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Sequencing Property Rights in the Context of Development: A Critique of the Writings of Hernando de Soto

Jonathan Manders†

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Introduction

In his 1989 work, The Other Path⁴ and in his recently published The Mystery of Capital,² Hernando de Soto argues that the key to development lies not in the pursuit of any classic economic variable, such as the expansion of savings,³ the influx of foreign capital,⁴ entrepreneurial know-how,⁵ or the introduction of technology.⁶ Instead, he claims that “most of the poor already possess the assets they need to make a success of capitalism,” whether they be natural, economic, or human, and that achieving economic growth simply requires unleashing these assets’ true potential.⁷

Specifically, de Soto sees developing nations’ prime hindrance as the lack of clearly delineated property rights.⁸ He maintains that without them...
"the poor lack easy access to the property mechanisms that could legally fix the economic potential of their assets so that they could be used to produce, secure, or guarantee greater value in the expanded market." 9 In fact, de Soto believes so ardently in the power of a legal regime to pattern and, in turn, stimulate an economy, that he claims "[a]n appropriate system of property rights, contracts, and extracontractual liability can spontaneously generate the efficient use of resources without a bureaucracy to decide or authorize how the resources must be used." 10

While de Soto presents a compelling argument, and provides a daunting amount of statistical evidence to support his proposition, 11 the question remains: Can we really assume that the formalization of property rights will solve underdevelopment - a complex problem that has endured for centuries? Developmental economists have long championed the notion that the key to progress can be found in one factor of development, arguing that if this key factor can be correctly aligned and exploited, development will quickly follow. 12 The multitude of these one-factor theories, however, has failed to spawn a durable theory of development. Should we now consider de Soto's proposal as being fundamentally different from the scores of one-factor theories that have come before it? While de Soto's premise that property rights further economic expansion through more efficient use of property, is a basic component to development, can it really be considered the preeminent component?

In this note, I agree with de Soto's proposition that formalizing property rights is often a crucial step in furthering development. I take issue, however, with how he has positioned these rights in the scheme of development and the relative importance he has accorded them. In particular, I attempt to show how de Soto raises the same question posed by classical growth models dating back to the 1930s and 1940s. Ultimately, I believe that de Soto's reliance upon traditional developmental economic models limits his work, as he neglects to address numerous questions that are crucial to enacting his program. Specifically, when should a developing nation formalize property rights, to what extent should these property rights be formalized, who should be entrusted with the property rights and who should relinquish them, and how quickly the process of formalization should proceed.

In an attempt to address, at least in part, some of these questions, Part II places de Soto's writings in the broader context of developmental economics, demonstrating how his writings frame development questions in a strikingly similar fashion to those of classical developmental economic theorists such as Roy Harrod and Evsey D. Domar, with the crucial difference

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9. Id. at 48.
10. See DE SOTO, THE OTHER PATH, supra note 1, at 184.
11. While de Soto includes both statistical and anecdotal evidence throughout his works, see generally Chapter 5, The Costs and Importance of the Law, in DE SOTO, THE OTHER PATH, supra note 1. In this chapter, he carefully shows how the inefficiency of many countries' bureaucracy has fostered the growth of an informal economy.
12. For a further discussion of one-factor theories see infra.
resting in how de Soto proclaims to have “solved” the problem of expanding capital and savings in traditional models. Part III suggests an alternative approach to the consideration of formalizing of property rights. This approach draws from the writings of Albert O. Hirschman, arguing that property rights are only one of many factors in development, and that careful attention must be given to the sequencing of these factors to compel development. Finally, Parts IV through IX apply this alternative approach to numerous developmental factors, attempting to demonstrate how development must be carefully patterned if growth is to be achieved.

I. Property Rights and Classical Theories of Developmental Economics

De Soto’s failure to progress beyond simply proclaiming the need for property rights can be attributed to the emphasis he places on the project of formalizing property rights. In particular, by presenting the formalization of property rights as decisive for steady, uninterrupted growth, de Soto simplifies the process of development, ignoring the complex interplay between property rights and numerous other developmental factors.

In this sense, the design of de Soto’s theory greatly resembles that of classical developmental theorists, who similarly pegged a nation’s aggregate development to the development of one decisive factor. To illustrate these earlier theories, it is worth considering the Harrod-Domar model, which initiated modern interest in growth theory, both framing its discussion and launching countless related studies. Simply put, the Harrod-Domar model holds that “growth depends only on the capital-output ratio and on the availability of capital as determined by the propensity to save

13. See de Soto, The Other Path, supra note 1, at 184. At one point, de Soto even goes so far as to state that “[a]n appropriate system of property rights, contracts, and extracontractual liability can spontaneously generate the efficient use of resources without a bureaucracy to decide or authorize how the resources must be used.” Id.

14. See id. at 178. “[T]he economic importance of property rights is not that they provide assets which benefit their holders exclusively, but that they give their owners sufficient incentive to add value to their resources by investing, innovating, or pooling them productively for the prosperity and progress of the entire community.” Id. “Basically, what property rights, contracts, and extracontractual liability do is reduce uncertainty for people who want to invest their labor or capital in the development of existing resources.” Id. at 180.

15. See Moses Abramovitz, Economic Growth, in 2 A Survey of Contemporary Economics 132-182 (Bernard F. Haley ed., 1952). While there are many factors crucial to the process of development, some of the most prominent include the supply of labor, the supply of land, the supply of capital, qualitative attributes of the population, business organization, the legal and political framework, and the discovery and dissemination of knowledge.

