Beliefs, Leadership and Economic Development; Making the Critical Transition, Brazil 1964-2012*

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Abstract

A lesson from the scholarship on institutions and development is that economic and political development does not reach most countries because it is not in the interest of those in power, whose goal is to protect their rents. We know more about persistence than we do about making the critical transition to sustained prosperity. We focus on the question: how have some countries managed to break away and transition to becoming open societies? We highlight the roles played by three concepts: windows of opportunity; leadership, and beliefs. We wed these concepts to institutions. After presenting our framework, we flesh out the dynamics with a case study of Brazil from 1964-2012. In the early 1990s Brazil seized a window of opportunity with the leadership of President Cardoso and his economic team. Over time, they changed beliefs within Brazil which has set them on a trajectory towards an open economic and political society.

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I. Introduction

Economic and political development is contextual, nevertheless there are some general elements in the process of institutional persistence and change.[1] Persistence or incremental changes are more common than countries making big changes in their economic and political trajectories. The early achievers, Great Britain, France and the U.S. broke with the past by accident not design. Other countries, e.g. the G-20 followed suit, but most countries remained either middle income or lower income despite knowing the attributes of the success stories. But, some countries have broken away from their past and Brazil is one such country in the midst of transition. Our framework allows us to better understand development in the modern world by which we mean that there exist developed countries and that the developing countries are aware of and can potentially learn from the developmental paths of the already developed countries.[2] We focus on middle income countries where at first blush it is a puzzle that a greater number have not transitioned to more open economic and political societies, given that there are role models they could emulate.[3] By emulate, we do not mean that institutions can be directly imported but only that the leaders of countries have a good idea of some of the key ingredients that all open societies possess: e.g. rule of law; clear, secure and impersonally enforced property rights; competent and honest bureaucracies; and open and competitive economic and political systems. Our framework consists of several interconnected

[1] By contextual we mean that there are many multiple paths to economic and political openness. We do not believe that it is best to first open up economically and then politically or vice versa. History has examples of either path as well as a relative balanced path between economic and political openness. Our book provides a detailed case study of Brazil from 1964-2012 which allows us to establish the importance of context and the heavy hand of historical institutional dependence. Our book complements and augments the literature on development by proposing a general framework along with a detailed case study. In this regard we are following in the footsteps of Acemoglu and Robinson (2006, 2012); Eggertsson (2005), Greif (2006); and North, Wallis and Weingast (2009). But, importantly we differ with our emphasis of the roles played by leadership and beliefs. In addition we focus on a Brazil, a large middle income country which we argue is in the process of making the transition to sustained economic and political development

[2] By developed countries we do not simply mean rich but rather that they are open economically and politically. The Human Development Index captures our notion of development better than GDP/P but the HDI also focuses on outcomes whereas we focus more on the process that produces the outcomes.

[3] We return to the issue of role models when we discuss leadership. Greif (2006: 195-196) recognizes the importance of role models: “Such comprehensive changes are more likely to be attempted if there is a “role model, a known alternative institution with better outcomes…”Candidates to the list of potentially developed countries include Brazil, Chile and South Korea. Remember we focus on the process of development and not the absolute outcomes, which in some cases will take a long time.

key concepts that we will first define in a static context and then utilize to show how they produce a dynamic of institutional change or persistence.[4] The concepts include: windows of opportunity; leadership; a country's configuration of power and the preferences of those in power; the beliefs of those in power; institutions; and political and economic outcomes. Our major contribution is stressing the interconnections among windows of opportunity, leadership and beliefs.

II. A Brief Review of the Literature on Institutions and Development

Today the primary role of institutions as a determinant of economic growth is widely accepted across disciplines and literatures. A major theme in this literature has been to explain why it is that, given this understanding, all countries do not put in place good institutions and reap the economic rewards. A less appreciated characteristic of much of the literature on institutions has been the notion that there is often a specific crucial moment in a country's history when new economic and political institutions emerged. These theories are what can be called 'Decisive Moment' explanations of why some countries prosper while others do not.[5] One of the most influential early papers to make this connection was '*Constitutions and Commitment*' by North and Weingast in 1989. They argued that the political institutions that emerged out of the Glorious Revolution in England in 1688 created the restraints on governmental opportunism that fostered circumstances in which investment and innovation could thrive, ushering in the subsequent centuries of high economic growth. Their argument pinpoints the moment in time in which England's developmental path took a distinct swerve towards economic development.[6] We show below that there has since been a large literature based on the notion that development most often starts with a distinct shock that creates a punctuated change in which the appropriate growth-enhancing institutions emerge.

[4] Eggertsson (2005) analyzes the factors that can account for "imperfect institutions," by which he means that actors are aware of alternative institutions that would produce more economic growth. He lays the major blame on social models. We will return to this in our section on beliefs. Eggertsson (2005: p.151) is also closest to us in arguing that experience and shocks shape mental models.

[5] A 'decisive moment' entails a specific event but for some authors a subsequent institutional deepening, e.g. North, Wallis and Weingast (2009). A 'moment' may be a decade century but is short in historical time.

[6] The North and Weingast hypothesis has sparked considerable debate.

Counterfactual theories suppose an ongoing process of gradual incremental change with corrections and adjustments continuously made along the way.

The framework we present in this paper fits this 'decisive moment' set of theories of economic development, as one of its crucial elements is the concept of a window of opportunity. A window of opportunity, carefully defined below, is one possible type of 'decisive moment' in a country's developmental path. Other such 'decisive moments' are critical junctures, exogenous shocks and plain old historical events. At the appropriate time we will explain what distinguishes these relatively similar terms. First, we will show that 'decisive moment' theories are indeed well established.

A 'decisive moment' theory postulates that at some point in a country's history an important shock took place that crucially changed that country's destiny. The shock, which can be technological, demographic, climatic, geographic or a combination of these and others, creates circumstances in which the extant economic and political institutions get significantly changed. These theories see institutions as the key determinants of economic growth so the change in institutions introduced by the decisive moment marks an important change in the country´s developmental path. In addition, 'decisive moment' theories have two further defining commonalities. The first is that the nature of the institutions determines the nature of the country's development. Good/open/inclusive institutions enhance long-term growth and bad/closed/extractive institutions lead to the opposite. Secondly, institutions are seen as having a strong reinforcing nature that exhibits strong persistence of power relations and outcomes over time. By defining who has power, voice and access to the economic rents, the new circumstances introduced by the decisive moment ensures self-perpetuating paths, where openness breeds more openness and fosters growth, while concentrated wealth and power endures and limits growth in the long run.

There have recently been spates of papers and books that rely on 'decisive moments."[7] Engerman and Sokoloff (1997, 2002) argued that different developmental paths across

[7] In the genre of the New Institutional Economics, North and Thomas (1973) was perhaps the seminal work. Alston and Ferrie (1993; and 1999) represent an early embodiment along the lines of a decisive moment as well, though the decisive moment in Alston and Ferrie was caused by technological change – the ability to mechanize cotton-

countries in the Americas could be explained by factor endowments encountered by the colonizers in the New World. Irrespective of the identity of the colonizing country the most preferred goal was to produce valuable tropical products such as sugar or to extract precious metals. The most profitable way of doing this was by coercing local or imported labor. This strategy was only feasible in those colonies where weather, geography and demographics provided the necessary factor endowments. Where these were not available colonizers had to settle for other less profitable strategies, such as family farms producing grains, cattle and other products that do not exhibit economies of scale. The main argument of their hypothesis that each of these initial colonizing strategies, by their very nature, became locked-in, leading to persistence over the centuries in the nature of the country's economic and political openness and consequently their relative economic growth. Those countries that at this decisive moment adopted strategies that concentrated wealth and power systematically pursued exclusionary policies in all areas including education, franchise, immigration, credit, and business organizations. The countries that started off with more inclusive economic and political policies became increasingly more open. The final element of the theory is that in the long run openness and inclusion lead to economic growth whereas concentration of wealth and power, though initially productive, eventually are unable to produce the necessary growth in productivity and innovation that is required for modern economic growth.

The Engerman and Sokoloff theory had a massive impact on the literature. Their basic research strategy involved exploring the fact that different factor endowments led to different types of institutions arising from the shock of the 'decisive moment' that was the discovery and colonization of the New World. This created a type of natural experiment that allowed the impact of different institutions on growth to be sorted out. The subsequent literature followed in their footsteps expanding and modifying their basic logic while ramping up the empirical techniques. The coverage was expanded from the Americas to much broader samples and a greater focus was put on testing the theories' predictions econometrically. Creative searches for ever more exotic 'decisive moments' ensued, which has unearthed some improbable

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which in turn had dramatic political ramifications at the national level and allowed the expansion of the modern welfare state.

datasets and widespread use of proxies for variables previously deemed as unquantifiable. This literature contributed towards significantly changing the way the profession pursues its craft. In the past decade economics has taken a decidedly empirical bent. Economic history has become in vogue and institutions are now a central fixture of mainstream analysis. Standards of econometric rigor have significantly improved, as the questions at hand required sorting out issues of causation and omitted variables in the relationship between growth and its potential determinants.

The purpose here is not to provide an exhaustive review of this literature, but rather to show the basic common elements of theories that rely on a decisive moment as the catalyst through which new institutions emerged and determined economic performance. This allows us to define where our framework fits within this literature and highlights our contributions.

All the papers cited below share a common structure. A decisive moment creates new circumstances that lead to new institutions. These institutions are the treatment that is hypothesized to determine the nature of development and growth. The way in which the decisive moment unfolds is such that the treatment is administered differently to different countries or regions. For the empirical strategy to work it must be that the way in which different countries are assigned to different treatments must be as if random. That is, the circumstances that determine whether or not the country receives the treatment must not directly impact that country's performance, except by nominating it for the treatment. For each of the papers we point out the decisive moment and the mechanism it contained that randomized the type of institutions that emerged. The remainder of the argument is common to all the papers and will thus not be repeated for each, that is, that initial institutions persisted over time and open (extractive) institution led to long-term economic growth (lack of growth).

The most influential paper to expand on the decisive moment approach was Acemoglu, Johnson and Robinson (2001) on the colonial origins of comparative development. Their decisive moment was the colonization spree that followed the discovery of the New World, but their sample includes other continents. Their randomizing mechanism is that disease environments induced different levels of settler mortality, crucially influencing whether growth-enhancing or extractive institutions emerged in different countries. In another paper

(Acemoglu, Johnson and Robinson, 2004) they argue that the same colonization shock also determined the economic destiny of the colonizing countries. In those nations where the colonial enterprise enriched a merchant class that subsequently pursued checks and balances on the powers of the Crown (England and Holland), virtuous institutions emerged. Where the colonial shock merely further enriched and empowered the Crown, the opposite ensued (Spain, Portugal and France). In this case the randomizing mechanism was having an initially independent merchant class that had access to the Atlantic.

The Acemoglu, Johnson and Robinson papers lead to a lively debate on whether institutions were the fundamental cause of long-term growth or whether other factors, such as geography, human capital or culture, were more important. Notably, Easterly and Levine (2003) and Rodrik, Subramanian, and Trebbi, (2004) sided with the view that institutions rule, while McArthur and Sachs (2001) and Glaeser et al. (2004) defended geography and human capital respectively, while culture based explanations such as Landes (1998) and Nunn (2012) still have many adherents.

Several recent papers have applied similar approaches to specific countries (or regions), mapping how colonization (a decisive moment), led to the emergence of differentiated institutions in different regions and consequently impacted long-term development accordingly. Following the literature, each paper finds in a country's history a different mechanism that randomly assigned institutions. For India, Iyer (2010) uses the assignment of direct versus indirect rule of sub-national governments in the colony and Banerjee and Iyer (2005) use historical property rights; for Peru and Bolivia, Dell (2010) uses the 'mita' system of coercive labor; for Brazil, Naritomi, Soares and Assunção (2012), Martínez-Fritscher, Musacchio and Viarengo (2009), Martínez-Fritscher and Musacchio (2009), and Summerhill (2010), all use shocks related to colonial export booms; for Africa, Nunn (2007 and 2008) uses the slave trade; for small islands, Feyrer and Sacerdote (2009) use wind and tide patterns. This is a very incomplete list.

Some authors have gone even further back than the start of the modern period in the search for decisive moments. Haber and Menaldo (2011) consider the period when the early territorial states began to replace tribal societies. The randomization in this case is provided by the variation in rain patterns. The data show a striking correlation of areas that currently have stable democracies with areas where there is moderate rainfall. The main mechanism through which rainfall could have affected regime type is through its effects on institutions. Moderate rainfall allowed the production of crops that produced surpluses and could be stocked over time. These circumstances created incentives for investing in trade and human capital and also created a demand for a state that could protect property rights. Areas that were too arid or too humid did not experience the same incentives and thus developed institutions that did not promote investment, innovation and growth. Mayshar, Moav and Neeman (2012) and Allen (1997) propose related mechanisms where the origin of the state is induced by local circumstances made relevant by the Neolithic Revolution.

But this is still not the earliest decisive moment that has been suggested. Other authors have focused on pre-historic times, when Homo-sapiens started to migrate out of Africa. Ashraf and Galor (2011) and Spolaore and Wacziarg (2009) analyze the pattern of genetic diversity that took shape as prehistoric humans left the cradle of civilization to populate the world. The first of these papers argues that the genetic distance between the populations that emerged from this diaspora created barriers for cooperation, trust and technological diffusion thus limiting the spread of development in those countries that were genetically further from the technological frontier in any given era. The second paper argues that in addition to the costs imposed by genetic diversity there were also benefits in the form of an expansion of the production possibility frontier. Therefore the net impact of genetic diversity on long-term economic growth is hypothesized to be shaped as an inverted-U with too much or too little diversity limiting growth.

The notion that decisive moments are a central part of the explanation for why countries succeed or fail is most explicitly put in Acemoglu et al (2008). They show that the positive correlation that is often found in regressions of democracy on income disappear once one controls (with fixed effects) for country-specific factors that affect both these variables. Instead of causation from income to democracy, as proposed by modernization theory (Lipset, 1959) they argue that political and economic paths are jointly affected by other factors that arise in decisive moments in a country's history:

> The development path a society embarks upon is partly influenced by its experience during certain critical junctures, which might include the early stages of colonization for former colonies, the aftermath of independence or the founding of a nation, the epoch of the collapse of feudalism for Western European nations, the age of industrialization (i.e., the nineteenth century), and the periods of significant ideological shocks such as the Reformation, the Enlightenment, or the rise of Islam. (Acemoglu et al., 2009: 308)

The framework presented by North, Wallis and Weingast (2009) also sees institutions as the main determinant of development, but in contrast to the papers cited above their theory is not based on the notion of a decisive moment but rather a series of **decisive moments** that are country specific in that the causal determinants for reaching the doorstep conditions and the transition vary from country to country. They see the transition from a 'natural state', where closed economic and political institutions create and distribute rents among elites as a means to avoid violence, to an 'open access order', where open competition for political and economic rents has arisen, as the definition of the process of development. The question is then how this transition takes place. Their framework divides this transition in two phases. The first takes place as a country acquires three 'doorstep conditions:' control over violence; a rule of law amongst the elites; and perpetually lived organizations. The second phase, which is the transition proper, involves extending that rule of law to all, so that personal privileges become impersonal rights. This does not fit former literature of **a decisive moment** pattern as a country can remain for long periods in the doorstep conditions and even the transition proper might be a slow and incremental process. But, the transitions occur in a relatively short historical span of time.

