



Elites, Ideas and the Challenge of the Double Incorporation THE CASE OF COSTA RICA

Securing well-paid formal jobs and providing universal public social services are two of the most significant challenges facing developing countries. Costa Rica is one of few countries to achieve this “double incorporation”, with most advances concentrated between the 1950s and 1980s. In this process, the state played a fundamental role: promoting policies that supported small and medium firms and cooperatives, expanding lending, creating public employment and increasing social spending. These policies were influenced by international ideas adapted to the local context, and driven by an emerging elite of small entrepreneurs and urban professionals who relied on their access to state power to increase their economic opportunities and secure social and political stability.

The successful double incorporation

Improving people’s lives in developing countries requires the simultaneous provision of good jobs, and accessible and high-quality social services. A well-paid job is the best tool to improve household income and reduce poverty. At the same time, people need rights-based entitlements to protect themselves against risks and contingencies. These entitlements should be granted regardless of participation in formal labour markets and be accessible for all.

Costa Rica is one of few developing countries that succeeded in accomplishing this double objective. During the 1960s and 1970s, unemployment mostly remained below 6 per cent, and by the late 1970s only 7 per cent of all jobs were in the informal sector. A growing number of people had free access to health care, education, pensions (either contributory or non-contributory) and affordable services such as water and electricity. In 1980, life expectancy at birth was almost 73 years, higher than in the United States and other developed countries.

Despite the challenges faced since the early 1980s, Costa Rica still has a larger share of formal employment and better universal public social services than many other developing countries. During the last half-century other countries and regions have succeeded in promoting good jobs (East Asia) or delivering social services (Kerala, India) but have seldom combined the two.

Meanwhile, most Latin American countries have suffered from high levels of informality and unequal provision of social services.

How Costa Rica secured the double incorporation

The prominent state role in market incorporation

The Costa Rican state played a fundamental role in the process of market incorporation. By allocating credit to specific sectors and companies, the government promoted the creation of good jobs in the private sector. Engines of employment were, first, an upgraded coffee sector and, later, manufacturing. Cooperatives and small- and medium-size firms provided a large share of these jobs.

The public sector became one of the largest employers nationwide as civil servants tripled their participation in the economically active population from 6 per cent in 1950 to 18 per cent in 1980. Employment in the central government and para-state agencies in charge of health care, telecommunications and utilities was a major driver of Costa Rica’s successful market incorporation. Public jobs were stable and, for many occupations, provided higher wages than the private sector. Between the early 1950s and early 1970s, these jobs were funded through steady increases in payroll taxes and service fees. However, by the late 1970s, the government increasingly resorted to debt.



In Costa Rica, social insurance, social assistance and basic social services are closely interconnected through both financing and distribution.

The state as a driver of social incorporation

The role of the state in securing social incorporation was even more impressive. The country's universal social policy regime was implemented in three different stages. In the 1940s, Costa Rica launched a unified social insurance system built from low-income groups upward. Social protection targeted the working class first, slowly extending coverage by successive increases in wage ceilings. During the 1950s and 1960s, social services and programmes were gradually expanded, including health care, pensions and education at all levels. The system was completed during the 1970s with the creation of preventive and primary health care measures.

The government also established an innovative social development fund, which provided resources for nutrition and education programmes. These programmes were designed as affirmative action measures for the poor to access universal services. For example, new nutrition plans contributed to school attendance, and medical check-ups facilitated access to specialized hospital services. Such programmes were implemented by the sectoral

Poverty Reduction and Policy Regimes: The Case of Costa Rica

This case study was part of the UNRISD project, Poverty Reduction and Policy Regimes (2007-2010), which studied the causes, dimensions and dynamics of poverty. Focusing on the institutions, policies and politics that made some countries more successful than others in reducing poverty and inequality, the project laid the foundations for the 2010 UNRISD flagship report, *Combating and Inequality: Structural Change, Social Policy and Politics*.

The Costa Rica study introduces the concepts of market incorporation and social incorporation (Martínez Franzoni and Sánchez-Ancochea 2012).

- Market incorporation refers to people's participation in the cash nexus through formal labour market participation.
- Social incorporation refers to people securing their well-being independently of formal market participation and wage income, for example through social assistance or other benefits and services provided by the state.