16. See generally R.F. Harrod, An Essay in Dynamic Theory, 49 Econ. J., 14, 14-33 (1939); see also Evsey Domar, Capital Expansion, Rate of Growth and Employment, 14 Econometrica 137, 137-47 (1946). I have chosen not to burden this note with a lengthy presentation of how Harrod and Domar derived their growth formulas. Those readers interested in learning more about Harrod and Domar’s economic models should review these articles, as they serve as a powerful overview of their basic premises.
and the inflow of capital from abroad." In other words, it reduces the entire process of development to a question of whether a developing nation can increase its access to capital. To a large extent, modern developmental economics has remained rooted in the concepts presented by this model; namely the savings function, the distribution of savings, induced vs. autonomous investment, and the productivity of capital.

In many respects, de Soto, too, has adopted the boundaries of the Harrod-Domar model. What has sparked the current interest in de Soto's project, however, is how he diverges from these earlier classical theories. Whereas classical theorists such as Harrod and Domar were ardent proponents of international aid programs, championing the creation of new wealth through infusing foreign capital, de Soto espouses turning away from foreign aid programs and foreign direct investment toward realizing a nation's already existing wealth. The significance of de Soto's theory cannot be understated, as it purports to have "solved" the Harrod-Domar theory's incessant need for capital, thereby reviving it and all its promise of steady and spontaneous growth. It is the manner by which de Soto shifts the locus of growth from attracting foreign capital and increasing national savings to the capitalizing of existing savings in the form of informal property that has captured the attention of international media, policy makers, and aid organizations, as it embodies a radical turn from traditional development programs.

Despite his innovative twist, however, de Soto's reliance on traditional developmental models ensures that his own theory will draw in all the same methodological flaws of these classic models. In particular, as in the Harrod-Domar model, de Soto's theory places one factor in a position of preeminence, as if it were a necessary and sufficient precondition to development, preventing his theory from considering the full complexity surrounding development issues.


19. See generally Growth Economics, supra note 18; see also Brenner, supra note 18, at 175-222. The Harrod-Domar, Solow-Swan-Tobin and Kaldor-Robinson models were particularly powerful early proponents of the need for foreign capital.

20. See de Soto, The Mystery of Capital, supra note 2, at 3-5.


22. See de Soto, The Mystery of Capital, supra note 2, at 5. Again, de Soto specifically writes that "most of the poor already possess the assets they need to make a success of capitalism. Even in the poorest countries, the poor save." Id. at 5.

23. See ALBERT O. HIRSCHMAN, THE STRATEGY OF ECONOMIC DEVELOPMENT 4 (1958) [hereinafter ECONOMIC DEVELOPMENT]. In commenting on prevailing developmental economics theories, Hirschman notes that "whenever any theory was propounded that considered a given value system a prerequisite of development, it could usually be effectively contradicted on empirical grounds: development had actually taken place somewhere without the benefit of the 'prerequisite.'" Id.
II. An Alternate Approach to Classical Theories of Developmental Economics

De Soto's study could escape an oversimplification of the problem of development by utilizing a more nuanced approach that not only considers a broader range of factors in development, but also the influence property rights have over other factors of development and vice versa. Such an approach can be found in Hirschman's work on sequencing, which was first set forth in his 1958 study The Strategy of Economic Development.24

Much like de Soto, Hirschman contends "development depends not so much on finding optimal combinations for given resources and factors of production as on calling forth and enlisting for development purposes resources and abilities that are hidden, scattered, or badly utilized."25 Unlike de Soto, however, Hirschman does not look to one factor to "call forth and enlist" existing resources and abilities, but rather to how a variety of factors interact, searching, in particular, for factors that function as inducing and mobilizing mechanisms,26 which thereby compel the development of other factors.27 Hirschman maintains that, given developing nations' need to prioritize their investments (and development projects generally), those factors that compel the development of other factors should be pursued first.28 He explains that

[the resulting 'strategy of unbalanced growth' values investment decisions not only because of their immediate contribution to output, but because of the larger or smaller impulse such decisions are likely to impart to further investment, that is, because of their linkages. The strategy has important implications for investment planning: it proposes that dynamic considerations, based on the linkages, should be allowed to complement the criterion of static efficiency.29

Hirschman further expanded his concept of linkages30 by considering differences between backward linkages31 (where further investment flows backwards from finished goods to semiprocessed or raw goods), forward

24. See id.
25. See HIRSCHMAN, RIVAL VIEWS, supra note 17, at 56.
26. See id. at 74. "The linkage concept, in short, invites the analyst to pay close attention to the differential technological and situational features of economic activities as a means of detecting how 'one thing leads (or fails to lead) to another.'" Id.
27. See Abramovitz, supra note 15, at 132-82.
28. See HIRSCHMAN, ECONOMIC DEVELOPMENT, supra note 23, at 76-79.
29. See HIRSCHMAN, RIVAL VIEWS, supra note 17 at 56-57.
30. See id. at 56-74. This chapter entitled "Linkages in Economic Development" provides the most concise and powerful statement of linkages and can, in some ways, be considered a reformulation of the conception Hirschman originally put forth in THE STRATEGY OF ECONOMIC DEVELOPMENT, supra note 23.
31. See id. at 57. "[An] existing industrial operation—relying initially on imports not only for its equipment and machinery, but also for many of its material inputs—would make for some pressure toward the domestic manufacture of these inputs and eventually would also provide a market for a domestic capital goods industry. This dynamic I called a backward linkage, since the direction of the stimulus toward further investment flows from the finished article back to the semiprocessed or raw materials from which it is made or to the machines which help make it." Id.
linkages\textsuperscript{32} (where further investment flows forward from a finished good towards other independent finished goods), consumption linkages\textsuperscript{33} (where domestic production of consumer goods carried out as newly earned income is spent on such goods), and fiscal linkages\textsuperscript{34} (where export taxes and tariffs can be used to finance investment projects). He also noted that by presenting these linkages he did not intend to exclude the existence of other linkages.\textsuperscript{35}