> Historic transitions occurred within relatively brief periods, typically about fifty years. Britain, France and the United States appear to have been on the doorstep in the late eighteenth century and made the transition to open access between 1800 and 1850, or in the case of France, by 1880. Although they have not completed the transition, both South Korea and Taiwan's experience seem to have paralleled that of Europe, taking approximately fifty years. Some of the countries in the periphery of Europe have made a quicker transition … These changes occurred within relatively narrow windows of historical time. (North, Wallis and Weingast, 2009: 27)

In our framework we argue that one of the most important and most neglected factors that emerge during decisive moments, changing institutions and ultimately outcomes, are beliefs of how the world works. Although beliefs do appear in some treatments in the literature surveyed above (in particular North, Wallis and Weingast, 2009), they are usually given a secondary role. Although we too do not have a fully satisfactory theory of beliefs, they play a more central role in our framework. We are not alone in giving beliefs a central role. Eggertsson (2005) and Greif (2006) both argue that beliefs are the key to understanding the institutions that those in power put in place. Eggertsson argues that Iceland was locked into “imperfect institutions” because of a social model held by the rural elite that fishing would make the elite worse off by driving up their wage costs. For Greif, differing beliefs in Italy versus North Africa led to more open institutions in Italy while in North Africa the beliefs led to institutions fostering a closed society. Before turning to the framework itself it is useful to state explicitly how it compares to the literature.

How Does our Framework fit in the Literature?

The guiding principle for which papers we included in the brief survey above was the presence of two elements in common: the importance of decisive moments and the impact of institutions on growth or political openness. Our framework presented below shares many of those commonalities yet has several differences of foci, of emphasis, and other nuances that distinguish it from previous studies. In particular there are three elements that we stress that are unrepresented or simply absent from many other treatments in this literature. To make it clear how our framework fits in the literature and what it contributes, we explicitly list and discuss first its similarities and then the differences.

The first commonality is the object being studied. We want to explain what determines why nations fail or succeed at reaching advanced stages of economic and political development. Our dependent variable, analogous to North, Wallis and Weingast (2011) is economic and political openness.[8] The second commonality is that it is accepted as a central

[8] Most of the papers/books discussed focus more narrowly on economic development though many recognize the critical role played by politics to reach economic development. See in particular the work of Acemoglu and Robinson.

tenet that institutions are the fundamental determinant of economic growth, with open and inclusive economic and political institutions essential for that growth to be maintained in the long term. The third commonality is that our framework relies on decisive moments as a crucial part of its dynamics. Although endogenous incremental change is an important part of those dynamics, punctuated endogenous or exogenous shocks are the central feature that sets into motion important changes in all the other elements of the framework. But, equally important and unlike most other frameworks, with the exception of North, Wallis and Weingast (2011), continual supporting institutional changes must follow in the wake of the decisive moment in order to be on the road to prosperity.

Most of the papers cited above focus on a specific event, such as colonization or the Glorious Revolution, and then proceed to show evidence, most often cross-country econometrics, to test their interpretation of those events and its impacts. Our book is closer in its objectives to four other prominent attempts at creating general conceptual frameworks, specifically North, Wallis and Weingast's (2009) *Violence and Social Orders*, Acemoglu and Robinson's (2006) *Economic Origins of Dictatorship and Democracy* (or in more accessible form in *Why Nations Fail,* 2012), Eggertsson (2005) *Imperfect Institutions: Possibilities and Limits of Reform*, and Greif (2006) *Institutions and the Path to the Modern Economy: Lessons from Medieval Trade*.

A major goal of our book is to propose a framework for understanding transitions and relative stasis. Frameworks are by definition more general, less detailed and should explain more than just one or a few specific cases. In particular our framework focuses on development in the modern world. That is, we are interested in what determines the success of countries who have the necessary conditions to develop given the current state of knowledge and understanding of what it takes to do so today. Although many of the essential problems and difficulties of the process of economic growth are timeless and are as relevant today as they were for the first countries that made the transition in the 18th and 19th centuries, there are also many new circumstances that change the nature of the game. More than the obvious technological advances and the unprecedented levels of globalization it is the richer set of shared experience from over two centuries of mostly failed and a few successful attempts at development that make the challenge very different for today's rulers than it was for those of the pioneering countries. In many ways it is a paradox that this greater shared experience and better understanding of how things work has ushered so few new countries to the rank of those with sustainable growth and high incomes.

The second difference stems from the first. Because we are interested in contemporary development, where there is greater comprehension of what is going on and a wider offering of tried and tested policy alternatives, the decisive moments we confront are different than those faced 200 years ago. To stress this difference we use the term 'window of opportunity' rather than 'critical junctures' to refer to the large shocks that initiate a process of change. Although the difference may sometimes be subtle, 'window of opportunity' suggests that there is a chance for leaders and policymakers to purposefully react to the new circumstances to change institutions and possibly even norms and beliefs. In addition, most decision makers in the past acted to solve current problems without seeing that solving a particular problem, e.g., corruption in banking, could have downstream positive (or negative) effects. In our framework decision makers are both backward looking (in the sense of solving a current problem) and forward looking - they can foresee (never perfectly) downstream consequences. [9]

A critical juncture, on the other hand, conveys the notion of a shock in the more distant past to which rulers and citizens reacted with less understanding of all that was involved and a weaker notion of what could possibly be done. This does not mean that windows of opportunity will always be seized or that they will lead to the efficient changes, as the configuration of power is often such that growth-enhancing change is blocked. Also, whereas it is relatively easy to look back at history and recognize a critical juncture, it is not straightforward to sort out which of the myriad events in a country's current life are consequential and may turn out to be windows of opportunity, and which are just full of sound and fury but will signify nothing tomorrow. The difference is the combination of a decisive

[9] Eggertsson (2005); Greif (2006); and North, Wallis and Weingast (2011) are closest to our concept of window of opportunity in that the process is not a 'big bang' and must be sustained over a period of time sufficiently long to affect beliefs in the general population about how the 'new' world works. We differ in our stress on the forward looking ability of today's decision makers because of the role models played by the pioneer countries.

action taken at time t when the window is recognized and the necessary downstream supporting actions taken to affect beliefs and outcomes.

The third difference is related to the second. Given that windows of opportunity are a chance that can be seized, who will do the seizing? In many instances realizing the opportunity requires leadership to perceive the situation, to propose what must be done, coordinate the effort and persuade the country to take the leap of faith. Many windows of opportunity go by undetected or unrealized due to the lack of leadership (which might be an individual or a group) to provide the necessary elements of change. The role of leaders is typically absent in the literature on institutions, but is often overplayed by historians and business scholars. We see a circumscribed, yet often crucial role for leaders as the catalysts during windows of opportunity.

The final distinguishing characteristic of our framework is the central role played by beliefs in the dynamics between institutions and outcomes. A central question in the literature on institutions has always been why all countries don't put in place good institutions given that they are widely recognized as the key to long-term growth. The standard answer is: new institutions have redistributive consequences that cannot be renegotiated due to transaction costs and commitment problems, such that those in power prefer to block the change and retain a larger expected share of a smaller pie. We agree that such social conflict issues are essential for understanding the process of development. However, this explanation requires that all economic agents can calculate without cost or mistakes the impact of each set of new institutions and rationally pick that which maximizes the discounted present value of the inherent rental streams. In the absence of such unrealistic powers of rationality, beliefs arise out of the need to interpret the way the world works. When assessing whether to pursue or block changes in institutions, those in power have to have a map in their heads of how each set of institutions leads to different outcomes. Beliefs are those maps. They provide an interpretation of cause and effect between how different institutions translate into economic and political outcomes. If the world were such that those maps varied little across different groups and circumstances, and that beliefs had a natural tendency to reflect reality very closely (when there even is a 'true' relationship between institutions and outcomes), then beliefs would not be very consequential. However, the diversity of human experience shows that interpretations of how the world works has varied dramatically across societies, so that understanding why particular institutions have emerged and persisted in specific countries requires careful and explicit attempts at understanding those belief.

III. The Building Blocks of Our Conceptual Framework

Windows of Opportunity

Windows of opportunity are historical occasions when there is a chance to change the trajectory of a country's economic and political outcomes by changing beliefs and institutions. Windows of opportunity result when: 1) the rental streams fall short of expectations to members of the configuration of power; 2) a new member or organization enters the configuration of power because of an unanticipated economic and political shock; and 3) the beliefs of some members in the configuration of power change either because of the change in the economic and political outcomes or because of an exogenous event.[10] All crises are windows of opportunity but windows of opportunity do not require a crisis.[11] There are undoubtedly many windows of opportunity but it is the interaction among windows of opportunity, leadership and beliefs that matters. Windows of opportunity are not only "windows" for changing institutions; they are windows through which leaders can change institutions to make societies **more** or **less** open, economically or politically.[12]

Leadership[13]

Leadership is a relatively absent concept in frameworks of institutional change.[14] By leadership we mean that certain individuals at certain moments in a country's history make a

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[10] For example, the recent financial crisis has affected the beliefs of many actors in the sanctity of the existing relative prices of securities or housing to reflect long run values. In short, many economists now believe that bubbles can and do happen. This is no surprise to economic historians, several of whom have stressed financial bubbles. See in particular Kindleberger and Aliber (2011); and Neal (1993)

[11] See Higgs (1987) for a convincing discussion of the important role of crises in the U.S. prompting and sustaining the growth of government.

[12] This is consistent with Eggertsson (2005:151): "…opportunities for reform are created by real factors that upset the political balance, by real shocks and exogenous impulses that induce actors to revise their models.."

[13] We thank Avner Greif and Barry Weingast for discussions on the roles of leadership and beliefs. For an excellent analytical survey of recent contributions to literature on leadership, see Ahlquist and Levi (2011).

[14] Exceptions include Greif (2006: 201-202) who discusses the importance of "institutional entrepreneurs,"; Harberger (1993) who strongly argues that leadership mattered enormously for the economic reforms in Latin

difference because of their actions. The counterfactual is that if someone else or another group of people were in the same position of power with the same beliefs, the forthcoming institutions could have been different. Our view is akin to the 'structural theories' of leadership and most similar to leadership as espoused by Schofield (2006). Ahlquist and Levi (2011:8) cogently describes Schofield's concept of leadership:

> For Schofield, pivotal moments in history—what he calls "constitutional quandaries"—occur when core beliefs no longer conform to reality or, slightly more formally, when there is extreme variation in individual assessments of the appropriate action relative to the common, shared understanding. When these moments occur, small shifts in the beliefs of a few may trigger a cascade that results in an entirely different configuration of beliefs. A leader is the agent most likely to trigger such a cascade. According to Schofield, "architects of change" must do two things: (*a*) communicate a model of the world in which there are specific outcomes associated with differing courses of action and (*b*) convincingly advocate a specific outcome.

We differ from Schofield in that we do not believe that beliefs change in a "cascade" but rather deepen depending on outcomes consistent with the beliefs initially held by a "few." We agree that leaders start the process because they hold beliefs about institutional changes that can set the country on a new trajectory. This change in trajectory is just a start and must be reinforced over time.

The fact that history is replete with the mention of individuals lends considerable anecdotal weight and circumstantial evidence to our argument that certain individuals *did* make a difference. Leadership comprises several non-mutually exclusive concepts: 1) Cognition; 2*) Heresthetics* or Coordination; and 3) Moral Authority.[15] Before one can be a leader, he has to cognitively be aware that a window of opportunity exists. In addition he must know how to take advantage of the window of opportunity. In short, cognition entails being able to address two questions: What is the problem or opportunity that we face? How can we solve the problem or take advantage of the situation? This should not be construed that we have leaders

America; Higgs (1987) and North (1981) who discuss "ideological entrepreneurs (for Higgs in times of crisis); and Jones and Olken (2005) who use deaths of leaders as an exogenous change in leadership and find that leaders matter for economic growth. Leadership has been recognized by the "Austrian" school as entrepreneurship but for the most part has been applied to business organizations not political organizations. See Wagner (1966) and Frohlich, Oppenheimer and Young (1971) for a role for political entrepreneurship. Political scientists have elaborated on leadership but mostly in the context of principal/agent models. See Fiorina and Shepsle (1989) for a discussion of formal theories of leadership in which they discuss the strengths and weaknesses of principal/agent models.

[15] See Greif (2012) for the leadership roles of cognition, moral authority and coordination, especially chapter 3.

who can perfectly foresee all downstream consequences but only that they see the problem and have a provisional 'game plan' on how to both correct the problem at time t and understand that they will have to react to downstream consequences in unforeseen ways to sustain the solution to the problem at time t + n. Indeed, without downstream institutional deepening the initial 'big bang' would not produce long run benefits. It is the combination of the initial institutional change which, if successful, affects beliefs in a way that will enable later institutional changes. Leaders also never act alone; it is the orchestration of other powerful organizations that allows the initial change to take place and subsequent institutional deepening. Another way of putting is: if the initial institutional changes produce outcomes that benefit extant organizations or create new organizations that win, the beneficiary organizations now have a stake is sustaining and deepening the new institutions.

An example from business is Amazon.com.[16] Jeff Bezos founded Amazon and went online as a bookseller in 1995. This was a very different way for consumers to purchase books and many pundits at the time did not envision the success of Amazon. Did Amazon succeed and become the world's largest on-line company by one change –selling books on-line? No, they got their start with a big idea; selling books on line because they could offer consumers a larger inventory then any bookstore. But, they succeeded because they moved into selling a myriad of goods and even services: electronics, apparel, beauty supplies, clothing, jewelry, groceries, 'cloud' storage for data, *inter alia*. Moreover, a large percentage of what Amazon sells is produced by other companies who find it in their interest to use Amazon as their intermediary. Other retailers find that they can make more money, even after paying Amazon, by listing their products on Amazon and using Amazon's web platform. Why? Because Amazon receives more 'hits' and sells more products in terms of value than any other on line merchant. Indeed, the value of Amazon's sales is slightly larger than the next ten biggest on line merchants. So, the success of Amazon can be credited to the initial and continued leadership of Jeff Bezos and others at Amazon. First, the big change of selling books on line and then by the downstream changes into other products and most importantly an efficient web platform such that it

[16] Most of the information in this paragraph comes from a series of daily articles in the *Financial Times* July 9-13, 2013.

became in the interest of other retailers to sustain the growth of Amazon. Jeff Bezos in 1995 did not have a vision of the huge platform that sustained his success but he did have the cognition to recognize the opportunity to successfully sell books on line in 1995 and the downstream cognition to sustain further changes in his company that importantly increased the number of other retailers that now had a stake in Amazon.

