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Reform, Reform the Reforms or Simply Regression? The 'Washington Consensus' and its Critics

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The 'Washington Consensus' analysis and policies are being disputed both analytically and for their effectiveness. This paper surveys first the debate on the definition of the 'Washington Consensus' vis-à-vis its apparent developmental shortcomings. Then it surveys the major areas where the 'Washington Consensus' is judged as a failure (with particular emphasis on the crises of the 1990s). In the next part it presents the main responses to the 'crisis' of the 'Washington Consensus'. Its supporters are categorised in the fundamentalists and the reformists whereas its opponents are divided in the post-Washington Consensus adherents and the Marxist critics. It is argued that the Marxist perspective offers a superior understanding and critique of the 'Washington Consensus'.

Key words: Development, Washington Consensus, Political Economy.

JEL classifications: A14, B50, O10.

INTRODUCTION: THE DEBATE ABOUT THE DEFINITION

The term 'Washington Consensus' was coined in 1989 by John Williamson (Williamson (2004b)). It was introduced in a period when the Keynesian dominance in economic theory and policy had collapsed –after the mid-1970s crisis and Keynesianism's apparent inability to solve it–and neo-liberalism (promoted by the Reagan and Thatcher administrations in the US and the UK respectively) had become the new orthodoxy. Williamson's aim was to codify that part of the neo-liberal analysis and policy proposals which have become commonly

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accepted within Development Theory and particularly in the circles of the big developmental institutions (primarily the IMF and the World Bank) seated in Washington. In Williamson's (2000, p.254) own words his effort 'was an attempt to distill which of the policy initiatives that have emanated from Washington during the years of conservative ideology had won inclusion in the intellectual mainstream rather than being cast aside once Ronald Reagan was no longer on the political scene'. Thus, 'Washington' refers to the influential circles and institutions based in Washington. And 'Consensus' refers to the part of neo-liberal policy prescriptions that had been widely accepted. There is another geographical dimension in the term 'Washington Consensus'. Its policy prescriptions were primarily issued for the Latin American economies in the 1990s, although they subsequently spread to the rest of the developing and less developed countries. Again in Williamson's (2000, p.251) own words, the term refers 'to the lowest common denominator of policy advice being addressed by the Washington-based institutions to Latin American countries as of 1989'. Williamson (1990, 2000, p.252-3) summarizes these policy prescriptions in ten propositions:

- (1) The imposition of *fiscal discipline*.
- (2) The *redirection of public expenditure priorities* towards other fields.
- (3) The introduction of *tax reforms* that would lower marginal rates and broaden the tax base.
- (4) The *liberalization of the interest rate*.
- (5) A *competitive exchange rate*.
- (6) The *liberalization of the trade*.
- (7) The *liberalization of inflows of foreign direct investment*.
- (8) The *privatization* of state-owned economic enterprises.
- (9) The *deregulation* of economic activities.
- (10) The creation of a *secure environment for property rights*.

The theoretical foundations of these proposals can be easily discerned. They are the usual analyses advanced by neo-liberal economic theory. Economies are in crisis because of impediments to the free operation of the market. The impediments came from the overinflated interventionist Keynesian state and its expansionary and redistributive policies that deform market data and signals. The solution, according to the neo-liberal mantra, would be the withdrawal of the state from the economy and the reinstatement of the unhindered operation of the market. Therefore, fiscal discipline should be imposed

on public activities and a return to the balanced budgets (as opposed to the Keynesian deficit and expansionary budgets). The now limited public expenditure should be directed towards fields that cover its cost (possibly through the imposition of compensative payments) and would support private entrepreneurship instead of paying for public works and redistributive policies. Subsequently, the tax system should be reformed so as not to hit hard business profits and the incomes of the upper strata, which were conceived as the locomotive of the economy. After all, the limited public expenditure can do with less taxes. Additionally, the operation of the financial system should be liberated from the state grip and prerogatives and be left to the free operation of the market forces. Thus, the interest rate should be determined more or less competitively. The withdrawal of the state from the economy required, also, the privatization of all the activities and enterprises that were state-owned and directed, the limitation to a minimum of all state regulations and adequate guarantees that there wont be any violations of property rights (as it had happened previously with nationalisations etc.).

With the advent of the second generation of neo-liberal theories, which emphasised the opening of the economies, the previous set of policy proposals was supplemented with three others that aimed to the liberalisation of international trade, capital movements and financial activities. Thus, protectionist measures had to be abolished and free trade movements established. Also, the free international movement of capital investments had to be secured. And, last but not the least, international financial transactions and, primarily, the exchange rate of the currency had to be set according to market prerogatives and not by state policies.

All these ideas had already been established as the orthodoxy in the developed countries in the 1980s. What the Washington Consensus aimed to do was to introduce them in the developing and less developed countries. As Williamson explicitly stated, there appeared to be a sort of global apartheid, which claimed that developing countries came from a different universe which enabled them to benefit from (a) inflation (so as to reap the inflation tax and boost investment); (b) a leading role for the state in initiating industrialization; and (c) import substitution. The Washington Consensus aimed to break this differentiation.

