From Current-Day Russia to Porfirio's Mexico

James A. Robinson

Good economic institutions promote prosperity. Yet bad institutions can persist because they induce patterns of distribution that benefit certain groups, which accordingly have a vested interest in the status quo. In *Without a Map: Political Tactics and Economic Reform in Russia*, Andrei Shleifer and Daniel Treisman show how politicians in Russia used a specific kind of deal, a mixture of expropriation and co-optation, to destroy these vested interests in the transition to a market economy. In this essay I show that there are close analogies between institutional change in contemporary Russia, and that which occurred in nineteenth-century Latin America, particularly in Mexico during the *Porfiriato*. After developing the analogy I draw some conclusions from the Mexican experience for the long-run implications of Shleifer-Treisman deals. The good news is that sustained economic growth is possible with the institutions that Russia seems to have developed. The bad news is that these may lead to extreme social conflict and ultimately revolution. I argue that there are two mitigating factors in Russia that provide grounds for optimism that revolution may be avoided. First, Russia is a democracy; second, the role of foreign investment is limited.

There is now wide consensus among social scientists that certain types of institutions promote prosperity. Chief among these are secure private property, an independent judiciary and system of contract enforcement, and an uncorrupt and meritocratic government bureaucracy. Nevertheless, other types of institutions can persist because they induce patterns of distribution that benefit certain groups. These groups have a vested interest in the status quo. Yet, since good institutions represent potential Pareto improvements, there ought to be a way around these roadblocks. By definition, if a set of institutions is Pareto inefficient, then there exists another set in which everybody is better off. The problem is how to move to that better set in the presence of imperfect capital markets and transactions costs.

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In *Without a Map: Political Tactics and Economic Reform in Russia*, Andrei Shleifer and Daniel Treisman show how politicians in Russia turned potential into actual Pareto improvements during the transition to a market economy. This involved either expropriating or buying off the vested interests blocking change. Of course groups which were expropriated were not made better off by policy change, but institutional change might still constitute a welfare improvement under a reasonable compensation criterion (see Graaff 1967: 82-90). Contrary to the claims of many commentators on the Russian transition, they argue that the strategies used were the best available given the political constraints, resulting in a set of institutions far superior to those of the status quo. They correctly point out that the correct metric to measure the success of the reforms is not whether or not the first-best set of institutions has been achieved, since this is infeasible. They argue (implicitly) that the Coase Theorem applies when the transactions costs in political markets are taken into account. The book therefore aims to correct the conventional wisdom that the transition in Russia has yet to induce changes that will promote good economic performance. For example, the EBRD (1999: 110) summarize their discussion of privatization in Russia by arguing "the consequences of the privatization strategy adopted in Russia have been highly adverse for the governance of enterprises and the allocation of resources, not least because of the clear failure to breach the political constraints on restructuring and company closures. The regime of the soft budget constraint has commonly been maintained."

Their book is provocative and convincing. Yet, in Shleifer-Treisman's focus on blow-by-blow accounts of deals, and the cut and thrust of compromises, one craves to be able to stand back and ask where the process of deal making is eventually going. As they point out, successful political reform strategies involve improvisation and luck, and "reform is always a complicated, risky process, implemented by flawed human beings in difficult conditions" (Shleifer and Treisman 1999: 177). Worryingly, if such factors are key they may generate a dynamic whose endpoint is highly uncertain. Given the short period of time since the initiation of transition in Russia, it is hard to see what this dynamic is converging to. In this essay I point out that there are some interesting historical analogies to the Russian experience which may help give some perspective on the implications of these specific kinds of Shleifer-Treisman deals.

