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Rustem Nureev

professor, Financial University under the Russian Government

DEVELOPMENT ECONOMICS: Neoinstitutional Approach of Hernando de Soto.



- 1. Hernando de Soto's "The Other Path": new view on illegal economy.**
- 2. Hernando de Soto's on the way to solving the capital.**

1. Hernando de Soto's "The Other Path": new view on illegal economy



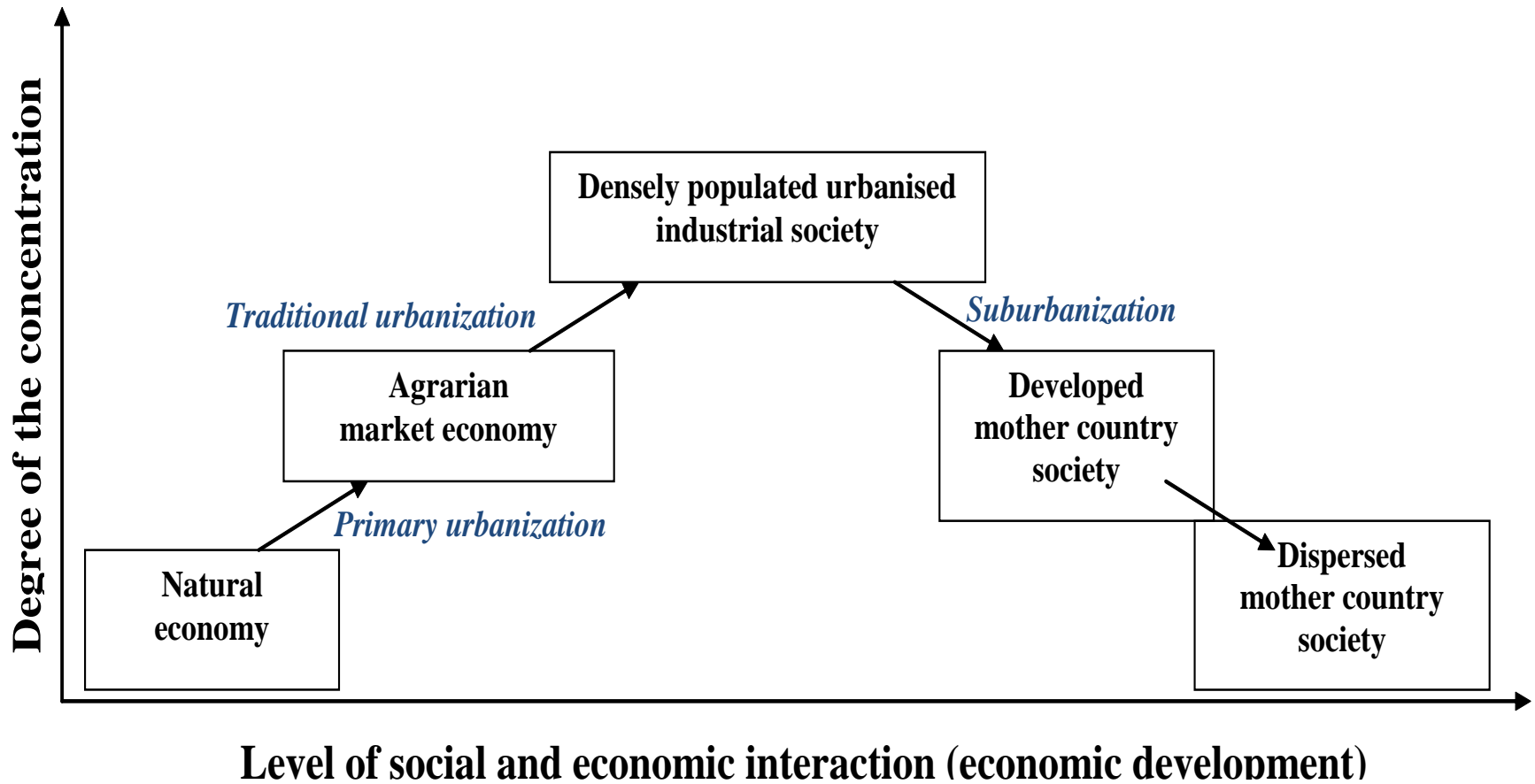
*1941z. Was born in Arequipa (Peru).
Has finished postgraduate study in Geneva
Worked as an economist in GATT.
Director of the Central reserve bank of Peru.
Now - chairman of mining firm,
the president of The Institute for Liberty and Democracy*

1989 г. - The Other Path: The Invisible Revolution in the Third World.