Market and social incorporation are analytically independent processes that need not take place simultaneously; in fact, many countries may be more advanced in one area but less so in the other.

To explore the determinants of market and social incorporation, the Costa Rica study considered, first, the set of economic and social policies that delivered positive outcomes. It then explored the political factors behind those policies, showing how dominant explanations based on democracy and state capacity are insufficient, and identifying alternative political economy drivers.

agencies and ministries rather than managed by a bureaucracy devoted to the poor alone. During the 1970s, Costa Rica also created non-contributory pensions financed with social security contributions.

The challenge of the double incorporation since the 1980s

Since the 1980s, Costa Rica's performance has been more contradictory in terms of market and social incorporation. Successive governments combined market-friendly policies of external liberalization and domestic deregulation with state-led industrial policies, particularly through the promotion of non-traditional agricultural exports and fiscal incentives for foreign investors. As a result, the country created new areas of comparative advantage in dynamic sectors like semiconductors. At the same time, small and medium firms and cooperatives suffered from the withdrawal of state support, and public employment creation stagnated. The labour market became more polarized, with a relatively small number of new well-paid jobs linked to the most dynamic sectors and a rapid expansion of informality.

Changes in social policy were less significant: a funded pillar was added to the public pay-as-you-go financed pension system. These pension funds were, however, financed by employers' contributions instead of workers' contributions. Hospitals became more autonomous but remained publicly run. New targeted measures were created, including a conditional cash transfer programme to promote attendance at secondary school. Despite formal stability in social policy, funding shortages and the expansion of private services undermined the quality and generosity of many public services and transfers.

Explaining Costa Rica's development success

Democracy was not the only factor

Costa Rica's success is often attributed to the contribution of democracy to human development. Yet many of the building blocks of modern Costa Rica, including nationalized banks and a professional and autonomous bureaucracy, were created by a de facto, non-elected transitional government that ruled for 18 months after the 1948 civil war. There were recurrent threats to elected governments during the 1950s, and the communist party was outlawed until the early 1970s. The creation of high-quality state institutions—another common explanation of Costa Rica's success—accompanied rather than preceded the double incorporation.

A new elite with deep social roots

By contrast, our research proposes an alternative explanation focused on the characteristics of a new elite with deep social roots. Since the late 1940s, a growing middle class of urban professionals and small coffee producers—which had historically been more important in Costa Rica than in neighbouring countries—provided political support for the double incorporation. Clustered around the newly created National Liberation Party (Partido Liberación Nacional, or PLN), this new elite relied on the state to (i) support its production activities; (ii) strengthen the bureaucracy and expand public employment; and (iii) manage conflict in the rural sector and between capital and labour.

Nationalization of the banking system (orchestrated by leading elements within the new elite after the 1948 civil war) and policies to protect the domestic market during the 1960s and 1970s are cases in point for how the emerging elite relied on the state for its own benefit. These processes generated significant rents: in 1974 preferential access to cheap credit resulted in an implicit yearly subsidy of 30 per cent of the value of production. Most rents went to specific people within the PLN leadership, but small and medium producers across the country benefited as well. A large share of these loans went to public agencies, which used them to create jobs.

The role of ideas

Specific features of policies implemented by the PLN must also be seen in the context of travelling international ideas. For example, the expansion of anti-poverty programmes in the 1970s resonated with the US “War against Poverty” and was also influenced by the World Bank’s ideas on social development and basic needs. Consolidation of fragmented social insurance programmes would have been unlikely without the ILO changing its position from occupation-based to unified social security architectures.

Changing roles of elites and ideas since the 1980s

Changes in the role of the elite and the transformation of international ideas also help explain the evolution of Costa Rica’s economic model since the 1980s and the growing challenge of securing the double incorporation:

- Controversies within the elite around the best development road emerged in the second half of the 1970s and intensified in the early 1980s. Young political cadres backed by growing segments of the business sector endorsed

liberal policies. Successful entrepreneurs were increasingly interested in exporting outside of Central America for two reasons: (i) the Costa Rican market was too small for them and building links with foreign companies particularly profitable; and (ii) civil wars in neighboring countries closed down regional markets.