Finally, when reassessing his work on linkages and sequencing, Hirschman noted the dangers that can threaten to destroy linkages' power to compel their predicate and thereby prevent progress; a problem he referred to as "getting-stuck."\textsuperscript{36} Significantly, he noted that some sequences are inherently not self-propelling, but rather strewn with resistance. That is to say, whereas the first steps are easy to take by themselves, these first steps can make it difficult to take further steps, as the initiating of some sequences actually involves building resistance towards realizing their predicates.\textsuperscript{37} This is especially true, Hirschman argues, when an existing reform is likely to be placed in jeopardy by a proposed reform (what he terms the "Jeopardy Thesis")\textsuperscript{38} or when there is a general unwillingness to put the status quo at risk.\textsuperscript{39}

III. Linkages between Property Rights and Other Factors of Development

When one applies Hirschman's conception of factors as sequences of linkages to formalizing property rights, it removes the issue from abstrac-

\textsuperscript{32} See id. "Another stimulus toward additional investment points in the other direction and I therefore called it a forward linkage: the existence of a given product line A, which is a final demand good or is used as an input in line B, acts as stimulant to the establishment of another line C which can also use A as an input." Id.

\textsuperscript{33} See id. at 64. "The mechanisms of the new linkages were more roundabout than the backward and forward variety. Thus consumption linkage is defined as the stimulus toward domestic production of consumer goods that will be undertaken as newly earned incomes are spent on such goods. In an open economy such goods will often be imported at first, but eventually domestic production will become an attractive proposition." Id.

\textsuperscript{34} See id. at 67. "[N]ew activities can also be established by the state as it interferes with such market forces. The state can tap the flow of income accruing to the exporters through various forms of export taxes, or it can impose tariffs on the imported articles on which a good part of the new export-related incomes will be spent. The resulting fiscal receipts can then be used, among other things, to finance public or publicly supported investment projects. These sequences spell out a new class of fiscal linkages." Id.

\textsuperscript{35} See ALBERT O. HIRSCHMAN, A PROPENSITY TO SELF-SUBVERSION 74 (1995).

\textsuperscript{36} Id. "[L]eisurely, sequential problem-solving is not necessarily a pure blessing, as has been so plausibly argued in the literature on political development. Sequential problem-solving brings with it the risk of getting stuck." Id. at 74.

\textsuperscript{37} See HIRSCHMAN, RIVAL VIEWS, supra note 17 at 57. Here Hirschman notes, for example, that established industrialists tend to resist backward linkages due to their preference to continue to rely on imports of a certain predictable price and quality.


\textsuperscript{39} See HIRSCHMAN, PROPENSITY TO SELF-SUBVERSION, supra note 35, at 51-56. He cites, in particular, Veblen's conception of the "penalty of the early start."
tion, allowing a consideration not only of the significance of formal property rights in and of themselves, but also of their significance in inducing other factors of development.

Some of the most significant factors of development readily linked to de Soto's conception of the formation of property rights - factors worth considering in greater detail - include issues of national politics, national economics, national culture, the national legal system, and globalization.

IV. The Linkage between Property Rights and National Politics

While de Soto recognizes the linkage between the formalizing of property rights and national politics, he fails to discuss the extent or sequence of their relationship. After stating, for example, that a "property revolution [is] always a political victory," he never addresses whether a particular political climate will facilitate a property revolution or whether a property revolution will itself induce political change.

A. Property Rights and Ruling Regimes

Significantly, while it is implicitly suggested by his writings, de Soto never explicitly acknowledges the way property represents real political power in many situations, and that fundamental changes to property regimes often result in struggles for power. As Galbraith notes, for example, "a land reform is a revolutionary step; it passes power, property, and status from one group in the community to another. If the government of the country is dominated or strongly influenced by the landholding groups... no one should expect effective land legislation as an act of grace." While there are, to be sure, many situations short of revolution where those in power have enacted fundamental changes to property rights, such reform is usually prompted by a specific national condition, such as rural unrest, ideological commitment, international climate, or population pressure.

Within the turbulent political scenes of many developing nations, however, perhaps the most important and common condition prompting property rights reform is the newly-formed political regimes' search for

40. See de Soto, The Mystery of Capital, supra note 2, at 106.
41. See Mario Vargas Llosa, Foreward to de Soto, The Other Path, supra note 1, at xiv. Notably, de Soto begins The Other Path with numerous statements maintaining that the poor's lack of political power has driven them to illegality. He states "when legality is a privilege available only to those with political and economic power, those excluded-the poor-have no alternative but illegality." Id. at xvii. Similarly, Llosa observes that de Soto views the rich as having taken little or no interest .in increasing the poor's position in society, claiming that "instead of favoring the production of new wealth, the system, owned, in effect, by the closed circle of those who benefit from it, discourages any such effort and prefers merely to re-circulate the ever-diminishing amount of capital." Id. at xvii.
42. John K. Galbraith, Conditions of Economic Change in Under-Developed Countries, 33 J. OF FARM ECON. 689, 695-96 (1951).
legitimacy, which seeks the maintenance and strengthening of their position against other political factions through an appeal to the public.\textsuperscript{44} In this sense, many property reforms are not the acknowledgement of societal changes, but rather political maneuvers carried out in the interest of a specific group of political elites.\textsuperscript{45} Unfortunately, de Soto ignores the political implications of inter-factional power struggles and the role that extra-political groups, such as the military, have played in the development of liberalized markets and democracy in many nations.\textsuperscript{46} One need only consider the example of Pinochet's Chile to understand the importance of this oversight.\textsuperscript{47}

Furthermore, de Soto fails to address the importance of political transitions in developing nations, ignoring their potential to completely uproot existing patterns of ownership. Amy Chua aptly illustrates this danger in her recent article \textit{The Privatization-Nationalization Cycle,}\textsuperscript{48} where she demonstrates that the current trend of privatization is far from intractable or irreversible, as Latin American and Asian nations have oscillated between privatizing and nationalizing property throughout the twentieth century largely as a consequence of forces such as ethnic nationalism.\textsuperscript{49}