Quite soon, after its formal declaration, the Washington Consensus came under criticism from many quarters. These criticisms emanated from mainstream economics (Atkinson (1999b) Rodrik (1992, 2002,

2003) and particularly a current associated with the work of J. Stiglitz (1998a, 1998b) and also from Marxist Political Economy (Fine (2001a, 2001b, 2002), Shaikh (2003, 2004)). An important point in this controversy was the very definition of the term 'Washington Consensus'. For nearly all its critics the term was synonymous with neo-liberalism and a blind fundamentalism of the market.

Williamson (1997, 2000, 2004a) made a feeble defence of his term arguing rather unconvincingly that it was not in his intentions a so close identification of the term with neo-liberalism. He maintained that he simply codified the consensus view within the big Washington institutions and his concept was a mere technocratic formulation devoid of ideological and political motivation. He also argued that his 'Washington Consensus' was not even a policy prescription but simply a list of policy reforms; although he is sympathetic to the former view and he accepts that at the time of the introduction of the term these two coincided (Williamson (2004a)). However, he added that his definition might be problematic in some aspects and also that he himself had reservations on some of these. For example, in retrospect, he doubts whether Washington institutions unanimously favoured the competitively determined exchange rate and the rapid abolition of capital controls. His reservations with the Washington Consensus' policies were that their poverty reduction policies had to be more emphasized and sophisticated and that a greater emphasis should be put upon institutions and their role.

Despite Williamson's arguments it cannot be denied—and even he cannot reject altogether—that the Washington Consensus has a definite ideological and political background: that of the neo-conservative policies of the last quarter of the 20th century. Furthermore, the Washington Consensus cannot be delegated to a simple sum of policy proposals. It has definitely a spinal column on the basis of which the whole edifice has been constructed. This is implicitly accepted even by Williamson when, in many papers, argues that there are three big ideas behind the Washington Consensus: macroeconomic discipline, market economy and opening of the economy (at least in respect of trade and foreign direct investment). Washington Consensus' macroeconomic discipline is of a particular type and has specific priorities that differentiate it from other types of macroeconomic orderly state of affairs. It has certainly nothing to do either with Keynesian macroeconomic prerogatives or with those of other more radical perspectives. In almost all cases it led to austerity budgets and policies that favoured the wealthier and worsen the position of the

lower strata. The same holds for the push towards a market economy and the opening of the economy. The first stems from a neoconservative conception of the economic role of the state and of its alleged inability to manage properly the economy. The second has the same origins complimented with the simplistic belief that it will lead to increased competition and thus consumers will in the end be better off. As it will be shown in the next chapter, these had the same negative effects as the first big idea. In this sense, the Washington Consensus is a perspective that dictated a policy prescription. Indeed, under its auspices, numerous reform programs were imposed—willingly or unwillingly—on less developed or developing countries.

The controversy about the definition established rightfully a meaning for the term. The actual content of a term is not given by the intentions of its founders but by the broader socio-political environment and the practical outcomes of the policies dictated by the term. On these grounds, it is overwhelmingly clear that in the 1980s and 1990s there predominated in official circles a current that considered as its main task the abolition of the state-run development policies and the restoration of the free operation of the market disregarding costs and special features of the developing economies. This current was clearly associated with neo-liberal theory and the Washington Consensus was its arm in the field of Development theory and policy. Consequently, the discussion of the concept cannot be constrained to the limited agenda of issues that its creator proposed but must encompass its whole spectrum of theory and applications. Williamson (2002) himself soon conceded the argument accepting that, from the time that the term became public property, its meaning is being set by the wider perception about it. Therefore, he declared that there is no meaning in struggling for the content of the term and called for an issue-by-issue discussion of the proposed policies.

WASHINGTON CONSENSUS AND ITS CONSEQUENCES

Besides the controversy on its definition, there is also a heated debate on whether the Washington Consensus promoted the development of developing and less developed economies or not. Today there is a widespread perception that it failed and that it led to crises and impoverishment. It would not be unfair to state that the term truly carries a bad reputation. This is accepted even by its defenders as, for example, by Naim (2002) who acknowledged that the Washington Consensus is a 'damaged brand name'. Criticisms and the concomitant bad reputation do not stem only from theoretical and ideological

opposition to the Washington Consensus but, most of all, from a series of persisting problems and crises that are, rightly or wrongly, associated with it.

Increase in Poverty, Inability to Catch-up and Social Upheavals

After the first years of implementation of Washington Consensus policies and reforms there was a growing sense, among friends and foes, that it failed its promises. More specifically, from the late 1990s and onwards, the Washington Consensus was facing major difficulties regarding a number of issues, which were not included in its declared objectives but are crucial for the development process. It was criticized for failing to organize a 'human face' adjustment process and, thus, for causing social upheavals. Additionally, it was criticized for failing to deliver significant advances in performance, let alone development. Several studies argued that its policies led to an increase in poverty and inequality both between developed and developing and less developed economies and within themselves. Additionally, the apparent inability of developing and less developed economies to catch-up the level of growth of the developed ones and, in many cases, the increase of the gap between them were attributed also to the policies instigated by the Washington Consensus.