But, cognition is not sufficient. As recognized by Wagner (1966) political entrepreneurship is needed to overcome the free rider problem associated with collective action. We refer to entrepreneurship, following William Riker (1996: 9), as *heresthetics* which Riker defined as: “the art of setting up situations –composing the alternatives among which political actors must choose- in such a way that even those who do not wish to do so are compelled by the structure of the situation to support the heresthetician’s purpose.” *Herestethics* involves strategy especially dynamically in the course of decision-making.[17] *Herestethics* is the “***art”*** of policymaking and is not justified by ex-post rational choice and could certainly not be designed ex-ante by a mechanism design approach. Successful leadership entails cognitive ability of knowing what to do along with the coordinative ability of getting others in power to go along.

Leadership can be in a leader’s and his supporters’ personal self-interest but leaders at times can take reputation or ‘moral’ rents into account (Greif 2008). Some leaders try to do ‘the right thing’ for their country by ‘playing for the history books. Harberger (1993) argues that several Latin American leaders from 1960s to the 1990s took courageous steps to help their economies with unselfish motives driving them. In addition to seeking ‘moral’ rents, some leaders have moral authority either because of their past or because they earned it. Moral authority does not necessarily make heads of state ‘leaders’ but it gives them legitimacy which in turn can induce a public to trust their motives which may lead more readily to accepting new beliefs during windows of opportunity. Nelson Mandela in South Africa or Vaclav Havel in the Czech Republic commanded moral authority because of their time spent in prison.

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[17] Riker (1983 and 1996) applies *herestethics* it to the establishment of the electoral college and the ratification of the U.S. constitution.

Leadership can change the trajectory of a society for better or worse. Leadership is only an important concept when there are windows of opportunity. For much of the time, countries are on “auto-pilot” such that the rental streams are within a tolerable band to those in power so that there is no reason to rock the boat by changing institutions in a big way. We are not arguing that all you need for development are ‘great’ leaders but rather that individuals and certain organizations at times make a difference. For example, if this was not the case, there would be no need to discuss France without Napoleon; the U.S. without George Washington; Great Britain absent Churchill; China after Mao and with Deng; Brazil after Cardoso and Lula; or Argentina after Peron. We believe that these individuals along with their allies made a difference. Similarly there are today discussions about Cuba after Castro; Venezuela after Chavez; Korea after Kim; and Egypt after Mubarak. If individuals did not matter then these discussions are pointless. The exit of individuals at times leads to significant changes in the country, even though the other economic and political organizations remain intact.[18]

Configuration of Power

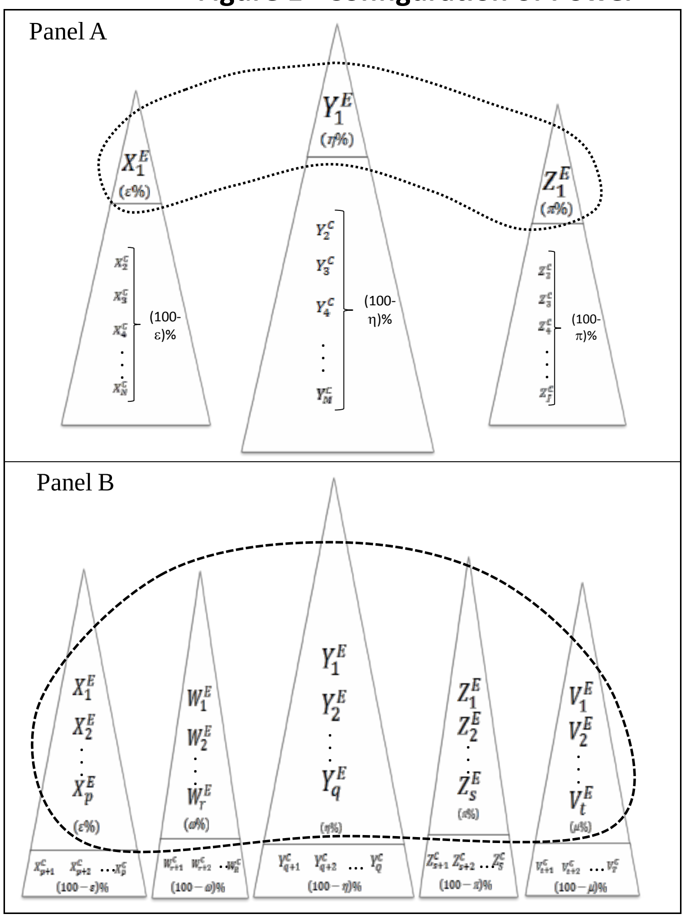
In our framework political power means the ability to change formal institutions, e.g. the laws of a society, and during windows of opportunity, the potential to change informal institutions by influencing beliefs. We are interested in explaining development or transitions to more open societies, particularly for countries that are upper middle income countries. In the North, Wallis and Weingast (2009) framework, we wish to explain the transition process for countries that are approaching, or already have the doorstep conditions: societies that have solved the violence problem[19]; have rule of law for elites; and there are perpetually lived organizations. The distinction is made in Figure 1, which shows how the nature of the configuration of power becomes more complex as development progresses. Panel A depicts an early stage of development, when there are few organizations (X, Y and Z) headed by elites

[18] We recognize that the exit of certain individuals may simply be a tipping point and that many other underlying economic and political organizations may have already changed. This appears to be the case for Cuba which has now embarked on reforms. As of this writing, the exit of Mubarak has not produced significant changes in economic organizations. The early signs indicate that North Korea under Kim Jong-un may change its path of development

[19] This is slightly different than North, Wallis and Weingast (2009) who argue that there is consolidated control over the military. In our view, the military can be leading a government but they simultaneously can be an agent of other organizations in the society. To this extent, there is control over the military.

(superscript E) and their clients (superscript C).[20] The elites in each organization possess some form of violence potential, which they use to control their clients and possibly to assault and appropriate wealth from other organizations. A group of kingdoms is an example of this scenario.

Figure 1 –Configuration of Power



The potential for increased productivity and economic gain from peace might prompt the organizations to establish a pact where each refrains from violence. The dotted line demarcates the dominant coalition formed by the organizations' elites. By refraining from violence each is able to reap greater rents than would accrue when violence was endemic. The dominant coalition is an adherent organization that will function only as long as the rents make compliance incentive compatible. Each individual organization, on the other hand, is a

[20] Panel A is an adaptation and extension of Figure 1 in Wallis (2011). We also borrow some terms, such as 'violence specialists' and 'adherent and contractual organizations', from Wallis (2011).

contractual organization that benefits from the third party enforcement provided by the dominant coalition, making it easier for each organization to control their own clients. The third party enforcement also allows for anonymous exchange among members of different organizations. The gains in specialization and productivity that can be achieved are limited, however, by the fact that the creation of rents which keeps the dominant coalition together requires entry into economic and political markets to be restricted. The barriers to creation of new organizations restrict investment and innovation with deleterious consequences for long term economic growth. Furthermore, periods of peace and cooperation are often precarious as shocks that change the violence potential of any of the organizations may cause peace to breakdown until a new coalition can be formed through a new configuration of rents. Many countries remain endlessly stuck in cycles of this nature.

While some countries have been able to achieve considerable progress under limited access, historical experience suggests that there is a limit to how much growth can be achieved under such arrangements. A few countries, however, are able to develop an increasingly complex social organization that expands access into the dominant coalition, allowing for even further specialization and trade. This situation is represented in Panel B of Figure 1. Note that not only have new (economic, political, religious, and educational) organizations emerged, including a central government, but access to the rents in each organization has become more widespread.

While in Panel A the proportion of the population that is in the elite (parameters ε, η and π) is extremely small, in Panel B greater numbers have been granted access to rents and to the creation of new organizations. This incorporation can take place as a strategic decision by current elites during times of upheaval as a mean to preempt unrest and revolution (as in Acemoglu and Robinson, 2000 and 2006). Alternatively, greater access may take place when the creation of new organizations increases productivity and growth in ways that expand the rents that the current elites appropriate (as in North, Wallis and Weingast, 2009). In this process the rule of law and impersonal exchange may emerge within the elite coalition, creating a society where rents and privilege, while still present, are increasingly dissipated by economic and political competition among this extended elite. In this book we are interested in countries at this stage in the development process. By granting open access to the creation of new organizations to increasing proportions of its population these countries create circumstances where the Schumpeterian process of creative destruction that underlies the success of most developed nations' growth trajectory may emerge.

In such circumstances the configuration of power is a complex network composed of myriad powerful organizations that can influence formal institutions. Because of the plethora of organizations 'at the table,' our view of power is expansive; it includes all of the organizations that can influence the outcomes of the political process. It consists of both economic and political interests. Together the economic and political actors/organizations determine the formal rules of the game. In today's world there are myriad of 'demand' side interest groups including environmental, health, economic, business and many other NGOs. For now we are not concerned with the factors determining what is in an individual or groups 'interest' but simply that some interests have power and others do not; power is a matter of the access to influence or shape institutions.[21]

In developed countries and some "developing" countries, citizens also matter because they vote. Politicians listen to public opinion because disregarding it could mean being voted out of office or forced out by a coup. But, the "demand" for government gets filtered through a political process which varies from country to country. Political bodies are the "supply" side of government. The supply components include such elements as: whether a country has a parliamentary system or strong or weak Presidential system; the number of active political parties; the independence of the Supreme Court; the independence of the central bank; the competence and honesty of the bureaucracy; the actual degree of electoral competition; and those who enforce the laws, e.g. the courts (from local to Supreme), and police. All of these forces combine to produce a *de jure* and *de facto* configuration of political power. It is this set of actors and their relative power that defines and enforces the formal institutions in a society. The institutions in a society are shaped by those with political power and their preferences, i.e.,

[21] For this reason, many interest groups give to all viable political parties in order to guarantee that they will have a "seat at the table." Wallis (2011) argues cogently that preferences; the range of choices; relative prices; and beliefs determine 'interests.

the outcomes that they would like to see but there is uncertainty about the precise impact of laws on outcomes. The actors/organizations differ in their beliefs about the cause and effect relationships between institutions and economic and political outcomes. It is the beliefs of the players, rather than their preferences that ultimately constrain and shape the institutions of societies.

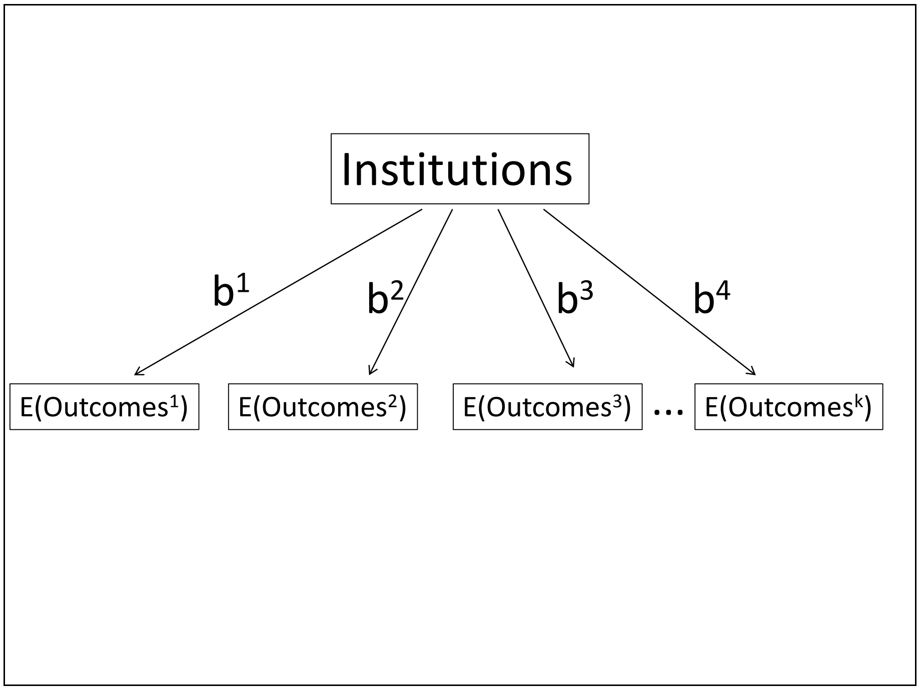
Beliefs[22]

By beliefs we follow North (2005) who defines beliefs as the subjective views of actors about the way the world works. Beliefs are very different from preferences which are views about what organizations would like to see transpire whereas beliefs are about perceived outcomes from institutional change, though because the world is non-ergodic there is will also be some degree of unintended consequences. Ultimately, beliefs about how the world works will shape the institutions that those leaders/organizations implement to achieve a desired expected set of political and economic outcomes.[23] But it is not obvious which institutions will lead to the outcomes they want, given the constraint of beliefs about how others will act. If there were some comprehensive manual mapping institutions to outcomes, those in power could look it up and see exactly which institutions they need to put in place to get the outcomes they want. But there is no manual; there is uncertainty about how things work and about the causal mechanisms between institutions and outcomes. As shown in Figure 2 a given set of institutions can lead to many different expected political and economic outcomes. The outcomes which are expected to emerge from a given set of institutions will depend on the beliefs of how institutions affect outcomes.

[22] Greif (2006) has analyzed the role of beliefs and institutions in detail in a deductive game theoretic fashion. In equilibrium institutions must be consistent with beliefs but we are interested in beliefs during windows of opportunity. Similarly Schofield argues that most of the time, societies operate on a "core" set of beliefs but during "constitutional quandaries" core beliefs become fragile. It is the fragile moments that enable societies to change their trajectories.

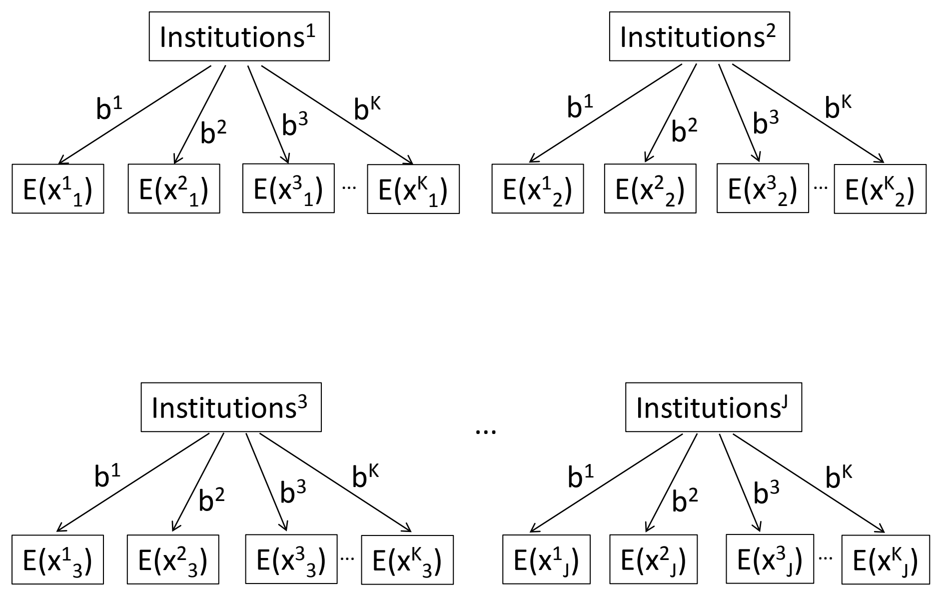
[23] This is consistent with Greif's definition of "internalized beliefs." He argues that internalized beliefs of those with power can motivate them to change institutions consistent with their beliefs.

