



Alphachat: Sebastian Edwards on the economics of populism

Cardiff Garcia How did you first start becoming interested in the economics of populism?

Sebastian Edwards Well, anyone that was born in Latin America and is interested in economics unavoidably ends up, sooner or later – sooner, in general – worrying about populism.

The early work started when Alan Garcia took over the presidency of Peru for the first time. There was Alan Garcia I and Alan Garcia II. [Garcia was first president of Peru from 1985 to 1990, and then again from 2006 to 2011.]

And Rudi Dornbusch and I were absolutely fascinated by the disregard that Garcia had for anything that resembled good economic policy, and how he just wrecked Peru. And we said, well, this is one more manifestation of a more general phenomenon that comes back again and again and again in Latin America. And we decided then to write our first paper, an article. We actually compared Alan Garcia to Salvador Allende in Chile. [Allende was president of Chile from 1970 to 1973. He committed suicide during a military coup to overthrow him.]

Cardiff Garcia Yes, Garcia was the 1980s.

Sebastian Edwards Right. And Allende was in the early 70s, from 1970 until the Pinochet coup in 73. And then we started working on other cases – [Juan] Peron in Argentina, Getulio Vargas in Brazil. And so we built a body of work and then convinced others to start working on populism, and then we did a book. And so that was a long time ago.

Cardiff Garcia I recently moderated a panel about the Mexican political and economic outlook. And something that the panelists said, and also a few people in the audience, was that Americans have been taken off-guard by some of the phrasings of Donald Trump and what he says is part of his agenda. But that if you're from Latin America, you've seen how a lot of this movie plays out before.

Sebastian Edwards That is correct. You've seen it before. The modus operandi is very similar. And it's very ironic. You have Donald Trump, and the way he approaches many of these issues is not too different to what Hugo Chavez did in Venezuela. And that's exactly what makes this whole story quite fascinating.

Cardiff Garcia Yes. Okay, so before we actually get to Donald Trump, which I think we're going to save for the end of the conversation, I want to get into some of the basics. When you talk about populism and populist leaders, what definition are you using? Because I get the sense that the word "populism" is sometimes used

differently by different scholars and by different people, and there's a lot of talking past each other.

Sebastian Edwards That is correct. So Rudi Dornbusch and I defined the economics of populism as an economic programme, a package of policies, that disregarded good, solid received wisdom on economics.

And in the case of Latin America, which is going to be interesting when we compare it to Donald Trump, disregarded all budget and monetary constraints – and violated all those constraints, as the populists do, in a way that generates euphoria in the immediate short run, but ultimately results in a very deep crisis that affects, in particular, those that were supposed to be benefited by the whole programme.

So populist economics is an economic policy package that disregards budget constraints, macroeconomic constraints, good solid productivity constraints, and generates short run benefits at the cost of crisis in the future.

Cardiff Garcia Yes, I get the sense that a big part of that also was a disregard not only for the principles of sound economic management, but for the extant institutions in place that are supposed to enforce those principles.

Sebastian Edwards That is correct. So those are the policies, what I described. And what the populist leader does then is that in a rhetoric that is quite extreme, and where he or she divides the population between “us, the people” and “them” – and it's a vague “them”, and we'll get to that in a minute... In that rhetoric, the populist leader takes the discourse directly to the people through big rallies, a referendum, plebiscites.

I'm talking about Hugo Chavez and Donald Trump, who continues to be, although he's now the president, in campaign mode. And in doing this [he] skips the institutions. For instance, they tend to dislike the central bank because it is an institution that tends to maintain sound policies in most countries.

First thing that Hugo Chavez did was fire Ruth de Krivoy, the Governor of the central bank of Venezuela, right. So they disregard the institutions, both economic and political. That is absolutely right.

Cardiff Garcia Yes, there's something else that's interesting about your work. Because you've spent so much time studying Latin America, it turns out that the majority of the populist leaders you've studied have been left wing. A lot of Marxists.

And it's interesting to me that in your work, you don't actually look at populism as a left-right issue. So can you elaborate on how that works?

Sebastian Edwards Yes. These false promises that the populist leader offers to the people may come from the right or from the left. In some ways, [Juan] Peron, who had great sympathy for the fascist movements – he was a great admirer of Benito Mussolini – was right wing in many respects.

So there is no reason why we cannot have corporatist right-wing populist leaders that favour specific groups in their rhetoric and in their policies and again, very clearly blame, in quotation marks, “the other” for the suffering of “us, the people”.

And in the case of Latin America, often “the other” was related to some foreign force – the multinationals, international speculators and, of course, the International Monetary Fund.