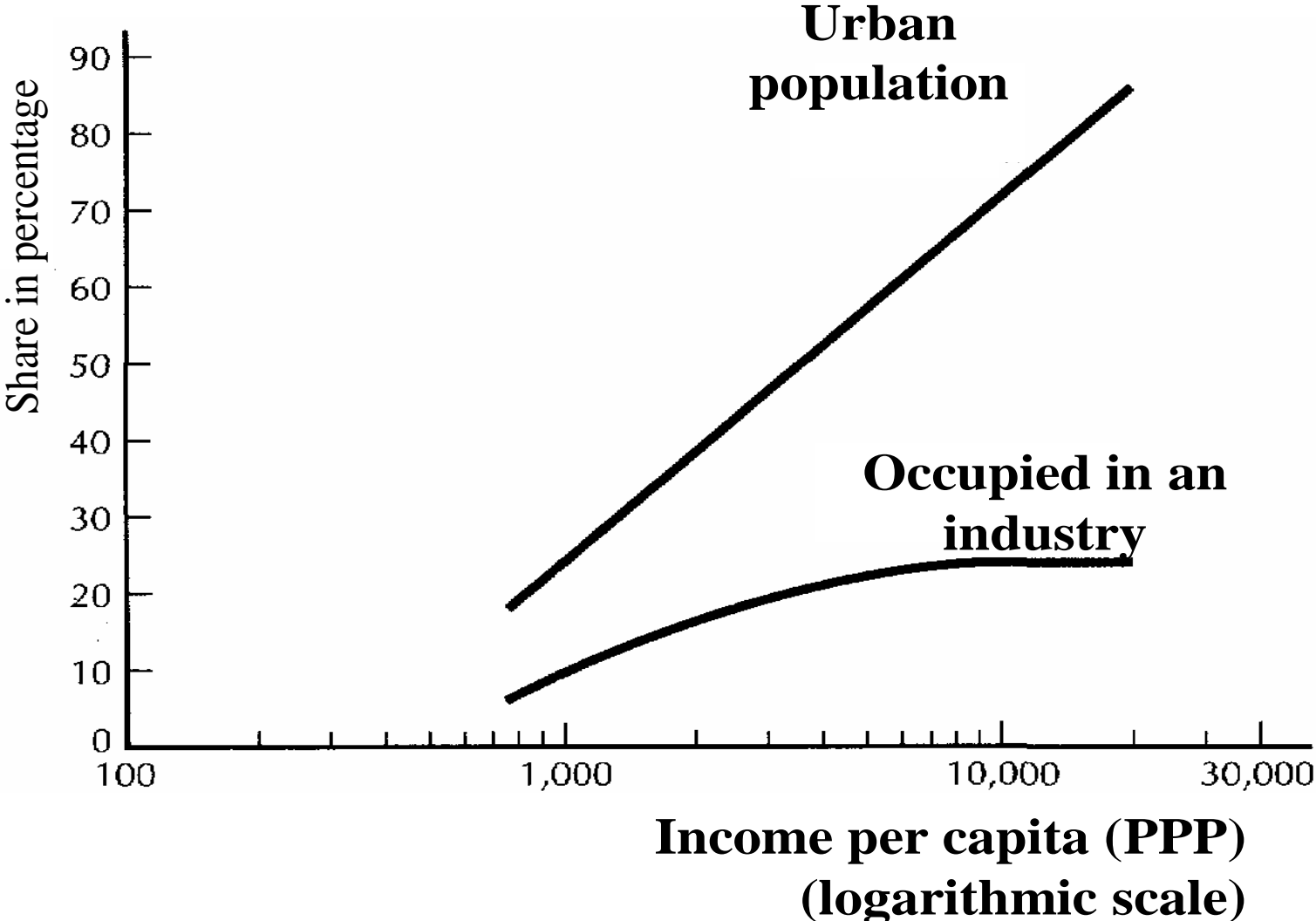
The example of Peru – the process of urbanization.

	Urban	Rural
1940	35	65
1981	65	35

URBANIZATION AND SUBURBANIZATION IN THE COURSE OF ECONOMIC DEVELOPMENT



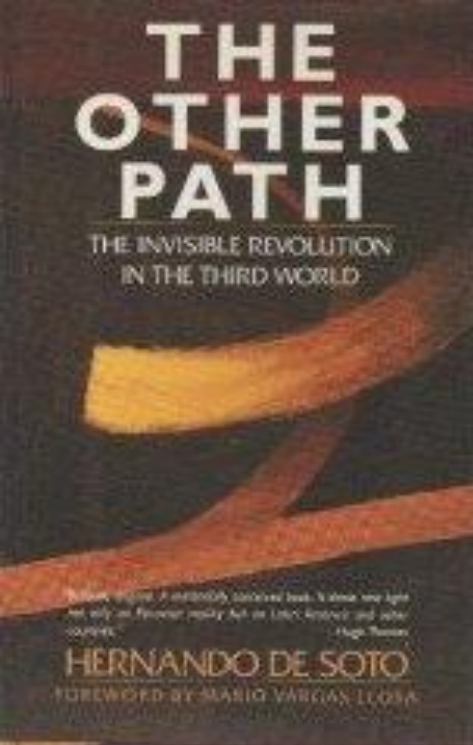
URBANIZATION AND INDUSTRIALIZATION



TYPES OF INCOMPLETE USE OF WORK IN DEVELOPING COUNTRIES

Type	Unemployment	Underemployment
Explicit	Mostly among recently urbanized population	Agricultural and seasonal workers
Implicit	Basically women (who ceased search for work)	Agrarian + city informal sectors (the latent unemployment)

Source: Gillis M., Perkins D.H., Roemer M., Snodgrass D.R, *Economics of Development*. 4th Ed. N.Y. 1996. With. 229



Part 1 - Empirical

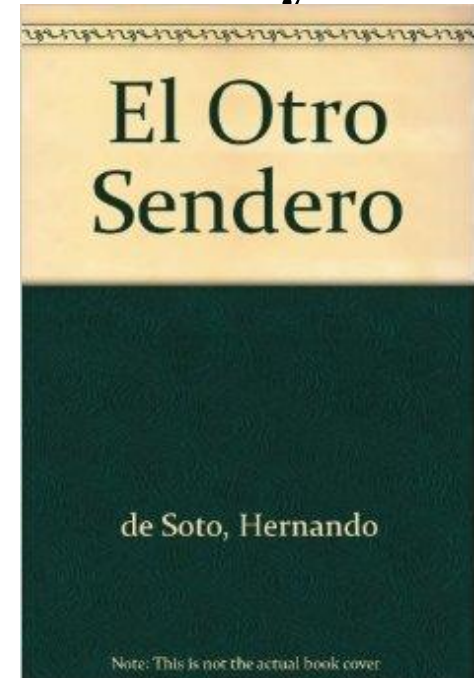
Three spheres of underground economy:

1. *House-building;*
2. *Trade;*
3. *Transportation.*



Part 2 - Theoretical

1. *Costs and value of the law.*
2. *Traditions of redistribution.*
3. *A parallel with mercantilism.*



EMPERICAL PART

I. ILLEGAL TRADE.

1.. Kinds of illegal trade.

1.1. Street

200-300 thousand street dealers.
20 % of the poorest districts..

Specialization of trade:

59,5 % - foodstuffs.