Figure 2 – Expected outcomes given a set of institutions.



For the leader/organizations in power formal institutions are a choice variable during windows of opportunities, although the choice process can be quite complicated in some polities. In addition during some windows of opportunity beliefs can also be somewhat endogenous to those in power. It depends on the size of the window of opportunity and the fragility of the ex-ante beliefs. Figure 3 shows the full set of expected outcomes that can emerge from the full set of conceivable institutions.

Figure 3 – Expected outcomes from all possible institutions.



where x^k_j = outcomes

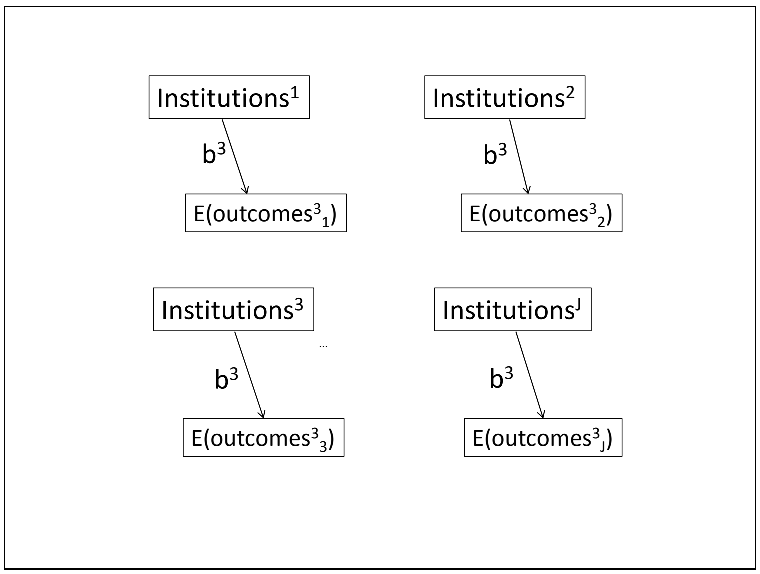
There are j=1, …J possible set of institutions, k=1,…K different sets of beliefs and expected outcomes x^k_j for each combination of institutions and beliefs. If it were clear how the world worked, then it would be easy to choose the institutions that lead to the best outcomes. But given the uncertainty it is not clear which branch b^k society is on. So those in power need some way to map –even though always imperfectly -from institutions to outcomes. Institutions shape choices that people make because they influence incentives. But, formal institutions are not the only influence on the choices that people make that determine outcomes. In addition to the unintended consequences from changing formal institutions, there are unintended consequences from informal institutions; and internal and external shocks which all play a role in the ultimate outcomes.

Beliefs emerge from history, experience, interaction and serendipity, though those in power have a greater scope to act on their beliefs.[24] Once beliefs emerge the choice in institutions becomes tractable. Given belief b^k emerges, the group in power will choose

[24] When outcomes are very different from expectations, beliefs change, at least for those in power, and a window of opportunity emerges for leadership.

Institutions^j , where j is the set of institutions that leads to the best outcome for them. If, for example, given beliefs b^3, $E(outcomes^3{}_3) > E(outcomes^3{}_i)$ for every $i \neq 3$, then the leader/organization in power would choose institutions that best fit their preferences[3]. In Figure 4 beliefs b^3 have arisen and the choice of institutions is then a matter of picking those institutions which maximize the expected outcomes for the group in power.

Figure 4 – Choice of Institutions given Beliefs.



Once those leaders/organizations with power choose and implement institutions, the outcomes that emerge have to match their expectations at least approximately or it will change the configuration of power, or the beliefs of those in power or both. The degree to which new institutions change outcomes depends on the extent to which they are compatible with the beliefs and norms of the economic and political actors in society. If the beliefs of the actors are firmly held, and inconsistent with the new incentives, the expected outcome for those in power will not materialize. Greif (2006) argues that the incompatibility of possible new institutions with the extant beliefs held by actors is a large part of the explanation for institutional persistence. We agree; but, if beliefs are malleable during windows of opportunity institutions can have a bigger impact on outcomes.

When expected outcomes do not materialize, there will eventually be a revision of the beliefs of those in power, or the dissatisfaction with the outcomes might, given a window of opportunity, lead to a punctuated change in the configuration of power, beliefs and institutions. We argue that experiences (political and economic outcomes) are the main factor shaping and changing beliefs of leaders/organizations in power as well as shaking the beliefs of citizens at large.[25]

We are not proposing a full theory of the determinants of beliefs. Our goal is more modest. Like, North Wallis and Weingast, we argue that "the cultural environment- the political, economic, social context- fundamentally influences beliefs" (NWW: 262). It is the beliefs of those in power that matter the most because those in power face windows of opportunity and make the laws. Nevertheless, the beliefs of citizens do matter. Indeed, the beliefs held by the citizens are a constraint on those in power. Those in power have preferences over outcomes but it is their beliefs that determine their actions. Our view on the role of beliefs matches Mokyr's view of the role of enlightenment in enabling the British Industrial Revolution:

> To sum up: Britain became the leader of the Industrial Revolution …thanks to the synergy of the Enlightenment: the combination of the Baconian program in useful knowledge and the recognition that better institutions created better incentives (Mokyr, 2009: 122).

According to Mokyr (2009: 40): "Enlightement beliefs followed in the footsteps of Bacon's idea of understanding nature in order to control her…" It was a belief that with the application of useful knowledge, a country could progress over the status quo. The application of knowledge in turn needed institutions that promoted 'progress.' At the time this was a new belief and, a belief not shared by all powerful actors at the time. It is the very nature of subjectivity of beliefs that gives rise to different views about the impact of institutions on outcomes. For a modern example, following the financial crisis of 2008, there is a lively debate amongst economists, politicians, and other interest groups about the impact of a stimulus plan versus an austerity

[25] Our view is very similar to Eggertsson's definition of a policy model: "Policy models are the operational models that guide decision makers, whether in the private or public sphere. Policy models define for the actor his or her choice set, rank the elements in the choice set, and describe relationships between means and ends (instruments and targets)" (Eggertsson, 2005: 26).

plan for promoting recovery.[26] The actions that get taken result from the relative power of the actors and beliefs of those with the power, as well as the role of leadership.

In today's modern world the political and economic actors can have a more forward looking view of beliefs because there are role models. Whereas the pioneer countries were trying to solve problems in light of their past experiences, today's countries can draw on the experiences of the already developed world for some of their beliefs. Not only can those in power draw from these experiences, but in some instances they do so inappropriately for a particular country. This was the problem with blindly relying on the "Washington Consensus." The failure of the consensus to work in certain countries most likely was a result of the incompatibility of the rules/incentives with the beliefs held by citizens. We stress that learning from other countries does not mean that the implementation will have the same effect, but nevertheless, it can affect not only their "belief" but the depth of their belief, which determines how long those in power will hold on to the cause and effect relationship. For example, if those in power want to control inflation there is a consensus that this is easier to accomplish if the central bank has independence from political pressure. So far, we have simply posited that beliefs shape actions, but if beliefs shape institutions it is paramount to posit how beliefs change, at least on the margin. We will do so later in this paper when we discuss the dynamics of the framework. For now we posit that belief-deepening depends on outcomes and the actions taken by others, including the support of citizens.[27]

Institutions

We follow in the now standard tradition of North (1990) by defining institutions as the formal and informal "rules of the game," along with the enforcement for non-compliance, that shape behavior. Formal institutions include the laws of society and how they are enforced. For example, laws are passed by some legislative body and may need to be approved by an

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[26] This is written in 2013 in the shadow of the 'euro crisis' and high unemployment in the U.S.

[27] For examples of how belief deepening depends on the outcomes being consistent with the prediction of those in power, who first held the belief see Bates, de Figueiredio, Jr. and Weingast (1998), who examine Zambia and the former Yugoslvaia; Eggertsson (2005) who analyzes the persistence and eventual change in beliefs in Iceland; Rakove, Rutten and Weingast (2000), who examine beliefs in the colonies leading to the Revolutionary War between the North American colonies (U.S.) and Great Britain; and Greif (2006) who examines beliefs in the context of Medieval trade.

executive branch or they could be united as in a parliamentary system. For countries that have the rule of law, laws are typically passed under the shadow of a Supreme Court. The size of the shadow of the court varies from country to country. For example, in Argentina, from 1946 to 2010, every administration but one (de la Rua) has either impeached Supreme Court Justices, forced resignations or added Justices (Alston and Gallo, 2010). This has led to little if no constraints on the executive and legislative branches. Informal institutions include the norms of behavior within a society. For example, trust varies across countries and will in turn affect how actors –private and public -negotiate deals/contracts to prevent ex-post opportunistic behavior (Williamson, 1985). Together formal and informal beliefs and norms provide the incentive structure for economic, political and social actions. By the incentive structure we mean the perceived reward structure faced by all individuals in political activity, in market activities, and within firms and other internal organizations. The perceived rewards vary enormously across individuals in political and economic activities. The perceived rewards, and the actions undertaken produce economic and political outcomes some of which may be consistent with the underlying beliefs of cause and effect as expected by those in power and others inconsistent with the beliefs of the designers of the formal institutions.[28]

The laws that countries pass will frequently entail political or economic side-payments. When the side-payments are transparent we call the process lobbying or 'pork.' When the process is not transparent we label the process 'corrupt.' Whether it is pork or bribes, many policy makers condemn these practices but, as North, Wallis and Weingast (2009) point out, they are the glue that prevents the entire system from unraveling into violence in less mature societies. For advanced societies, the 'pork' may enable welfare enhancing measures and eliminating pork may make policy change impossible (Alston and Mueller, 2006). In the process of institutional change, we need to recognize the important developmental role of "pork' and in some instances 'corruption.'

[28] Deep seated behavioral and internalized beliefs (as defined by Greif 2006) may often be the cause for why the outcomes deviate from policymakers' belief. In short the set of beliefs held by those in power about how a new institutional change will affect expected outcomes deviates from the actual outcome because the actors in society hold onto their set of beliefs which differs from those in power who can change the rules.

Economic and Political Outcomes

The institutions of societies generate incentives for economic and political activity which in turn produce economic and political outcomes. Again we recognize that it is not simply formal institutions that determine the full set of incentives; norms matter as well as the differing relative prices or costs of taking certain actions – which in turn depend on institutions - and the perception of actors of the outcomes from choices. It matters for those in power if the outcomes are consistent with their beliefs because they enact institutions to change incentives which in turn will produce outcomes that they perceived as beneficial for their goals. Political outcomes include narrow outcomes, e.g., politicians want to get re-elected, and broad outcomes, e.g., the degree of personal freedoms in a society. Economic outcomes, as well, are narrow and broad, e.g. did import protection increase the profits of a particular industry? Or, broad, e.g., how did policies impact unemployment levels, economic growth per capita and income inequality? The economic and political outcomes can have two effects. If they are sufficiently different from expectations or repeatedly different from the expectations they can affect the beliefs of those in power.[29] In addition to affecting beliefs, the political and economic returns can change the relative power of the economic and political actors. It is the change in beliefs or the change in power that generates the *dynamics* in our framework, producing either incremental institutional changes or more discrete large institutional changes when a window of opportunity opens along with the necessary leadership.

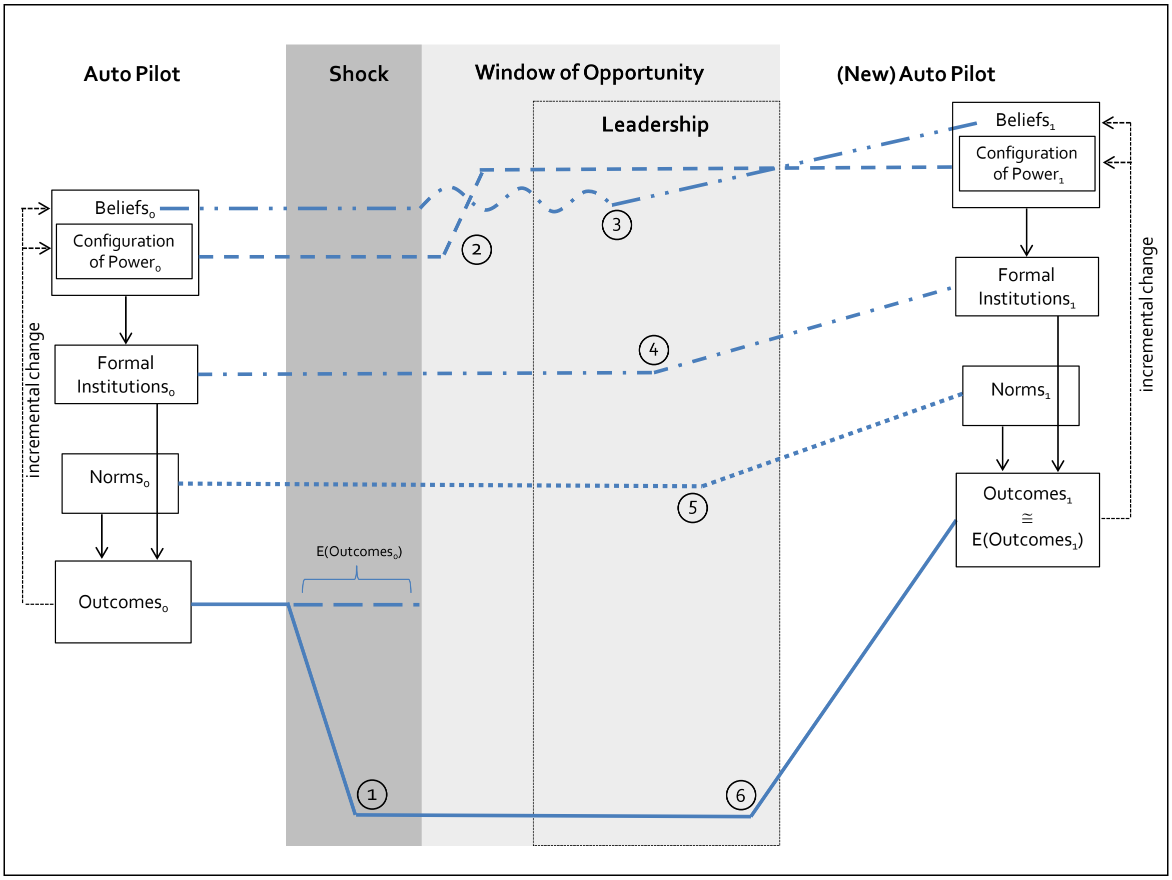
Dynamics

Now that we have the elements we can discuss in broad terms the dynamics of the framework, which is summarized in Figure 5. The left-hand side of the figure represents a society at some moment in time when there is relative stability in terms of the configuration of power, beliefs, institutions, norms and outcomes. This situation is labeled as being in "auto-pilot" to indicate that during this period there is generally no role for leadership as defined above. There are people in charge of government and organizations, but they do not affect beliefs except in indirect and incremental ways. The world that the players face is never static

[29] This is consistent with Eggertsson's (2005) argument that experiences affect social/policy models.

so they always take some actions to change some institutions, though others they may leave as fixed.