And what is very ironic is that in the case of Donald Trump, foreigners also are blamed for the plight of the people and, in this case, they are immigrants, the Chinese and international terrorists.

Cardiff Garcia Yes, okay. Let’s go through some of the findings of your work. And let’s start by talking about the conditions in place that usually precede the rise of a populist leader.

Sebastian Edwards Well, yes, the first phase is a deep public dissatisfaction and discontent. And this dissatisfaction and discontent is of two types. Sometimes it’s quite abrupt. And in Latin America, usually that abrupt crisis has been associated historically with a very large devaluation of the currency. So we go back to in Argentina 2001, 2002, peso-dollar, one to one for ten years, and all of a sudden there is a huge crisis and the currency goes from one peso-one dollar to three to four pesos-one dollar. And that generates a very deep sense of dissatisfaction, of betrayal. So there is the crisis.

In other cases, the crisis develops much more slowly and it’s a simmering crisis. And that is what we can see in the United States where there is a simmering dissatisfaction, in particular among white, blue collar workers. So first phase, great dissatisfaction. And you can see it in country after country after country.

Venezuela, caracazo and the big riots; Argentina, the big devaluation; in Peru, the failed presidency of Fernando Belaúnde after the return of democracy; and we can go on and on and on. And in the case of the US, it’s income stagnation, wage stagnation among a large group of manufacturing-sector and natural resource-producing people. I’m thinking of coal in West Virginia and Kentucky and so on.

The second phase is the emergence of this populist leader, very charismatic, who operates outside of the political institutions.

In general, he or she – it mostly has been men – does not have a political party or is a newcomer into politics. So Peron comes from the armed forces. Alan Garcia has a political party, the APRA, but the APRA in Peru has been outlawed for so long, that has not played a role. Chavez comes from the military. Rafael Correa in Ecuador, he’s a technocrat, he has a PhD from the University of Illinois, so he has been a technocrat that has been completely outside of the traditional political system. Evo Morales, same thing. Now, Donald Trump, of course, disconnected and, in fact, disliked by [the establishment parties]...

So this leader that comes out is extremely forceful, very articulate, and in rallies and in direct appeal to the people, provides this very nationalistic rhetoric and gets the

people to approve this particular political programme that disregards all sorts of constraints of good, solid economic management.

And either you cut yourself off from the International Monetary Fund -- famously, Peru stopped paying its debt to the IMF, one of the few countries in the history of the IMF... -- and in this phase, there is a fantastically positive reaction in the economy. More so in Latin America than what we're probably going to see in the US, because what the Latin American populist leaders do is that they blow out the international reserves that the country has, and they fix the exchange rate at an artificial level, and everything is good while they are spending all the resource that they have for that particular time.

And then comes the crisis. The next phase is the crisis.

Cardiff Garcia Right. Before we get to that next phase, still talking about the conditions that lead to the emergence of a populist leader and of populist economics, you mentioned wage stagnation and dissatisfaction. What about income or wealth inequality as a precursor to fomenting a lot of the anti-elite sentiment?

Sebastian Edwards That, of course, goes with it – for several reasons.

Most of these crises have a different effect on different social groups and income groups. And again, if we go back to the work that Rudi and I did originally, if the crisis has a nature of very high inflation and eventually large devaluation, the upper classes of course have moved all their money into dollars or foreign currency and then moved it to Miami banks – banks in Miami or Panama, so they are protected from the crisis.

So there is a dissatisfaction that is much stronger among lower income people, which is also the case in the US. The Argentine crisis of 2001, 2002, which resulted in the successive presidents and ended up with Duhalde and a long Kirchner presidency, Nestor and then his wife, was particularly severe in terms of income distribution. And the poor in Argentina suffered very significantly during that period.

Cardiff Garcia Okay. So we have this phase that follows the enactment of populist economic policies, where the economy gets a big sugar high essentially and, you mentioned in the case of Latin America, they start blowing through their FX reserves, they start exploding their budget deficit. What happens next?

Sebastian Edwards So here is where the story probably is going to depart and it's going to play a little differently in the US.

What has happened in Latin America and in other parts of the world – Russia, Turkey, it's very generalised – is that as the international reserves are depleted then the country, at some point, cannot import goods anymore using the very cheap currency value.

And usually the first step is that the price of gasoline and oil-related goods is hiked, and that results in the price of public transportation going up, and that results in riots. And these are generalised riots – and we saw that in Caracas, we've seen that in

country after country after country – that as soon as the price of public transportation is doubled, sometimes it's tripled, then the population becomes very, very unhappy. It is a direct hit to their pockets and there are manifestations and/or riots.

