abuses?

Unlike other political systems, democracy may be abused by those in power, but is open to peaceful correction. Correction in Latin American democracies may lie in greater simplicity and uniformity. Simplicity should be a goal of democratic processes. The simplicity of electoral systems may increase with the literacy of their constituent populations. Minorities have more leverage for a stranglehold on processes and outcomes if political systems are ruled by arcane technicalities. By simplifying we can develop elegance and efficiency, inspiring admiration and confidence.

#### 4.3 Taxation and Democracy

A slogan of the 18th Century struggle of the United States for independence from Britain was: "Taxation without representation is tyranny." The slogan can be inverted to read: "Representation without taxation is a farce." As the Bolivian sociologist Roberto Laserna observed: "Democracy cannot be consolidated while citizenship is conceived merely as a consumer of rights. Taxation measures the commitment and responsibility of citizens, and generates the resources needed for operation of the State. It is critical to expand the country's tax base and make citizens responsible for the achievements and problems of the State."

In colonial Spanish America, an elaborate but futile system of fiscal controls was created by the Madrid monarchy. Royal orders and decrees prescribed in great detail how tax accounts were to be kept to avoid evasion and embezzlement in a loose system in which collection often was franchised to tax farmers. Taxation was based mainly on foreign trade, a dependence that persisted in republican times well into the 20th Century. At the time of the First World War, no Latin American country obtained less than 50% of public revenue from customs duties, a reliance that reached 70% in many republics, with per capita revenues in 1913 as low as US\$8 in Brazil and US\$4 in Bolivia, Mexico, Peru and Venezuela.



Peasant leagues, Pernambuco, Brazil, 1968.

The biggest share of taxes went to pay public debt. Meanwhile, low taxation led to even more borrowing and inflationary finance as political demands on governments and social complexity grew. Governments relied increasingly on the inflation tax (seignorage), or the profits gained from printing more money, but were punished by collection lags and corruption that reduced the real value of taxes in an inflationary environment.

Low taxation has been a structural feature of Latin American economies since independence, except for Brazil recently. Brazil is the great exception in Latin America with its impressive advances in taxation. Many Brazilians now complain that their tax burden, 36% of GDP, is too high for a country in their per capita income class. However, this level of taxation enables Brazil to pay for past and present errors and distortions in its fiscal structure, the heavy interest burden on its public debt and wasteful allocation of resources, generating very little public investment. Mailson da Nóbrega, a former Finance Minister, argues that “public spending in Brazil, especially so-called social spending, basically benefits the non-poor.”

By contrast, Argentina’s tax burden was only 15% of GDP in recent decades. Mexico, Colombia, Peru and Bolivia collected only 12%-14%, or less than half the share of GDP taxed in the United States and Japan (30-33%) and one-third of European taxation (40-50%), all of these much wealthier countries, and even one-third less than that of India (20%). Taxation at these low levels deprives Latin American governments of enough resources to sustain the fiscal commitments of modern societies. The cost and scope of these commitments expanded radically in the late 20th Century, especially in education, health, regulation and for physical and organizational infrastructure for transportation, communications and energy supplies.

Civilization exacts its price. A question to be asked of all democracies is whether citizens shall pay for the maintenance and expansion of modern societies, or if the acquired rights of

voters entitle them to remain free riders in a process financed by others. This question embraces a wide range of specific issues, from pensions to paying for vital supplies of drinking water and electricity. As F.A. Hayek trenchantly observed:

*Mere existence cannot confer a right or moral claim on anyone against any other....Rights derive from systems of relations of which the claimant has become a part through helping to maintain them....Only expectations produced by long practice can create duties for the members of the community in which they prevail, which is one reason why prudence must be exercised in the creation of expectations, lest one incur a duty that one cannot fulfill.*

In all countries, rich and poor, democracy lives under constant pressures and threats bred by demands of the Many for distribution of the state’s limited resources. Aristotle described the problem long ago:

*What is to be the supreme power in the state? Is it the multitude? Or the wealthy? Or the one best man? Or a tyrant? Any of these alternatives seems to involve disagreeable consequences. If the poor, for example, because they are more in number, divide among themselves the property of the rich, – is this not unjust? No, by heaven (will be the reply), for the supreme authority justly willed it. But if this is not injustice, pray what is? Again, when in the first division all has been taken, and the majority divide anew the property of the minority, is it not evident, if this goes on, that they will ruin the state?*

How can fiscal resources be raised to increase security and opportunity in these societies?