Figure 5 – The Dynamics of Development in a Modern World



Many institutions remain fixed because the incentives that the institutions produce generate outcomes that produce a sufficient rental stream to the organizations such that they see no reason to "rock the boat."[30] For other institutions they tinker on the margin. They make decisions, e.g. pass laws, issue decrees, and render judicial decisions, *inter alia.* All of these institutional changes change incentives on the margin but do fundamentally affect beliefs. We

[30] Eggertsson (2005) argues that for centuries Iceland held on to "imperfect institutions" because they benefited the agricultural elite. He argues that they held a misguided partial equilibrium social model. The landed elite feared that fostering fishing would drive agricultural wages up. They neglected to see that 'a rising tide, raises all boats' i.e. reaping the benefits from fisheries would foster economic growth sufficiently to increase the rent for landowners as well.

are in a world which Greif (2006) argues the institutions are consistent with the beliefs of economic and political organizations.

Beliefs about the impact that the institutional changes will have on incentives and in turn outcomes determine the institutions put in place, though the institutions also produce some unintended consequences, sometimes small and sometimes large.[31] To the extent that the overall outcomes produce adequate rents to the players in the configuration of power we will not see 'big' institutional changes and societies may cruise along in this "auto-pilot" mode for decades.[32] Societies function and operate under a belief system of: "this is the way our world works." The system is meeting the expectations of those in power as well as citizens; it is like a tide that washes over society. The belief system is predictable and is sustained by the social fabric of society, i.e., familial, religious, social and cultural relationships. In such a world, outcomes are consistent with expectations so there is no one in a position of power to push for big changes nor do actors outside the configuration of power question the legitimacy of the extant institutions.[33]

But, at some historical moment, the cumulative effect of small changes reaches a tipping point, or there is an exogenous shock, either internal or external to a country, which creates a window of opportunity. The shock is shown in Figure 5 with time moving from left to right. The lines that emanate from each concept represents change when it moves either up or down, and stability when it remains flat. At this level of generality we are not interested if the change was positive or negative, but simply whether something has changed or not. When a shock takes place the only thing that changes in a first moment are the outcomes, which now no longer match expectations (see (1) in Figure 5).

[31] Unintended outcomes result from a myriad of forces: formal institutions alone do not feed directly into outcomes; norms matter as well as the relative prices of choices faced by organizations. See Wallis (2011).
[32] This is analogous to how most of us live our lives. Most of us operate according to certain routines and it takes something out of the ordinary, e.g. a heart attack, to cause us to fundamentally change our way of life, though again we tinker on the margin.
[33] The rents are sometimes termed 'corruption' but they are necessary to sustain the social order. In advanced countries legitimate 'pork' plays the same role. For example, many pundits bemoan the use of earmarks in the U.S. or 'pork' in Brazil yet they are part of the political and economic process that produces institutional changes and allows the society to make some other wealth enhancing gains. We recognize that pork and corruption do not always produce institutional change; frequently pork and corruption sustain a redistributive function.

If this effect is large enough it may create pressure for change, leading to a window of opportunity. As shown in Figure 5 in a window of opportunity there are changes in the organizations in power, beliefs, institutions, norms and outcomes. The way these changes take place depends on the country and the situation and there are infinite possibilities. As drawn in Figure 5 the first element to change is the configuration of power with some or all of the previous elites being substituted. This can take place through riots, revolution, impeachment, elections or any other means (see (2) in Figure 5). Tipping points seem most likely in the case of mass movements, e.g. the demise of the Soviet Union or, perhaps, the 'Arab Spring.'[34] The economic/political system no longer meets the expectations of those organizations in power or citizens for a variety of reasons, some endogenous to the system and other external shocks: e.g., the gains from Import Substitution policies, though initially high, slow down and produce stagnation; or world relative prices change causing a different configuration in economic rents or political power.

In these moments the beliefs of some of those organizations in power about the cause and effect relationships of policies may change. As the previous understanding of how things work decays and is not substituted by a new set of beliefs, there is uncertainty about which new institutions should be put in place to achieve the desired outcomes. The wavy line at point (3) in Figure 5 represents the uncertainty in the beliefs of those in power and or the citizens in general.

It is in such situations that leadership may become relevant. In Figure 5 leadership comes into play within the window of opportunity when beliefs have become uncertain. After point (3) a new set of beliefs is in place. Change happens ultimately because beliefs about the way the world works have changed. In many cases the new beliefs simply emerge as a result of the shock, but in others they can be purposefully influenced by leaders.[35] Not everyone changes their set of beliefs simultaneously and some organizations in power may never change their beliefs. But if leaders can exercise cognitive and coordinative roles, a big institutional

[34] On tipping points in the former Soviet Union see Kuran (1995).

[35] In some situations the shock was sufficiently large that no matter who was in power the actions taken would have been similar. As an example, after 9/11, every conceivable President in the U.S. would have vowed to "hunt down" Bin Laden.

change affecting the trajectory of a country is possible. In Figure 5 the change in beliefs leads to new formal institutions (point (4)) and also to new norms or informal institutions (point (5)). These changes in turn affect the incentives faced by individuals and organizations affecting in turn their choices. All of this leads to new outcomes (point (6)), which now once again match expectations. In the right-hand side of the figure the society is once again in "auto-pilot", which means that leadership or changes in beliefs are no longer a major source of incremental institutional change. Compared to the situation before the window of opportunity there are new beliefs, new organizations in power, new institutions, new norms and new outcomes. The outcomes might be better or worse than before but are stable in the sense that they accord with what is expected. The outcomes will naturally vary over time as they are affected by small internal and external shocks, leading to incremental changes in beliefs and organizations in power (see feedback loops from outcomes to beliefs and configuration of power in Figure 5). Occasionally large shocks or endogenous tipping points might lead to new windows of opportunity and the process may repeat, though usually within a different context and with different details. Note, however, that there is no reason to expect that with each new cycle the country will be more open and developed. On the contrary, the historical experience suggests that such trajectories are rare, and countries are more likely to shift from one underperforming state to another or to cycle forward and back without much overall long-term improvement.

The key element in the dynamic is the change in beliefs. When beliefs become uncertain, some leaders can sway which beliefs get acted upon in terms of the institutions that get established. This can come about through agenda control coupled with the power of persuasion. If the new institutions produce incentives that in turn generate outcomes that are viewed as 'good' or consistent with the subjective view of the way the world works as expounded by the organizations that implemented the institutional change, then beliefs about the causal role of institutions on incentives and on outcomes deepens. For example, Rakove, Rutten and Weingast (2000) argue that prior to the Revolutionary War between Britain and her North American colonies, only a minority of those in power in the New England colonies "believed" that Britain would take away the liberties of the colonists. Actions taken by British, including the quartering of troops in New England and the disbandment of the Massachusetts legislature, gave credence to the beliefs of the New Englanders and overtime this belief in 'the British will take away our freedoms' propelled the colonists to take up arms against the British.

Another example comes from Brazil during their initial 'miracle' years. There was a belief in the mid-1960s until the late 1970s held by the majority of the business elites and the political elite in power (the military government) that 'developmentalism' increased the size of the economic pie for Brazil.[36] Increasing the size of the pie was more important than the distribution of the pie; concerns over distribution would come later. Consistent with this belief was the central planning role of the military along with some degree of authoritarianism and censorship. Of course not all elite groups held this belief. The intellectual left and the unions did not hold this belief but these individuals and organizations did not have sufficient power to change the prevailing *de facto* belief in the face of a system that produced double digit economic growth. Only when growth slowed down in the late 1970s did the majority of economic organizations begin to question their belief in 'developmentalism'. This change in beliefs by the business organizations proved crucial for bringing down the military, and bringing in its wake a belief in a more open and participatory economic and political system.

The beliefs of the benefits from change do not happen in a vacuum: those in power (and at times, citizens at large) can view the impact of institutions (and their resulting incentive structure) around the globe, e.g., an independent judiciary, secure property rights or less trade protection. In addition many of the economic and political elites acquired part of their education in wealthy countries which shaped their beliefs and their perceived benefits of importing institutions, though with modifications to suit their needs. Knowledge of institutions from the outside world also allows leaders more conviction "to stay the course" when there are upfront costs for downstream benefits from institutional change.

During a window of opportunity it is the competing and incompatible beliefs amongst organizations within the configuration of power, either the new players or old players with new beliefs, that brings about the potential for new institutions that change incentives and (at times

[36] In Brazil 'developmentalism' meant state run technocratic planning.

beliefs) and move a society towards a more open political and economic society.[37] In such a situation, competing powerful organizations are constrained by the beliefs of each other and their relative power. A new set of institutions emerges through leadership (which could be consensual group of organizations) in the Riker sense of coordinative activity that enables a new belief system to take hold amongst a winning coalition of organizations. In the case of Brazil, the winning coalition following the military government consisted of business organizations, who were disappointed in the slow rate of growth, some centrist politicians at the state and local level, and the "social reformers," consisting of the union leadership and "intellectuals" (academics, artists and others who opposed the censorship of the military).[38]

Leadership entails orchestrating powerful groups to react to the perception of a problem and that the perceived solution to the problem is shaped by the beliefs of leaders about the likely consequences of the new incentives emerging from the new institutions. In this sense our actors are both forward and backward looking.[39] Here is where today's threshold countries can learn from the experiences of countries that have already transitioned to open societies. Of course those in power can't perfectly foresee the outcomes of their actions but they can make an educated prediction.[40] In addition today's leaders recognize that a 'big bang,' e.g., the dissolution of the former Soviet Union is not sufficient for development but it was necessary. As we stressed earlier, the 'big bang' must be sustained with complementary changes in beliefs along with further downstream institutional deepening. All leaders can foresee is that putting in place certain incentives – through institutional change – will have some likely foreseen outcomes and some unforeseen outcomes. Leaders must be responsive to

[37] Competition only brings about the "potential" for moving to a more open society. It depends on the beliefs of those who win the competition for power. Our concept of "windows of opportunity is similar to that of Acemoglu, Johnson, Robinson and Yared (2008) who argue that economic growth does not necessarily lead to democracy and whether it does they label a critical juncture. They reach this conclusion after an econometric exercise which convincingly demonstrates that country specific effects make the difference.

[38] In the empirical chapters in our book manuscript (in progress), we discuss the leadership roles played by different individuals and organizations.

[39] This differs from the North, Wallis, Weingast (2009) view where the actors are primarily solving extant problems and not as forward looking as today's leaders/organizations can be. But, we agree with North, Wallis, Weingast that actors are solving current problems, the difference is that today's leaders can be more forward looking because of the experiences of other countries.

[40] Of course this does not dismiss the role for unintended consequences of which history redounds.

downstream unanticipated consequences. North (1990) referred to this process as ‘adaptive efficiency.” For example, most of the open societies in the world have been lowering import protection since the Bretton-Woods agreement after WWII.[41] Economic growth accompanied the lowering of tariffs. A country on the threshold today can learn from the experience of lowering trade protection over time and then it will be a decision for economic and political decision makers whether to retain the current rents from protection or open up.[42] Of course knowing what to do differs from the incentive to change. In many countries it is in the economic and political interests of the dominant coalition in power not to open up. Not everyone wins with creative destruction from open markets. But, our point is that it is not a cognition issue as it may have been 150 years ago when the belief in protecting ‘infant industries’ still undergirded many policies.

Opening up either politically or economically is problematic because the future has uncertainty – though today less than for the pioneer countries of the past- and some groups will lose, e.g. the military elite in Brazil in the mid-1980s. Moreover, generally opening up the economy entails considerable upfront costs, e.g., stabilization policies typically have short-run costs with long run benefits. This means giving up political and economic rents in the short run for some unknowable but positive probabilistic increase in rents in the future for society as a whole, though with unforeseen distributional consequences. Part of the solution to development is recognition that a winning political coalition of organizations foresees more advantages from promoting openness than the extant status quo. This is why windows of opportunity are so important. As we will see, the *Plano Real* (the stabilization plan of 1993) succeeded in part because after a series of hyperinflationary periods and failed stabilization plans, those in the winning coalition in Brazil believed that taming inflation was the number one priority for Brazil in the early 1990s. Enacting political and economic institutional changes requires some risks to those in power and this is where the leadership of Cardoso and his

[41] The General Agreement on Tariffs and Trade (GATT) eventually transitioned into today’s WTO which is a forum for expanding world trade by reducing trade barriers across its members.

[42] In this sense our actors are forward looking, similar to the Acemoglu, Johnson, Robinson (2005) versions of England and Spain responding differentially to oceanic trade. In other versions of Acemoglu and Robinson (2006; 2012), the elites are forced by citizens to give up rents. We believe that citizens have a greater role to play in the developmental process in proportion to the extent that the rule of law pertains to a greater percentage of citizens.

economic team mattered. Opportunities present themselves but not all potential leaders take advantage of the opportunity, either because: they lack the perception to see the opportunity; they perceive an opportunity but lack the knowledge of what to do; or they lack the art of policymaking in the dynamic sense expounded by Riker (1984, 1996).

Recognizing a role for leadership is a departure from the standard economic and political rational choice models consisting of "representative agents." We recognize that this leads to a certain degree of arbitrariness which is why analytical narratives entail thick description in the same way that courtrooms need to rely on circumstantial evidence when there is not a 'smoking gun.'[43] Windows of opportunity allow leaders to affect institutional changes that can lead to incentives that produce less or more political or economic openness than the previous order. Windows of opportunity are not unidirectional in proceeding from less to more openness; the reverse is equally likely. For example the revolution in Cuba was a window of opportunity that did not bring about greater political or economic openness but rather led to the sustained power of Fidel Castro, a leader of the revolution and subsequent President of Cuba.

At times, leaders enact 'big' institutional changes that lead to incentives producing outcomes consistent with expectations and also lead to greater economic or political openness because a greater number of organizations see a higher expected gain from the new institutions. This requires a complementary change in the way the world now works. For example, in the political arena, if the electorate rewards politicians for increasing political and economic openness within a framework of rule of law there is a tendency for the dynamic to become virtuous with institutional deepening, i.e. successive smaller institutional changes buttress the initial "big" institutional change. Belief deepening must accompany institutional deepening (Greif 2006). Institutional deepening is necessary for countries to transition to a sustained path of economic and political openness – the big institutional change is not sufficient. Moreover, many seemingly 'big' institutional changes never are sustained because they are not buttressed with other supporting smaller institutional changes and not

[43] On the role of circumstantial evidence in history see Fogel (1982).

accompanied by changing beliefs amongst the general actors in society. In short whether institutional changes are really 'big' can only be judged ex-post.