B. Property Rights and Political Participation

An equally challenging issue is the possible political effects that formalizing property rights may have upon the political participation of a nation's poor. While de Soto\textsuperscript{50} (and many others)\textsuperscript{51} concentrates simply on the question of aggregate economic growth, believing that it will alleviate other social problems, evidence suggests just the opposite. In Irma Adelman and Cynthia Morris' landmark study \textit{Economic Growth and Social Equity in Developing Countries,}\textsuperscript{52} they found that "economic growth itself not only tends to be accompanied by actual declines in political participation..."\textsuperscript{53}
but is one of the prime causes of income inequality."\(^{52}\)

Curiously, while de Soto continuously argues in terms of a nation's aggregate resources, he never addresses exactly how these resources will be distributed or how the formalizing of property rights may effect this distribution.\(^{53}\) While it may seem intuitive that formalizing property rights will serve as a means of fragmenting political and economic power, de Soto never confronts the fact that formalizing property rights also makes those rights alienable. When taken together with his call for expanded capital markets, this fact could simply allow for those already possessing political and economic advantage to leverage their power and achieve greater concentrations of property rights, further exacerbating social inequalities.\(^{54}\) Therefore, although de Soto acknowledges that "[e]conomic freedom is the counterpart of political freedom, and only when the two are united—two sides of a single coin—can they really function,"\(^{55}\) he has failed to show why formalizing property rights will safeguard either.

C. Property Rights and Demographics

Finally, when discussing the massive migrations from rural areas to urban centers throughout the developing world, de Soto argues "migration... is hardly an irrational act," and that it "has little to do with 'herd instinct.'"\(^{56}\) While evidence, in fact, supports de Soto's assertion, this evidence is in itself problematic, underscoring the general problem many developing nations' poor have in acquiring any form of property rights to land and housing.\(^{57}\)

In part, these migrations have been the public's logical response to ever-increasing concentrations of wealth and power in the developing world's urban centers, and their consequent promise of higher wages and better living conditions.\(^{58}\) While it is true that real wages are often higher in most cities than in the countryside\(^{59}\) and that cities offer lower infant

\(^{52}\) IRMA ADELMAN & CYNTHIA MORRIS, ECONOMIC GROWTH AND SOCIAL EQUITY IN DEVELOPING COUNTRIES 2 (1973).

\(^{53}\) See Llosa, supra note 41, at xvii. Although de Soto fails to address questions of distribution directly, Llosa describes de Soto's analysis in Chapter 5 of THE OTHER PATH, when he states that "instead of favoring the production of new wealth, the system, owned, in effect, by the closed circle of those who benefit from it, discourages any such effort and prefers merely to recirculate the ever-diminishing amount of capital." Id.


\(^{55}\) Llosa, supra note 41, at xx.

\(^{56}\) See de Soto, The Other Path, supra note 1, at 81.

\(^{57}\) See generally Hendrix, supra note 54.

\(^{58}\) See generally Hirschman, Economic Development, supra note 23.

\(^{59}\) See THE MEGA-CITY IN LATIN AMERICA 12-13 (Alan Gilbert ed., 1996). It should be noted, however, that there is great social inequality within developing nations' cities, as the poor often pushed to slums located on the outer margins of cities and generally have vastly inferior terms of employment.
mortality rates and higher average life-spans, these advantages often come at the price of further dependency upon those elites who actually possess wealth. In this sense, while it is true that a significant number of migrants to the cities are able to claim an informal, expectative property right over an area of land, exactly in the manner de Soto describes, the majority of migrants (and often the majority of a city's inhabitants), never able to secure any form of autonomous property right, be it formal or informal, are forced to live in run-down tenement houses. Brazil's corintios provide a vivid example of the strength of this trend towards profiteering, in the housing market for the poor, as a response to the population pressures that have made inner-city tenements highly profitable. In 1981, for example, the Folha de Sao Paulo reported that "over 80 percent of the older houses and mansions in the central part of Sao Paulo have been converted into tenements. Between 9 and 22 families live in most of these tenements, 5 people to a room, which is rarely bigger than 4 square meters."

The migrants' plight has only been further exacerbated by real estate agents who, as a form of land speculation, have stimulated urban expansion at cities' periphery. With a ready supply of buyers searching to free themselves of exorbitant rents and gain the security and prestige of owning their own houses, many lower and middle class individuals have been willing to pay a premium for deeds and titles. In Brazil, brokers (loteadores) have seized upon this opportunity not only by selling false deeds and titles, but also through strategically capitalizing on subdivided tracts of land sold piecemeal, these sales net higher prices due solely to former purchasers'...
improvements to the property.\textsuperscript{67} These settlements generally fail not only due to their lack of perfect title, but also due to the fact that the brokers have made no provision for the extension of basic utilities into the areas (including electricity, sewage, and water systems).\textsuperscript{68}

Furthermore, as Hirschman notes, the rationale behind the migration can be "traced to the problem of property rights in the countryside."\textsuperscript{69} This, in turn, raises the question of why de Soto does not address the failures of agrarian reform, a solution that gained particular weight in the 1960s and 1970s.\textsuperscript{70} If land reform in rural areas failed, why should formalizing property rights largely in urban areas - areas which possess infinitely greater possibilities of harboring conflicting claims - be expected to fare any better? Additionally, if individuals were able to leverage their property toward creating capital, would not this capital be best applied in the context of labor-intensive industries - industries such as agriculture that generally make poor use of urban lands?