The first criticism, 'adjustment with a human face', touched upon the many cases where reforms dictated by the Washington Consensus had led to abrupt changes and a disruption of social cohesion. The imperatives of the Washington Consensus' policies were usually implemented in a technocratic manner, disregarding social and political complexities. This, in return, created major problems and led to social and political upheaval. This was particularly true in cases of 'shock treatment' reforms.

The aforementioned criticism was also closely linked to the second one, i.e. the inability to exhibit an unambiguously better economic performance and to promote development. Issues of poverty, the environment, and of women's position, had been overlooked drawing criticism over both the desirability and the efficacy of adjustment policies. Of all these issues of particular importance came to be the rise in inequality and poverty (see Atkinson (1999a)).

For almost all critics, Washington Consensus' inability to address issues of poverty and inequality lays in its analytical perspective. The Washington Consensus held the view that poverty and inequality were problems of a secondary order, which more or less would have been alleviated once the market was free to operate undisturbed by the

impediments of ineffective state intervention. In particular, it was thought that if the domestic markets were liberated from any impediments, then the free operation of capital, domestically, but mainly internationally will provide all the stimulation and the efficiency necessary for feasible development (see Kozul-Wright & Rayment (2004)).

Against this market-fundamentalist presumption, most of the critics point out that during the last twenty years of the 20th century after the implementation of Washington Consensus' policies and structural changes there was a marked increase of poverty and inequality (see Chossudovsky (1997)). Critics coming from the Marxist Political Economy stream attribute this upsurge to the class nature of the Washington Consensus, i.e. that it is a set of policies that promotes capitalist interests and moreover the interests of big imperialist powers. Some mainstream critics argue that advocates of the Washington Consensus confront only the so-called 'traditional causes' of inequality (such as land concentration, dominance of natural resources, unequal access to education, and urban bias (in pricing policies, allocation of public expenditure and investment and so on)). For them, while such traditional factors were clearly responsible for the high-income concentration observed in the 1950s through 1970s and their persistence at a high level in the subsequent two decades, they cannot (with the possible exception, in some regions, of educational inequality) explain the widespread surge in inequality observed over the past twenty years of the Washington Consensus. Instead, several 'new' factors – such as technological changes with 'new technologies' generating a demand for skills and an earnings distribution more skewed than the emanating 'old technologies' – have had more relevance to the recent rise in inequality. This critique might be pertinent but it is beyond doubt that the Washington Consensus cannot address even the 'traditional causes' of inequality.

The Crises of the 1990s

The problems mentioned above were brought forward and emphasized in the mid-1990s after a series of crises in the developing world: the 1994-5 Mexican 'Tequila' crisis, the 1997 Asian crisis, the 1997-9 Russian 'Vodka' crisis, the 1998 Brazilian crisis and finally the 2000 Argentinean crisis. In all these cases, the Washington Consensus policy prescriptions were blamed since these crises happened while these countries were implementing its policies and structural reforms. A common feature of all these cases is that they ended up as exchange rate crises. However, it is also true that each case had its own specific characteristics.

In the first case, Mexico, the problems were caused by the attempt to open the economy and introduce financial liberalisation. This led to the collapse of the peso and the default of the Mexican debt. In the Asian case the crisis was caused by the attempts to conform to an international environment a-la Washington Consensus and at the same time to reform their internal structure away from the Asian developmental model and towards the Washington Consensus prescriptions. The crisis took again the form of an exchange rate crisis and led to abrupt abandonment of these reforms. The Russian case is different since it stems from the transition process towards a market economy. Shock adjustment policies, the opening of the economy and its increased financialization made it vulnerable to contagion effects of the Asian crisis. This caused the collapse of the stock market, subsequent devaluations of the rouble and finally the suspension of its convertibility. In the Brazilian case the attempt to introduce financial liberalisation backfired. The imposition of fiscal discipline by redirecting public expenditure towards other fields and the reform of the tax system towards Washington Consensus standards demolished the Brazilian fiscal and tax system. This led to an exchange rate crisis again. Finally, the Argentinean case encompasses all the features of the Washington Consensus prescription. It began with an ambitious plan of budget, trade and monetary reform and quite soon proceeded to a currency board, i.e. the pegging of the peso to the US dollar on an one-to-one basis. These reforms created serious problems in the economy and led to the biggest sovereign default in modern history.

A closer look to each of these cases will enlighten the inherent problems of the Washington Consensus prescriptions and the causes of its bad reputation.

