

development

BEYOND ECONOMICS

2000 Report

**Economic and Social Progress
in Latin America**

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A Statistical Appendix with up-to-date economic data on Latin America and the Caribbean is available online at www.iadb.org/int/

DEVELOPMENT BEYOND ECONOMICS
ECONOMIC AND SOCIAL PROGRESS IN LATIN AMERICA

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Development Beyond Economics

Latin America begins the 21st century while still shaking off its most recent crisis. As has often happened, disturbances from outside the region have spoiled the optimistic projections and plans of many governments. Growth has been unsatisfactory in recent years, forcing governments to focus their concern once more on maintaining fiscal discipline and price stability, and on deepening economic reforms that will strengthen confidence and improve chances for recovery.

Most Latin Americans find this state of affairs quite discouraging. While governments direct their efforts toward dealing with macroeconomic turbulence, many people of Latin America and the Caribbean see little being done to solve their countries' most critical problems, such as scant employment opportunities, lack of education, poverty, corruption and crime. Some even believe that striving for macroeconomic stabilization unnecessarily aggravates these problems at a time when lasting solutions seem increasingly remote.

On previous occasions, the *Economic and Social Progress Report* has fueled this debate by analyzing the implications of volatility and the consequences of macroeconomic policies in the region. This year's report, however, examines the problems of Latin American development from a broader perspective. We do so not only because the beginning of the century is a propitious occasion for considering overarching questions, but also because we believe that this is what Latin Americans are demanding.

The purpose of the report is twofold. First, it compares Latin America's development to other regions of the world, with the understanding that "development" means not only economic progress, but also human development and the capacity of people of a

society to work together. Second, the report highlights the influence of three sets of structural factors on economic and social development: demography, geography and institutions. These factors are major determinants of long-term development, yet they have received little attention, in part because addressing them goes beyond the conventional scope of economics.

The State of Development

There is no single snapshot that conveys the state of development in Latin America. Rather, the picture is one of sharp contrasts. It is not just that the countries in the region vary widely in terms of their development. More importantly, while the region stands out in some ways as relatively more advanced than other parts of the developing world, in other ways it displays truly worrisome indicators.

In terms of economic development, Latin America can today be classified as a medium-income region. Worldwide, it occupies fifth place in terms of per capita income, behind the developed countries, Southeast Asia, the Middle East and Eastern Europe. Only the countries of the rest of Asia and Africa are below it. That differs dramatically from a half century ago, when only the now-developed countries were ahead of Latin America. This downward trend indicates that Latin America has not performed especially well in recent times in terms of economic development. Besides being modest, economic growth has been quite unstable—actually a chronic problem in the region, although it may be that some of the recent manifestations of volatility have been more conspicuous and pernicious than in the past.

The greatest concern about Latin America's pattern of economic development is the way income is distributed, a topic to which the previous edition of this report was devoted. Some Latin American countries are among those with the worst income distribution in the world, and even countries in the region with somewhat better distribution have indices of income inequality that are above the world average. Poor income distribution is thus a trait common to the entire region.

In contrast to this discouraging picture, many human development indicators in Latin America are outstanding. In terms of the United Nations Human Development Index, levels in the region are quite close to those of the Southeast Asian countries, and are surpassed only by the developed countries. The foundation for these relatively high human development levels is Latin America's impressive achievements in terms of longer life expectancy, lower infant mortality rates, and higher literacy rates. Although some countries in the region still have serious shortcomings in these areas, practically all the improvements are greater than what could be expected solely on the basis of countries' per capita income levels. It is remarkable that major advances in health have continued through the turbulent 1980s and 1990s. Unfortunately, however, the same cannot be said of education. Although initial access to the educational system has been extended throughout the region and enrollment is high in the lower grades, years of schooling attained by current cohorts of Latin America's young are not much higher than they were 20 years ago. On average, Latin Americans remain in school for fewer than nine years, only a year and a half more than two decades ago, and much less than the average schooling of 13.5 years for young people in the United States or the 12 years plus in Korea or Taiwan.

Nowhere are the contradictions and contrasts in Latin America's development more pointed than in indicators that measure the capacity of societies to live and work together. On the one hand, the region has progressed toward democracy over the past two decades at an extraordinary and unprecedented pace. While Latin American democracies are far from perfect and still a considerable distance behind the developed countries in terms of consolidation, citizens of the region have come to enjoy broader freedom to participate in public processes, oppose governments, and

otherwise express and inform themselves. With significant differences between countries, Latin Americans today enjoy more protection from arbitrary action, discrimination and injustice than ever before.

On the other hand, consider the change that has taken place in terms of crime. As far back as the 1970s, murder rates in the region were on average the highest in the world, and since then they have risen in almost all countries, in some instances reaching levels 40 times higher than those of the developed countries or Southeast Asia.

