BOOK REVIEWS

Latin America's Political Economy of the Possible: Beyond Good Revolutionaries and Free-Marketeers
Javier Santiso
Cambridge, Mass.: MIT Press, 2006, 250 pp.

The subtitle of this book caused this reviewer concern. A book that equates free markets with populism, blames both for Latin America's failure, and eulogizes pragmatism is something that needs to be challenged. (I refer to the Latin American brand of populism, not the Jeffersonian kind, of course.) However, a classical liberal such as the author of this review can live with much of the book's content—provided there is some clarification about the terms employed to describe what works and doesn't work. It is thought-provoking, well-argued, and intelligently constructed.

Two different definitions of pragmatism can be applied to Santiso's argument. An analogy lies in a dilemma posed a century ago by American philosopher William James. He imagined a squirrel going around a tree, and a man on the opposite side of the tree trying to catch a glimpse of it. Every time the man moves around the tree, the squirrel moves around quicker so that the tree trunk is always between the man and the squirrel. Is the man actually moving around the squirrel? By some definitions, says James, he is; by others, he is not. It depends on the practical meaning of the words "going around the tree."

If by "going around the tree" we mean that at some point the man is to the north of the squirrel, and then to the east of the squirrel, and then to the south of the squirrel, and then to the west of the squirrel, then, yes. But if we mean that at some point the man is in front of the squirrel, and then to the left of the squirrel, and then to the back of the squirrel, then, no, the man is at no point in those positions. So the answer to the question depends on the practical meaning of the words "going around."

One could say something similar about the word *liberalismo* (classical liberalism), which the author criticizes, equating it at some stages with populism, and calling both of them failed utopias. He makes the case that in the 1990s the market replaced the state as a paradigm and failed to trigger development, just as populism had failed in the past, and that this

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failure opened the doors to the current, more successful, era dominated by pragmatism. By some definitions, however, *liberalismo* means something similar to what Javier Santiso means by pragmatism, and, therefore, does not mean what he means by utopia.

This can be clearly seen if we look at the second, more traditional definition of pragmatism—the idea that beliefs do not represent reality, that they are simply dispositions that prove either true or false according to how much they help accomplish the desired goals. By that definition, *liberalismo* is compatible to some extent with Santiso's definition of pragmatism because, when tested against reality, its precepts—limited government, individual responsibility, equality before the law—have proved much better at achieving the goal of development and prosperity than all the alternatives.

Santiso posits that Latin America has grown weary of utopias and has come to "a pragmatic political economy that combines neoclassical orthodoxies with progressive social policies" (p. 4). Latin America was discovered at a time of profound transformation in Europe, characterized by a great belief in the future. From the beginning, the New World was seen as the land of utopia where everything was possible. The vision that paradise could be brought to earth impregnated Latin American culture to the point of dominating its political economy for a long time—until failure opened the door to pragmatism.

The 20th century, the argument continues, was dominated by the tempestuous search for the ideal through revolution, first of the statist, populist kind, then of the free-market "liberal" type. In the process, some changes took place. One was the surge of democracy, which entailed a change in Latin America's idea of time because it placed constraints on the governments where there were none before. Arising from the failure of the statist populism of the left, there came an economic adjustment that was also temporal because the timeless, utopian state gave way to the quick pace of the market.

The market revolution, however, was also impregnated with the old utopian culture and therefore lacked certain institutional underpinnings that might have fostered the kind of environment that has accompanied economic modernization elsewhere. Eventually, pragmatism, a moderate version of the market society that combines orthodox fiscal and monetary policy with more equal wealth distribution, began to emerge. Governments like those of Lula da Silva (Brazil), Michelle Bachelet (Chile), or Tabaré Vásquez (Uruguay) on the left, and Alvaro Uribe (Colombia) on the right, represent this new paradigm. Others, meanwhile, like Hugo Chávez in Venezuela and Néstor Kirchner in Argentina, "testify to the region's still-powerful attraction to the siren's song" of populism.