The 1994-5 Mexican peso crisis could be classified as a Balance of Payments crisis. The rapid liberalization of domestic markets caused imports to grow much more rapidly than exports. Tight monetary policy to reduce inflation produced high interest rates, which attracted foreign capital inflows to deregulated and liberalized domestic financial markets, which financed the trade gap. It was attempted to introduce competitive exchange rates, which implied that domestic interest rates had to be liberalised. But this caused the real appreciation of the peso, which worsened further the trade balance by turning relative prices against exports. The capital inflows also encouraged import growth as foreign borrowing allowed domestic banks to compete for domestic market share by lending to households to finance consumption and to arrange foreign exchange loans to domestic business at international

interest rates. The result was continually increasing Mexican payments deficit, along with record increases in bank's non-performing loans, a fall in private savings and low domestic investment, with slow growth and rising unemployment accompanying a fall in the rate of inflation and a government budget surplus. In February 1994, the increase of US interest rates led to withdrawal of investors and, thus, to the collapse of the peso (i.e. the inability to keep its peg to the dollar) and finally to the default of the Mexican dept. However, the crisis would have occurred irrespectively of the reversal of US interest rate policy since the real appreciation of the peso would eventually have collided with the increasing external deficit, and Mexico would have experienced an exchange rate crisis that would have been aggravated by a domestic financial crisis due to bad bank loans to households and foreign currency exposure of business clients.

The Asian crisis of 1997 has been very different. Most of the countries engulfed in it (Thailand, Korea, Taiwan, Singapore, Indonesia and to a certain extent Malaysia) had no macroeconomic imbalances. Yet, there was a discernible tendency towards deterioration in foreign account caused by a fall-off in the rapid growth of exports in most countries. But, this was caused not by changes in what had until that time been successful internal stabilization policy (following the Asian developmental model), but rather by changes in the external environment (towards Washington Consensus standards), over which they had little control and there were few policy responses available. This is a characteristic of the world of increased economic interdependence and free global capital flows. Thus, unlike Mexico, it is impossible to argue that excessive domestic bank lending and real exchange rate appreciation led to a consumption and import boom which eventually created an expanding foreign deficit that speculators recognised as unsustainable since both the real exchange rate appreciations and the increased domestic bank lending occurred well after the beginning of the decline in trade balances and the increase in foreign bank lending. Rather, the process appears to have been the opposite. It was the rise in short-term bank inflows and the decline in the developed countries' demand in the presence of liberalization of domestic financial markets that led to the deterioration in the trade balance, which was then further aggravated by dollar appreciation and rapid domestic credit expansion. It is for this reason that the crisis was not a foreign exchange crisis caused by a payments imbalance, since there was no clear evidence that exchange rates were inappropriate. Reserves were extremely large, external balances were moving in the

right direction and official international agency assessments of country fundamentals suggested that the external positions were sustainable at existing exchange rates.

In the Russian case of 1997-9 the crisis followed a different path. Following the collapse of the Soviet Union, a transition process to a market economy was initiated. Policies of shock adjustment to a liberalised, privatised and open economy were systematically employed. The result was the tremendous transfer of wealth and resources to a handful of previously unknown foreign capitalists and to groups of previous managers. On the other hand the Russian economy shrank considerably and large segments of the population were impoverished. The opening and the financialisation of the economy brought foreign investors to the Russian stock market both for easy hefty returns and in order to diversify their portfolios. When the Asian crisis occurred in 1997 many of them withdraw from the Russian market in order to cover losses in Asia while the IMF made the same mistake it made in Asia, i.e. pressing the Russian government to go further to the liberalisation of the economy towards Washington Consensus standards. Thus, in June 18th 1998 it delayed a \$670 million tranche of a loan to Russia. After that the Russian government succumbed to the IMF demands and increased land taxes. Although the IMF released the loan and also gave an additional one, political and social tensions (e.g. a miners' strike) scared investors, who withdrew for a second time from the Russian market. This ultimately led to the fall of several governments and, despite initial refusals, to subsequent big devaluations of the rouble forcing – in the end – the suspension of its convertibility.

In the case of Brazil the whole affair was born out of the neoliberal fixation with hyperinflation which existed but, contrary to other Latin American economies, was not creating significant problems as the foreign account was not excessively imbalanced, the exchange rate was not overvalued, net public debt as a share of GDP was declining, and while low from historical perspective, its growth rate was on average above other economies in the region. Following the neo-liberal mandras active fiscal policy and the monetary control were abandoned and high real interest rates were used in order to stem hyperinflation. However, this reinforced hyperinflation by causing:

- a direct increase in the costs of capital since there was no long-term capital market,
- an increase in the government deficit, since the outstanding debt was directly linked to short-term rates.

- an increase in the rate of inflation through the impact on capital costs and on the fiscal imbalance.