There are two areas of weakness. One is the low collection of taxes on income (individual and corporate) and on property. Governments rely too heavily on turnover taxes, which tend to be redundant, cascading to high and often unenforceable levels in the course of production and distribution. Revenues from income taxes are very low (less than 5% of GDP) in Brazil,

Mexico and Colombia, especially when compared with wealthier federations such as Australia, Canada, Germany, Spain and the United States, which depend heavily on income taxes. In rich countries, the total of people paying income taxes is roughly equal to the number of voters, while in Brazil there are 115 million voters but only eight million taxpayers because there are so many poor people exempt from personal taxation. In the United States, income taxes generate 51% of government revenues, against only 17% in Brazil. Nearly half of U.S. income taxes are paid by the wealthy (earning more than \$200,000 yearly), while in Latin America the rich easily evade income taxes. Meanwhile, property taxes are low or non-existent. While towns and cities have grown fast in recent decades, creating new demands for local government services, property tax assessments have lagged far behind market valuations. Rural land escapes virtually all taxation. While taxation theory allots property levies to municipalities on the ground that local knowledge strengthens enforcement, efforts to increase local tax collection often meet ferocious resistance.

A second weakness is that the major Latin American republics recently have been engaged in the worldwide trend toward governmental decentralization, which in Brazil, Argentina, Bolivia, Peru, Colombia, Venezuela and Mexico has meant developing new forms of distributing resources from central governments to regional authorities with huge differences in wealth and management capacity. Since the 1980s all these countries have been struggling with forms of fiscal federalism for transfers of funds from central to regional and local governments in order to resolve political and economic imbalances.

The weakest link in Latin America’s democratic development is the municipality, a weakness that contrasts strikingly with the critical role of the free municipality in Europe’s political modernization over the centuries. Europe’s municipalities were independent financially, with few social obligations, while Latin America’s are dependent on transfers from national and state governments as they assume increasing roles in public health and education while collecting few taxes.

However, with technical support from federal agencies, Brazil’s municipalities increased tax collections in the decade since passage of the 1988 Constitution three times faster than the federal government and twice as fast as the states. Municipal tax collection is concentrated in state capitals and the big cities, the largest of which remain in permanent fiscal crisis, along with most of the world’s megacities. Most of the increase in tax collections was generated by investment in information systems.

Argentina, Bolivia, Chile, Colombia, Costa Rica, Mexico, Nicaragua, Peru and Venezuela tried to raise their level of taxation in the 1990s, in some cases with backsliding after initial success. Brazil conducted the most successful effort in Latin America, both in the long-term and in recent years. Since 1947 Brazil increased its tax burden from 14% to 36% of GDP, a long-term rise punctuated by relapses during surges of chronic inflation (1958-64 and 1982-94). Peru increased its tax income from roughly 13% of GDP in the early 1950s to 20% in 1980, only to fall back to 8.5% of GDP in the escalating



Santo Domingo, Dominican Republic, 1967.



*Mapuche Land Seizure, Cautin Province, Chile, 1972.*

political turbulence and inflation of the late 1980s. The latest increase in Brazilian taxation came during the stabilization that began in 1994. The alternative to raising taxes under the Real Plan would have been default by the government on payments of its public debt, its swollen pension obligations and federal transfers to states and municipalities. Since 1994 the tax burden rose from 24% to 36% of GDP, while monthly inflation fell from roughly 50% in 1994 to less than 1% in 2001. Furious political battles continue over distribution of resources. These disputes so far have been conducted within the framework of a strengthening of the institutions of public finance that has taken place since the mid-1980s, with gradual clarification of information, limits and obligations that reached a climax with passage of a Fiscal Responsibility Law in 2000. Without these legal instruments, Brazil's governments would have little chance of containing inflation.

Many Brazilians complain that their tax system is unfair, redundant and too complicated. Poor people are less aware of what they pay, since indirect taxes are embedded in retail prices. Efforts to reform the system repeatedly have ended in impasse and failure, with the new government, after long negotiations with Congress and state governors, succeeding only in protecting and slightly increasing federal revenues. While reform of tax laws is a gradual and piecemeal political process, public finances can be strengthened by investments in tax administration, mainly in information systems and training, in a bureaucracy that must be seen

as apolitical. To this end, Brazil's federal tax agency has funded advanced degrees for career personnel. Appraisals of tax liability should be made on the basis of financial transactions and apparent standards of living. "Taxes on financial transactions, while controversial, are extremely efficient, hard to evade and entail low collection costs," says Everardo Maciel, former head of Brazil's federal tax agency (1995-2002). "Apart from this, they provide valuable information for other forms of collection."

Taxation and the viability of democracy are tied together through sharing of burdens to end fiscal parasitism, shifting public spending away from consumption and toward productive investment. The dangerous alternative is a return to the debt traps and serial defaults of the past, reviving chronic inflation, destabilizing politics and impoverishing society. Since winning independence in the 1820s, Venezuela has defaulted on foreign debts nine times, Mexico eight times, Colombia and Brazil seven times and Argentina five times.

