



February 2009, Quarterly Issue

Institutions and Development in Latin America: A Comparative Analysis

Background

How do institutions affect national development? That was the central question in an ambitious project sponsored by the Princeton Institute for International and Regional Studies and the National Science Foundation that brought together a multinational team of scholars under the direction of Alejandro Portes (Princeton Center for Migration and Development). The main findings of the study are included in a paper recently completed by Portes and Princeton doctoral candidate in sociology, Lori D. Smith.

Institutions have long attracted the attention of economists, political scientists, and sociologists but few studies have investigated the relationship between institutions and national development in “real time” or through field research. The project summarized here did just that. It focused on three key institutions (stock exchanges; aeronautical authorities; and postal services) in three major countries (Chile, Mexico, and Colombia). For each institution and each country, 15 to 30 detailed interviews were conducted, divided about equally between internal and external respondents. The key idea was to triangulate different methodologies so that each investigator could arrive at an authoritative assessment. All case studies included: 1) compilations of the legal rules governing the activities of each institution; 2) compilations of internal reports and evaluations; 3) compilations of academic and journalistic reports; 4) interviews with institutional personnel at various levels; 5) interviews with outside informants; and 6) interviews with strategic users of institutional services (i.e. commercial airlines, pension funds investing in the stock market, and mass mail marketers).

Building Social Capital

Beyond contrasts in the actual performance of the three institutions, the study found significant differences among the countries selected for analysis. The institutional panorama of Chile was the most promising. This was demonstrated not only by the superior performance of the Santiago Stock Exchange, which has emerged as a modern and technologically advanced entity, but also by the Civil Aviation Authority (*Dirección General de Aeronáutica Civil*), an agency that possesses solid internal cohesion and aspires to become the best of its class in Latin America. Even the



As “threatened Islands of Excellence,” civil aviation agencies depend on external oversight to fulfill their critical functions in countries like Mexico

Postal Service, despite its uneven history, is taking an upward trajectory.

Mexico occupies an intermediate position where that country’s participation in the North American Free Trade Agreement (NAFTA) has produced a rapid transformation of its old corporatist regime, but without affording the levels of probity and efficiency of its NAFTA partners. The Mexican Stock Exchange displays advanced technological development and has generated seven subsidiary companies specializing in different sectors of the market, all under the institutional umbrella of the *Bolsa Mexicana de Valores*. On the other hand, the stock exchange continues to be shallow, owing to the small number of companies participating, the relative absence of institutional investors (such as the pension funds that have played a decisive role in Chile), and the absence of an investment culture” among the general public. Remnants of clientelism and *amiguismo* (exchange of favors among friends) persist among brokers, although the advent of the electronic market has eliminated most undercover manipulations, giving greater transparency to stock transactions. More questionable is the condition of Mexican civil aviation; the country has not built an institution comparable in weight and authority to the U.S. Federal Aviation Administration (FAA).

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Colombia presents the most difficult case. An exception is its Stock Exchange, which has managed to consolidate and modernize, following the example of large Latin American exchanges. On the other hand, the market is small and relatively shallow, given the resistance of the largest firms to be listed by the exchange and of the public to invest in it. As in Mexico, the Colombian middle-classes are more inclined toward real estate investments than putting their money in the stock market. Worse is the situation of the aeronautics authority (*Aerocivil*). Suffering from a scarce budget, limited personnel and an absence of external allies, that organization barely meets its basic institutional goals but has no proactive capacity or voice vis-à-vis government.

The weakness of Colombian institutions culminates with the Post Office, which ceased to exist shortly after fieldwork for this study had been completed. Like other Latin American postal services, the Colombian *Adpostal* suffered from union conflicts, lack of managerial competence, instability, and corruption. As a result, a series of private companies came to dominate lucrative market sectors, relegating the official agency to the most isolated and unprofitable regions of the country. Confidence in *Adpostal* diminished so much that even government agencies ceased to use it, turning instead to private contractors. In contrast with Chile, successive efforts to reform the system and increase its institutional adequacy failed, leading to institutional demise.

Organizational Similarities

First is the tension experienced in the three countries by the Stock Exchange between its character as a for-profit corporation and its function as a source of credit for national development and depository of the public trust. In all countries, stock exchanges began as associations of the economic elite—“gentlemen’s clubs”—playing a double role as private companies and as platforms for the dominant class. This double identity was especially apparent during the government of the *Unidad Popular* in Chile when the directors of the Santiago Stock Exchange became the principal adversaries of the nationalization policies implemented by the socialist government of Salvador Allende.