The reinforced inflation spiralled into indexed inertial hyperinflation, and impeded the full development of private long-term capital markets. Thus when policies of market liberalization were introduced according to the Washington Consensus prescriptions - to replace the system of government directed development financing - there was no private sector market structure available to take its place. The financial system operated as a rentier on the float created by the adjustment lags in the indexing system of financial contracts. Indeed, there was hardly any long-term business financing to be done. Only the State continued to invest in any appreciable magnitude and this peculiarly Brazilian characteristic of efficient state financing of investment was under increasing attack from the rapid deterioration of government finances and the neo-liberal push towards increased liberalisation. Then the Real plan was introduced, which was in many respects similar to earlier reform plans (e.g. de-indexing of wages and prices, using the nominal exchange rate as the anchor for price stability). Nonetheless, interest rates continued to be the major instrument of economic policy. Its implementation had as a consequence the reversal of the exchange rate policy of the previous period from maintaining competitiveness through devaluation to maintaining competitiveness by creating pressure on domestic producers from foreign imports. Since it was difficult for domestic producers to adjust their costs rapidly; the real appreciation of the Real produced a growing payments imbalance in the new context of liberalised foreign trade. The foreign capital inflows that matched the growing trade imbalance also had an impact on fiscal conditions, since the Central Bank adopted a policy of sterilization of inflows in order to protect its inflation-fighting monetary policy. As result, the continued reliance on high interest rates reinforced the imbalances on the foreign and domestic (fiscal) accounts and reversed the economy from one of inertial inflation to tendential deflation. This ultimately led to an exchange rate crisis.

Notwithstanding, the Argentinean is the most characteristic of all the crises caused by the Washington Consensus prescriptions and, at the same time, the most severe one. Argentina is the country that most enthusiastically embraced the economic model promoted by the IMF and the U.S. Treasury: market liberalization, opening to foreign investment (particularly foreign direct investment) and a reduced role for the state in the direct production of goods and services, but also as a promoter of development. As such, for almost a decade Argentina

was promoted as a model showcase till December 2001 when it fell dramatically from grace. All started in 1991, when the finance minister Domingo Cavalho, under the auspices of the IMF, introduced his budget, trade and monetary reform plan. This was a series of economic shocks, followed by the subsequent introduction of a currency board, which had as its primary aim to fight hyperinflation and to stabilize the economy following the standards set by the Washington Consensus. The balancing of the budget was achieved first, through extensive privatisations, tax reforms, cuts in state expenditure, etc. The achievement of fiscal discipline was immediately followed by the tightening of monetary policy, which allowed for the introduction of the most revolutionary of all the reforms, a currency board linking the domestic currency, the Argentinean peso on a 1:1 basis to the dollar. The introduction of this parity aimed at anchoring permanently Argentine's monetary policy to the US, in order to make the former more credible both domestically and internationally with regard to the stabilization of the economy and permanent price stability. It was one of the first dollarisation experiments. However, the linkage of the peso to the US dollar and consequently directly to the US monetary policy, meant that the Argentinean monetary policy had to adjust towards the needs and aims of the American interest rate policy. As the Argentinean interest rates had to follow the US interest rates in order to keep the parity of the peso to the dollar, this put tremendous pressure on the domestic economy. As a result, exports fell dramatically while imports increased, business defaults increased, unemployment increased, government tax revenue fell dramatically, and a domestic debt-deflation process started affecting the banking system and increasing dependence on external capital flows in order to keep the currency board. The process ended by the end of 2001, when two interrelated events accelerated the crisis. Firstly, on 6 November, Argentina's sovereign credit rating was downgraded to 'sovereign default', following the decision of President Fernando De la Rúa's government to carry out a distressed debt exchange. This resulted in a panicky run on banks, which culminated in deposits decreasing by US\$1.8 billion on the single day of 30 November. On 3 December, the De la Rúa government imposed a freeze on bank deposits known as the 'corralito' ('little fence'). This severely limited the amount of money that could be withdrawn from banks accounts, and trapped many people's savings in failing banks. On 5 December, the IMF announced that it was suspending loans to Argentina because the De la Rúa government had failed to meet conditions on public-spending cuts,

and refused to disburse a scheduled \$1.3 billion Special Drawing Rights tranche needed to pay debt obligations and to support the currency peg.

The combination of these two events led to a process that brought the Argentinean economic, political and social system to the brink of meltdown, crystallizing a longer-term process of crisis. Widespread political unrest erupted as a result, and on 20 December, as the protests intensified, De la Rúa resigned. Argentina then went through five nominal heads of state in ten days. During this political turmoil, the dollar-peso parity was abandoned and Argentina defaulted on its debt of about US\$150 billion. The countrywide protests diminished after the fall of De la Rúa, but discontent has simmered on, particularly as the economy has gone into free fall. The Argentinean economy contracted dramatically, with GDP falling by a record 16% and manufacturing output falling by almost 20% in the first quarter of 2002, and industrial production in general by 17% during the first seven months of 2002. The currency collapsed to about one quarter of its original value, and inflation has spiralled. Unemployment has soared, public services have disintegrated, schools have closed, and state pensions and public sector workers' salaries have gone unpaid.

Williamson ((2004b) p.6, (2004a) p.11-12) makes an unconvincing attempt to divorce his definition of the Washington Consensus from the Argentinean fiasco. Although he praises the rest of the Cavalho reforms (and indeed Cavalho himself) he disavows (a) the imposition of a fixed exchange rate which became overvalued and, (b) the lack of an orderly fiscal system which made impossible the use of the surpluses of the boom years in order to bring down the debt/GDP ratio. Both arguments are weak.

