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On *The Politics of Property Rights* by Haber, Razo, and Maurer[1]

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1. *Introduction*

Everyone knows that political instability is inimical to economic growth. So what would be expected of a country in which:

A military insurrection overthrew authoritarian rule;

Supporters of the old regime then staged a counterrevolution, provoking a civil war;

The first two presidents to preside over the subsequent peace were assassinated, as were their leading military leaders; and

The military attempted three times to overthrow the civilian government during its first decade in office.

With thoughts turning to Congo (Zaire), this reader would think "basket case" and assume a negligible (or negative) rate of growth. And this reader would be wrong.

The case is Mexico, 1876–1929. After collecting and analyzing data on banking, manufacturing, mining, petroleum, and agriculture, Stephen Haber, Armando Razo, and Noel Maurer conclude that from 1876—i.e., the date of the ascension to power of Porfirio Diaz—to 1929—the *anno miserable* that bounds so much of modern economic history—the Mexican economy grew. "If investment and output rose in petroleum, manufacturing, mining, banking, and agriculture," they argue, "then in aggregate the economy was growing" (p. 15). However discomfiting, their conclusion appears inescapable: "There is no *necessary connection* between political instability and economic stagnation" (p. 15).

As recognized by Haber et al., econometric analyses of cross-national data have failed to find strong evidence of a relationship between political instability and the rate of growth of incomes. As stated by one study, the evidence that instability "causes a decrease in the growth rate of per capita income seems much weaker than generally believed."[3] So counterintuitive are these findings that they tend to have been ignored. While evidence from a single country cannot carry an argument, the micro-level data presented by Haber et al. suggests that the

[1] Stephen Haber, Armando Razo, and Noel Maurer. *The Politics of Property Rights: Political Instability, Credible Commitments, and Economic Growth in Mexico, 1876-1929.* Cambridge, New York and Melbourne: Cambridge University Press, 2003. Hardback, Pp. *xx*, 382. ISBN 0-521-82067-7. $75.00.

[2] I wish to thank John Coatsworth and Jeffrey Williamson for their comments, and to absolve them of responsibility for any errors that may remain.

[3] Nauro Campos and Jeffrey Nugent 2002, pp. 164–65, quoted in Haber et al. p. 8. See Campos and Nugent (2002). See also Aymo Brunetti (1997); John Londregan and Keith Pool (1990; 1992).

cross-national evidence is not anomalous and needs be taken seriously. If there is a political villain, they teach us, it is political violence, not political instability.

2. *The Study*

While each industry, they find, exhibited a surprising level of resilience, they did not all exhibit the same economic trajectory. The petroleum industry behaved as if immune to the political chaos about it.

Mexican petroleum output increased regardless of political instability, or increases in the tax rate. In fact, even the period of civil war (1914–17) could not stop the upward surge in output. Every single year from 1910 to 1921 witnessed higher levels of crude oil production (p. 212).

In banking, by contrast, firms failed to recover rapidly from the period of intense violence (1914–17). The warring armies had plundered the vaults; each faction subsequently issued its own banknotes; and the reestablishment of the financial system posed a major challenge to later governments. "While the banking system grew rapidly," the authors note, "it did not achieve anything like its pre-revolutionary size" (p. 114).

In agriculture, the export sector expanded throughout the period of turmoil, increasing its shipments to the United States. The production of staple crops did not. For the most part, however, food shortages were local in extent and short term in nature; aggregate supply largely kept pace with demand, with price series yielding little evidence of widespread or protracted shortages.

Manufacturing and mining, by contrast, virtually came to a standstill during 1914–17 but quickly recovered when the violence ceased, rail transport resumed, and supplies could be purchased and products shipped to market. By the mid-1920s, the level of output well exceeded that exhibited at the beginning of the time of troubles.