And, of course, the populist leader continues to blame the international speculators and price gauging by the elite, and so on and so forth. The IMF may come into the country, but the populist leader says, "they want to impose on us austerity and we're not going to accept that". We've seen that in Africa again and again, for ages.

And this gets prolonged until, politically, it's untenable and something happens. And in Latin American, many times that something was a coup d'état – and the military stepped in and there were people killed and, at the end, there was a lot of repression. And the poor, who were supposed to be those that would benefit from the populist programme, end up being much worse off.

Cardiff Garcia Yes, there's a nice point made in one of your early papers with Rudi, where you write that the problem with the outcomes that you described, in addition to what's obvious, is that capital can flee but labour is trapped in the country.

In other words, the investment that might've been necessary to keep propping up these asinine policies can turn around and leave the country. But the workers themselves have nowhere to go – they're stuck there. And so the people who were supposed to benefit end up losing out the most.

Sebastian Edwards And that is related, of course, to what I was saying earlier in the sense that the rich always have a way of putting their money in Miami banks, or when it came to Cyprus, they moved their money to Greece. And they protect themselves.

Cardiff Garcia Yes. It invariably leads to a very sad outcome.

Sebastian Edwards But what is very interesting is that, as we said and as you reminded me, capital can flee. The people are trapped, but they try to get out. So the saddest picture to the eye in Buenos Aires in the early 2000s were the lines of professional young people in front of the Spanish and Italian embassies – the Spanish crisis had not occurred yet – people that were trying to emigrate from Argentina, trying to get around the fact that they were trapped there.

Cardiff Garcia Let's talk about something that you alluded to earlier but that might also be a part of the US story, in addition to having been a part of these Latin American crises, which is the degradation of the rule of law.

In other words, when you talk about going around the institutions, ignoring them, one of those institutions is just the simple faith and confidence of the people who invest in these businesses in Latin America and in the US. When you see the leaders of these businesses either being berated by a political leader or, in the more extreme cases of Latin American, in some cases nationalised by the government, it ends up undermining dramatically the faith and confidence in all of the remaining businesses. And eventually you get into a situation where nobody wants to do business in your country because nobody has any faith in the legal architecture.

Sebastian Edwards Right, that is correct. So one of the most important aspects of capitalism is that it should be quite impersonal. And all companies should be treated by the authorities equally. And that, of course, is translated in international trade to the Most Favoured Nation where every nation should get national treatment.

And what we see in many of these populist extremisms in Latin America is that the authority starts picking up on specific companies, firms, conglomerates. And the strong man or the strong woman (Cristina in Argentina) would call the CEO or the controlling figure of that company and would threaten him or her personally or would denounce that company in public rallies, and would direct the mobs to riot and to maybe even break into those stores.

And then they are called in and they are told, you have to reduce your prices, or you have to do this, or you have to do that, and you have to raise wages by 50% while, at the same time, you cannot increase the prices of your product.

Which, of course, is a variant of what Trump is doing with companies that want to invest and start plans in other parts of the world.

So the rule of law, and in particular, the impersonal treatment – equal treatment of everyone in front of the regulators, and so on and so forth – starts to disappear.

And since the populist leader maintains himself in power by feeding this notion that there is this foreign force outside the country that is trying to keep the people down, he needs these enemies and it's a little bit unavoidable. And again, we can see the parallels with what is happening right now in the US with Donald Trump.

Cardiff Garcia It seems, by the way, like your definition of what constitutes economic populism is similar to a definition I've seen of political populism that's been recently advanced by a political scientist named Jan-Werner Müller. He says that it's not enough for someone just to be anti-elitist; the real key is that they are also anti-pluralist. In other words, that they identify either people, or entities, or companies outside of the "true" people – and those entities and people have to be delegitimized. Because only that populist leader has access to the real feelings and the real needs and the real wants of the people. And the people are, of course, however he defines them to be.

Sebastian Edwards It is very similar in that regard. And there is this notion that the populist leader presents himself as illuminated and being able to see through clouds and through all sorts of impediments – including political parties, the legislature, the Supreme Court, the central bank, the budget office – and then is able to undertake particular policies that are going to solve everyone's problem.

And, of course, it doesn't happen like that. Checks and balances are gone quite early on in the Latin American populist experience. It happened in Turkey, it happened in Russia. But I don't think it's going to happen in the US. I cross my fingers.