While the Russian transition is in many ways unique, the government of Russia in the 1990s is not the first to try to radically alter existing social and economic institutions. In fact, history is full of other examples. These experiences can tell us a lot about the long-run implications of Shleifer-Treisman deals, their costs and benefits, and any possible externalities. In this essay I argue that the history of Latin America, and in particular Mexico, is one such source of information. When Latin American countries emerged from the colonial era in the early nineteenth century, they inherited a web of social and economic institutions which are generally thought to have seriously impeded their economic development during colonial times. These institutions persisted into the independence era because they generated rents for certain key groups. Indeed, political competition in nineteenth-century Latin America is portrayed as a battle between those with a vested interest in the persistence of the colonial system, "Conservatives," and those who fought against this, "Liberals" (see, for example, Safford 1978). Institutional changes typically had to wait until the political triumph of the Liberals. Often (for example, in Guatemala in the 1870s) this was achieved militarily and conservative groups were fully expropriated. Sometimes (for example, Colombia after 1849) this was achieved democratically with the Conservatives having more chance of making a comeback (in the Colombian case with the "Restoration" after 1886). However, exactly the type of mix of strategies described in *Without a Map* were often employed. The best example of this is Mexico. In this essay I therefore study the nature of policy reform in nineteenth-century Mexico. I argue that there are very interesting analogies between the way this is portrayed by historians and the way that policy reform in Russia is depicted by Shleifer and Treisman. The analogies suggest several tentative conclusions about the implications of Shleifer-Treisman deals.

The essay proceeds as follows. In the next section I sketch the logic of Shleifer-Treisman deals and how they worked in Russia. This involves specifying who were the agents or groups with a vested interest in inefficient institutions and how they were bought off or expropriated. In the next section I provide an overview of Liberal reforms in nineteenth-century Mexico, focusing on the *Porfiriato*, the period from 1876 to 1910 when Porfirio Díaz ruled. I show that all of the categories that Shleifer-Treisman use in describing the Russian transition have close analogies during this period. Just as Yeltsin and his team of reformers expropriated and bought off certain groups, so did Díaz and his supporters. Moreover, the short-run outcome of this strategy seems remarkably similar. What is interesting in the Mexican case is that we also know what the long-run outcome was. Having established these analogies, the final section then draws some tentative lessons from the comparison.

The Logic of Shleifer-Treisman Deals

Shleifer and Treisman (1999) study three main areas of policy reform in Russia: privatization, macroeconomic stabilization, and tax reform. In each case they outline the existing set of inefficient institutions that emerged from the Soviet era (often significantly altered by Gorbachev) and the different groups, the "stakeholders," which had a vested interest in these institutions. They then outline how the different reform strategies in these three areas can be understood in terms of attempts to either expropriate or buy off these stakeholders. In their words, "to be successful, a [reform] strategy must remove all vetoes over enactment and implementation of reform. There are two ways that a stakeholder can be neutralized. Either he must be *expropriated*...or he must be *coopted*... persuaded not to exercise his power to obstruct" (Shleifer and Treisman 1999: 8). In the Russian case, however, the strategic options were limited by the "virtual impossibility of government imposed expropriation of the anti-reform stakeholders" (Shleifer and Treisman 1999: 9). In the case of privatization and stabilization these strategies succeeded. Soviet industry was transformed from state-owned to privately-owned, and inflation was brought under control. In the third case, tax reform, the adopted strategy failed. Shleifer and Treisman show how this failure can be understood as a misguided strategy which failed to fully take into account the political constraints.

Three main ingredients of their analysis are of immediate interest. First, what were the main institutional changes that needed to be accomplished; second, who were the stakeholders; and third, how were they overcome to create better institutions?

The main institutional changes required were, (1) creating private property rights over assets previously "collectively owned," particularly assets of firms; (2) creating complementary institutions, particularly in the financial sector; (3) creating a legal and regulatory framework for these new structures; and (4) creating a fiscal system to match this new system of property rights, including hard government budget constraints.