Perceptions

Most Latin Americans are unfamiliar with these comparative indicators. Yet their opinions faithfully reflect the development problems of the region. According to surveys in 17 countries taken over three consecutive years during the 1990s, only 10 percent of Latin Americans characterize their country's current economic situation as good. An overwhelming 60 percent believe that their parents were better off, despite the fact that current per capita incomes are better than they were several decades ago. The surveys reflect widespread impressions by many Latin Americans that add up to concerns about economic instability and inequitable income distribution. Half of those surveyed pointed to one of five issues—unemployment, low wages, inflation, poverty and job instability—as the most important problem facing their country.

Beyond the economic dimensions of development, the main concerns of Latin Americans have to do with education, corruption and crime. Four of five Latin Americans believe that crime has risen a great deal in recent years, and two of five say that they or their close relatives have been victims of a crime.

Structural Factors that Affect Development

Some of Latin America's problems in terms of development may have been exacerbated in recent years by changes in domestic policies or the international context. Globalization or neoliberal policies are often mentioned as causes of the region's slow growth, instability, income inequality, or other shortcomings. Yet none of these problems is new, so the blame can

hardly be placed squarely on any one of them. And since the effects of economic policies on Latin America in a global world have been roundly discussed and debated, we turn here to broader and less popularized structural factors that affect the region's development: demography, geography and institutions.

These three variables share fundamental characteristics: they are historical in nature and change slowly, yet their influence on development can be changed through the adoption of appropriate policies. Unto themselves, they do not constitute a specific design for medium- or long-range development. But if their importance is ignored, or perhaps simply obscured by the development issues of the day, they can have uncontrolled effects harmful to development.

The Demographic Opportunity

Public discussion of demography traditionally has focused on the consequences of population growth and on the pros, cons and ethical implications of birth control. Ironically, while debate on these issues raged, many of the more important ways in which demography influences development were virtually ignored.

From the standpoint of economic and human development, the key demographic variable is not the population growth rate, but the age composition of the population. Obviously, both factors are related, but the policy implications are radically different. While focusing on population growth leads to often contentious debate over birth control, emphasis on age composition means facing the challenges and exploiting the opportunities posed by each stage of the demographic transition.

The Latin American countries today are at the stage of the demographic transition when the largest population groups are young adults who are beginning productive activities or will do so in the coming decades. Opportunities for economic and social progress are extraordinary at this stage of the transition because the rates of dependency of children drop quickly while the proportion of elderly is still low. There is in effect a window of opportunity to increase the incomes of families (and thus the economy as a whole), boost savings and investment, and offer a better education to what will be a smaller number of children in the new generation. But it is also a time of great challenge, because sources of employment must be created quickly,

educational opportunities must be extended beyond basic schooling to help new entrants into the job market find productive employment, and social mechanisms must be put in place to head off social disaffection among the young and an increase in crime.

How the opportunities and challenges posed by this stage of the demographic transition ultimately balance out will depend on economic and social policies. Choosing or adapting the right policies depends on a thorough understanding of the economic and social implications of the demographic change. It would therefore seem a serious mistake to continue to ignore demography, yet that is just what is happening in official and academic circles in many countries of the region.

In the decades ahead when the demographic transition is in full force, labor policies will have to facilitate incorporation of women and young people into the labor market. They will have to be given opportunities to obtain social security, a benefit until now available disproportionately to adult men. Social security systems will have to be transformed to take better advantage of the savings potential of people of the current generation, and to ensure that when they reach retirement age they will not become a burden to future generations. Education systems will have to be transformed to respond more flexibly and efficiently to the changing age composition of the population, providing the diversity of educational services required by heterogeneous population groups. One of the main challenges of the current stage of demographic change will be controlling juvenile crime, especially in large cities. Each country and city will have to find the policy mix that broadens prevention efforts, improves cooperation between government agencies, incorporates communities into crime detection and prevention efforts, and makes the normal channels of justice function as they should.

Realizing the Potential of Geography

Geographical variables have often been ignored when discussing and designing public policies in Latin America, in part because of concerns that addressing them somehow implied yielding to notions of fatalism and even racism. But the cost of disregarding geographical realities has been high. There has been little technological development suited to the agricultural

conditions or diseases endemic to tropical areas. Mechanisms to prevent and respond to earthquakes, floods and other natural disasters lag behind. The region lacks adequate criteria for investments in transportation and communications infrastructure. Uncontrolled growth of cities remains practically unaddressed.

Economic, social and human development in Latin America has been and continues to be influenced in various ways by both physical geography—such as climate, land characteristics and topography—and human geography, which is the settlement patterns of populations. Key factors include productivity of the soil, distance to world markets, and health conditions. The possibilities for sustained growth and for economic and human development are lower in more tropical countries, and in countries located far from world markets. But such difficulties can be overcome, as has been shown by some of the more successful Southeast Asian and Eastern European economies. Geographical limitations also tend to become less relevant to the extent that countries pass beyond a certain threshold of economic development, perhaps because of urbanization and access to the technological advances that accompany development.