While, in many ways, the Latin American migration to the cities is irreversible,\textsuperscript{71} rural lands nonetheless pose a far more defensible solution to distributing property rights, as rural lands are not only more plentiful, but also generally do not require dispossessing their formal owners to the same degree. These questions, namely how a nation is to decide between existing formal claims (however weak they may be) and informal claims (however strong they may be) and what compensation formal landlords should be given for their dispossessed lands, are of immense importance. In fact, leaving them without any clear solution could quickly undermine the legitimacy provided through the social contract that de Soto believes is so vital to the success of any property rights regime.\textsuperscript{72}

D. Sequencing Property Rights and National Politics

These observations suggest that favorable national politics precede formalizing property rights in a forward linkage; albeit a very weak one, as it is unclear to what extent favorable national politics compel the formalizing of property rights. The linkage is particularly difficult to assess in the context of development due to many nations' relative political instability and the profound implications that political change carries for the maintenance of property rights regimes.

\textsuperscript{67} See id.
\textsuperscript{68} See id.
\textsuperscript{69} See HIRSCHMAN, ECONOMIC DEVELOPMENT, supra note 23, at 9.
\textsuperscript{70} See generally AGRARIAN PROBLEMS AND PEASANT MOVEMENTS IN LATIN AMERICA (Rodolfo Stavenhagen ed., 1970) [hereinafter AGRARIAN PROBLEMS].
\textsuperscript{71} See generally THE MEGA-CITY IN LATIN AMERICA, supra note 59; see also LATIN AMERICAN URBANIZATION: HISTORICAL PROFILES OF MAJOR CITIES (Gerald Michael Greenfield ed., 1994). Both books trace the rise of urbanization in Latin America, demonstrating how Latin American cities can be expected to increase in size in the future.
V. The Linkage between Formalizing Property Rights and National Culture

While de Soto acknowledges, at least implicitly, the existence of a variety of linkages between the formalizing of property rights and other factors in development, he expressly rejects the importance of any linkage between formalizing property rights and national culture, maintaining that "[t]he disparity of wealth between the West and the rest of the world is far too great to be explained by culture alone." 74

A. Cultural Conceptions of Property

When discussing property, de Soto conflates differences between national cultures, arguing simply that "people are prepared to think similarly about property rights in very similar ways." 75 This assertion is difficult enough to maintain when considering seemingly related cultures such as those of the United States and Europe. 76 One need only consider the drastically different standings given to property within the U.S. 77 and German constitutions 78 for an example of how seemingly similar cultures do, in fact, diverge in how they conceive property. 79 When this assertion is stretched further still, taking into account African and Asian societies, it appears completely untenable. Consider, for example, the manner in which Daniel Etounga-Manguelle 80 has noted how African thought largely rejects any view of the individual as an autonomous and responsible being, and that consequently, many African tribes continue to maintain property regimes based upon communal ownership, which stresses the needs of the community over those of the individual. 81

73. See generally de Soto, THE MYSTERY OF CAPITAL, supra note 2. In fact, the thrust of this book is the interconnection between property rights and capital, and specifically how, by formalizing property rights, capital will be unleashed as a direct consequent.
74. See id. at 4.
75. See id. at 179.
77. See U.S. CONST. amend. V. Commonly referred to as the Takings Clause, stating "nor shall private property be taken for public use without just compensation." Id.
78. Grundgesetz GG art. 14 (F.R.G.). As translated in DAVID. P. CURRIE, THE CONSTITUTION OF THE FEDERAL REPUBLIC OF GERMANY 349 (1994). "(1) Property and right of inheritance are guaranteed. Their content and limits shall be determined by statute. (2) Property imposes duties. Its use should also serve the public weal. (3) The taking of property is permissible only for the public weal. It may be effected only by or pursuant to a statute regulating the nature and extent of compensation. Such compensation shall be determined by establishing an equitable balance between public interest and the interests of those affected. In case of dispute regarding the amount of compensation, recourse may be had to those courts of ordinary jurisdiction." Id.
79. For a thorough comparison of the differences in constitutional standing afforded to property under American and German law, see Alexander, supra note 76.
81. See id.
B. Tendencies Towards Informality and Formality

Furthermore, when de Soto argues that "the choice between working formally and informally is not the inevitable result of people's individual traits but, rather, of their rational evaluation of the relative costs and benefits of entering existing legal systems," he fails to realize that any cost-benefit analysis necessarily incorporates preferences, which themselves are largely derived from culture. In this sense, all major determinants of culture, from education to religion, have an impact on individuals' preferences.

C. Examples from History

Additionally, in drawing examples from world history, in an attempt to illustrate that all property regimes were first codified informally and then legitimized by governments through an incorporation into national law, de Soto ignores crucial differences in the history of developing and developed nations. How can the formation of property rights in modern-day Peru be considered the same as the formation of property rights in the United States (where property rights developed along with westward expansion into vast, open tracts of land) or England (where property rights developed slowly over centuries)? While de Soto's historical examples do underscore the role that property rights can play in development, they hardly offer any insight in terms of how a developing nation should go about implementing such rights within their borders.

One need only consider de Soto's own writings to discover the limits of his attempt to compare developing nations' current situation with that of the early history of the United States. Notably, the process of formalizing property rights in the United States, as chronicled by de Soto, occurred at the frontier or in other sparsely populated tracts of land and was sanctioned, at least in part, due to the prevailing interests the government (who had legal claim to the frontier lands) had in ensuring their cultivation. How can de Soto compare sprawling metropolitan areas such as modern day Mexico City with early 19th century U.S. territories? In fact, given the peculiarities of the early history of many former colonies', would it even be fair to consider them on the same general track as the United States? De Soto ignores, for example, basic distinctions between settlement and expansion in the United States onto lands owned by the government and

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82. de Soto, The Other Path, supra note 1, at 185.
83. See de Soto, The Mystery of Capital, supra note 2 at 150-51. Generally, de Soto freely discusses historical examples as illustrative of the process of formalizing property rights, yet makes no attempt to proscribe how such a process can be undertaken in the present day. Ultimately, de Soto himself realizes the challenge of adapting such historical examples to the present day, when he states that "this is not to say that developing and former communist nations should slavishly imitate the U.S. transition. There are plenty of negative consequences in the U.S. experience that they should be careful to avoid." Id. at 150.
84. For a general introduction to the subject, see Bernard Bailyn, The Peopling of British North America: An Introduction (1986).
85. See de Soto, The Mystery of Capital, supra note 2, at 109-10.
settlement and expansion in countries such as Brazil onto lands that had been entrusted to a few wealthy individuals (in an effort to encourage colonization, the Portuguese divided Brazil into fourteen land grants to Portuguese nobles during the years 1534 to 1536, allowing the grantees complete dominion over their grants—an act that entrenched a system of concentrated land ownership).  