We will argue later in the book that the *Plano Real* led to taming inflation but it was the subsequent smaller institutional changes from 1994 through today that have produced a very different Brazil from the one in 1994, or 1985, the end of the military regime. Politicians find it in their interest over time to provide public goods to secure votes, and citizens in a competitive political system tolerate less corruption in society. Increasingly, the rule of law applies to political rulers in the sense that they are not above the law; impeachments are a sign that leaders are not above the law.[44] In the economic system, regulation and loans can be used preferentially or in patron-client fashion but politicians come to realize that such treatment no longer delivers the same political support nor generates economic growth for consumers. The virtuous dynamic produces a more impersonal society but a more open society, though progress is neither continuous nor always towards more openness.

From the lenses of history we know that reaching a sustainable virtuous dynamic is not an easy task and is not inevitable. Indeed those countries who have achieved relatively sustainable open societies are the exception rather than the rule (North, Wallis, Weingast, 2009; Acemoglu and Robinson 2012). The answer appears to be so highly country specific that generalizations can only take the form of very broad frameworks such as the one we presented here. Nevertheless, by applying the framework to Brazil, which we claim to be one of the few countries currently making the transition, we can both explain the real 'Brazilian miracle' and gain insights for understanding the general process.[45]

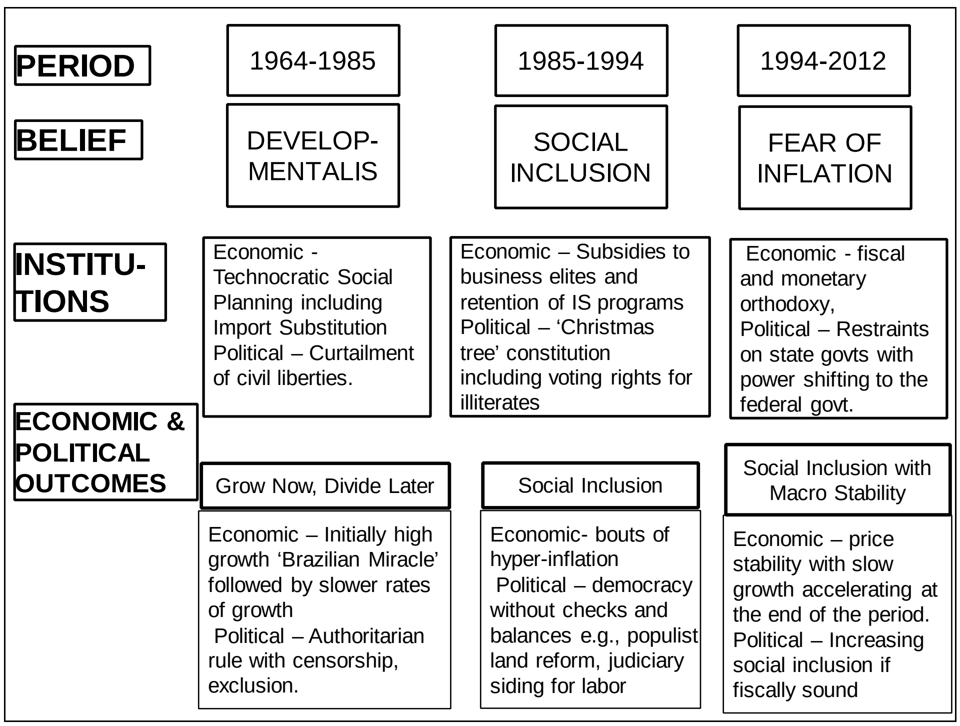
[44] In our chapter (book manuscript in progress) on the early years of democratization, Collor, the first elected President in Brazil, was impeached for corruption and yet the transition of the Vice-President to the Presidency was peaceful, and the process evolved according to the formal institutions put in place in the constitution. There was never a hint that the military would take over government.

[45] In the 1960s some development economists referred to the period as the 'Brazilian Miracle,' though with hindsight they narrowly focused on economic outcomes and not the sustainability of the economic and political processes that brought about the unsustainable period of growth.

IV. Brazil 1964-2012

Figure 6 presents our interpretation of the three periods through which Brazil has passed from 1964 to the present. The figure provides information on a series of central elements from our framework along a timeline: 1964 to 1985, 1985 to 1994 and post-1994. The top portion of the figure shows three periods and the key beliefs that prevailed in each period. Below the beliefs are the institutions that beliefs produced and then the subsequent illustrative political and economic outcomes.

Figure 6 – Brazilian Development since 1964.



Clearly different groups will evaluate outcomes differently as there are many distributive consequences of each situation. Our goal is to depict the beliefs of those in power. Although subjective, in most cases our classification will not be controversial. In some cases the classification hinges on a comparison with the previous period, so outcomes may not be ideal but interpreted relative to the outcomes from a previous period. We give details and the connections between each of the elements as we discuss each of the periods in turn.

We begin our analysis of Brazil's move towards an ultimate virtuous path of development with the 1964 military coup. Here we will not to give a detailed account of the history, but analyze each period in light of our framework and to show the forces leading to change. In order to do so we need to establish: What were the windows of opportunity? Who were the leaders during the transitions? Who held power? And, what beliefs prevailed?

We will not enter into the pre-1964 period except to note that the coup came about due to the dissatisfaction with both the economic and political outcomes. Recurring periods of high inflation and low growth mired in populism and political volatility set the stage for the overthrow of democracy with significant approval, or at least a lack of resistance, by most of the elites and the population in general (Bresser Pereira, 1994: 193; McDonough, 1981b; Von Mettenheim, 1990; Skidmore, 2003: 244). McDonough (1981a) underscores how the failed policies of the past shaped the perceptions of the actors in the subsequent period:

> Among Brazilian elites, the judgment that a trade-off must occur in favor of economic over social development derives not only from academic principle or from the casual observation that resources are limited and the time to catch up is short but also from their recollections of the populist era immediately preceding the 1964 coup. However short-lived, the experience of double-digit inflation and of stagnation in real growth during the last year of democratic rule left many of the elites with a deep skepticism about the feasibility of equitable development. (McDonough, 1981a: 537)

Similarly, on the political side McDonough (1982: 90) traces the lack of enthusiasm in defending democracy after the coup to "bitter recollections of the electoral frauds - the double voting and voting by citizens long buried - practiced by local bosses in pre-authoritarian days." But who were the elites that emerged in the early military period? Identifying those in power is not always an easy task as it involves disaggregating 'the elites' into separate groups that have distinct sources of power as well as distinct objectives. These distinctions can arise from *de jure* versus *de facto* sources of power, as in Acemoglu and Robinson (2006), or can be thought of as differences between political versus economic elites. In any case, given its authoritarian nature, identifying the elites during the military period in Brazil is not terribly controversial.

The authoritarian period consisted of two sub-periods, with a clear inflection in the direction of economic growth and the subsequent political support for the regime after 1974. In both sub-periods political power was clearly in the hands of the military as well as the technocrats to whom they delegated the running of the governmental machine. As for the economic elites, for the early sub-period Frieden (1987: 100), identifies the following 'new growth coalition':

> A powerful grouping of economic actors was especially important to national development after 1964. The domestic banking system grew institutionally and financially stronger. The state firms expanded continually, bringing along with them networks of suppliers, especially in the capital goods industries, where the parastatals accounted for two-thirds to three-quarters of domestic orders. The multinationals, which dominated the consumer durables sector, had the opportunity to tap a rapidly growing national market of middle-class consumers, many of whose purchases were financed by the vibrant financial system. (Frieden, 1987: 100)

Who was left out of the elite, besides the masses? According to McDonough (1981: ???) "… many formerly well-entrenched groups were also marginalized: politicians as a class, labor leaders, many intellectuals, some members of the business community and, gradually, the church."

But what were the beliefs of the new groups with power? It is axiomatic that each group prefers policies that promote their own welfare but under the shadow of what belief? Beyond that consideration we can identify different prescriptions for how the country should be organized. McDonough (1981a) conducted 250 interviews in Brazil in 1972 and 1973, the height of the 'Brazilian miracle,' in a study of the elites. He identified three broad trends. The first is preference for prioritizing quick economic growth above all other goals, epitomized in the saying that first you should make the pie grow so that you can divide it later. The second priority preferential goal was the establishment of democratic values that promote inclusion and participation of all members of society. The third preference as stated by the interviewees was to reduce poverty, inequality and other social ills. By far and away the dominant view was clear according to McDonough (1981a: 542): "Most Brazilian elites rank national priorities along a hierarchy of needs, the foundation of which is the nation's economic might, with the luxury of politics in last place."

Although the views in the previous paragraph sound like beliefs they are preferences as they refer to how the agents would like the country to be if it were in their power to make it happen. Our conception of beliefs refers instead to the perceptions of organizations about how things actually work, given the configuration of power in place. As indicated in Figure 6, the key belief we identify for the authoritarian period is based on the notion of 'developmentalism'.

'Developmentalism prioritizes fast industrial growth through state-led investment in large infrastructure projects and protection of selected private industries. It includes heavy doses of nationalism and the quest for national champions. As a belief, 'developmentalism' was the recognition that given the military regime's hegemonic power and their preference for strong and orderly economic growth, policy would necessarily pursue those objectives whatever the costs in terms of other goals such as equity, democracy, justice, and environment. The belief in developmentalism grew initially over time and then declined in its latter years. Austerity and restrictive measures to combat inflation marked the first three years of the period. In the subsequent years, peaking in 1974 and then only gradually declining, the belief in developmentalism was at its height, underlying and being confirmed by what became known as the 'Brazilian miracle':

> From 1967 until 1980, the growth coalition succeeded extraordinarily well in utilizing previously installed productive capacity, a reorganized financial system, and foreign finance to obtain impressive rates of industrial growth. The booming international trading and financial systems helped accelerate the economy's upward trend, and it was not difficult to maintain a level of political agreement among major economic interests so long as the world and local economies were growing. (Frieden, 1987: 100)

In the period 1964 to 1974, inflation averaged 24% per annum and yearly real GDP growth averaged almost 9%. This contrasts with the previous period (1960-1964) where the averages were, respectively, 60% and 5.7%.[46] These positive economic outcomes brought about relative prosperity to many, and thus approval or at least acquiescence of the regime's performance (Frieden, 1987: 101). Yet on the political margin the level of dissatisfaction gradually increased, especially after the hardening of the regime in 1968. The sentiment against the military started with those former powerful members that found themselves excluded but progressively spread as repression, torture and censorship became increasingly routine. Although it is generally accepted that the level of repression in Brazil was milder than in most other Latin American military dictatorships, it came to have an extremely profound impact on the country's beliefs. Skidmore (2003: 246-247) stresses the subtle way in which the perception by many in the elite changed regarding the legitimacy of strong-handed methods to maintain

[46] The GDP differences become even starker if one considers only the years after 1967.

order and pursue the policies that so benefited that same elite. The military regime's methods of social control disturbed not only the Church, lawyers and intellectuals but, according to Skidmore (2003: 247), even factions within the military evinced dissension.

While the economic performance continued to improve, dissatisfaction with repression was only enough to induce very subdued pressure for change. In 1974 the regime announced a 'slow and gradual' process of opening whereby command of the country would be returned to civilians in a controlled and orderly manner, maintaining the rights and prerogatives of the current political elites. However as the economic situation took a downturn with the economic crises of the late seventies and early eighties this orderly process became increasingly hard to control. In our framework we stress the role of endogenous and exogenous events in producing pressure for change through their impact on outcomes. The deterioration of the economy in this period was a result of such interplay, with external factors (oil prices) triggering and amplifying the internal dysfunctionalities of the economy. With the now negative economic outcomes adding to the already negative political outcomes the pressure for change increased. Frieden (1987) describes how the magnitude of discontentment destroyed any hope the regime had of closely dictating the nature and pace of the process of redemocratization:

> By 1981 the cycle had ended. Foreign finance, parastatal orders, and domestic finance all dried up. The "miracle" was definitely over, and its end spelled the collapse of the coalition of economic interests that it had supported. … (T)he Brazilian economy began a downward spiral that drove increasingly influential social groups into opposition and culminated in a new civilian opposition government assuming power in March 1985. … By 1982 business discontent with the regime was widespread; by 1984 it was nearly universal. The regime had lost most of its popular and elite support. (Frieden, 1987: 115-116)

In light of our framework, the transition to civilian rule in 1985 was a window of opportunity with new leadership, new elites in the power structure and a new set of prevailing beliefs. In this case the window of opportunity took place over an extended period of time and there was no single 'big bang' event as in the 'revolutionary' transition of 1964. The framework does not assume that all shifts in 'status quo' take the same general form; on the contrary, each case will have its own specificities. Importantly the window of opportunity brings with it new configurations of power, and beliefs.

The elites which came to power with democratization were led by the nation's modern industrial sector which had precipitated the fall of the previous regime as it abandoned the ruling military coalition. They included industrial workers and the urban middle classes, including technicians, bureaucrats and intellectuals. According to Frieden (1987: 121) "… in the simplest terms, the national industrial bourgeoisie had both come of age and come to power." Domestic bankers had been among the last to abandon the previous regime and only gradually transitioned to the new coalition. Politically the opposition candidates who had been elected as governors in the 1982 election became particularly powerful, especially those of the industrial southeast, as the vote legitimized their position *vis-à-vis* the indirect route to power by President Sarney.

What were the beliefs of this new and expanded coalition? Politically, the new coalition rejected the exclusionary practice of the previous regime. The long experience without voice or vote, subject to repression, censorship and torture, led to a strong reaction against those practices and instilled high regard for democratic values of participation and citizenship, that quickly overturned any attempt to limit the pace and scope of the opening. Rochon and Mitchell (1989: 318) note that although the Brazilian middle class had historically supported an elite-centered democracy instead of one based on mass participation:

> … as the transition to a civilian government unfolded it proved impossible to maintain the carefully circumscribed electoral democracy envisioned by the outgoing authoritarian rulers. Within months after the inauguration of President José Sarney, the government enfranchised illiterates (25 percent of the population) and ended campaign restrictions, the ban on cooperation between parties, and the prohibition of split ticket voting. The Sarney administration also made plans for the first direct presidential elections. Both the partisans of civilian control and the partisans of mass democracy, both the democratic legalists and the populists got what they wanted. (Rochon and Mitchell, 1989: 318)

Economically the preferences that prevailed were centered on anti-austerity measures that moved radically away from the financial conservatism of the last years of the previous regime. The hardships of the previous crisis and resentment against foreign indebtedness instilled preferences for growth-oriented policies, strong industrial growth and abhorrence to foreign dependence.