17,5 % sanitary-and-hygienic goods.

13,7 % services.

9,3 % - household goods and the equipment for offices.

Total sales:

6,2 million \$ in a week;

322 million \$ in a year.

A monthly turn of a point: from 155 \$ (services) up to 431 \$ (foodstuffs).

TWO TYPES OF STREET TRADE:

1.1.1 Peddler.

- *Insignificant capital;*
- *Inaccessibility of the credit (cash);*
- *Investments into the human capital (gathering of the necessary information);*
- *Definition of favourable places and aspiration to be fixed on them.*

1.1.2. Trade in the certain places of street.

Capture of street:

- finding-out of a place value;
- definition of size of the expected net profit;
- overcoming the resistance of:
 - shopkeepers;*
 - inhabitants;*
 - authorities.*
- Search of allies:
 - transport;*
 - other dealers - agreements, etc.*
- Shopping-streets - minimarkets;
 - division of labour and specialization;*
 - expansion of assortment;*

The special property rights - *interrelation between a seller and the place which he or she was fixed on.*

- **Advantages:**

- Recognition of the seller is a sign of his reliability;
- Reputation at buyers and suppliers;
- Possibility of reception of credits (illegal).

- **Disadvantages:**

- The property right is unstable and illegal;
- Exile threat;
- Impossibility to make long investments;
- Difficulties of resale (only to "fellow countryman").

- **Ways of resolutions of conflicts:**

- Use of carts (cars) – product line enlargement;
- Trade by turns;
- Payment of the tax to municipal authorities

(For municipal authorities in Lima such tax in 1.7 times is more, the tax from official dealers)

The self-defence organisations

- **Functions:**
Maintenance of the order;
Cleanliness.
- **Forms:**
Self-organising;
Attraction of national guards or municipal police;
- **Levels:**
The local;
The federal.

1.2. THE MARKET

1.2.1. The markets and fairs

Role:

- The basic
Lima: 274 illegal markets (82,8 %)
57 state (17,2 %).
- The arrangement more convenient for the poor.

The maintenance organisations – the association:

- **Building of the markets;**
- **Maintenance of order;**

1.2.2 Evolution of illegal trade

Evolution factors

- **Mass movement;**
- **Clashing interests;**
- **Disputes and violence;**

The basic stages

- **De Soto allocates 13 stages of evolution: replacement of lawful society and expansion of the illegal one.**
- **Two basic moments:**
 - Fight for the special property rights;*
 - Fight for the markets.*

II. ILLEGAL TRANSPORT

Public transport in Lima in 1984r (%).

	The legal	The illegal
Buses of all kinds	9	91
All public transport, including a taxi	5	95

Types of illegal means of transport.

Routeing taxi - on 5 persons.

Minibuses - of 8-11 persons.

16-18 sedentary (only 43).

Buses of 71-90 passengers.

Cost of illegal park of buses - \$620 million in 1984

1. Grab of routes.

1.1 Conditions of the beginning of a business activity

- **The account of interests;**

Passengers;

Competitors;

Police and bureaucracy;

- **Contact to officers;**

Bribe to the officer of the ministry;

Giving the official application;

1.2 Right to the routes appropriation.

- **The conditional;**
- **Limited to the right of other members;**

1.3 Illegal organisation of drivers.

- **Forms:**

Committees of drivers - illegal immigrants of one route;

Their associations - federations;

- **Advantages**

Decrease in working costs;

Regularity of the services supply;

Cost-saving of negotiations with the authorities;

Protection of a route against a competitiveness from beginners.

- **Functions of the organisations:**

Organizational-economic (on route operation), including price-fixing;

Struggle for legalisation of the rights;

Creation of the joint insurance fund;

2. Evolution of illegal transport.

Since 1874 - de Soto allocates 17 stages.

1. Passenger-fare regulation - main costs of legalisation;

The official recognition of carriers is considered not as a rule but as a privilege granted in exchange for acceptance political interferences, including the passenger-fare control

2. Traffic safety decrease (owing to decrease in the sum of fines)

In road accidents in Peru perishes
in 11 times more people, than in Germany
in 19 times - than in the Great Britain

III. ILLEGAL HOUSING CONSTRUCTION

The area of Lima has grown 1940-1981 on 1200%.

Housing construction in Lima, 1982 (%)

	Illegal	Legal	
		Buildings	Slums
Share of buildings	42,6	49,2	8,2
Share of population	47	45,7	7,3
Value of Buildings	90,6	9,4	

Source: *De Soto. The Other Path. The Invisible Revolution in The Third World. Moscow, 1995. P. 54*

1. Ways of the illegal property grab:

1.1. Grab

- Gradual (in existing settlements);
130 cases from 157 suburbs of Lima.
- Violent (on the new earths).
24 cases.

The contract on grab.

The expected property right.

- Presence;
- Amateur enumeration;
- Negotiations with the authorities (take about 20 years).

The illegal organisations

- adjustment of negotiations with the authorities.
- Legitimacy and order maintenance

- Associations of urban development;
- Associations of settlers;
- Settlement organisations;
- Municipal committees, etc.

1.2 Illegal land sale.

Acquisition of agricultural lands through the organisations and co-operative societies.

In the conditions of agrarian reform (liquidation of surpluses) 1985 г - 269 organisations have attached of 3400 hectares to a city. The agricultural lands = 34 million m².

2. Evolution of illegal housing construction.

2.1 Occurrence of illegality.

The occasion was given by the authorities in the beginning of 20th century, infringing upon laws regulating town development.

2.2 Recognition through resettlement.

2.3 Political recognition.

Support of political parties and movements.