The main groups of stakeholders opposing these changes differed according to the issue. The managers and owners of formally state-owned firms had implicit ownership rights in the assets they controlled and often strong political connections. They opposed privatization and hard budget constraints. Also of great importance was the decentralized nature of the Russia political system. Shleifer and Treisman (1999: 135) characterize it (following William Riker) as a "crumbling peripheralized federalism, which the center has kept together mostly through a policy of fiscal appeasement and political accommodation." Regional governments benefited both from inefficient state ownership of industry and the inefficient fiscal system and "during...1990-91, most of the ethnically defined subunits had declared some degree of autonomy, and in 1992-93 challenges to the center's authority spread even to ethnically Russian regions. As the 1990's progressed, regional interests combined with economic interests to provide a powerful challenge to the central government" (Shleifer and Treisman 1999: 178). Strong regional governments therefore opposed privatization and fiscal reforms. Next, financial institutions and banks opposed hard budget constraints since they benefited from federal redistribution. Finally, all owners and operators of firms and financial institutions wanted to manipulate the regulatory environment in their favor, for example by restricting entry and competition.

Thus, to implement institutional changes, all these groups had to be confronted. Given the inability to expropriate stakeholders, reformers had to concentrate on co-option. Stakeholders had to be bought out. Shleifer and Treisman (1999: 9) argue that "transforming stakeholders from opponents to supporters of reforms often requires the creation of rents by the government that these stakeholders can be offered in exchange for their support." Thus, "the government's strategy...was to co-opt a subset of large commercial banks, major energy sector companies, and regional governors, by providing them various rents and benefits in return for their help in isolating and selectively appeasing those who stood to lose from reform" (Shleifer and Treisman 1999: 182). Yet this an improvement on the status quo since, "The task of the reformer in a weak state is to persuade stakeholders to give up socially inefficient ways of receiving rents in exchange for less socially costly payoffs'' (Shleifer and Treisman 1999: 182). In the case of privatization of state assets, this took place in two ways. Insiders with strong de facto property rights were given large blocks of shares at a discount. Second, in the infamous “loans for shares” deal, commercial banks acquired large tranches of shares in key firms (with particularly valuable raw materials and energy interests) at huge discounts. These transfers were part of an attempt to buy out the interests of these banks in a soft government budget constraint. Such outcomes occurred because, “to prevent the Russian privatization program from being completely obstructed by a formidable array of political opponents, the privatizers compromised. They gave up on the hope of creating an optimal allocation of property rights” (Shleifer and Treisman 1999: 33). In addition to this, first-best regulatory goals were sacrificed since an easy way to guarantee stakeholders rents was to block competition. For example, competition in the government bond market was restricted so that authorized dealers could make large non-competitive profits.

Thus successful institutional change necessitated large transfers of assets and rents to stakeholders. Unsurprisingly, these processes have led to rather spectacular increases in inequality in Russia since the late 1980s. As the EBRD (1999: 110) notes, “under the ‘shares-for-loans’ scheme implemented in 1995, many of the key resource based companies fell into the hands of a small group of financiers, the so-called ‘oligarchs.’ This has led to very sharp increases in wealth and income inequality—by 1997 the Gini coefficient for income in Russia is around 0.5, a level comparable with those in Colombia or Malaysia.” Shleifer and Treisman (1999: 140) agree, noting “many of the big banking-and-raw-materials empires...had been helped into existence by the loans-for-shares auctions, which the reformers used to repay their political allies.” In the same report the EBRD gives more detailed information on inequality showing that the income Gini increased from 0.269 in 1990 to 0.483 in 1996 (EBRD 1999: 260). Similarly, they report an increase the percentage of people below the poverty line from 2 percent of the population in 1987-1988 to 50 percent in 1993-1995 (EBRD 1999: 16, Table 1.1.2). At the same time there have been significant rises in infant mortality and declines in life expectancy.

The oligarchs and their large diversified asset holdings which emerged from these processes subsequently became closely connected with the government. For example, Boris Berezovsky and Vladimir Potanin actually became members of the government.