The currency board was the way to rapidly control hyperinflation. Otherwise a more smooth process would have been adopted. The shock adjustment was chosen because otherwise the whole process might be derailed. The currency peg to dollar was hailed as a bold new attempt to push even further, more rapidly and beyond the point of return the Washington Consensus prescriptions. In this way the peso was supposed to acquire more credibility and since this other currency was the dominant international currency, to reflect the operation of an open liberalised economy. Thus, the exchange rate would be competitively determined without any state intervention or old 'Latin stratagems' (i.e. the silent devaluation of the currency in order to acquire trade competitiveness). Thus, its subsequent disavowal sounds as *ex post* sophistry. On the other hand, the fiscal system and the indebtedness of

the Argentinean economy got out of control not because of the lack of fiscal order or a high debt/GDP ratio but exactly because of the attempt to impose internal macroeconomic 'discipline' and external openness almost automatically through the currency board.

FRIENDS AND FOES OF THE WASHINGTON CONSENSUS

Three broad streams can be discerned regarding the evaluation of the Washington Consensus. The first stream encompasses its defenders and supports, critically or uncritically, its legacy. The second one stems also from neoclassical economic theory but assesses negatively the impact of the Washington Consensus and also disputes part of its analytical framework. This second stream is associated with the post-Washington Consensus argument. Finally, there is a third stream coming from Marxist and Radical Political Economy that not only assesses negatively the impact of the Washington Consensus but also adheres to a completely opposite analytical and ideological perspective.

Reformists and Fundamentalists

The supporters of the Washington Consensus are subdivided in two camps. The first one comprises of the fundamentalists that argue that the failures of the Washington Consensus were the result of faulty implementation and reluctant reformers (e.g. Krueger (2000), Franco (1999)). The second camp argues that there should be 'a reform of the reforms', i.e. that despite Washington Consensus merits it is necessary a reappraisal of its agenda (e.g. Kuczynski & Williamson (2003), ECLAC (1995), French-Davis (2000)).

For the fundamentalists both the neo-liberal character and the policy prescriptions are correct. What went wrong is the way they were applied. Thus, in pushing through the reforms careful consideration has to be given to state capacity, bureaucratic constraints and agency problems. Issues of effective governance and even 'second-best options' have to be taken into account. There is, however, a new element that creeps in their defence of the Washington Consensus. By focusing on these issues, they have to pay attention to the role of the institutions; an element rather alien to the pure versions of the neo-liberal approach.

However, a growing majority of the adherents to the Washington Consensus recognizes that its problems are much more serious than simply implementation errors. This approach has been enforced by internal disagreements within mainstream economics. The poor record of the Washington Consensus has caused significant uneasiness within the mainstream, which culminated, from the mid-1990s and onwards,

to a series of critiques (e.g. Fisher (2003), Krugman (1990), Rodrik (1992), Sachs (1987)). For these critics the original version is too rigid (by disregarding intermediate positions between the extremes of indiscriminate liberalization and arbitrary interventionism) and jumps to policy recommendations based simply on the maximization of liberalization. Thus, a search for a reformist version began. Several versions of this have been proposed ('reform of the reforms', 'augmented Washington Consensus' etc.). Williamson (2003, p.237) himself led this process by acknowledging that the results of even his definition of the Washington Consensus have been disappointing for three main reasons:

- (1) As proved by the series of crises, the Washington Consensus did not emphasize crisis avoidance. Additionally, it is guilty for reckless enthusiasm for capital account liberalization.
- (2) The reforms were incomplete, particularly regarding the labour market where dualism persisted. Also fiscal reform did eliminate budget deficits but did not foresee to create in good times surpluses as a buffer for bad times when deficit spending is required. Additionally, there was a disregard for reform of institutions and good governance.
- (3) The objectives of the reforms were narrow (simply to restore growth) without concern for employment, income distribution, poverty and other social issues.

However, he argues that these failures do not necessitate the abandonment of the Washington Consensus, nor giving socialism another chance or introducing industrial policy or closing the economy. For Williamson (2003, p.330), the way forward is to liberalise the labour market but in a civilized way, to improve income distribution and to recognize the role of institutions. He even plays down the differences with the post-Washington Consensus critics by arguing that their sole difference is that the latter presents its agenda as a repudiation of the WC whereas he argues for its continuation and reform. Similarly, Williamson (2004a, p.1) applauds – with minor corrections – Rodrik's (2002) Augmented Washington Consensus, despite the latter's explicit rejection of its feasibility (see Rodrik (2002, p.1)). Rodrik has argued that in the end of the 1990s emerged a revised version of the Washington Consensus, which augments the initial agenda with the following items:

- (1) Corporate governance
- (2) Anti-corruption
- (3) Flexible labor markets

- (4) WTO agreements
- (5) Financial codes and standards
- (6) 'Prudent' capital-account opening
- (7) Non-intermediate exchange rate regimes
- (8) Independent central banks/inflation targeting
- (9) Social safety nets
- (10) Targeted poverty reduction

In a similar vein, Ffrench-Davis (2000) and ECLAC (1995) offer a mixed account of the impact of Washington Consensus reforms on Latin American economies and argue for the need of a 'reform of the reforms'. For them, the initial reforms imposed macroeconomic discipline on local authorities, defeated hyperinflation, improved budget balances and fiscal savings and promoted exports. On the other hand, new imbalances were caused (particularly regarding the external sector), policies were too rigid and could not adapt to changes in the macroeconomy and social dimensions were neglected, thus causing social clashes.