As might be expected, the data that drive this conclusion are highly imperfect. For some years—usually during the height of the violence, 1914–17—they do not exist. Covering an era in which much was destroyed, the sample is censored in a way that could induce a bias in favor of economic growth. By cutting into the problem from different angles, however, the authors seek to counter the first limitation. They gather data not only on inputs, outputs, and levels of productivity, but also on profitability, rates of return, expected rates of return (as inferred from the valuation of stocks), exports, imports, capacity utilization and other indicators of economic activity. To address the second limitation, they take care to gather data from failed firms. In addition, they "norm" industry trends before characterizing them, as by comparing the performance of Mexico's mines with that of mines in the contiguous regions of the United States or machine imports by Mexico with imports by other Latin American countries over comparable periods. The conclusion seems clear: despite political turmoil, disorder, and war, Mexico in the late 1920s was vastly more prosperous than Mexico in 1876. There had been economic growth in the midst of political disorder.

In this essay, I shall explore the way Haber et al. confront this anomaly. In so doing, I shall also press their work into service, assessing its implications for other eras and other portions of the world. In particular, I shall relate the approach of Haber et al. to the political turmoil and *lack* of economic development in contemporary Africa—what William Easterly and Ross Levine (1997) have termed a modern "growth tragedy."

3. *Exposition and Interpretation*

Both common sense and economic reasoning give rise to the expectation that political instability should undermine economic growth. Political instability leads to uncertainty, most relevantly with regard to property rights. As stated by Hobbes, where there is political conflict, "there is no place for industry because the fruit thereof is uncertain, and consequently no cultivation of the earth; no navigation, nor use of the commodities that may be imported by sea; no commodious buildings…."[4] And as argued by Douglass C. North and Robert P. Thomas (1973), by aligning the social and private rate of return, property rights strengthen the incentives for productive effort. If economic activity takes place amidst political turmoil, then changes in the laws, regulations, or policies might alter the expected value of an investment program. Insofar as political turmoil thus increases economic uncertainty, investors will discount the future more heavily, leading to less capital formation and less growth.

Why, then, do Haber at al., like Nauro Campos, John Londregan, Jeffrey Nugent, and Keith Pool before them, find economic reality at variance with expectations? The key, Haber et al. argue, is that property rights are private, not public, goods. In the midst of political chaos—indeed, in response to political chaos—political entrepreneurs will strive to provide property rights. In doing so, they target particular people, firms, or industries, not the entire economy. They do so in order to reward their friends, to build and consolidate a constituency, and to generate financing for their political machines. In the midst of chaos, then, investors will find political patrons eager to protect them, in exchange for political and economic support.

The politics of developing countries is, in general, unstable: thus the initial comparison of early twentieth-century Mexico to contemporary Africa. The politics is also characterized by the private manipulation of public power, a phenomenon variously characterized as cronyism (A. Fishlow, C. Gwin et al. 1994), rent seeking, (Anne Kreuger 1974) or corruption (P. Mauro 1995). Spurred by their unexpected finding—that economic growth can take place amidst political instability—Haber and his colleagues invite us to look again at these phenomena, focusing on their benefits as well as their costs, and on the political processes that underlie them.

In addressing the private manipulation of public power, economists tend to emphasize the demand side of the "political market." Those with money either bribe officials, secure protective shelters, or, by purchasing insider positions, gain competitive advantages in the market place. Political scientists emphasize the supply side. Politicians compete; the political environment defines what it means to win and the strategy that best responds to the challenges posed by competitors. Some, such as myself (Bates 1987), Daron Acemoglu and James Robinson (2001), and others (e.g. Barry Ames 1987), view the political distortion of markets and patterns of intervention in the economy as reflecting the efforts of politicians to organize a core constituency, to disorganize the opposition, and thus to survive and prevail in the competition for power. In their analysis of the several industries that dominate the Mexican economy, Haber and his colleagues come to align themselves with the latter approach. They analyze the ways in which politicians capture firms and industries; regulate them in ways that generate supra-competitive rates of return; and govern them in a manner that gives assurances to investors, thus attracting capital and yielding growth.

In doing so, Haber et al. formulate a theory of "vertical political integration."[5] By this they mean not only the alliance of politicians with investors, but also the alignment of incentives. Insofar as politicians succeed in attracting investment to particular enterprises, and insofar as they supply conditions that generate non-competitive rents and

[4] Thomas Hobbes (1651).