- Changes in international ideas also explain the reorientation of Costa Rican policies. Worldwide, the Washington Consensus challenged social-democratic ideas and provided a theoretical rationale for trade and financial liberalization. Yet the actual menu of ideas internationally available was broader than critics of the Washington Consensus sometimes assume. Countries like Singapore and Ireland showed that active industrial policies that “picked winners” were compatible with a liberal approach to economic policy. For Costa Rica, these countries became powerful examples of the positive results of growth models that focus on targeting specific transnational corporations in high-tech sectors.

Policy lessons

The state must play a role in the creation of jobs in both the public and private sectors

Economic growth needs to be driven by employment creation in different sectors and used to create further employment. This balanced strategy, where the public and private sectors, and small, medium and large firms, are all important is unlikely without active state intervention. Public employment can play a significant role and should not be seen as inherently inefficient. For example, the Costa Rican Institute of Telecommunication—a public state-owned enterprise—is considered one of the most successful utility companies in Central America. Furthermore, a large share of public employment in Costa Rica concentrated on social services like health and education. Because public employment is a major source of better jobs for women, these can have a particularly positive impact on their market incorporation.

Over time, market incorporation requires economic upgrading and job creation

Successful market incorporation is characterized by processes of structural change that are both employment-intensive and technology-intensive. Costa Rica has struggled to simultaneously create formal jobs and secure technological upgrading. Between 1950 and 1980 the country succeeded in creating better jobs and effectively funding its social policy regime, but failed to upgrade its comparative advantages. Excessive dependence

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on traditional exports like coffee and bananas left Costa Rica subject to price volatility and contributed to excessive foreign borrowing—ultimately leading to the 1980s debt crisis.

Since 1980, Costa Rica has earned a worldwide reputation for having managed to develop new high-tech sectors like semiconductors. However, this strategy has gone hand in hand with growing differences between these leading sectors, which provide few good jobs, and the rest of the economy, which lags behind in terms of productivity and decent work, creating informal (and often highly feminized) jobs.

Intertwining basic social services and social insurance facilitates social incorporation

While social insurance and most social assistance programmes aim to deal with risks like old-age, sickness and disability among workers and the poor, respectively, most basic social services are designed to create skills and enhance capabilities for all. While the two are usually separated in policy analysis, trying to make clear-cut distinctions between social insurance, social assistance and basic social services in the Costa Rican case poses enormous difficulties. There, basic services and contributory-based social policy are closely interconnected, in particular through financing and distribution links. For example, social insurance contributions funded training and increased capabilities among the poor. And nutrition and health programmes that targeted poor areas of the country constituted a first step for low-income groups to access health and education services for all.

Different elites pose different demands on the process of state-building

The study of Costa Rica clearly shows that in order to understand agendas of state-building, the preferences and interests of elites—which

are not the same in all countries—need to be carefully considered. Particular vested interests do not always get in the way of the double incorporation. In particular, when middle-class groups with limited access to capital and property get into power, they may promote an agenda for the expansion of employment opportunities and social services that benefit a majority of the population.

International ideas play a crucial role in shaping constraints and opportunities

International variables—whether ideas or other, more material, resources—do not, by themselves, determine market or social incorporation at the national level. But international factors are a necessary condition for establishing inclusive policy regimes. The Costa Rican case shows that at various points in time, political elites—and actors mastering knowledge about specific policies—drew on international ideas and blueprints. These included international recommendations on how to design social insurance, and regional advice on import substitution. Contemporary policy formation should take advantage of the window of opportunity provided by the current emphasis on universal social policies and active industrial policies in order to promote a development agenda that is conducive to the double incorporation

Further reading

J. Martínez Franzoni and D. Sánchez-Ancochea. 2012. *The Double Challenge of Market and Social Incorporation: Progress and Bottlenecks in Latin America*. Desigualdades.Net Working Paper No. 27.

J. Martínez Franzoni and D. Sánchez-Ancochea. 2013. *Good Jobs and Social Services: How Costa Rica Achieved the Elusive Double Incorporation*. UNRISD and Palgrave Macmillan, Basingstoke.

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