To a large extent the reformists attempt to drop the overtly neo-liberal character of the Washington Consensus by attacking neo-liberal fundamentalism and arguing for a practical policy-oriented debate rather than ideological and general-theoretical controversies. They also emphasize the role of institutions—which is a shy alias to the state—and the importance of social issues (such as poverty and equity). They, therefore, concur—setting aside individual grievances—with aspects of the post-Washington Consensus thesis although they, usually, reject the label.

Post-Washington Consensus: A Critique from Within

The post-Washington Consensus thesis, launched in 1998 by Joseph Stiglitz, is the most ambitious attempt to resolve the Washington Consensus problems, from within mainstream economics. What distinguishes it from other mainstream critiques of the Washington Consensus is that it is sharply critical of the latter and that it is based on a differentiated analytical approach, the 'economics of information'. For Stiglitz (1989), there is no perfect information, as the neoclassical mainstream posits. Instead, informational asymmetries exist which allow for transaction costs and market imperfections. Thus, the definition of market imperfections is broadened and the argument for state intervention to mitigate them is reinforced. This contrasts directly

with the Washington Consensus, where the state is not seen as a corrective power. It contrasts also with the old Keynesian big government policies. The early Keynesian opposition to the Washington Consensus has often accepted the latter's terms of debate, i.e. to counterpose the state and the market and to favour state intervention whether in getting prices wrong, picking winners, or guiding the private sector through public expenditure. On the contrary, for Stiglitz (1998a, p.25) there cannot be a return to old Keynesian policies but the state must focus exclusively on what he calls fundamentals, i.e. economic policies, appropriate regulation, industrial policy, social protection, basic education, health, infrastructure, law and order, environmental protection. For him the question is not whether the state should or should not be involved, but rather the question of how it should be involved. His main argument is that the state is not anti-market force but a complementary one.

On this alternative analytical approach are based the 'New Development Economics' (Nobel (2001)) and the post-Washington Consensus, which emphasise history and institutions. Through the emphasis on institutions it attempts to bring the social dimension back into the analysis as the means of addressing, and potentially correcting, market imperfections. It also aims to differentiate itself from old Keynesian statism.

For Stiglitz (1994, 1998a, 1998b) the Washington Consensus fails because the simple liberalization of markets does not suffice for their normal operation, particularly in the developing countries. The existence of information asymmetries, that prevent markets from allocating resources efficiently, and the lack of complete and efficient institutional systems to mitigate these asymmetries are the causes of this failure. Thus, development policy should not aim only to the markets but also to the institutions. In a sense, the post-Washington Consensus shares the same agenda with its predecessor but with some crucial modifications. The removal of the constraints and controls on the markets and the international capital mobility and privatizations should be done through a smooth and gradual process and by taking into account the specific historical and social situations. Essential part of this process is the creation of new institutional regulatory frameworks that can guide, correct and control the market. Moreover, more room is allowed for discretionary and active policies. On top of all these, Stiglitz rejects the Washington Consensus monistic focus on fighting inflation and puts priority on the stabilization of output and the promotion of long-run growth (through education, transfer of technology and several

other channels that are being neglected by the Washington Consensus). Finally, he emphasizes the role of the financial system (the 'brain' of the economy) and argues that the aim should not be a liberalized financial system but a properly regulated and efficient one.

The Radical Critique: Capitalism's Structural Problems and the Developing Countries

There is also a more radical critique of both the Washington and the post-Washington Consensuses coming from the Marxist Political Economy. This approach follows a different analytical course by focusing on social classes and the struggle between them rather than on maximising individuals (as both Consensuses do). In this context the Washington Consensus is a vehicle for the exertion of imperialist dominance by the developed capitalist economies (and primarily the US) over the developing and less developed countries. Its set of policies advances the specific interests of these economies, which are similarly advanced with the so-called globalisation.

Thus, Shaikh (2003, 2004) disputes that trade and financial liberalisation promotes development, as both the Washington and the post-Washington Consensus (more qualified) believe. Empirically, the now developed economies have, in the past, systematically used activist and protectionist trade and financial policies in order to attain their present status and, in many cases, they follow them even today. Also, as even mainstreamers accept (e.g. Rodrik (2001), p.7), it has been proven that liberalisation policies do not lead to higher growth rates. Thus, the pressure to liberalise favours the developed over the developing by prohibiting for the latter to follow the path of the former. Shaikh, also, shows that these ill-guided policies stem from the erroneous orthodox 'theory of comparative costs' and he argues that an approach based on the classical theory of 'competitive advantage' is both analytically and empirically superior.