[5] Infelicitously shortened by Haber and all to "VPI." Why must so many who venture into the realm of positive political theory be enticed to substitute acronyms for reasoning?

artificially high rates of return, then the temptation to engage in predation grows. Investors, being rational, recognize the incentives at play. In order to provide them assurances, politicians must render themselves hostage to the performance of the firm. In particular, they must attach their political future to its economic performance, thus signaling that even when political times are hard and the future therefore uncertain, they will not opportunistically defect from their commitments. The micro-level arrangements that produce macro-level growth are the introduction into the industrial structure of agents who are willing and able to collude in destroying the political fortunes of the leader that put them there: organized labor, in the case of manufacturing; powerful elites, in the case of banking; and the United States, in the case of petroleum and mining.

In viewing property rights, scholars have, along with Hobbes, referred to sovereigns; that is, they have focused on the national level. Alternatively, they have looked at the manner in which sovereigns "tie their own hands," as through sharing power with parliaments (Douglass North and Barry Weingast 1989). Such approaches are too macro, Haber et al. imply; the key lies instead at the micro-level—the level of industrial organization. Even in the midst of aggregate political chaos, incentives at play at the level of the firm can provide sufficient security that investors find the expected returns sufficiently high to warrant risking their capital.

In advancing this argument, Haber et al. isolate factors that amplify or diminish the capacity of politicians to forge an economic base. One is the time horizon of the politician. When there is no tomorrow, then there is no incentive to behave with restraint. If there is a meaningful future, other factors then come into play. One is the nature of the product produced by the firm. When it is virtually appropriable, as in the case of cash deposits, then the incentives to predate are overwhelming; when the firm must be operated in order to generate value, as in mining or manufacturing, then the politicians have stronger incentives to act as custodians rather than predators. A second factor is the technology. If knowledge of the technology can be acquired only at high cost, politicians face stronger incentives to nurture rather than displace the owners of the asset. Economic returns must then be elicited rather than extracted.

4. *Extensions*

Returning to the initial comparison between Mexico in the past and Africa today, do Haber et al.'s findings give reason for optimism: be it ever so unstable, politically, might Africa, like Mexico, nonetheless grow? Not where there is actual violence, the Mexican data suggest: in 1914–17, every industry, save oil, virtually collapsed. How about when there is the threat of violence, i.e. when, as in Angola or Liberia, politics takes the form of bargaining between armed groups and warlords? Here there does appear to be room for greater optimism. The materials that Haber and his colleagues present suggest that military leaders seek to build political organizations; that they need to generate a flow of revenues to support these organizations; and that they therefore have an incentive to protect and nurture an economic base. The implication of their work is that if the leader is shrewd enough to introduce a governance structure that signals to those with capital that his political future is forfeit, should he engage in predation, then investment is likely and growth possible, even in the midst of state failure.

Haber et al.'s study of economic growth in Mexico is both scholarly and provocative. Rich with insights into economics, politics, and history, it is laden with implications for the study of conflict. Its basic lesson is, of course, that the costs of political disorder can be surprisingly low. But how might students of modern Africa react to that assertion? Taking myself as a sample of one, I confidently proclaim that the reaction of these scholars will come in two stages: first skepticism, and then curiosity.

Returning to Haber et al., we can perform comparative statics on their "theory" of vertical political integration and note the factors that influence the incentives for those with political organizations to govern prudentially. The strength of these incentives will vary with the following:

The Discount Rate of the Warlord. If military pressure threatens the demise of his forces, then the level of destruction will be high, not only because he has little incentive to conserve productive capacity but also because of the fear of that capacity falling into the hands of his rivals.

The Technology. The more sophisticated the technology of production, the more costly it is to master the technology, the stronger the incentives to leave those who have mastered it in place, the more likely is the productive organization to be taxed than appropriated.

The Temporal Characteristics of the Production Process. When production is multi- rather than single-period, then warlords are more likely to exercise restraint.

Given the implications that flow from the notion of vertical political integration, we gain insight into the disparate economic performance of the troubled polities of Africa and Mexico.