2.4 Legislative recognition (since 1961).

**Settlements;
Private property;
The illegal organisations.**

3. Results

1.1 Has gone on advantage to low-yield people.

1.2 Has saved a city from transformation into continuous slums.

1.3 Promoted private property strengthening.

	1981/1961
Number of private houses.	+375 %
Number of leased houses.	-34 %

THEORETICAL PART

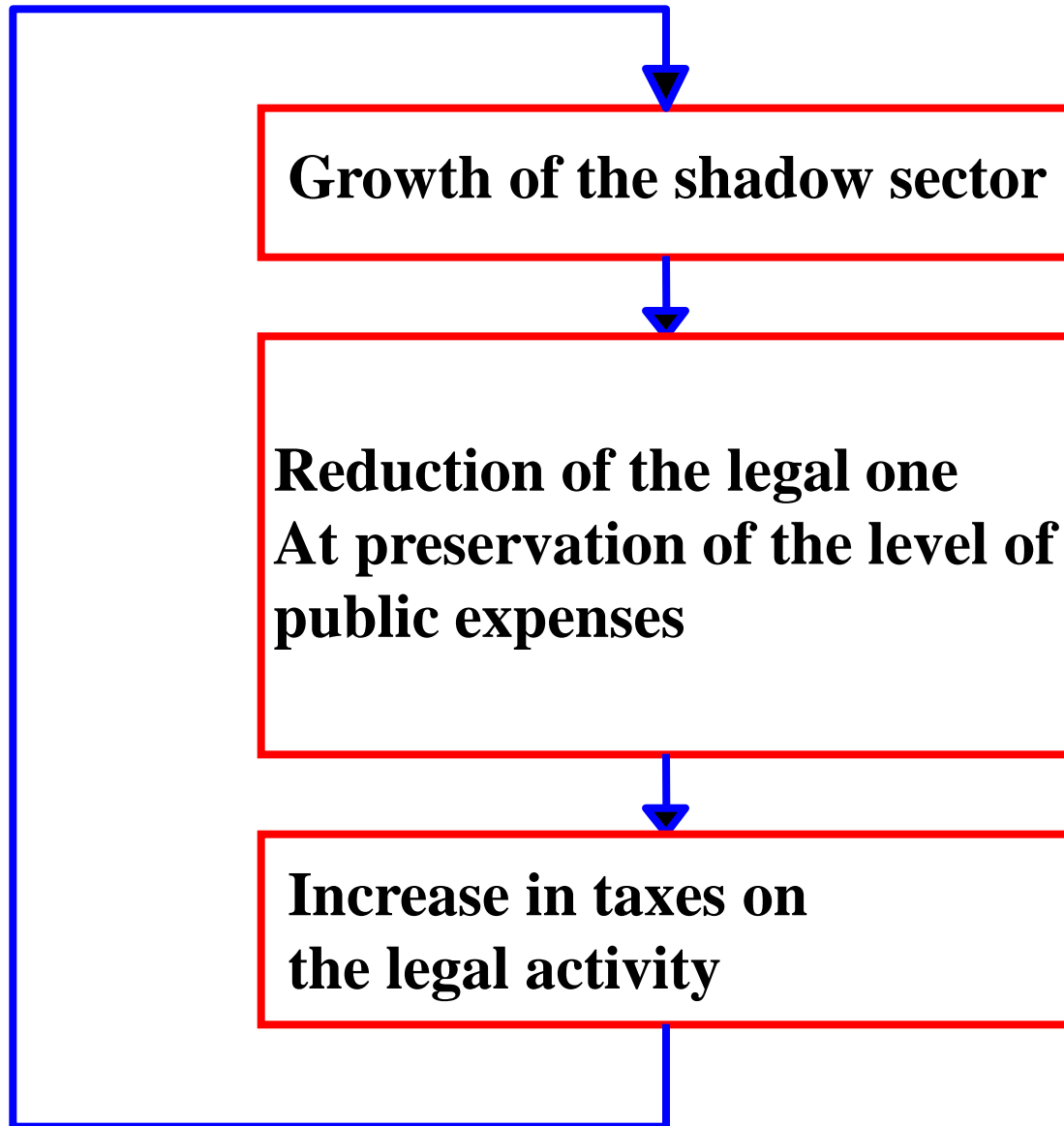
"THE PRICE OF SUBMISSION TO THE LAW" IN PERU

(Experiments of The Institute for Liberty and Democracy of H de Soto)

