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The productive bottlenecks of progressive social policies: lessons from Costa Rica and beyond //

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In developing countries, social policy is currently receiving renewed attention. In Latin America, the "turn to the left" has contributed to an expansion of cash transfers and some attempts to strengthen universal policies. Although some of these efforts are leading to reductions of poverty and inequality, most countries still fail to transform links between social and productive policies. As a result, the gains in poverty reduction may become unsustainable in the long run.

Key points:

- In Latin America, production regimes have limited the chances to establish universal welfare regimes. Even Costa Rica, a showcase of universal social policy, shows how challenging it is for many other developing countries to build and sustain productive regimes that enable truly redistributive welfare regimes.
- A primary challenge has been the difficulty to simultaneously upgrade the leading sectors while modernizing the low productivity sector.
- Many Latin American countries have recently witnessed poverty reduction and decreased inequality due to a simultaneous expansion of social assistance and secondary education. Nevertheless, a sustained reduction of poverty and inequality may require the consolidation of universal social systems that are accompanied by successful production regimes that demands skills while providing funding and formal jobs.
- In terms of policy implications, it is critical to promote both leading and low productivity sectors as well as securing stable funding sources for welfare regimes.

Can gains in redistribution be sustainable without more attention to production? How can the production regime support a universal welfare regime, which simultaneously tackles poverty and inequality?

Nordic countries succeeded in gradually building positive interrelations between welfare and production regimes. In sharp contrast, in the global South, even relatively successful countries have had a hard time securing stable funding sources for social policy and making an effective use of their human capital. Costa Rica is a case in point. It shows, first, how challenging it is for developing countries to build and sustain productive regimes that enable truly redistributive welfare regimes. Second, it demonstrates that dysfunctional relations between the welfare and production regimes can remain for a long time. Third, it suggests that, over time, unless productive regimes undergo substantial transformations, this relationship copes with significant tensions.

The experience of social-democratic North Europe

Much of the political economy literature on the OECD assumes that most developed countries establish constructive and stable relations between their economic institutions and their social systems. Complementarities between the production and welfare regimes are not only expected but are considered particularly desirable for simultaneously achieving economic growth and income distribution.

The social-democratic model in the Nordic countries constitutes one of the best examples. Low inequality and high social spending went hand in hand with successful export performance and dynamic technological upgrading. Close collaboration between governments and firms contributed to the rapid expansion of new manufacturing activities and productivity in agriculture (Bloomstrong and Meller, 1990). As a result, the production system generated enough resources to fund a generous welfare system that reduced poverty more effectively than more targeted regimes (Korpi and Palmer, 1998). Nordic countries and others in Continental Europe promoted high spending in education and active labor policies that provided firms with a high-skilled, highly productive labor force (Hall and Soskice, 2001; Huber, 2002).


(Ariana Araujo)

Latin America's shortcomings and exceptions

In Latin America, even those countries with more generous welfare states like Chile, Argentina and Uruguay, weaknesses in the production regime have resulted in problems of financial sustainability and job creation (Bulmer-Thomas, 2003; Huber and Stephens, 2005; Filgueira, 2005). As a result, inequality has been historically high and the state's efforts to reduce poverty and inequality often ineffective (see for example Blofield 2011).

Costa Rica is a partial exception to these trends. The country has been considered a showcase of human development and universal social policies and an example of social democracy in the periphery (Sandbrook et al, 2007). In recent years, it has succeeded in maintaining its generous social services while simultaneously developing comparative advantages in high tech sectors. Comparatively within Latin America, inequality and poverty are lower. Have positive complementarities between a universal welfare system and the production regime been created? Is Costa Rica a successful example for others in the 'periphery'?

Lessons from the Costa Rican showcase

Between 1948 and 1980, Costa Rica established a generous and universal welfare regime. Some positive links between productive and welfare regimes contributed to this end. Rapid accumulation of capital, public incentives to develop new economic sectors and overall state expansion promoted the growth of well paid jobs which in turn helped to fund the welfare regime. However, the production regime was unable to transform the newly created human capital into an upgrading in the leading economic sectors. Costa Rica's comparative advantages continued to revolve around coffee and bananas, neither of which required significant amounts of skilled labor.

Since the early 1980s the country underwent a systematic attempt to develop skill-intensive comparative advantages. New sectors received generous tax incentives and subsidies and were expected to attract human capital, expand productivity and support the resilient universal welfare regime. Although new comparative advantages were indeed created, the productivity gap between high and low productivity sectors grew and posed new challenges upon Costa Rica's social policies—still largely reliant on payroll taxes.

At the heart of Costa Rica's mixed performance—and Latin America's pervasive lack of complementarities—lays the of structural heterogeneous production regimes. Between 1950 and 1980, Costa Rica succeeded in promoting low productivity sectors, expanded formal employment and consolidated a stable funding mechanism for its social policies. Nevertheless, the leading sectors failed to use the skills provided by the welfare regime. Nowadays, the low productivity sector has been left behind.

Far from occurring to Costa Rica alone, most production regimes in Latin American, have limited the chances of establishing universal welfare regimes.

The challenging road ahead

In recent years, a simultaneous expansion of social assistance and secondary education has helped many Latin American countries reduce poverty and inequality (López Calva and Lustig, 2010). Cornia (2010) even talks about a new "policy model of fiscally prudent social democracy". These changes, however, have taken place in the context of production regimes that remain specialized in primary resources and are structurally heterogeneous (ECLAC, 2010). As Costa Rica shows, at the end, universal social systems can only help reduce inequality and poverty if production regimes provide the required funding, the formal jobs and the demand for skills.

(Alessandra Baltodano @ Agencia Wimblu)

Our analysis has significant theoretical and political implications in the post-retrenchment, post-Washington Consensus era. Theoretically, our contribution highlights the obvious need to consider the material bases for the development of more generous welfare policies in developing countries. In terms of policy, it stresses the importance of promoting both leading and low productivity sectors and of securing stable funding mechanisms for the welfare regime.

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