The incentives for armed groups in contemporary Africa to husband rather than destroy may be weaker than those in Mexico because the armies are weaker and more vulnerable. The Mexican army had twice recently fought a major power, the United States. Even when it fragmented during the civil war, with different regiments aligning with rival political factions, many units retained a professional core. While selected forces in Africa's militaries exhibit technical proficiency and professional discipline, most do not. Many are made up of unemployed youths, who find in fighting the excitement and opportunity that they lack in civilian life.

Moreover, the technologies of production in Africa yield fewer incentives for political husbandry. Many of the resources that form Africa's economic base are eminently lootable. Coltan lies in surface deposits and can be dug by hand; diamonds can be screened from gravel; cattle can be stolen; and trees felled by axe and saw. Where readily appropriable, these resources have been confiscated by force; many of the wars in Africa are resource wars.[6] But, as in Mexico, where deposits of metal, petroleum, gems and ore lie deep underground or require processing before acquiring value, then private wealth is left largely intact. Firms operate, and investment does take place.[7] Part of Africa's growth tragedy may thus derive from the extent to which its extractive industries employ technologies that can be mastered at very low cost.

In addition, to a great degree in Africa, the economies of the war zones are based on annual crops. Absent the need to refrain from looting today for fear of scarcity tomorrow, armies have few incentives to refrain from pillaging today. The dry land savannahs of East Africa, the woodland savannahs of Central Africa, and the equatorial zones of West Africa—the economies of each are based on the production of cereals: millet, sorghum, and maize. The evidence of the impact of the resultant incentives is the well established link between warfare and famine in Africa, something differentiating it from the Mexican case.

The analysis of Haber et al. would also suggest that armies that receive external sources of financing would behave differently than those that generate their own revenues. Sponsorship of local militias by foreign governments is a common feature of

[6] Collier, Paul and A. Hoeffler 1998.

[7] It is notable that in the war-torn portions of Southern Africa, e.g. Congo Brazzaville and Angola, petroleum production continues and new investments flow into the region for exploration, production, and refining. The combatants guard rather than loot these assets.

military conflict in Africa. And the assurance of funding from abroad would decrease the incentives to protect productive capabilities at home, much less to invest in them.

There is another important factor at play, which is largely omitted from Haber et al.'s analysis. While there was civil war in Mexico, there was not, it would appear, state failure. That is, save for some short periods and in some relatively isolated areas, local and state governments continued to operate, even in the midst of the revolution.[8] Such is not the case in much of Africa, where in Somalia, Liberia, and other places, the state has either collapsed, or itself become but one of several contending forces. The absence of a powerful third party, able to mediate among contending factions, distinguishes conflict in Africa from that in Mexico.

Implicit in Haber et al.'s analysis are not only insights into economic costs of conflict but also into the prospects for demilitarization. An implication of their analysis is that the conditions that yield economic success may impose political costs, in the sense of rendering political demobilization more difficult. One of the economic fruits of political antagonism is the generation of rents, as politicians strive to protect the industries that yield them revenues. The rents accrue to the politicians, of course, but also to the groups that mediate their political fortunes; in the system outlined by Haber et al., it is they who are the guarantors of the politician's pledges of property rights. The political origins of the rents thus rest on the need for military and political protection. Should the political elite become more secure, then their value would decline. The implication is that even if elites should seek pacification, their retainers will oppose them. This opposition is the more likely the more successful they have been in underpinning political restraint and eliciting productive investment. The retainers, the logic suggests, might thus constitute an insider lobby against pacification. And, suggestively, this lobby is more likely to form in countries that are more prosperous.

[8] John Coatsworth, personal communication.

5. *Conclusion*

In *The Politics of Property Rights*, Haber, Razo, and Noel give us pause: they demonstrate that political disorder need not undermine economic growth. Reconceptualizing property rights as private rather than public goods, they specify the micro-foundations for what they term "vertical political integration:" a form of industrial organization that lends credibility to political assurances. They apply this approach to the political economy of turmoil in Mexico, 1876–1929. In this essay, I have extended it to the political economy of contemporary Africa.

This study is highly suggestive and freighted with implications, not only for economics but also for politics, and not only for historians, but also for those concerned with development in the contemporary world.

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