D. Unique Paths of Development

Ultimately, one is left asking why de Soto chooses to argue against the many thinkers who have linked development to the inherent uniqueness of a given nation. Weber, for example, identified “beliefs, attitudes, value systems, climates of opinion, and propensities which they have found to exert a favorable influence on the generation of enterprise and of developmental initiative.” When forecasting how the continent would industrialize, Marx concluded that Germany and other nations would follow a somewhat different path due to their national history and legal traditions. Why then does de Soto ignore issues of culture? One could argue that countries often fail to take advantage of their development potential not because of political or economic policies, but “because, for reasons largely related to their image of change, they find it difficult to take the decisions needed for development in the required number and at the required speed.” In the end, it seems far more realistic to conclude that uniform solutions to development simply lead one away from considering the roots of problems of development. Therefore, one should remember that efficient sequences are likely to vary widely from region to region, and that they must be constructed by incorporating all the peculiarities of the culture that they are being designed to serve.

E. Sequencing Property Rights and National Culture

These observations suggest that national culture precedes formalizing property rights in a forward linkage. Again, however, there is no evidence that culture will compel the formalizing of property rights, bringing into question the force of this linkage.

VI. The Linkage between Formalizing Property Rights and National Economics

In basing the thrust of his work on the linkage between property rights and the formation of capital, de Soto generally ignores several other key economic linkages. Most notably, he fails to adequately address how

89. Id. at 25.
90. See id. at 83.
formalizing property rights may effect either the distribution of existing wealth or the creation of further wealth.

A. Distribution of Wealth

The closest de Soto comes to discussing distribution is in his criticism of the behavior of entrepreneurs acting within the system: "[i]nstead of favoring the production of new wealth, the system, owned, in effect, by the closed circle of those who benefit from it, discourages any such effort and prefers merely to recirculate an ever-diminishing amount of capital."91 De Soto argues that "[a] legal system whose sole purpose is redistribution thus benefits neither the rich nor the poor, but only those best organized to establish close ties with the people in power."92 Without question, de Soto opposes government efforts to instill equality, citing their frequent failures in the past.93 The question remains, however, as to just how much economic inequality can be tolerated before it hampers aggregate economic growth. This is a question well worth answering for many Latin American countries such as Brazil, where wealth disparity has only accelerated since the 1960s94 and governmental efforts to improve housing through the National Housing Bank (BNH) have generally helped only the middle and upper classes (both directly, through actual investment in their residences, and indirectly, through their involvement with the construction industry).95

B. Balanced Growth vs. Unbalanced Growth

De Soto also fails to clarify the pace at which he believes the formalizing of property rights should be conducted. The closest he comes to giving an answer lies in the Mystery of Capital, where he states that "[t]he lesson of the West is that piecemeal solutions and stopgap measures to alleviate poverty were not enough. Living standards rose only when governments reformed the law and the property system to facilitate the division of labor."96 In this passage, he considers that reform must be effected both swiftly and completely, seemingly espousing, therefore, that growth must be balanced.97 Yet, as Hirschman notes, "balanced growth theory reaches the conclusion that an entirely new, self-contained modern industrial economy must be superimposed on the stagnant and equally self-contained traditional sector," posing a problem in that "its application requires huge amounts of precisely those abilities which we have identified as likely to be in very limited supply in underdeveloped countries."98 Hirschman

91. Llosa, supra note 41, at xvii.
92. Id. at 191.
93. See id.
94. See Skidmore, supra note 86, at 183.
95. See Social Struggles and the City, supra note 62, at 122-23.
96. See de Soto, The Mystery of Capital, supra note 2, at 75.
97. By balanced, I mean that growth will be linear, always progressing and never retreating. I do not mean to imply any timeframe for growth in calling it balanced—balanced growth may happen instantaneously or over decades.
therefore maintains, "if a country were ready to apply the doctrine of balanced growth, then it would not be underdeveloped in the first place."99 While the process of registering informal rights would certainly take some time, making it appear that de Soto is not arguing for such a drastic push, it would be wrong to label this time lag the equivalent of an unbalanced growth approach.

C. Maximizing Wealth

Furthermore, de Soto believes that there is a linkage between formalizing property rights and maximizing the aggregate wealth of a nation. Specifically, he claims that "[c]ontrary to the belief widespread in Latin America, the economic importance of property rights is not that they provide assets which benefit their holders exclusively, but that they give their owners sufficient incentive to add value to their resources by investing, innovating, or pooling them productively for the prosperity and progress of the entire community."100 While de Soto's statement is based largely on the proposition that property rights often serve to incorporate externalities into ownership and thereby benefit the community at large, de Soto unduly extends the idea that property rights benefit the community by maintaining that private owners exploit their property in the public's interest. This is certainly not the case in Latin America, where property owners have routinely hoarded the wealth yielded by their property.101 One need only turn to examples of the fazendas and haciendas throughout Latin America (whose progression from systems of slavery to state coercion to the current system of contracting labor from landless or land-poor peasants in a buyer's market) to see how thoroughly, in fact, some owners have exploited their property in their own self-interest.102