Cardiff Garcia Sure. To give you a couple of other examples where Trump seemed to be leaning in that direction, although it's really hard to tell right now how far he would go: In addition to the tweets that you mentioned where he criticises

specific companies for not going along with his agenda, we have to remember that he said during the campaign that elections are legitimate if he wins, but they're rigged if he does not win. The media that praises him is fine, but if not, then the media is the "enemy" of the American people. Those are his words. The intelligence community is okay if they're digging things up on Hillary Clinton, but if not, then they're like the Nazis. Again, from a tweet of his. I'm not just saying that for exaggerating effect.

And so what's hard for me to tell is whether or not he's using these tactics from the populist playbook to try to further his agenda because he's seen that they work, or if he himself actually has ambitions to go that far, to test the limits of those institutions.

Sebastian Edwards I don't know what the answer is. There are two alternatives. Either the level of ambition and desire to grab power is much greater than what any of us imagine, or the level of knowledge of US history and how institutions function in the US is very low. I, at this point, think that it is the latter, that there is a deep degree of ignorance in terms of the way the system works.

I'm writing now a book about what happened in the US in 1933, which is when FDR came to power. The Democrats had an incredible majority in Congress, and after the 1936 election, it was absolute, in every sense. But yet, FDR had to act according to the institutions. And when he tried to pack the Supreme Court, it was his own party that turned against him. And Senator Burton Wheeler was the one that led that effort, who was a populist from the Midwest. So I think the checks and balances go early in the populist experiences in Latin America, and I suspect that President Trump does not quite understand that there are severe limits to executive power.

Cardiff Garcia You mentioned earlier, going back to the economics, that you suspect that in the US, the outcomes of these populist tactics or these populist attempts will play out a little bit differently from the way they did in Latin America. I totally agree with you, but let me first just ask how you think it will differ from what happened in all these different Latin American instances.

Sebastian Edwards Yes, very important is that I think that independently of any desire, attempt or effort by President Trump, the Federal Reserve will continue to be the Federal Reserve. It's a very important, solid institution. It's about 100 years old – it was founded in 1913. And we are not going to see the kind of disregard for good economic policy that resulted in the huge inflations in Latin America. I think that that's the first thing.

And the second thing is that the US has judicial review, and the judges interpret what the Constitution says. That's very unique of the United States, and that's not the case in Latin America, [where] it's much easier to fire judges or pack the courts. Cristina Fernandez, in Argentina, packed the court several times.

Cardiff Garcia I want to stay with this idea that institutions are probably stronger in the US. Not probably – they certainly are stronger in the US than they were in Latin America, and thus better able to handle whatever testing of their limits the Donald Trump presidency attempts.

In terms of the Federal Reserve, I actually do worry a little bit. Not that the Federal Reserve is going to be overthrown or anything so dramatic, but that because the Republicans are in office now, that there might be some kind of an erosion of its independence.

Especially if Janet Yellen starts to raise interest rates faster than Donald Trump might want her to if he tries to pass some kind of a large fiscal package, if they actually manage to get that through, and that then she starts raising rates – and either he starts packing the Fed with what you might call political appointees (in other words, he'll slowly politicise the Fed) or the Republicans actually manage to pass some kind of Audit-the-Fed bill. That's one thing that I do worry about a little bit.

The second is that if he ends up passing some combination of infrastructure spending and a large income tax cut, which was included both in his campaign proposals and is part of the Republican proposals that were offered last year, that it'll be like in the 2000s – quite a regressive tax cut. And that if it blows out the deficit, that it'll limit the political manoeuvrability to combat the next downturn. That's another thing that I worry about a little bit.

But I think my biggest worry is that he continues on this path of berating companies, that he takes this approach that seems both corporatist and crony-est, that something else will come out that will just lead to a slower diminution of faith and confidence in American markets.

And it could come from all kinds of places. The most recent example I can think of is that tourism is going to slow down because of these executive orders on immigration and on the so-called Muslim ban, and that that's worrying a lot of people. They just don't want to travel to the US because they feel like it's going to be unpleasant, which makes sense.

And then, finally, that it'll overturn longstanding norms of abiding by large, multilateral institutions, like the WTO, that will have a slower kind of protectionism which is itself bad for the economy in the long term. (So it might even produce a short-term wage boost to lower skilled, native born workers, if you have less immigration or if there's even emigration.) And so I worry that it's a slower but still significant erosion of the norms and traditions that have made the US economy strong in the past. What do you think?

Sebastian Edwards Yes, I think that you have a very strong point there. And, as I said earlier, the dissatisfaction in the US is more of a simmering type, and it has built through a long time and it's not explosive, as it happened in Argentina, for instance, with the devaluation at the end of the de la Rúa presidency.