Out of these preferences and the new structure of power emerged the first of two beliefs that played a crucial role in setting Brazil on its current path. The essence of this belief is that inclusion, participation, citizenship and equality should permeate the behavior of governments, firms and individuals.[47] Remnants from the authoritarian past such as censorship, top down decision-making and lack of accountability and transparency would not be tolerated. We call this a belief in 'social inclusion.' It does not mean that from one moment to the other there was equal access to political and economic resources to all and that social justice would always prevail, but rather that there came to rule a presumption that behavior and policies would, if not actually progress towards these values, at least not explicitly contradict them. Often times this belief would be counterproductive, other times innocuous as it would simply affect the packaging and not the content. Nevertheless we argue that the existence of this lens through which those in power perceived the world did and still does have profound impacts in the path Brazil has followed.

An anecdotal indication of this belief is the way in which after 1985 practically no politician admits to being on the political right, opting instead for terms such as 'center'. According to Powers (2000: 206-207) this phenomenon of an 'abashed right' could be seen in the way "conservative public figures were continually uncomfortable, apologetic, and generally squirming in the presence of journalists and intellectuals."

Two other early manifestations of the belief in social inclusion was the extraordinary rise in social movements and the surprisingly powerful role assumed by the *Ministério Público* as a truly independent and effective defender of the diffuse and collective interest against government ineffectiveness and incompetence. Similarly the proliferation of councils as a means of policy-making in the most diverse areas, from education to health, from river basins to the environment, at municipal, state and federal level, are all expression of the social inclusion belief.

We have not made any claims about the desirability or the nature of the impact of the mode of governance that emerged under this belief. We will elaborate on the consequences of

[47] Many on the left including the intellectual elites and the union leadership always held this belief but these groups never had power. Now the belief became shared by the business elites.

the belief in social inclusion below. For now we simply provide a clear notion of what the belief encompasses to convince the reader of its importance. Land reform is an area in which the belief in social inclusion is particularly evident. Land reform played a key symbolic role in both the 1964 and the 1985 transitions. Rural unrest, land invasions and the growing demand for land reform were one of the major issues that prompted the military coup in 1964. Ironically the military regime nevertheless actively pursued a redistributive land reform as it recognized the need for a modern agricultural sector as a crucial input in their quest for economic might. Similarly, in 1985 one of the flagship policies of the new civilian government, and a regular staple in the new democratic discourse, was the realization of a massive and widespread land reform. It seems contradictory that a new government that was intent on severing any resemblance to the previous regime would put such emphasis on a policy that had previously been championed by its predecessor. The explanation of this paradox is in the beliefs that justified the policy in each period. Whereas the early land reform effort was sanctioned by the belief of developmentalism, in the New Republic it was advanced as a case of social justice.

The clearest manifestations of the belief in social inclusion is the 1988 Constitution, as Constitutions by definition are places where powerful groups delineate guiding principles, general rules and the accepted outlook on how things should be setup and operated.[48] The fundamental spirit of the new Constitution was exactly to make a break with the past, abandoning the development-at-any-cost nature of the previous regime and embracing values of equality, social justice, human rights, inclusiveness, citizenship, and participation. These values not only oriented the content and tone of much of the text, but several were explicitly highlighted as fundamental principles. Article 1 establishes at the outset 'citizenship,' 'dignity to the human person,' and 'political pluralism' as fundamental principles. Article 3 proclaims it a fundamental objective, among others, to 'build a society that is free, just and has solidarity.' Similarly, Title 5 of the Constitution, dedicated to Fundamental Rights and Guarantees has 78 items, assuring things such as the 'inviolability of the right to life, liberty, equality, security and prosperity (Article 5). Clearly much of this is the regular window dressing that tends to ornate

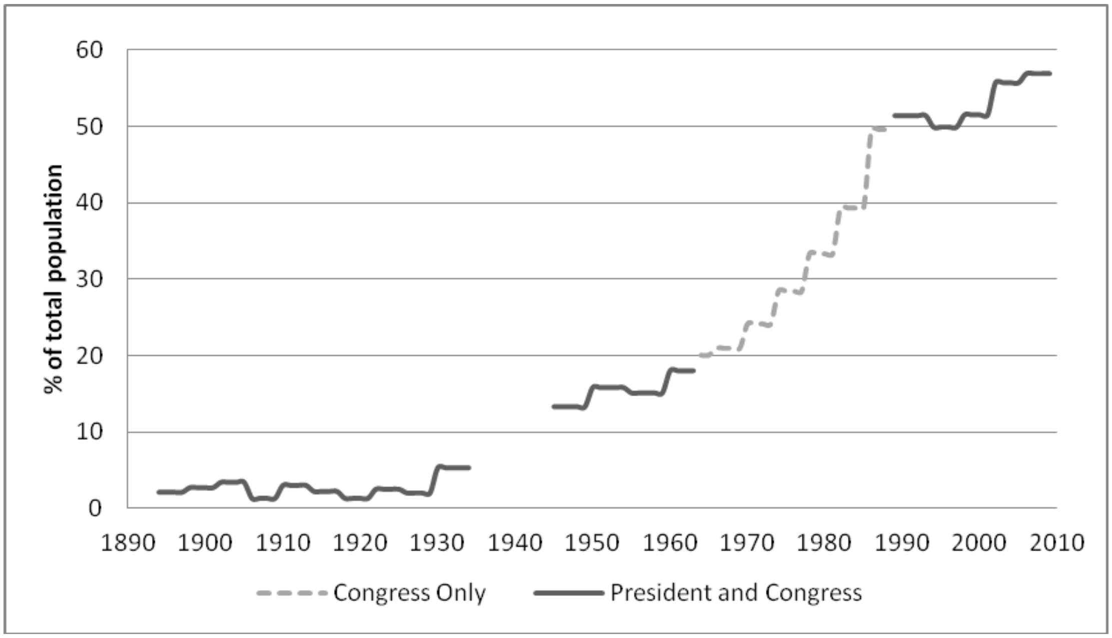
[48] Here we refer to "true" constitutions rather than the numerous sham constitutions that are window dressing but are not statements of guiding beliefs.

many Constitutions throughout the world, and certainly many articles privileging specific groups at the expense of the collective found its way into the 1988 Constitution, given the way it was drafted by the elected members of Congress. Nevertheless this inclination of the Constitution has not been innocuous, as its content has frequently been exploited by politicians, parties, social movements, judges, district attorneys and even individuals to significantly affect governmental policies and decisions. This has become increasingly the case in Brazil given the independence of the judiciary and the extreme 'constitutionalization' that has evolved in Brazilian Law.[49] The fact that the judiciary has become a major locus of policymaking in Brazil implies that the social inclusion bent of the Constitution does in fact have palpable consequences.

A key change that was squarely compatible with the new belief and that would corroborate the above mentioned impact of the new Constitution was the extension of the franchise that took place with re-democratization. Figure 7 shows the evolution of the proportion of total population that effectively voted for President and Congress from 1894 to 2006. Only in 1985 did Brazil authorize the right to vote to illiterates, so the first time that a majority of the Brazilian population voted for President occurred in the 1989 election. The previous presidential election had been almost 30 years earlier and less than 20% of the population voted in that election.

[49] Increasingly over time Brazil tied the hands of politicians by making a 'law,' a constitutional amendment. In addition after the Constitution many parts had to be excised as constraining the ability of the government to meet its fiscal target.

Figure 7 – Percent of total population that voted for President and Congress, 1894 – 2006



Source: Nicolau (2003) and Tribunal Superior Eleitoral for the elections of 2002 and 2006. The data is for the total number of voters that actually voted and not the number eligible to vote. Data for Congressional elections is for the period after 1933 and is very close but not identical to that for Presidential elections.

Although Congressional elections took place during the 1964-1985 period, these were clearly of a less significant nature. This implies that the political scenario initiated in the 1990s was remarkably different than anything that the country had ever experienced. The incentives of politicians were thus of a very different nature than those of previous periods. This is particularly true and relevant for the case of the President given the strong presidentialism that prevailed after the 1988 Constitution.[50]

More than in any other time in Brazilian history there were strong electoral incentives for policy to pursue the public good rather than private interests. This effect has probably grown over time becoming stronger in each subsequent election as voters and politicians have come to understand and believe in the new rules of the game. Similarly, candidates in electoral races are clearly shedding bad electoral practices which were the norm in the past, such as

[50] Brazil authorized very strong powers to the executive branch relative to most Presidential systems. The executive in Chile has similarly very strong powers of agenda control.

clientelism, vote buying and the use of public office by incumbents in the electoral race.[51] The inception of greater political openness, equality and inclusiveness changed the negative approval along the political dimension which had prevailed throughout the authoritarian period.

Along the economic dimension, however, dissatisfaction was not eliminated. Although the new civilian government radically altered fundamental economic policies, economic outcomes deteriorated. In Figure 8 we show that average yearly inflation increased from 98% in 1974-1985 to over 1000% in the 1985-1994 period.

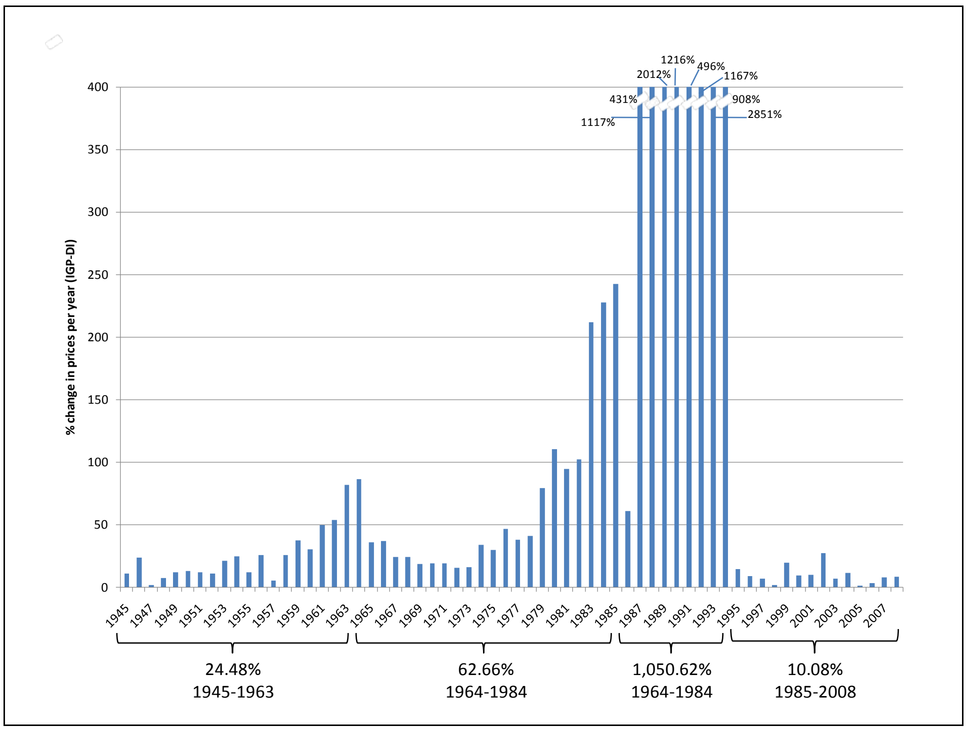
Over the same period, GDP growth fell from 4% to 2.8%. The new levels of inflation are so high that they could not be shown proportionally in Figure 8. In order to provide more detail, Figure 8 shows the yearly inflation levels from 1945 to 2007, yet even here it was not possible to fit the 1985-1994 period in the graph at actual scale without making the other years indiscernible to the eye. This was not simply another bout of high inflation that had been recurrent in Brazilian history. This was in fact a Weimar Germany-style hyperinflation with all the associated pain and disruptiveness.

The adoption of new economic measures caused the hyper-inflation bouts. The belief in social inclusion that undergirded the choice of policies was a natural reaction by the new coalition seeking to redress what it saw as the errors and injustices of the previous government. This belief led to a strong presumption that policy would thereafter be inclusive and promote social justice. The 1988 Constitution epitomized this process not only in terms of political rights, as noted above, but also by distributing economic benefits to large arrays of the population. An example of this is the extension of social security and pensions to non-contributing rural workers. This has had an important redistributive effect but at the same time added

[51] Today elections in Brazil are widely recognized as fair and well run, with a competent Electoral Tribunal in charge and, since 2000, 100% computerized voting which increases the speed of the process and reduces the possibility of fraud (Kinzo, 2004; Sadek, 1995). The fact that the Electoral Tribunal has removed from office since 2000 more than 460 mayors and vice-mayors and 5 governors shows that there are still abuses of electoral practice. More importantly, it shows that contrary to previous periods in Brazilian history effective enforcement mechanisms have started to evolve that dissuade those practices.

considerable pressure to the system's precarious fiscal balance. Other examples include the universal education and health benefits, and the guarantee of job stability to civil servants. Together with these social and universalistic transfers in the Constitution, interest groups also managed to embed their own particularistic transfers and so insulate them from future alterations. The result of this unmitigated inclusiveness was naturally a sharp jump in public expenditure.

Figure 8 – Inflation in Brazil 1945 – 2008, % per year

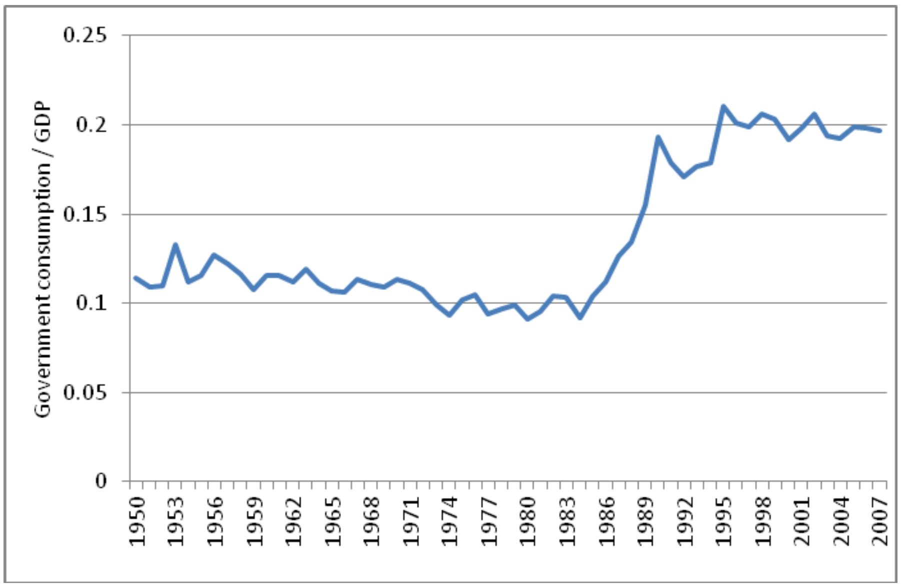


Source: Fundação Getúlio Vargas, IGP-DI

Figure 9 shows the distinct upward shift of government expenditures as a percentage of GDP that resulted from re-democratization and the 1988 Constitution. Clearly this abrupt doubling of government expenditure is causally connected to the surge in inflation that was observed at the same time.