The author's general conclusion, expressed early on in the book, is conveyed in his view that "the great news we have from Latin America is this: Open societies emerge (to paraphrase Karl Popper) politically and economically from societies that give a preferred place to the vices and virtues of democracy and free-market principles" (p. 8).

Santiso is right to call the 1990s a failure. But what failed in the 1990s was not free-market liberalism. What failed is the fact that free-market liberalism was tainted with populism—and, yes, by utopia; that is, by the idea that the enlightened actions of those very governments that purported to liberate the energy of society opening the economy and projecting the region onto the global firmament controlled the key to the future.

Those caudillos who thought they were the antithesis of their populist predecessors in fact prolonged the tradition of placing men above institutions. What was lacking was an institutional underpinning—including an effective judiciary—capable of protecting the individual against encroachment by the power of those strong enough to bend the rules. Every inconsistency in the reforms of the so-called *neoliberal* era derived from this fundamental flaw—the continuous growth of public spending, the privatization of government-owned entities under monopoly conditions, the explosion of regulatory mandates and bureaucracy, and the rigidity of labor markets.

If one looks at specific reforms, one finds so many examples of undue government intervention that it cannot in all honesty be said that the so-called Washington consensus amounted to a free-market era. Public spending in Argentina went up by 100 percent in the 1990s while GDP growth totaled 40 percent, two and a half times less, in that same period. Public spending in Brazil went up by 33 percent. The Latin American state did not shrink.

If we look at the banking system in Mexico, we will find that it was controlled by an oligopoly and did not constitute a competitive environment in which consumers called the shots. The result was the collapse of the financial system, which cost taxpayers $70 billion to pay for irresponsible loans and banking practices that originated in a privilege-driven system.

The same can be said of labor laws, for instance, in Argentina. The government's refusal to reform legislation dating back to the Perón era (inspired by Mussolini's social codes) meant that collective bargaining by trade and absurd firing norms kept aspiring workers out of the market. That is why, despite the fact that $100 billion of foreign capital flowed into Argentina during that decade, unemployment consistently hit double digits.

It could be said that, on the whole, there was a move toward liberalization and privatization across the region. But the absence of clear principles regarding the workings of the free society translated into a reform that better resembled a transfer of assets rather than the decentralization of power. With the exception, perhaps, of El Salvador, where reform was more consistent, the result was the perpetuation of the basic divide between those who influence government action and those who are left out of the state-mercantilist system.

Under such conditions, it is no surprise that investment levels were relatively modest—an average of 18 percent of GDP across the region, far from Asia's 25 to 30 percent mark, or even Chile's current 25 percent. Much of the economy went from government hands to private ownership, but did not become much freer and therefore it was not productive enough to significantly reduce poverty.

There are about 3 million small- and mid-sized companies in Peru—98 percent of all the businesses in the country. These are mostly owned and managed by poor people who do not have much of an education but who have an entrepreneurial drive. Given the conditions in which they operate, they are not able to produce very much. Their combined production amounts to about 30 percent of the total GDP of the country, while 2 percent of the companies of Peru produce almost 70 percent of the nation's wealth.

Entrepreneurs of small- and mid-sized companies in Peru, as in many Latin American countries, are suffocated by taxes, regulations, and the absence of a judiciary willing to enforce the principle that all citizens are equal under the law. The best that can be said about them is that they get on in life, but not at a pace that can be compared with what is happening in other parts of the world, such as Estonia, the Czech Republic, Ireland, or New Zealand (which has slowed down a bit in recent years). And it certainly cannot be compared with what is happening in China, where 250 million people were pulled out of poverty in the last 20 years, or in India, where about 300 million people comprise the middle class today. The pace of progress is slow and there is frustration at the social base—the reason why many left-wing candidates have won elections in recent years.