Furthermore, the idea that increased income leads to increased investment, while supported by economic theory, has not always been the reality in Latin America, where wealthy property owners have exhibited a clear liquidity-preference over investment, thereby "keeping themselves and their funds uncommitted or 'liquid' so as to take advantage of the unusual opportunity whenever it comes."103

D. Capital Formation

Finally, de Soto's linkage between formalizing property rights and the formation of capital, the crux of his work, while incredibly powerful, is not, in itself, conclusive. While, de Soto looks to employ the six effects that he feels have allowed the West to produce capital (including: fixing the economic potential of assets; integrating dispersed information into one system; making people accountable; making assets fungible; networking

99. Id. at 53-54.
100. DE SOTO, THE OTHER PATH, supra note 1, at 178.
101. See generally Skidmore & Smith, supra note 60.
102. See Agrarian Problems, supra note 70, at 17.
people; protecting transactions), he never proves that capital is, in fact, what is lacking in developing countries. One need only consider how little has been accomplished through injecting foreign capital into developing economies to see the importance of this question. Additionally, as Wolf and Sufrin note, a shortage of capital is seldom found to hinder projects that have been carefully planned and promise to be competently managed.

E. Sequencing Property Rights and National Economics

These observations suggest that formalizing property rights will precede capital formation, indicating that a strong forward linkage will exist, as individuals are induced to act upon property rights to maximize the value of their assets. No conclusive remarks can be made concerning how property rights will effect wealth distribution and wealth maximization, however, as there is evidence to support conflicting conclusions.

VII. The Linkage between Formalizing Property Rights and National Legal Systems

The closest de Soto comes to explicitly considering linkages can be found in his treatment of the relationship between property rights and national legal systems and, in particular, in his discussion of the formal and informal sectors.

A. The Growth of Informality

Far from attributing the growth of informality to an attempt to evade the law, de Soto holds that informality arises out of the failure of a formal legal regime to adequately represent and enforce the populous' conceptions of justice and fairness. He claims that "informal activities burgeon when the legal system imposes rules that exceed the socially accepted legal framework - does not honor the expectations, choices, and preferences of those whom it does not admit within its framework - and when the state does not have sufficient coercive authority." De Soto argues that the only feasible way that governments can correct the legal regime's failure to secure property rights is through acknowledging the informal rights that he claims already exist. Arguing against the

104. See de Soto, The Mystery of Capital, supra note 2, at 47-62.
106. See Llosa, supra note 41, at xviii.
107. See de Soto, The Other Path, supra note 1, at 6. Specifically, de Soto cites "[t]he inefficiency of the law courts has given rise to a growing disenchantment with, and loss of confidence in, law-enforcement mechanisms." In turn, he claims this disenchantment leads to "[a] complete subversion of means and ends has turned the life of Peruvian society upside down, to the point that there are acts which, although officially criminal, are no longer condemned by the collective consciousness." Id. at 5-6.
108. de Soto, The Other Path, supra note 1, at 12.
109. See de Soto, The Mystery of Capital, supra note 2, at 172-82.
state's imposition of mandatory laws that he believes are often created de novo, de Soto appeals to authorities to simply enter communities and formalize existing patterns of land use, whether it be plainly evident uses, such as the cultivating of crops, or tacitly acknowledged through community recognition. De Soto explains this process when he mandates that "what governments in developing countries have to do is listen to the barking dogs in their own communities and find out what their law should say. Only then will people stop living outside it."

B. Extent of Legal Reform

Although de Soto's appeal for legal reform is certainly convincing, what he does not consider is the extent to which reform must be enacted and whether such sweeping reforms are feasible. De Soto depicts the Peruvian legal system, for example, as a maze of laws extending in all directions and supporting all propositions. Additionally, he underscores that "[t]he inefficiency of the law courts has given rise to a growing disenchantment with, and loss of confidence in, law-enforcement mechanisms." Given this complexity and inefficiency, the question arises as to whether formalizing property rights actually secures rights or simply exposes their holders to new liabilities (such as taxes). If the government has sanctioned informality to the extent of allowing informal tribunals and the enforcement of informal property rights, why would people not be drawn to simply complete and strengthen the informal sector? Are the advantages of formality so great as to outweigh the costs of instituting it (both in economic capital through titling claims and political capital through gaining their recognition)? De Soto carefully notes that many developing nations' legal systems have become cluttered with legislation (often passed by the executive) rendering these formal legal systems ineffective. Yet, this only raises the question as to whether informal economies have organized their legal systems well enough to not only reform or supplant property law, but also nearly every other branch of law (including contract law, procedural law, and administrative law)?

C. Adopting Informality

De Soto believes they have, citing how people form and secure informal expectative property rights under what he terms the "people's law"

110. See id. at 187. "The truth is that lawyers in these countries are generally too busy studying Western law and adapting it. They have been taught that local practices are not genuine law but a romantic area of study best left to folklorists. But if lawyers want to play a role in creating good laws, they must step out of their law libraries into the extralegal sector, which is the only source of the information they need to build a truly legitimate formal legal system. By examining the 'people's law' and understanding its logic, reformers can get a sense of what they need to do to create a self-enforcing legal system." Id. at 186-87.
111. Id. at 179.
112. See Llosa, supra note 41, at xviii.
113. Id. at 6.
114. Id. at xviii.
During a gestation period that enables a later transition to formality. Yet, there is evidence to suggest that the codification of informal rights could just as easily lead to the institutionalizing of informal rights. Michael Heller, for example, has argued that, close-knit communities may develop informal norms and institutions to manage resources efficiently.\textsuperscript{115} In this sense, while de Soto argues that "it is simpler and cheaper to bring the formals and informals together by changing the law than by trying to change the characteristics of the people,"\textsuperscript{116} he may be missing a crucial point; namely that it is far cheaper (figuring in transaction costs, the extent of political, legal, and economic change required) for the people to remain informal in some instances.\textsuperscript{117}

D. Sequencing Property Rights and National Legal Systems

These observations suggest that before property rights can be formalized, initial "expectative" property rights must be created and a legal system must adequately enforce such rights. Therefore, the development of informal property rights and adequately efficient national legal systems may be considered to precede formalizing property rights in a forward linkage.