Over the same period, GDP growth fell from 4% to 2.8%. The new levels of inflation are so high that they could not be shown proportionally in Figure 9. In order to provide more detail, Figure 9 shows the yearly inflation levels from 1945 to 2007, yet even here it was not possible to fit the 1985-1994 period in the graph at actual scale without making the other years indiscernible to the eye. This was not simply another bout of high inflation that had been recurrent in Brazilian history. This was in fact a Weimar Germany-style hyperinflation with all the associated pain and disruptiveness.

Figure 9 - Government Expenditure / GDP, 1950 – 2007



Source: Central Bank of Brazil in IPEADATA.

The ten years of hyperinflation that followed re-democratization produced a time of economic distress and uncertainty. Inflation at this level systematically reduces real incomes, drains government effort from other policy domains, and wreaks havoc on any attempt at planning for the future by individuals, firms and government. It is a tax that falls disproportionately on the poor, quickly wiping out the gains achieved through the new inclusive policies. Even for those who had access to financial instruments that afforded protection from rising price levels, unanticipated inflation posed substantial transaction costs and uncertainty.

When salaries have to be corrected almost monthly to keep their value, labor relations become strained and strikes endemic. Similarly, when delaying a payment by even one day can yield a significant gain in the overnight market and at the same time a significant loss to the creditor as prices will rise in the meantime, the probability of conflict and litigation over contracts increased greatly. These ten years witnessed several economic plans devised to end inflation. In the few cases where the plans managed to stem the rise in prices, the effect was fragile and temporary, eventually reverting to even greater inflation. Repeated failures undermined the hope that stabilization was possible. To many it came to seem that inflation, with the accompanying pain and disruption, had become an inherent and unavoidable characteristic of Brazilian life.

By the early 1990s the situation was arguably becoming set for some sort of coup, as public opinion became increasingly disillusioned with the merits of the new institutional arrangements. Instead, what took place was the *Plano Real* in 1994 and the sudden demise of inflation. How this window of opportunity arose, why it was successful and what resulted will be analyzed below. First we need to describe the second belief that we contend has been crucial in the recent transformation in Brazil. At the heart of the belief is the notion that inflation is perverse, impending and to be avoided at all costs.[52] The 'fear of inflation' is still very strong today and underlies the entire policymaking process constraining choices and actions. The collective strife of the hyperinflationary decade created an implicit understanding of the kind of policy that translates into inflation and a tacit consensus that such behavior must be curtailed. This does not mean that the 'fear of inflation' eliminated political opportunism or the pressure for redistribution by various interest groups. It does mean that there were now countervailing forces to those natural instincts. When voters instinctively understand the link between the price level and fiscal and monetary discipline, politicians, and in particular the President, have greater incentives to pursue better macro-economic policies. In this sense the combination of increased franchise and the inflation-aversion belief had an important impact having set the tone of all presidential administrations, independent of party affiliation, establishing a clear precedence of fiscal and monetary discipline over other demands.

In many instances the social inclusion belief and the inflation-aversion belief are in direct opposition to each other. In such cases which one prevails? When Lula came to office in 2003 his flagship project was the Zero Hunger Program, which had the noble goal of eliminating

[52] Germany today still holds this belief.

hunger and sub-nutrition throughout the country. Although the program proved to be popular from the outset, with individuals, firms and celebrities vowing to help, it was eventually sidelined and ostracized by the President himself, who quickly perceived the greater importance of consolidating and maintaining monetary stability and fiscal discipline. As with this example most policy choices since 1994 have shown that the 'fear of inflation' belief takes precedence over the social inclusion belief. This does not mean that inclusiveness and citizenship are no longer important policy objectives, but rather that they depend lexographically on monetary stability before they can be directly pursued. With inflation in check both Presidents Cardoso and Lula pursued policies of greater social inclusion. With increased economic growth, Lula could expand social inclusive policies to a greater extent than Cardoso and in turn deepen beliefs in fiscally sustainable social inclusion

Brazil tackled inflation with the *Plano Real* in 1994 which we see as a window of opportunity. Here the interest is to continue the analysis of Brazilian development through the lens of our framework. The period after 1994 can be seen as a one with a new set of beliefs, which succeeded the set of prior set of beliefs, unsustainably anchored on solely social inclusion. As we have seen, the previous situation had led to substantial political openness but displayed the poorest economic performance in several decades, with average GDP growth of only 2.8% and quadruple digit inflation. As a result, there was widespread dissatisfaction and pressure for change. The success of the *Plano Real* resulted in both positive political and economic outcomes, the first time we see such a result in our period of Brazilian history starting in 1964. Average inflation fell by two orders of magnitude and GDP started to grow at a moderately higher pace with significantly less variation and uncertainty.[53]

The post 1994 'status quo' dynamic has lead the country along a virtuous path of development in which both political and economic competition and openness have taken root and evolved. Policymakers significantly extended the rule of law to greater portions of the population and political and economic institutions have gradually evolved to increasingly

[53] The standard deviation of GDP growth from 1985 to 1994 was 3.82 while the figure for 1995-2008 was 1.95. Whereas Brazil exhibited slower growth than many other countries in the same period, such as Argentina, the process proved to be more sustainable over the long run.

sustain impersonal economic and political exchange. The implication is that this new 'status quo' set of beliefs will continue to lead to greater institutional strengthening and economic growth. Because both the economic and political dimensions have reached stable positive outcomes, positive feedback will tend to reinforce the beliefs in place though there is always the possibility that a big enough exogenous shock can knock the country off that path.

This is not a trivial claim. It goes against much of the received wisdom that highlights the deep structural, social and cultural problems inherited from the past and sees the recent changes stressed above as merely superficial and not addressing the deep-rooted causes, such as inequality, corruption, and a flawed political system. The claim also flies in the face of most Brazilians, who in our experience often counter it with a list of the recent scandals, negative statistics and examples of the daily absurdity from the morning paper; "How can you make this claim, the reasoning goes, in a country where such things can happen?" We will not attempt to defend our claim in this section.. Given that this is an issue where there is no 'smoking gun', the verdict must be reached through a preponderance of circumstantial evidence.

The purpose here is to understand the process that led to the transition from the previous configuration of power and beliefs to the new set of power and beliefs. If we are correct that this transition has led the country to a virtuous path of development, then it is important to understand how and why this has happened as it is clearly an exceptional achievement in the modern world and, in the light of only a few years ago, in the most unlikely of countries. The idea is not that the process can be replicated directly elsewhere, but rather to understand the more basic elements that operate in the developmental process. In particular we stress the roles of windows of opportunity; leadership; and beliefs.

To understand the shift in power and beliefs that took place in the mid-1990s it is important not to be fooled by the benefit of hindsight into perceiving as inevitable the changes that ended inflation and started reforming the country's institutions. By the time of the *Plano Real* the country had been mired in hyperinflation for nearly a decade and a large number of explicit economic plans and other assorted policies had been tried, yielding only temporary reprieve and collapsing back to what increasingly seemed an inescapable order. Given the cumulative experience of previous failures each new attempt at dealing with inflation and associated macroeconomic problems elicited less and less hope of success. In contrast to the public elation generated by the first few months of the *Plano Cruzado* in 1986, the public greeted the *Plano Real* with resignation and skepticism.

The protracted cost of inflation on firms and individuals made the likelihood of some form of political upheaval ever more likely: if this was what democracy had to offer, then many might be less resistant to some other form of government that might offer less suffering and hopelessness. Although this could come about through a military coup, given the social inclusion belief and the experience of other Latin American countries in the same period, it could also come about in the form of a Chavez-like government in Venezuela. Alternatively the series of stabilization plans could have continued indefinitely and even have been successful, following the general trend in Latin America, yet without initiating a process of deeper institutional change. The question is then: why did the *Plano Real* succeed and why did institutional deepening transpire in its wake? Once again, in this overview, we want to answer this question not in its specific details, but more generally in the light of our framework. As discussed earlier, the *Plano Real* is interpreted as a window of opportunity in which a jump was made to a new configuration of power with new beliefs. Because the change took place when it did, it may seem with hindsight to have been obvious or preordained. This is because we are most aware of successful policies during a window of opportunity. Many other windows of opportunity that open are not perceived or realized and therefore leave no legacy. In this sense windows of opportunity have a strong element of serendipity in that they are unpredictable and unexpected. This does not mean that they are simply happenstance. Although windows of opportunity come about unplanned and often by surprise, they require that someone be able to recognize and act upon the opportunity. This is why leadership is so important. A leader must: recognize the window of opportunity; know what to do; and either persuade or coordinate others into going along with the new belief, awaiting outcomes that will deepen or truncate the new belief.

It is quite possible that other events prior to the *Plano Real* had presented windows of opportunity for change, such as the Constitution of 1988 and its failed revision of 1993, or the impeachment of Collor in 1992, or even some other instance of which history books are now unaware. During those periods the dissatisfaction with the economy was sufficiently large to generate a demand for change. Yet it was only with the *Plano Real* that the shift to a new set of beliefs took hold.. Several key elements contributed to allow such a shift. The first was the fact that the prolonged hardships of life under hyperinflation made society more willing to accept sacrifices that held the promise to lead to a solution to those problems, though as noted before past failures made each new attempt seem increasingly futile. In 1990 the Collor Plan revealed this willingness to sacrifice when the government announced a surprise freeze for 18 months of all but a small margin of the populations' bank deposits and savings accounts. This is a measure that in other circumstances might lead to despair or rebellion. Yet, in a situation of 80% inflation per month, the population accepted the Collor Plan with passive resignation. The second contributing element was the lack of a coherent game plan by the opposition, due to scandals and other political events that we detail elsewhere. In addition, the cumulative experience with failed plans as well as lessons from other countries that were undergoing similar problems had increased the knowledge of the kinds of policies that work and especially the kind of policies to avoid.

Yet even with all these elements in place there was nothing inevitable about the way things turned out. Realizing that the elements were there, and could be exploited in a very precise way to reach an envisioned outcome required leadership in the form of an individual or a group that was serendipitously at the right place at the right time with the right powers so as to coordinate the necessary actions. Despite the facilitating circumstances noted above, change of this magnitude requires persuasion and strategy to overcome disperse and specific resistance, actions which were all the more difficult in Brazil given the limits imposed by the social inclusion belief.

We view the leadership roles played by Fernando Henrique Cardoso as an essential element in the shift to a new set of beliefs that resulted in the end of inflation and the start of a long period of reform that dramatically changed the nature of the Brazilian economy, polity and society. Cardoso's role started as finance minister with the coordination of the team that devised and implemented the *Plano Real* in 1994, so as to realize the window of opportunity that had presented itself. More importantly, Cardoso's leadership continued with the capitalization of the popularity that arose from the success of the plan. Following stabilization Cardoso initiated a process of long term structural reform that not only modernized and liberalized the economy in many important ways, but more importantly established political institutions that locked-in and reinforced that direction of change by affecting the constraints and incentives of individuals, organizations and especially politicians. The institutions created an evolving set of property rights, checks & balances, and rule of law that we see as the foundation of the virtuous developmental path that Brazil has since pursued.

Many alternative coalitions could have emerged. Actors faced high uncertainty and looked backwards in a problem solving fashion. There were upfront costs and coordination problems that required Cardoso's leadership due to the high uncertainty. Crucial for the success of Cardoso's strategy was that the new economic actors developed a stake in the reform process and formed a constituency which did not exist before: firms redeployed their assets in new profitable ways. In addition, citizens as consumers updated their beliefs in the benefits of liberalization and price stability. Citizens´aversion to inflation and economic elites´ failure fatigue following six failed economic stabilization programs set the stage for the exercise of leadership.

A number of factors helped making the reforms of Cardoso credible, particularly the *Real* Plan. They included a number of contextual factors – Itamar Franco´s weakness as president, a national front government in the wake of the impeachment of President Collor, a congress in crisis because its leadership was implicated in a corruption scandal - and in particular the approval of the constitutional amendment allowing the reelection of presidents. A stronger president rather than a lame duck was able to engage in necessary amendments to the Constitution in order to sustain a fiscal balance. The second term of Cardoso articulated a pattern of coalition management and a host of compensatory measures that did not compromise the overarching lexicographic goals of maintaining the stability of the currency and fiscal stability.

With institutional deepening during Cardoso's second term, the role of leadership took a quantitative change. Although the decisions of the leader are still important in navigating the country forward, they are nevertheless decisions within the prevailing bands of the new status quo of beliefs; and not decisions that impel a jump to a new set of beliefs. In this sense the leadership of Cardoso lies mainly in the recognition of the latent belief in the priority of macro stabilization and the establishment of an institutional environment where the government pursued all other objectives subject to this preponderant macro stability constraint, as well as the secondary, sometimes conflicting social inclusion constraint. Once society accepted this dynamic path and elected Cardoso to a second term, his leadership role receded to the background. The country was by then on ‘auto-pilot’ in the sense that changes became incremental within the prevailing configuration of power and set of beliefs. The strongest evidence of this interpretation is the unexpected conversion of President Lula to the macro stability constraint and further institutional deepening along the same lines initiated by Cardoso, culminating with Brazil becoming investment grade and poised for higher rates of economic growth and political openness. President Dilma Rousseff’s economic team remains committed to a belief in macro-stability as its top priority: ‘Inflation is my permanent preoccupation” Guido Mantega, Finance Minister of Brazil (Financial Times July 13 2011:8). Since taking office, inflation has remained under control despite an initial upsurge in foreign investment and an increase in the value of the *Real.*

V. Conclusion

Most countries in the world remain on a trajectory of economic and political development where changes are marginal. This explains why so few countries have broken into the world of the high GDP per capita countries whose inhabitants live in a world where economic growth is almost always positive. The reason for only marginal changes is because the returns to those in power are sufficient to sustain them in power. Economic and political power are often goals of those in power. It is not in the interest of those in power to make discontinuous changes; but, once in awhile, a country breaks from its past. The necessary conditions to break from one’s past include a window of opportunity and leadership. Successful leadership towards sustained economic and political openness entails: a leader who wants to make his nation great, i.e., his primary goal is the historical record; a leader who knows what should be done; and a leader who knows how to coordinate activity to achieve his goals, i.e., the art of policymaking.

Knowing what to do entails causal beliefs about how institutions will affect outcomes in ways that will lead to a virtuous path of economic and political development.

During windows of opportunity leaders shape beliefs when their actions achieve results that most citizens perceive as positive. This also enables leaders to engage in institutional deepening which is part and parcel of economic and political development. In the early 1990s Brazil seized a window of opportunity with the leadership of President Cardoso and others in his administration. Over time, beliefs changed about how Brazil functions and subsequent administrations have deepened institutions that created a more open Brazil, both economically and politically. This in turn created a virtuous dynamic because an increasingly large number of players have a stake in the new open system. Will the virtuous dynamic persist? Only history will tell, but for now Brazil has embarked on a trajectory analogous to other nations that have succeeded.

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