There is currently a paradoxical situation. On the one hand, the macroeconomic figures are looking very healthy across Latin America, in part because the "pragmatists" have indeed engaged in sound monetary policies and shown a measure of fiscal responsibility. From 2003 to 2006, economic growth averaged 4.5 percent a year. The ratio of debt to GDP has gone down to about 53 percent—not bad by Latin American standards. Yet, many countries have seen the emergence of radical, populist, anti-establishment forces. There is clearly a disconnect between the rosy macroeconomic statistics and the sentiment of people at the grassroots.

This disconnect probably has to do with frustration with the reforms of the 1990s that some attribute to neoliberalism and others, like the author of this review, attribute to the fact that neoliberalism was tainted with utopia and populism, manifested through persistent government intrusion in economic and social life.

Latin America needs to move toward reform. If it continues along the current path, sooner or later the positive international conditions will change, as they have so often done in the past, and many governments will be seen to be a lot less "pragmatic" than we think.

Argentina is a good example. They seem to be doing everything wrong—inflating the currency, controlling prices, nationalizing private companies, and yet they seem to be getting everything right: the macroeconomic statistics look wonderful. Many of the mistakes of the past have been repeated in operatic form by a government full of demagogues. President Kirchner spends part of his time going from supermarket to supermarket telling the attendants what prices to charge for what items. He has even banned the exports of meat because he thinks that by creating a superabundance of meat within the country he will force prices down.

The same happened in the energy sector. He maintained the price controls on natural gas that he inherited from the former president. Investment stopped. Soon there was an energy shortage and the government responded by creating a state-owned energy company. However, the extraordinary international conditions, such as the high demand for the country's commodities, are helping conceal these realities for the moment.

Brazil—and Javier Santiso is right to point this out—is on a better footing. But not much reform is taking place. The government seems to believe that monetary and fiscal stability will produce high investment levels and that it should use the revenue produced by booming exports to hand out cash to poor families in exchange for a commitment on the part of parents to send their children to school and take them to medical checkups. But the fact is that to eliminate the poverty that affects some 70 million people, the country needs a productive revolution that will only come from profound institutional reform.

Brazil has a very heavy state with about 10 million public employees, if we count the various levels of government. It has a pension system that has not been privatized (unlike most of other Latin American pension schemes) and costs almost $20 billion. Its complex political structure makes decisionmaking very hard. Part of the corruption scandals involving bribes paid by the party in government to obtain legislative support over the last two years have resulted from the labyrinthine political framework.

Managing the legacy in a responsible way, which is what President Lula has done, is a positive development for Brazil because many people on the left look up to that leader and could well learn the importance of monetary and fiscal discipline from him. But unless Lula da Silva transforms this legacy, the weaknesses at the heart of the system will be exposed eventually.

Mexico offers similar lessons. Although Vicente Fox should be commended for continuing to open up the political system and guaranteeing freedom of the press as well as for maintaining macroeconomic stability, he has failed to push through the types of reforms that might have helped his country leap forward and build a constituency for the acceleration of structural change. Because he couldn't untie the many knots that keep productivity low, the big divide between the small segment of society that is fully global and the masses who gravitate toward the informal economy or toward the U.S. border has not been bridged. With an average annual growth of 2 percent, the economy has failed to pull people out of poverty these past six years. The only reduction in poverty Fox can point to comes from cash transfers that provide only temporary relief.

The failure to modernize means, for instance, that oil production is showing signs of decline. The Cantarell complex, which accounts for 60 percent of Mexico's oil production, will lose half its output capacity by 2008. Since private investment is banned, the possibilities of expanding production in other fields equal zero. This is just one example of how the system holds back production—to say nothing of high energy costs and taxes that account for Mexico's drop in various competitiveness rankings.

By all means, Latin America should feel relieved that populism is giving way to pragmatism and therefore shedding many of the policies that led to hyperinflation and social deprivation. But pragmatism can be understood to mean the conservation of good macroeconomic figures, temporary poverty alleviation programs, and no reform—or it can be understood to mean heeding the examples of other countries where free-market reforms have proved effective and helped unleashed a torrent of entrepreneurship, as well as empowering poor Latin Americans desperate to move from subsistence to wealth creation.

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