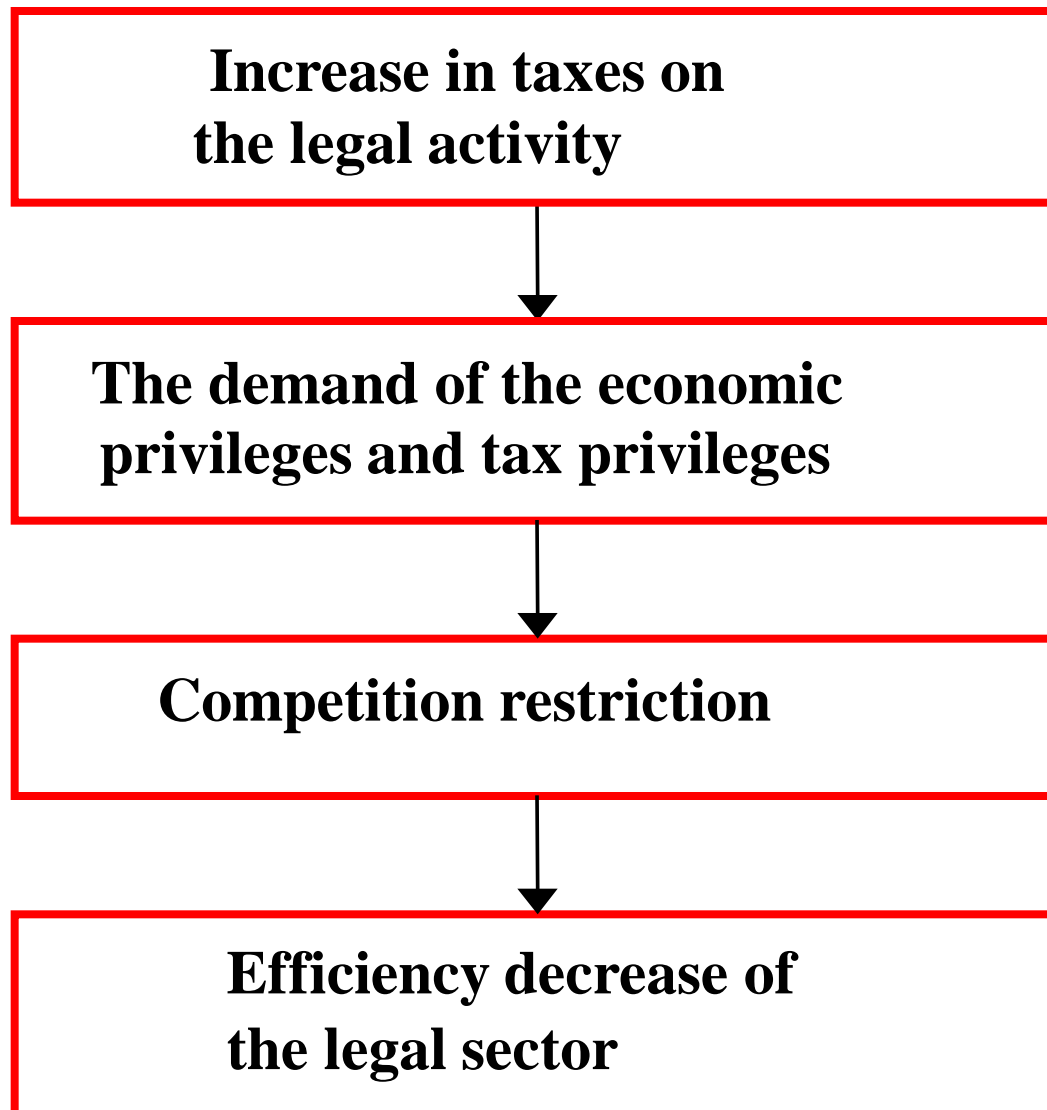
ACTIVITY KIND	EXPENSES	
	TIME (days)	MONEY (minimum of the salary *)
FACTORY REGISTRATION ON TAILORING	289	32
RECEPTION OF THE LICENCE for trade in a street booth	43	15
RECEPTION OF THE LAND LOT for housing accommodation building	2500 (about 7years)	56

- The minimum monthly wages in 1983 in Peru were equal \$38,47
- It is made on: de Soto H., The Other Way, With. 12-13

THE VICIOUS CIRCLE OF ILLEGALITY



CONSEQUENCES OF THE VICIOUS CIRCLE OF ILLEGALITY



DISTINCTION BETWEEN GOOD AND BAD LAWS

(BY HERNANDO DE SOTO)

The good law - GUARANTEES AND INCREASES EFFICIENCY OF THE ECONOMY AND PUBLIC WORK, THAT IT REGULATES,

The bad law - DESTROYS OR COMPLETELY LIQUIDATES THE ONE, AND THE OTHER.

WHY IN PERU BAD LAWS DOMINATE?

THE GOVERNMENT TAKES ATTENTION FIRST OF ALL TO REDISTRIBUTION OF PRESENT INCOMES, INSTEAD OF CREATION OF NEW RICHES.

MAIN COSTS - ARE CONNECTED WITH CONDUCTING REDISTRIBUTIVE WARS.

RESULT - ABSENCE OF EQUALITY OF PEOPLE BEFORE THE LAW

- 1. ONE LAWS PROMISE PRIVILEGES,*
- 2. LAWS ARE NOT ACCESSIBLE TO THE OTHERS.*

OVER 98 % OF ALL LAWS OF THE STATE STARTING BY ADMINISTRATIVE AUTHORITIES WITH INFRINGEMENT AND BY PASSING ELEMENTARY DEMOCRATIC PROCEDURES AND ALMOST ARE NEVER PUBLISHED.

THERE IS NO MECHANISM OF EFFECTIVE RIGHTS PROTECTION OF THE MAJORITY OF CITIZENS FROM THE STATE

IT IS TYPICAL BOTH FOR THE RIGHT, AND FOR THE LEFT PARTIES.

BOTH THOSE, AND THE OTHERS

1. EXPANSION OF THE STATE ACTIVITY;
2. DIRECTLY INTERFERE WITH ECONOMY.
3. DO IT BY MEANS OF BAD LAWS.
4. SEE THE REASON OF FAILURES NOT IN ABSENCE OF INSTITUTIONAL CONDITIONS OF ECONOMY DEVELOPMENT AND PRODUCTION OF REAL RICHES, BUT IN INCAPACITY ACCEPTED BY THEM (BAD!) LAWS.
5. ACTUALLY PROMOTE NOT TO MARKET ECONOMY DEVELOPMENT, AND ITS DISCREDIT IN THE OPINION OF THE MAJORITY OF THE POPULATION.

∑ ENTERPRISE RESOURCES OF THE COUNTRY CAN BE SHOWN ONLY WHEN IT ALLOWS BY DOMINATING INSTITUTES.

WHAT IS NECESSARY TO MAKE?

IT IS NECESSARY TO APPROXIMATE THE LEGAL SYSTEM TO THE REALITY.

TO SOLVE THE INSTITUTIONAL PROBLEMS:

- IN THE PRESENT,
- IN THE FUTURE.

For the present

REMOVING THE OBSTACLES THAT ARE OPPOSED TO INTEGRATION OF LEGAL AND SHADOW SECTORS, CREATION OF UNIFORM LEGAL AND ECONOMIC SYSTEMS EXCLUDING DISCRIMINATION. IT ASSUMES:

- 1. SIMPLIFICATION** I.E. OPTIMISATION OF FUNCTIONING OF LEGAL INSTITUTIONS BY REMOVAL OF DUPLICATING AND UNNECESSARY LAWS;
- 2. DECENTRALISATION** I.E. TRANSFER LEGISLATIVE AND MANAGEMENT RESPONSIBILITY FROM CENTRAL TO THE REGIONAL GOVERNMENTS TO APPROXIMATE THE AUTHORITIES TO A REAL LIFE AND ESSENTIAL PROBLEMS;
- 3. DEREGULATION** I.E. GROWTH OF RESPONSIBILITY AND POSSIBILITIES FOR PRIVATE PERSONS AND THEIR NARROWING FOR THE STATE.