Policy Reform During the *Porfiriato*

When Latin American countries won their independence from the Spanish Empire in the early nineteenth century, they inherited a host of institutions which had been designed by the Spanish to extract resources from the colonies to be transferred to Spain. Discussing the Mexican case, Vernon (1963: 29-30) describes them thus:

> The system of the Spanish Crown...was one of pervasive law and regulation. Economic life was organized by highly detailed and particularistic provisions, aimed at granting and maintaining a complex web of privileges and monopolies. Trade with any country

> other than Spain was illegal. Import and export licenses for trade with Spain could only be obtained through a board, sitting in Seville, controlled by Spanish merchants. Trade inside Mexico was controlled almost as rigorously as foreign trade; local monopolies, trading privileges, and tax exemptions proliferated in every area of the colony. And production was controlled even more than trade. In principle, nothing fabricated in Spain could be produced in Mexico; and what was produced in Mexico was subject to the minutest regulation. This conception of the relation of business to the state still prevailed in the mid-nineteenth century.

These institutions survived the colonial era since, while they were inefficient from a social point of view, they generated rents for an elite group of Mexicans. In fact, one of the driving forces behind Mexican independence (which finally came in 1821) was to preserve these institutions from liberalizing currents spreading from Spain, such as the Cadiz constitution. For example, Coatsworth (1978: 95) notes that

> Mexican independence came through a virtual coup d'état by the colony's Creole elite, carried out largely to separate Mexico from the liberalizing process under way in the Mother country...The principal proponents of these conservative efforts was a limited social group of major landowners and industrialists in the center of the country…who had been the principal beneficiaries in the colony of the crown's interventionism or who, like the large merchant houses of the capital, sought to regain privileges the crown itself had abolished in the reforms of the late Bourbon era.

It is now widely accepted by historians that these institutions are the key reason why Latin American countries experienced relatively poor economic performance in the eighteenth and nineteenth centuries. This is argued in depth by Engerman and Sokoloff (1997); North, Summerhill, and Weingast (1998); and Coatsworth (1999) both generally and for Mexico in particular (1978) (see also Stein and Stein [1970]). Conservative groups attempted to keep these institutions in place and battled against Liberals who opposed them. At some point, which varied in different countries, the Liberals took over and instigated a process of institutional change. As Coatsworth (1999: 39) puts it,

> In the second half of the nineteenth century, virtually every Latin American country carried out a series of similar...reforms that eliminated or substantially reduced the most important of the institutional constraints inherited from the colonial era. In most cases, the process began with the elimination of state monopolies, Church and military *fueros* (exemptions from ordinary civil and criminal jurisdiction) and other privileges, a wide array of domestic taxes and fees, and archaic property rights (entail, ecclesiastical and indigenous mortmain, and slavery), and continued with the privatization of public lands, the enactment of new civil and commercial codes

The Liberal triumph in Mexico came with the military victory of Liberal armies in 1855. The following period brought a new Liberal constitution in 1857. However, this early phase was cut short by the intervention of French armies and the reign of Maximillian from 1862 to 1867. After Maximillian's defeat and execution, Benito Juárez became president in 1867, followed on his death in 1872 by Sebastián Lerdo de Tejada. Porfirio Díaz seized the presidency in 1876 and ruled continuously until 1910, except for the period from 1880 to 1884 when his close associate Manuel González 1880-1884 was president. However, although the Juárez and Lerdo regimes had attempted to alter institutions, little had actually been achieved by 1876 other than the expropriation of Church wealth. Coatsworth (1978: 98) describes the lack of real progress in the following terms:

> despite constitutional provisions that specifically outlawed them, colonial fiscal measures like the internal customs still provided most of the revenue for state and municipal governments. Economic activity of all kinds still required special permits and licenses for which special taxes and fees were charged. Though Church wealth had been expropriated, the corporate holdings of the Indian villages remained unaffected throughout the country...a new superstructure of laws and institutions for a capitalist society had yet to emerge.