Of course, government policies can also mitigate more unfavorable geographical factors and channel the more favorable ones in a positive direction. The benefits of investments in infrastructure, technology and information are of particular importance. Infrastructure investments can change the influence of geography by making lands more productive, facilitating access to markets, and improving basic water, sewerage, power and communications services. But resources are often limited, so investment projects must respond to clear policy priorities, which in turn must be based on a thorough understanding of the geographical factors of each country and region. The most efficient investments from an economic standpoint are usually those in areas more favored geographically and with greater population density. However, for reasons of social equity, meeting the basic needs for services of the entire population must be considered alongside economic efficiency criteria.

The variety of problems posed by geography cannot be addressed without having available the information needed to overcome them. Yet in many Latin American countries, this information either does not exist or is not disseminated adequately. This is par-

ticularly important for natural disasters. With better information on risks and how to prevent them, ways can be found to prevent settlements in high-risk areas, adapt appropriate technologies for infrastructure and housing, and better prepare for handling disasters. Obviously, information is not enough—the incentives framework and institutional organization are also decisive for the success of any prevention effort.

Some of the most serious problems rooted in geography cannot be resolved with national policies, since these problems often result from biased technological development worldwide. Agricultural productivity has grown slowly in tropical areas because technological development has concentrated on agriculture in temperate zones. For market reasons, international pharmaceutical research has also essentially ignored the health problems of tropical regions. Solving these problems requires transnational efforts by groups of countries, guided by multinational bodies that specialize in agriculture and health.

The Importance of Institutions

According to the econometric analyses presented in this report, more than half the difference in income levels between the developed countries and Latin America is associated with deficiencies in the institutions of the latter. To one degree or another, all of the Latin American countries have problems with the rule of law, corruption, and the ineffectiveness of governments in providing essential public services. These three problems with Latin America's institutions are serious even in comparison with other developing regions. Taken together, they constitute a significant barrier to the region's economic progress and social development.

Although demography and geography are important factors that help explain differences in development levels between countries, their relative weight is less than that of institutions, and more importantly, their influence varies strongly from country to country, depending on the particular circumstances. The association between the quality of institutions and economic, human and social development is especially close across the boards, partly because institutions are themselves influenced by the development process.

The importance of institutions has been recognized increasingly by Latin American governments and societies, and has recently received a great deal of

attention from scholars and international agencies. No one now doubts that effective institutions are critical to hastening the development process. The question that has still not been answered satisfactorily, however, is how to go about changing institutions.

From an analytical standpoint, the factors that determine the quality of institutions must be understood first in order to then take up the problem of how to change them. Government institutions are by their nature the expression of the political forces through which societies address their collective problems. Thus, the quality of public institutions is inevitably influenced by the rules and practices of the political game. Yet the relationships between politics and the quality of institutions have been studied very little, even by international organizations for which these relationships have important implications. In this report, we have decided to make a foray, with some trepidation, into the difficult terrain of political science.

The quality of public institutions constitutes the bridge between development and politics—development depends largely on public institutions, but they are in turn created and transformed in the context produced by levels of development. It is not rash to say that economic, human and social development depends on having political institutions that facilitate effective representation and allow for public control over politicians.

Which political institutions make it possible to best achieve those objectives cannot be determined without taking into account the specific conditions of each country. For example, electoral institutions that make room for minority interests in legislative bodies might be suitable for a country with complex social conditions, but not necessarily for a more homogeneous country. Similarly, the reelection of presidents might be a good idea in a country that has elaborate systems of control over the use of public funds for elections, but not such a good idea in countries lacking such controls. Consequently, this report refrains from drawing concrete recommendations; rather, it objectively discusses the merits and drawbacks of various kinds of political institutions. The analysis does not seek to be exhaustive. The emphasis is on electoral institutions and political participation. These two dimensions, central as they are in the political game, have two further advantages from a methodological standpoint. Both can be described quantitatively, fa-

cilitating comparison between countries, and both have clear and important connections with the quality of public institutions.

Electoral institutions play a preponderant role in politics. Whether politicians will direct their efforts toward satisfying collective or individual interests depends on electoral institutions. Likewise, electoral institutions ultimately determine the size and strategies of political parties. In turn, political participation—which is not merely a matter of going to the polls but also entails taking part in the process of discussion, selection and oversight of public decisions—is the very essence of politics. Without participation there is no real democracy: citizen interest will not be reflected in decisions, politicians will not be subject to public control, and political spaces will be occupied by pressure groups and open to purposes contrary to the public interest.

A Final Note

This report is inspired by the conviction that the state of development in Latin America and the Caribbean is largely the result of the region's own circumstances that to date have not been sufficiently understood or controlled. Deficiencies in development cannot be attributed to the passive position played by the region in the worldwide geopolitical chess game, as was commonly believed during the Cold War. Nor can it be attributed to the interventionist and import-substitution orientation of regional economic policies, the fashionable view of the "Washington Consensus" and the interpretation most widely presented by international organizations in explaining the miracle of the "Asian tigers." Naturally, the forces of world geopolitics and the orientation of Latin America's economic policies have an impact on growth. But such factors cannot satisfactorily explain away the region's income levels, inequalities, quality of education or crime levels. This report is an effort to look beyond the trends of the time for the deeper roots of these problems and for the solutions that can turn them around.

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