For the future

IT IS NECESSARY TO CHANGE PROCEDURES OF NOVELS ACCEPTANCE. IT ASSUMES:

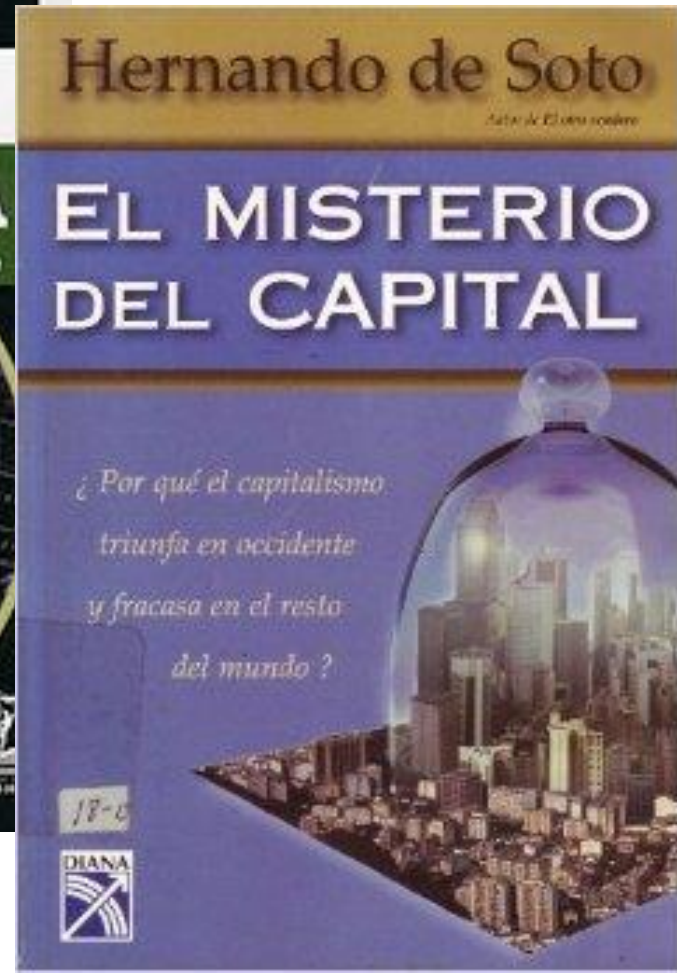
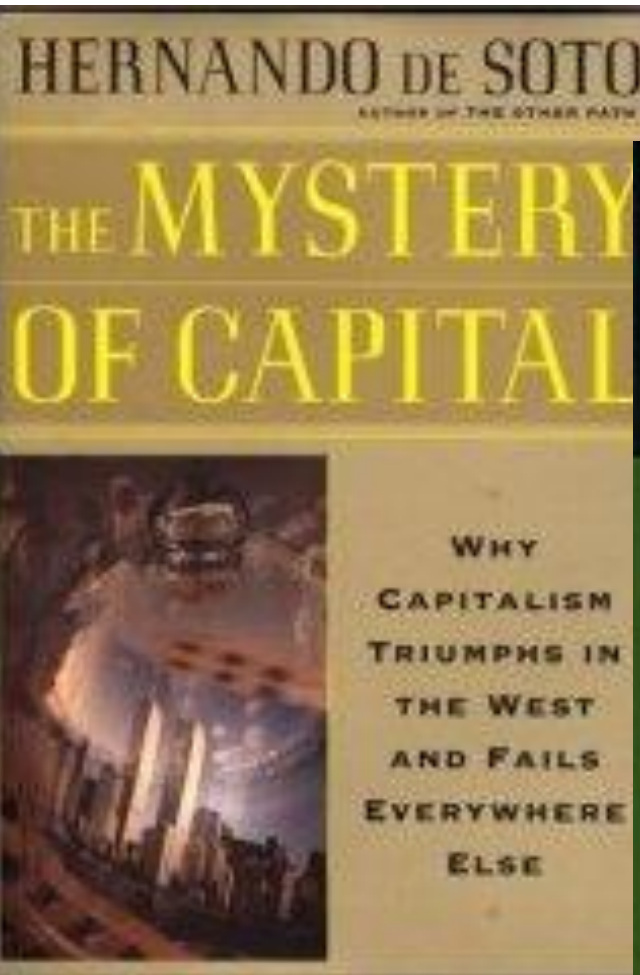
- 1. PUBLICATION OF LEGISLATIVE PROJECTS FOR THEIR FREE DISCUSSION;**
- 2. THE ANALYSIS OF LEGISLATIVE PROJECTS IN TERMS OF COSTS-BENEFITS,**

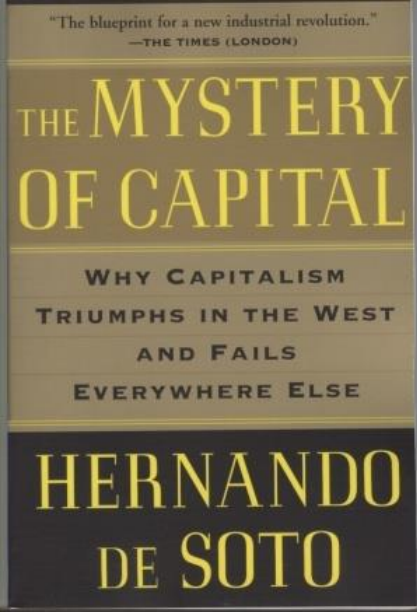
FOR THE DISCIPLINING EFFECT ON THE GOVERNMENT AND TO DENY IMPERFECT LEGISLATIVE PROJECTS BEFORE THEIR PUBLICATION.