VIII. The Linkage between Formalizing Property Rights and Globalization

Although de Soto wrote The Mystery of Capital in order to illustrate why many developing nations are unable to participate in global capitalism, he nevertheless ignores the linkage between formalizing property rights and globalization.

A. Foreign Investment

Specifically, de Soto fails to address how informal property rights can serve to protect property interests against foreign investment. Consider, for example, a developing country that successfully formalizes property rights according to de Soto's proposal. This implies that illiquid (due to a lack of title and imperfect market information), informal rights are replaced by liquid (due to perfect title and perfect market information), formal rights that can be freely bought and sold on open markets. If these markets function as efficiently as de Soto maintains they might,\textsuperscript{118} the


\textsuperscript{116} De Soto, The Other Path, supra note 1, at 187.

\textsuperscript{117} See De Soto, The Mystery of Capital, supra note 2, at 85. Actually, when discussing the organization of the informal economy in Brazil's favelas, de Soto himself alludes to this possibility when he quotes Donald Stewart's statement that "in spite of the apparent lack of resources, this informal economy functions efficiently. In the favelas there are no rent controls, rents are paid in U.S. dollars and renters who do not pay are rapidly evicted. The profitability of investment is good and as a result there is an abundance of supply of housing." Id.

\textsuperscript{118} See generally id.
basic question arises as to why the developed world would not intervene and buy significant amounts of the developing nations' property rights for themselves? This seems all the more likely when one considers not only that the developed world could price the developing world out of its own property market, but also the developed world's relative expertise in concluding such transactions on open markets.\footnote{119} Similarly, one must ask whether it can be assumed, for example, that through simply bestowing formal property rights upon individuals, they will in turn be able to understand how to leverage these rights so as to raise capital? Assuming that this is not the case, it seems as if formalizing property rights would work to create a dangerous window where developing-world owners, due to their lack of expertise, would remain unable to raise capital through financing or when given a new opportunity to raise capital through selling their property (especially when one considers that the newly developed market would be larger and generate higher prices than the owners would have previously encountered).

B. Dual Economies

Globalism also complicates development in that it allows for dualism to pervade developing countries' economies. While de Soto maintains that "[what] is understood all too rarely is that the Third World and former communist societies are experiencing nearly the same industrial revolution that arrived in the West more than two centuries ago,"\footnote{120} and that "[t]he difference is that this new revolution is roaring ahead much faster and transforming the lives of many more people,"\footnote{121} he ignores the fact that development is fundamentally different in today's world. Generally, developing countries include some individuals and industries that are able to participate in global capitalism, enabling them to live much as the citizens of developed nations do.\footnote{122} Yet, these individuals and industries nonetheless exist within countries that are, by all accounts, developing.

Furthermore, far from serving as a catalyst for development, these affluent elements tend to simply render this dualism more intractable, as the affluent populations' demands often continue to be met through imports rather than driving domestic investment and fueling domestic development.\footnote{123} In many ways, contemporary dualism within the developing world has, in effect, removed a decisive element of countries' capital bases, leaving them in a more difficult position than that which previously faced the developed world.\footnote{124} In this sense, the developing world often remains vulnerable to the "development of underdevelopment," whereby it

\footnote{119. See id. at 212-18.}
\footnote{120. See id. at 70-71.}
\footnote{121. Id. at 71.}
\footnote{122. SKIDMORE & SMITH, supra note 60.}
\footnote{123. See HIRSCHMAN, ECONOMIC DEVELOPMENT, supra note 23, at 25.}
\footnote{124. See de SOTO, THE MYSTERY OF CAPITAL, supra note 2, at 109. "Only in the Western nations and small enclaves of wealthy people in developing and former communist nations have the capacity to represent assets and potential and, therefore, the ability to produce and use capital efficiently."}
will simply continue a neocolonialistic relation to the developed world.\textsuperscript{125}

C. Sequencing Property Rights and Globalization

These observations suggest that formalizing property rights precedes globalization, as property markets will remain localized and rather dormant until clearly delineated property rights are put in place. Therefore property rights may be seen to precede the globalization of a property market in a forward linkage.

Conclusion

De Soto’s work is invaluable in calling attention to the role that formalizing property rights may play in assisting with development, and, in particular, how property rights often precede developments in national economics and globalization in forward linkages. Yet, by holding property rights as the key to progress rather than simply a factor in development, he exaggerates their true importance, ignoring how the formalizing of property rights is generally preceded by national politics, national culture, and national legal systems in forward linkages, and evidence that property rights can only be formalized when numerous other factors are present.

In this sense, before de Soto’s program of instituting formal property rights can truly further development, he will have to address the more basic questions raised by Joseph Singer in his introduction to \textit{Entitlement}.\textsuperscript{126} After noting the political implications of property, Singer states, “the property problem goes beyond deciding whether to recognize particular property rights, or when to limit them; rather it forces on us more urgent questions: What shall property be? What shall it mean? What kind of property regime should we construct?”\textsuperscript{127} Then, and only then, will de Soto’s model have a chance of delivering on its promises of development and progress, and separate itself from the progression of one-factor theories that have come before it.

\textsuperscript{125} See Andre Gunder Frank, \textit{The Development of Underdevelopment}, \textit{MONTHLY REV.} 17-31 (1966).

\textsuperscript{126} \textit{JOSEPH W. SINGER, Entitlement: The Paradoxes of Property} (2000).

\textsuperscript{127} \textit{Id.} at 9.