Díaz therefore had to embark on the task of moving to a new set of institutions. Shleifer and Treisman argue that understanding why policy reform occurs at a particular moment is a conceptually distinct issue from understanding what constitutes a successful strategy for reform once initiated. Similarly, I focus not on why Díaz wished to reform, but how he did so. In order to do so he was faced with either expropriating or co-opting key agents and groups with a vested interest in the status quo. His strategy of *pan o palo* (bread or the club) mixed both tools. Faced with groups that benefited from inefficient colonial institutions, Díaz had to either persuade them to surrender their rents from these, or simply abolish them and risk the resulting consequences. The two biggest challenges were the privatization of communal and government-owned land and the removal of inefficient colonial institutions. Land privatization was opposed by Indian communities who had access rights to communal land and regional political bosses (*caciques*) who were tremendously powerful due to the weakness of the central state since independence. The *caciques* were also the primary beneficiary of the local regulations, trade restrictions and taxes, such as the *alcabala*, which Díaz wished to abolish. Díaz set about expropriating politically unmobilized groups. The most extreme version of this being the Yaqui Indians from Sonora who, after their land had been expropriated, were sold into slavery to work on the sisal (henequen) plantations of the Yucatan, and inducing the politically powerful to give up their existing rents in exchange for others with less damaging aggregate economic effects.

These strategies have been well documented by historians. Katz (1991: 70) describes how Díaz "carried out a complex policy of concessions and repression," and "with respect to the upper classes, Díaz practiced a policy of divide and rule. He removed from power local caciques...nevertheless, as long as they did not resist him, he allowed the men he removed to keep their property and to expand their economic influence. For many *hacendados*, loss of political power was more than offset by Díaz's policy of selling public lands, which gave them great opportunities for enrichment" (Katz 1991: 66). Similarly, Hansen (1970: 149) argues that Díaz's precept was to "buy off the strong by appealing to their desires for social and economic mobility, whatever the cost. Thus Díaz succeeded in pacifying the emergent mestizo regional and national ...elite." Yet, he then adds, "short-term success bore the seeds of long-term disaster" (Hansen 1970: 152).

Institutional change was accomplished by allowing elites to compensate themselves for their losses by permitting them to expropriate both communal and government land. Land privatization therefore led to large increases in land inequality. Hansen (1970: 25-27) shows that 2 million acres of Indian land was privatized during the *Porfiriato,* and in 1883 Díaz initiated the division of public lands with eventually 27 percent of the total land area of Mexico being distributed. All of this land essentially went to a relatively small group of people. Before the latter half of the nineteenth century when it began to acquire value, much land in Latin America was free or communally owned and not intensively used. Bulmer-Thomas (1994: 93) notes

> the area in private ownership in the 1820's was only a fraction of the area in private ownership in 1914. The increase over nearly a century was enormous and would have provided many opportunities to alter the concentration ratio if the new lands in private ownership had been allocated more equally. The failure owed more to the balance of political power...than to inherited colonial patterns.

Land policy was complemented by a strategy of aggressively encouraging foreign investment, which was particularly important in railways. Vernon (1963: 43) states that "of Mexico's total investment outside agriculture and the handicraft industrial, foreign interests accounted for two thirds." This investment had the effect of increasing the value of land and cementing the interests of the elite in the new set of institutions. For example, Coatsworth (1974) showed how the expropriation of Indian and public lands by local elites was closely correlated with the expansion of the railroad network during the *Porfiriato*.