The modernization of the Stock Exchange has been associated, in every case, with a growing tension between shareholders of past generations, devoted to their traditions and privileges, and new actors vying

for greater transparency and access to information. If current tensions affecting Latin American stock exchanges are related to their elite origins, their resolution also shares a common cause: economic globalization. Globalization has played a key role in forcing institutional modernization. Without it, institutions would have been shut out of international capital flows and condemned to irrelevance. Almost without exception, technological and organizational innovations come from abroad. Latin American stock exchanges incessantly copy Wall Street and, to a lesser extent, the *Bolsa* of Madrid as well as more advanced stock exchanges within the region. The transformation of the Colombian Stock Exchange, the weakest among those studied, was largely based on models provided by counterparts in Mexico and Chile.

The second similarity is that evaluations of institutional quality depend largely on external entities. The clearest example is presented by civil aviation authorities, for which periodic evaluations by international organizations such as IATA, ICAO and the Federal Aviation Administration of the U.S. are vital. Without the approval of such agencies, airplanes do not fly to particular countries, and necessary links to the rest of the world disappear.

Civil aviation agencies constitute “threatened islands of excellence” because their capacity to thrive mostly depends on a delicate balance between the internal need to protect their vital functions and the required presence and evaluation of external actors fulfilling oversight functions. Something similar occurs with postal services: when abandoned by external partners, their viability is compromised. Efforts to rescue the national post office inevitably require agreements with companies such as FEDEX and UPS, or with the postal services of developed countries.

Differences among institutions have their fundamental roots in factors internal to each country but organizational similarities and common processes of change arise largely from abroad, particularly from the homogenizing pressures of globalization. The fear of being left behind or pushed to the margins of global circles of transportation, communications, and capital flows is what motivates governments and dominant classes to modernize and to train an increasing number of cadres abroad. As a result, Latin American institutions are becoming more and more similar, as they copy the same external models and observe each other.





Conclusions

First, the study identified important differences between institutions and countries but also significant variations that reflect the original goals, resources, and national context of each institution.

Second, differences are primarily associated with the internal characteristics of each institution and each country, while similarities correspond to influences and external pressures related to the process of globalization. That process has led to increasing modernization and homogeneity, making institutions both more similar among themselves and more oriented toward the organizational practices and models of the world centers. The evolution of stock exchanges in the three countries best reflects that trend.

Third, the study’s comparative and qualitative analysis reveals the crucial role of proactivity in the profile of institutions capable of realizing significant contributions to development in their respective spheres of action.

This research should help move the field of institutional analysis beyond speculative typologies and vague declarations that “institutions matter.” The study demonstrates the viability of empirical comparative research with institutions as units of analysis, and shows how the application of state-of-the-art methodologies can uncover trends and results unseen by the naked eye. A larger sample of such units will enable future studies to arrive at new findings of the ways that institutions can lead to developmental outcomes in terms of sustained economic growth, more equitable distribution of wealth; and democracy and observance of human and civil rights. This institutional analysis is compatible with the view that the state must be actively involved in the economy if development is to be achieved.

– Alejandro Portes and Lori D. Smith (2008) “Latin American Institutions and Development: A Comparative Study.” *Studies in Comparative and International Development*, Volume 43, No. 2: 105-128.

Center for Migration and Development Spring 2009 Colloquium Series

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Thursdays at 12:00 PM
Bressler Conference Room – 165 Wallace Hall

- Feb 12** – *The Second Generation In Eight European Countries: Does The Integration Context Matter?*
Maurice Crul
University of Amsterdam
- March 26** – *The New Demography of America’s Schools: Immigration and the No Child Left Behind Act*
Jeffrey Passel
PEW Hispanic Center
- April 2** – *Global Crises, Past and Present*
Beverly Silver
Johns Hopkins University
- April 9** – *Nationalist Versus Dependent Capitalist Development: Alternative Pathways of Asia and Latin America in a Globalized World*
Atul Kohli
Princeton University
- April 23** – *A Movement Wrestling: American Labor’s Enduring Struggle with Immigration 1866-2007*
Janice Fine
Rutgers University
- April 30** – *Islam in Democratic States: Muslims in Europe and the United States*
Joselyne Cesari
Harvard University

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May 13 – 15, 2009