ONLY UNDER SUCH CIRCUMSTANCES PEOPLE

- WILL FEEL TASTE TO INDEPENDENCE,

2. Hernando de Soto's on the way to solving the capital.





1. Six effects of private property

A. Smith:

«capital is the totality of property (assets), accumulated for the production purposes».

The greater accumulated capital, the wider possibility of specialization and the higher labour productivity.

- *The phenomenon of capital arose as a result the natural progress of humanity from society of hunters, herdsmen and ploughmen to commercial society.*
- *So that the accumulated assets would turn into the active capital and would serve expansion of production, they must obtain the specific form and be personified in the specific object.*

1-st – Fixation of the economic potential of assets

- *Capital appears because of its reflection in the records about **property rights**, about the guarantee, in the text of contracts and etc.*
- ***Property** – this is not house itself, but the economic concept of relative house, personified in the juridical documents.*
- *In the West the large part of objects of real estate can be with the ease used as the additional guarantee of credit as source of investment means as address of the collection of debts, percentages and taxes.*

2-nd – Integration of separate information

- *To majority of the citizens of developing and former socialist countries closed access to legal private property; therefore them it is necessary to manage extra-legally.*
- *In XIX century was undertaken the attempt to gather into the united system the separate facts and the rules, which determine property relations in the cities and villages, factories and farms.*
- *As a result long study and analysis was legalized information about the presence of active memberships and about their potential profitableness. This facilitates estimation of objects of real estate and operation with them, are created advantageous conditions for the creation of capital.*

3-rd – Owner's responsibility

- *Release of owners from under the forging action of local standards and assignment by them possibilities to act within the framework united legal system increases their responsibility.*
- *The laws, which protect not only property rights, but also adherence to the treaty, bring up in the citizens of Western countries respect for the property.*
- *Third World Countries and former socialist camp does not give the possibility to conclude profitable agreements; therefore they do not have access to the credit, insurance.*
- *They do not risk to lose the property, which do not have, they; therefore they cannot be received seriously as participants in the agreements.*

4-th – Increase in the liquidity of assets

- *In contrast to objects of real estate, property rights on them easily to combine, to divide, change, use for stimulating the economic operations*
- *Because of system of private property united factory can be in property of many investors, any of them can sell its portion of property, and this will not affect integrity and functional fitness of enterprise.*

5-th – Development of the social bonds

The system of private property makes it possible to establish:

- *the history of assets,*
- *owners,*
- *correlation with the concrete owners, which creates the legally efficient addresses,*
- *condition for execution of contracts,*
- *network of easily identified and personally critical agents of business forms from the citizens of Western countries.*

6-th – Certification of bargains

- The important special feature of western systems of private property, is the fact that they are protected from the loss and forgeries.
- Public Archives store entire information about the facts, which limit or which increase the value of assets - against the presence of mortgage, additional rights (to the passage), about agreements of lease, about burdensomeness by debts.
- Archives guarantee accuracy and opportuneness of the renovation of information, simplicity and the ease of access to it.



2. Forgotten lessons of history of the USA

150 with the small of the years ago USA were one of the Third World Country.

- Factors, which bring together America XIX cent. with the modern developing and former socialist countries:
- Mass migration of population
- Explosion of illegal activity
- Political agitations
- General dissatisfaction with obsolete legal system

Parallels with the history of the USA

The reasons, for which specialists in property relations practically did not deal with the study of problems of passage from the illegal rights to the united system of legal private property :

- Historical process is not yet completed
- The analysis of property relations traditionally is conducted on the material of developed countries
- It is difficult to trace history of creation of institute of property

2.1 Fall outside the limits of the obsolete British right

XVI cent.—unprecedented migration of Western Europeans into North and South America.

Initially order was supported according to the principles of English property rights.

However, subsequently it ceased to answer realias of the life of colonists.

Reasons:

- Absence of uniform system of the geodetic works
- The conflicts apropos of the agrarian property did not have precedents in the English usual right

Self – dependent land capture is an old American tradition

Squatteration is a self-dependent occupation of vacant lands.

Squatteration is the older than the nation and government.

Migrants occupied lands without any legal grounds.

2.2 New social contract: «tomahawk rights»

Types of property right:

- «tomahawk rights»
- «cabin rights»
- «sowing rights»

These illegal rights were:

bought,
sold and
given.

– all are as official property rights.

Breakthrough in the region of the legislation: “primary rights”

«Primary right» - the legal innovation, which made possible for settler to redeem organized land by him before it will put out to the public auctions.

- In the next 200 years this principle played key role in process of legalization of illegal property in the USA.

More than legal obstacles - it is more than the illegal

- In 1784-1850 years. USA joined - as a result purchases or achievements - the almost 900 mln. acres.
- Since 1784 year. the congress of states works at the limitation of encroachments of general national land.
- Demarcation and sale government's land: sections with an area of 6 sq. miles - 36 smaller, with area 1 sq. mile (640 acres).
1 acre = 1\$.

North Western ordinance (1787year.)

- Affirmed concept “without conditional or unlimited property rights” (eternal property of objects of real estate with the unlimited right buy or sell it);
- Created first in the history of the USA guarantee of freedom to conclude transactions
- Although the federal laws outlined the elegant structure of legal sale of government' s of lands, they were unable either control or hold in control displacements in the outskirts of state of growing number of migrants.

Main land administration (1812year.)

- Confirmation of documents, which certify property rights to land;
- Registration of purchases of land by credit

«Land's certificates»

- Soldiers, who participated in the revolutionary battles
- War veterans 1812year.
- Participants in the war with Mexico. .

In the middle of XIX century. the Black Market for land certificates, which whipped both the speculation and illegal seizure of land, arose

Of 100 of those received land certificates 84 they sold them on the Black Market.

2.3 Lawlessness or collision of the legal systems?

Migrants created our own “laws” on basis of the confluence of English legal tradition, the emergent in America rules of law and our own common sense.