Even though these changes "required...Díaz to make major concessions" (Haber et al. 1999: 7), they allowed him to push through institutional changes. Apart from the creation of private property rights in land, in 1884 there was a new commercial code which Coatsworth (1978: 99) describes as "the single most important piece of economic legislation since independence." This was followed in 1887 by an important new mining code which allowed private ownership of sub-soil rights, and the first banking codes in 1897 and 1908. Reform of the fiscal system begun in 1881 with reorganization of the treasury, new tax laws, tariff schedules, and public debt reorganization. Vernon (1963: 40) notes that "state and local trade barriers flourished all through Mexico in spite of the 1857 constitution...In 1884 and 1886 Díaz amended Juárez's constitution so that the illegality of these internal restrictions was made clear beyond question...and in 1896 Díaz put his amendments into practical effect." There is also a consensus amongst historians that, as Haber et al. (1999: 16) put it, "Díaz's policies increased the security of property rights in land, encouraging the development of large-scale commercial agriculture.'' The outcome was economic growth. Yet the same authors then note the other side of this phenomenon: "This, however, produced an increasingly vocal peasantry that clamored for the return of lands they considered theirs" (Haber et al. 1999: 16).

This process of reform cemented the economic power of the *caciques* who were able to create large diversified agricultural, banking, and industrial conglomerates, including men such as Luis Terrazas and his son-in-law Enrique Creel in Chihuahua (see Wasserman [1984] for a fascinating study of the Terrazas dynasty and Saragoza [1988] for an equally interesting related study), Ramón Corral and Luis Torres in Sonora, and Francisco González Cosío in Querétaro. These regional bosses became politically tied to the regime with, for example, Enrique Creel becoming foreign minister, and Olegario Molina, the governor of Yucatan, becoming minister of development (Haber et al. 1999: 9).

These outcomes may not have been what many Liberals wanted, nor were they necessarily first-best efficient. While the economy grew, it might have grown faster with a different set of institutions. For example, it may be that smallholder agriculture is more efficient than large-scale production. Similarly, Haber (1989) argues that the highly concentrated nature of banking and industry which developed in this period led to adverse long-run consequences for Mexican development. While attempts were made to create an egalitarian outcome in the redistribution of Church lands and the privatization of Indian and government lands after the Ley Lerdo of 1856 had effectively ended communally held Indian land, in neither case did this work. Katz (1991: 50-1) notes that under Juárez, "the expropriation of church land did not give rise to a class of small farmers...[but] only added to the economic strength and political cohesiveness of an already dominant class of *hacendados*.'' Unfortunately, the type of Homestead Act which was passed in the United States after the Civil War was just not a political equilibrium in late nineteenth-century Mexico. Politically powerful elites had to be given *pan* (bread) to remove their incentive to block change and giving them land was the way this was done. Skewed though it was, the type of growth achieved was the best that could be hoped for given the political constraints.

The same has been argued for the banking regulations. These were essentially written by the bankers themselves, severely restricting entry and creating large rents. For example, the General Banking Act of 1897 effectively guaranteed that each state would have a single bank of issue protected from competition. Yet, Haber et al. (1999: 13) note "while the financial laws were suboptimal in some abstract sense, it is not clear that alternative options (such as some form of free banking) were politically feasible." These banks then became the basis by which the new entrepreneurs lent themselves money and created large diversified business empires (Haber et al. 1999: Ch 4; Maurer 1999). They therefore consolidated the inegalitarian pattern of growth. Indeed, income inequality as well as asset inequality appears to have risen rapidly during the *Porfiriato*. Despite the fact that aggregate income was rising, Hansen (1970: 30) finds that average real wages fell by 25 percent between 1898 and 1910. At the same time infant mortality rose and life expectancy fell.

Comparison and Conclusions

The last two sections showed that there are interesting analogies between the way that Shleifer and Treisman characterize the process and outcome of policy reform in Russia, and the way that historians discuss the politics of institutional change during the *Porfiriato*. I now draw some tentative conclusions from these analogies. Of course no analogy is perfect. Russia and Mexico underwent institutional changes at very different stages of development. Russia had experienced sixty years of state-controlled industrialization, while Mexico was primarily an agrarian pre-industrial society. Thus in Russia the main type of asset over which private property needed to be established was capital, while in Mexico it was land. Similarly, Mexico in the 1870s had suffered from sixty years of political instability, while instead Russia had fought the Second World War and the Cold War. Moreover, the type of inefficient institutions that formed the status quo, the Soviet and Spanish colonial systems, were radically different.