While public debts declined in the first half of the 1990s, thanks to renegotiations under the Brady Plan, they have risen sharply again since then. In Argentina, public debt rose from 30% of GDP in the early 1990s to 150% by 2002, when it again defaulted. Brazil's public debts rose from 33% of GDP in 1996 to 58% in 2003. This swelling of debt was caused by compounding of very high interest rates, which rose from 19% in 2002 to 23% in 2003, and by the need to pay for perceived risk of default and by federal absorption of state government debts

as part of the fiscal stabilization effort. Interest on public debt rose from 2.8% of GDP in 1996 to 9.5% in 2003, or more than double the huge primary budget surplus (4.3% of GDP) that Brazil had to generate just to prevent public debts from increasing at an explosive rate. Economists predict that the debt burden will decline slightly in 2004, thanks to lower interest rates and more economic growth. But it will be very hard for Brazil to sustain debt payments on this scale for long. It would be futile for Latin American republics to remain trapped in the casino of international bond markets, with its manic-depressive cycles of liquidity and droughts, and erratic pricing of debt. Why should the debt of unstable country like Ukraine have a risk premium of only 3% over U.S. Treasury bonds, while Brazil now pays 5% and had to pay a 24% premium during the 2002 pre-election panic? Countries can defend against these violent swings only by consolidating their public finances, a process that is underway in much of Latin America.

Chile provides a democratic model for reducing public debt. After its military regime defaulted on its foreign public debt in the 1980s, Chile's democratic government, after coming to power in 1989, reduced its debt from 54% of GDP in 1990 to 21% in 2002. It improved tax collections, contained spending, obtained more revenue from reformed state enterprises, prohibited the Central Bank from lending to the government and prohibited provincial governments from borrowing. For Chile, the survival of democracy was at stake, following the disorder under the



*Incaic plowing, Hacienda Lauramarca, Cuzco, Peru, 1970.*

leftist government of Salvador Allende (1970-73) and the repression of the military dictatorship of Augusto Pinochet (1973-89). This is the path that other democracies will have to pursue. Brazil and Peru, among other countries, have embarked along this route and face testing times.

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This essay has proposed three paths of advance for consolidating democracy in Latin America: (1) creating centers of excellence in education; (2) restructuring party and election rules to improve the quality of representation, and (3) increasing taxation to pay for modern government. These goals may seem very ambitious at first. Yet they would be less daunting if we take into account the progress achieved over the past half-century, especially in recent decades. An obstacle to further achievement is a lack of conviction that we can do better. Lack of conviction feeds upon and reinforces the weakness of institutions.

The advance of the welfare state in Western Europe and the United States contrasts with the post-colonial experience of Latin America in terms of levels of wealth and skill, the role of citizenship and the culture of taxation. Indeed, Latin American republics have sought to borrow, borrow, borrow without being able to tax, lacking the pressures of wars that drove the development of public finance in Europe. These difficulties aggravated distortions in the distribution of resources among the One, the Few and the

Many, in the form of onerous interest payments and endemic fiscal fragility.

*Can Democracy Endure?* This is the title of a skeptical essay, still unpublished, by my friend William McNeill, who views the rise of democracy in the West in terms of the mobilization of populations and resources for war, as in the struggle of a handful of Greek cities against the Persian empire, in the American Civil War, Bismarck's Germany and World Wars I and II, the latest of these fought as an ideological struggle of democracy against tyranny, leading to the spread of democracy worldwide in the late 20th Century. Of the French Revolution, McNeill writes:

*Ideals of liberty, equality and fraternity embodied in universal male suffrage were accompanied by universal conscription of young men for war. As a result, hastily trained and vastly enlarged French armies were able to defeat successive coalitions of their European foes.*

In Latin America, except perhaps for Bolivia's disaster in the Chaco War with Paraguay (1932-35), mobilization for war contributed little or nothing to creation of democratic institutions. However, these republics were adopting European social legislation well before the ideals of democracy were spread during and after World War II. Indeed, both Europe and Latin America are struggling to sustain the heavy fiscal burdens of welfare states with only minor commitments to military spending. In Latin America, rigidities imposed by social legislation

– exaggerated payroll taxes, job security and public sector pensions – divert resources away from strategic investments in education and infrastructure and create obstacles to the labor market flexibility needed for adaptation by families and nations to changing conditions in the world economy.

My optimistic view is that the forces of cooperation in human experience ultimately have proven stronger than the forces of dissolution. Otherwise, civilizations would not exist and humanity would not have evolved. In modern democracies, we continually return to the dilemmas and opportunities faced by earlier republics. Most democracies and republics live turbulent lives. We remain exposed to the challenges posed by the civic humanism of the Renaissance. They involve an old struggle described by Machiavelli, in the language of civic humanism, as a tough-minded moralist concern with problems of liberty and corruption. This is why conviction is so important. Conviction in pursuit of justice, learning and opportunity enhances the prospects for survival and even excellence in the development of our institutions. Poverty and injustice are old stories in Latin America, as elsewhere, but we have been moving forward, not backward, in a climate of rapid change. Belief in the prospect of further advances can mobilize resources into more productive organization of politics and society.

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