Result - “plurality of vested rights of property”, determined in two different legal and economic systems:

- codify and reflected in the arch of the laws;
- Used in the everyday practice.

USA began to live within framework of pluralistic legal system.

2.3.1 Fight with lawlessness: policy of the states

- Politics increasingly were inclined to support of illegal.

History of adoption of laws, which recognized right to land after the fact who its organized by, in the USA XIX cent. - this is history of lift of illegal as political force

They ceased to be “malodorous law-breakers”, who insolently seize the best land of the country, and they became into “valiant pioneers”, diligently of the workers above its development, and also potential voters.

2.3.2 Fight with the lawlessness: policy of federal center

1830 year. – the coalition of congressmen of western and southern states conducted general law about the primary rights to land.

1832, 1838, 1840 years. – congress renewed law about the primary rights to land.

To 1841 year. Law about the primary rights so was affirmed that the congress accepted the general law, which is applied to the future periods.

2.3.3 Fight with the lawlessness: action of illegal

the illegal organizations, which served protection those not recognized as law of property rights

Associations of aspirants to land- extended in the American Middle West in the first middle of XIX cent.

- Assiduous regulations of mountain regions, which covered the West of the country after discovery of gold in California.

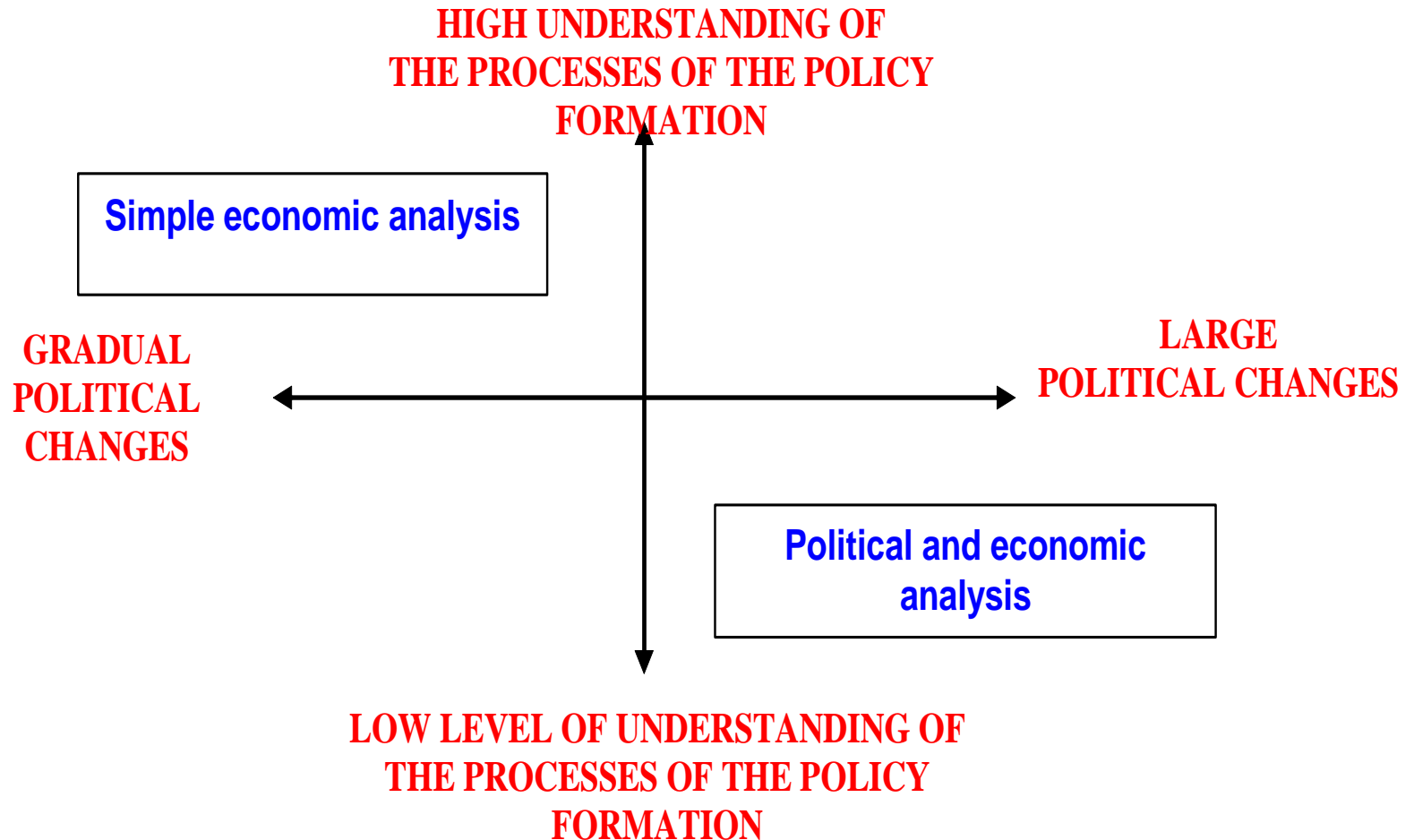
2.4. Lessons of American experience for the Third World Countries and former socialist camp

In transformation of USA into the most powerful and most abundant by capital market economy of peace central role played the acknowledgement of legality of illegal property rights, their integration into general national system of private property.

American experience shows that change of legal system in developing and former socialist countries is this the triune task:

- To explain that the real property relations represent by themselves
- To integrate them within the framework legal law
- To advance political strategy, capable of ensuring success of reforms.

Types of Economic analysis and its influence on the political changes



An aerial photograph of a densely populated city, likely Rio de Janeiro, Brazil, with a mountain range in the background. The city is filled with numerous high-rise buildings and residential structures. The lighting suggests it is either early morning or late afternoon, with a warm, golden glow. The text is overlaid in a bold, yellow font.

Thank for your attention!

Obrigado pela sua atenção!

Gracias por su atención!

Спасибо за внимание!