Yet the conceptual problems faced by Yeltsin and Díaz were the same. In both cases the existing institutional structure entailed inefficient communal control of assets and inefficient regulations. Nevertheless, certain key groups of agents benefited from these arrangements and had to be eliminated or appeased. The response in both Russia and Mexico was to combine strategies of expropriation and co-option (*pan o palo*). Although Díaz was certainly able to indulge in more *palo* then Yeltsin, the strategies led to remarkably similar outcomes: large increases in wealth and income inequality and the creation of a class of "oligarchs" with diversified financial and industrial (and in the Mexican case agricultural) interests and considerable political power. In both the Russian and Mexican cases, since many of the groups of "stakeholders" were not mobilized politically they could be expropriated. In Russia this was the majority of citizens with nominal rights to collectively owned assets, and in Mexico it was the Indians who enjoyed access to communal land. In both cases therefore, assets were not distributed evenly to agents who might have been thought to have some right to them, but rather in a highly inegalitarian fashion that reflected the realities of political power as the reforms took place. In Russia the politically powerful beneficiaries were insiders in formally state-run firms and the nascent "oligarchs," while in Mexico they were the regional *caciques*. This was despite the fact that in both cases attempts were made to create more egalitarian distribution of assets, in Russia with "voucher privatization" and in Mexico with attempts by Juárez and Lerdo to promote smallholder agriculture in redistributed land. In both Russia and Mexico these policies took place in the context of Riker's "crumbling peripheralized federalism," a weak central state whose fiscal position was undermined by the very institutional changes it sought to implement.

The experience of Mexico under Díaz brings good and bad news for Russia. The goods news is that, as Shleifer and Treisman argue, sustained economic growth is perfectly consistent with the type of economy which is now emerging in Russia. During the *Porfiriato,* growth in real GDP averaged 3.7 percent—2.7 percent in per-capita terms—which is a very high rate for the nineteenth century and respectable for the twentieth. Moreover, exports rose by over 600 percent in real terms and there were large expansions of industry and commercial agriculture (see Haber, 1989). Given the far greater possibilities for "catch-up growth" in the early twenty-first century, one might conjecture a much higher rate for Russia. Thus the creation of private property, even if in an inegalitarian way, generates incentives for the new asset holders to increase the value of their assets. The bad news is that the *Porfiriato* shows that this type of development can cause explosive social pressures. These ultimately led to revolution after 1910 in Mexico. Stating clearly the view common among historians, Hansen (1970: 136) notes, "the political system as it operated under the Porfirian dictatorship led almost inevitably to the Mexican revolution" (see Knight [1986] for a seminal study of the revolution and its causes).

All scholars agree that a prime cause of the revolution was precisely the dual impact of the strategies of expropriating the politically weak and placating the politically powerful. However, there seem to be at least two ways in which Russia is significantly different from Mexico during the *Porfiriato*, both of which give grounds for optimism. First, Russia is a democracy and has political institutions that can hopefully respond to social pressures created by Shleifer-Treisman deal-making before they reach a critical point. The Porfirian political system was unable to adapt to the forces it had unleashed and was swept away. Second, a key cause of pre-revolutionary tension in Mexico was the important role played by foreign investment and capital in the development of the economy. The accusation of *vende patria* turns out to be a powerfully emotive one in Latin America. As Coatsworth (1978: 100) puts it, "the Revolution of 1910 was produced by the discontent of precisely those elements in Mexican society whose importance in the nation's political and social life would have increased...in the absence of foreign resources." (Vernon [1963: 50] records that by 1910, foreigners owned about a seventh of Mexico's land area.) The influence of foreign capital has been kept deliberately small in the Russian economy for nationalistic reasons, and this may turn out to be an important source of political stability in the future.

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