And in the same way, I think that the erosion in the US will be much slower than Latin America, as you pointed out. And I agree with you that all of those are issues to be worried about.

But my main concern is protectionism. But still, it's unclear how it is going to play itself out. It's not impossible to think that NAFTA is going to come to an end, for instance, and that's pretty unilateral. They have to give notice and then, first, there has

to be some attempt at renegotiating. But I just came back from Mexico and the degree of anxiety among political leaders of any party – PRD, PRI and PAN – in Mexico is much, much higher than what most people imagine here in the US.

So protectionism, I think, is the way this will play itself out. I don't know, however, if we're going to see the border tax adjustment. It's just too complicated. I don't know if Trump himself understands it. If we insist in going that way, the WTO is going to say no, and we may try to pull out or ignore the WTO. So again, erosion of institutions.

And there we will see that there will be pockets of wage boosts, or one town or another town in the Midwest that will get 1,000 jobs or 355 jobs because some company decided not to go to Mexico and actually to invest, I don't know, in Michigan or somewhere.

But of course, the final effect is going to be very negative for the lower classes in the US. Basically, Walmart prices will, I don't know, will double. And the rich don't shop in Walmart. They buy Ferragamo suits and Hermes ties in Paris.

Now, the tourist effect that you mentioned is a very interesting one because that is one that Trump will understand. And I am not sure if he owns properties that are subject to the very high seasonal demand for help. But of course he does understand how hotels in Aspen and in Sun Valley and in Deer Park and so on, where the elite go and play during the winter, can only function because they have all these foreign people that come and work there. That come from all over the world. From Iceland, from Sweden, from Norway. These are not only brown people coming from Mexico.

And definitely at every level, be it run of the mill, middle-class type of facilities in Vegas, all the way to big resorts in Jackson Hole or wherever it is, they are going to suffer from the kind of approach that he's taking towards immigration.

And I think that that is going to be very interesting. So he will understand that, he will get his friends and associates, his sons, telling him that this is going on. And I don't know how he's going to react to that.

Cardiff Garcia Yes, it's a good point that right now, all of these things are hypotheticals, these are things to be worried about – they are not exactly certainties.

In part because Trump is himself such an unusual figure that it just makes it hard to know how quickly he might change his mind on a bad idea if he gets enough pushback from the right institutions. There have been a few hopeful signs in that regard, some of them coming from the national security apparatus within the US, that he is amenable to getting rid of the people that should never have been there in the first place, and replacing them with people who are a little more qualified. I don't know how that'll take shape in the economic realm.

But my last question, I guess, is: you've studied so many Latin American leaders; which one does Trump remind you the most of?

Sebastian Edwards Well, I don't think that there is one particular person that comes to mind...

Cardiff Garcia Which combination of leaders and which traits does he have in combination?

Sebastian Edwards Well, his nationalistic view reminds me, of course, of [Juan] Peron, in some regards. The anti-migrant approach is absent in most of these Latin American populist experiences.

Large migrations within Latin America have been rare in history. There was a very large migration out of the Southern Cone into Venezuela, for instance, in the 1960s and 70s. But these were all middle-class or upper middle-class professionals – engineers, doctors, lawyers, and so on and so forth. And there was no pushback in Venezuela because the oil economy was doing so well that they needed these people.

What we're seeing now, in terms of rejection of migrants, is coming out of Chile. But no one imagined that because Chile has been so successful, and it has become such a wealthy country in relative terms that now there are a lot of people that come from Haiti and Colombia and Bolivia. And there's some pushback in Chile. So yes, I would say some Peron. The rest is difficult to pin him down.

Someone may say that he has some resemblance to President Piñera from Chile because they are both very wealthy. But Piñera understands economics. He has a PhD in economics from a so-and-so university, from Harvard. So he does understand economics. And Trump, although he went to Warton, doesn't seem to really grasp what's at play here.

Cardiff Garcia Your most recent book, I said earlier, was *Left Behind: Latin America and the False Promise of Populism*. What's the title of your upcoming book?

Sebastian Edwards The title of my upcoming book is *Broken Promises*, and it deals with 1933 in the US and the abandonment of the gold standard and the large devaluation of the dollar, which was very Latin American in style and in magnitude.

The dollar was devalued by almost 50%. That's very Argentine. What were the consequences for income distribution, for politics, for the investment community, for financial markets, and so on? So it's a long book on only one year, and I'm having a great time working on it.

Cardiff Garcia Yes, that was a hell of a year though.

Sebastian Edwards It was a hell of a year and there were lots of good things: the New Deal started. Lots of bad things: Hitler.