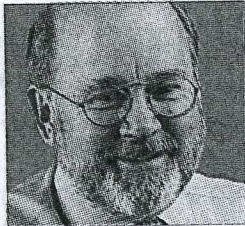


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'Dead capital' holding back poor in Peru



**SCOTT
BURNS**

CUSCO, Peru — In Peru, bricks for making houses are everywhere. They tell a story.

The bricks are made just as they were made in the time of Moses — by hand from mud and straw. After they have set, they are laid out to dry, which is why you see so many of them along any road you travel.

Adobe bricks are used to build the small houses that line the roads and dot the hillsides of rural Peru. Most of these houses don't have electricity or running water.

The same bricks are used to build the houses that line the steep hillside roads only a few miles from the center of downtown Cusco, a city of 300,000 people at 11,000 feet, the departure point for the Machu Picchu train and excursions into the Manu Bio Reserve.

As in the United States, a house is the most valuable asset that most people own.

But in Peru they have little or no financial value. Unlike your house or mine, which is deeded, titled and

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Reanimating 'dead capital' is crucial to Third World

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(probably) mortgaged, not to mention specifically located so that it can receive electricity, gas, and water utilities and be billed for local taxes, most housing in Peru is what Hernando de Soto calls "extralegal." He means it exists outside the legal system of private property.

And this, Mr. de Soto believes, is very important.

I first heard Mr. de Soto in 1987, when he spoke at a luncheon sponsored by the National Center for Policy Analysis in Dallas. His subject, then, was his book, *El Otro Sendero (The Other Path)*, in which he demonstrated the size and power of the informal — or underground — economy in Peru.

"This is the economy that works outside the law. We estimate that 65 percent of the Latin American population works outside the law," he said then.

He explained that "the underground economy was the response of Peru's poor population to a mercantilistic system. They were economically locked out of the formal or legal economy. So they created their own market-based economy."

His figures are astonishing, showing that the poor had built some \$8.3 billion worth of housing; that informal businesses provided 96 percent of all public transportation; that 52 percent

of all manufacturing and 60 percent of all retailing was underground.

What hamstrung economic development in Peru, he said, was something few people thought about: the lack of a simple and efficient system of property rights.

Now, Mr. de Soto has extended this revolutionary view of economic development to the Third World at large by performing similar research in other countries. The results will be available this September as *The Mystery of Capital: Why Capitalism Succeeds in the West and Fails Everywhere Else* (Basic Books, 320 pages).

Examining Haiti, Cairo and Manila, and then extending his findings to all Third World and former communist nations, he estimates that real estate held "but not legally owned" by the poor is worth about \$9.3 trillion, or "about twice as much as the total circulating U.S. money supply."

Measured another way; he finds that housing owned by the Third World poor is worth nearly as much as "the total value of all the companies listed on the main stock exchanges of the world's 20 most developed countries."

More important, he also estimates it as "46 times as much as all the World Bank loans of the past three decades and 93 times as much as all development assistance from all advanced countries to the Third World in the same period."

Unfortunately, all of this housing (which is only the most obvious asset

created by the poor) is "dead capital." If the owner tries to obtain title, he will spend years doing it. Worse, he will risk having the property condemned and torn down.

As a result, the financial value of property in most of the Third World is impaired. The ability to finance it or sell it is reduced or nonexistent.

Much the same happens with business assets. Wealth is created — but without legal standing it lacks the magical animation of the living capital that you and I take for granted.

In America, we can borrow to buy a house because it has a deed. We get credit offers in the mail simply because we have an address. We can borrow to buy a car because it has a title that is easily registered and transferred.

In America, we create access to fluid capital and cash because we have a system of property rights, contracts and promises that works to make all property liquid.

This system is lacking in most of the world. Working to create that system, Mr. de Soto believes, is the most important task any Third World government can undertake.

Questions about personal finance and investments may be sent to: Scott Burns, The Dallas Morning News, P.O. Box 655237, Dallas 75265; faxed to 214-977-8776; or e-mailed to scott@scottburns.com. Check the Web site: www.scottburns.com. Questions of general interest will be answered in future columns.