Similarly, Fine (2001a, 2001b, 2002) criticises the Washington Consensus for consciously neglecting crucial aspects of the development process in order to push the neo-liberal reforms that promote the interests of dominant capitalist economies. He also criticises the post-Washington Consensus for not being a true alternative to its predecessor and for, ultimately sharing the same analytical and policy agenda. Despite its vociferous opposition, it actually shares the same analytical foundations, namely methodological individualism, with the additionally flavour of the emphasis on informational asymmetries. This reductionism to individual behaviour,

even when supplemented with an emphasis on institutions, cannot grasp the social dimension and moreover class and power relations. Furthermore, despite again Stiglitz's newfound focus on history, it cannot grasp the qualitative dimensions of development and particularly its nature as a transition from one stage of development to another and reduces it to the arrangements required for dealing with market imperfections. Finally, Fine argues that both Consensuses are part of the same 'imperialist' attempt by orthodox economics to colonise fields (such as Economic Development theory), which have hitherto remain no-go areas.

On policy issues, Marxist economists argue that markets, instead of promoting stability and equality, are potential destabilisers and that free competition increases poverty and inequality. This holds especially for financial liberalisation and international capital mobility, which – as the experience of the 1990s reconfirmed – increase domestic financial fragility and trigger balance of payments crises. Additionally, financialisation drains resources that might have fostered the growth of production and employment and increases unproductively the returns of financial intermediaries. Finally, they claim that unbridled competition leads to the concentration and centralisation of capital and, thus, to the creation of national and international monopolies, which impose their interests on the poorer strata and the less developed economies. Ultimately, this process leads to growing divergence between economies, contrary to the orthodox beliefs. In terms of the domestic economy, the Washington Consensus' policies lead to adverse income distribution, since they put the onus on the poorer strata and they systematically erode workers' bargaining power (via greater wage flexibility, reduced regulation and minimum wages). Adverse income distribution worsens even more with privatisations (that make more costly the provision of utilities) and the erosion of the state's redistributive role (through regressive changes in taxation systems and the curtailment of public expenditure).

For the radical critique the way forward for the developing countries is neither the Washington nor the post-Washington Consensus. Instead, another developmental model is required in which the state must have an explicitly active role in promoting trade and industrial policies and positive income redistribution. Moreover, these new state economic functions should be democratically accountable and based on popular movements. Such an alternative developmental strategy would necessarily have to strive against hegemonical international economic relations.

DEVELOPMENT AS A SOCIAL PROBLEM

In the beginning of the 21st century the Washington Consensus is, nominally at least, dead. However, the way forward is far from obvious.

From a long-run point of view the world economy is still living in the aftermath of the 1973 structural crisis. The fact that since then almost all the crucial macroeconomic variables exhibit a rather dismal record is tantamount to that. This crisis ended the previous *modus operandi* of capitalism and called for a new architecture of the system. From the perspective of Marxist Political Economy, this was not a simple periodic overaccumulation crisis, but its structural character had to do with the exhaustion of the core elements (relation between paid and unpaid labour time, production and circulation processes, social and political edifice etc.). The first systemic attempt to overcome it followed the prescriptions of the then economic orthodoxy, i.e. Keynesianism. Thus, conservative Keynesian policies were employed. Their main feature was that they regarded the crisis simply as an underconsumption one and attempted to solve it via a contradictory reinforcement of demand. In particular, they resorted to austerity measures (where the curtail of any wage increases reduced workers' income and the labour cost and promoted profitability) and state policies (tax cutting, state orders and subsidies) that supported capitalist consumption and the demand between capitalist enterprises. These policies failed, in the long - run, because they weakened intra-capitalist competition, thus deterring the destruction of less competitive capitals.

Then followed the neo-conservative currents, first with their national (monetarism) and then with their internationalised (neo-liberalism) version. Some of their main features were the emphasis on the supply-side, the permission to competition to work unhindered, the withdrawal of the state from the economy and also its opening. The withdrawal of the state from economic activities created new spaces for capitalist profitability through the privatisations (seldom at basement prices). It curtailed also the ability of the working and popular classes to press for concessions and economic benefits. Together with the liberalisation of internal and external markets, it applied in all markets (including the labour market and for this reason neo-conservatism's attack on workers' position was much more severe than that of conservative Keynesianism) rules of strict competition. These permitted the full application of the clearing force of competition (the survival of the fittest)—with limited ability of the state to adulterate this process—as a means of overcoming the crisis. The Washington Consensus is the brainchild of these currents in the field of Development

theory and policy. As such it has similar merits but also suffers from similar deficiencies with its developed countries' blueprints. It has sustained capitalist profitability in the mid-run by providing new areas for investment, reducing labour wage and non-wage costs and clearing the economy from unviable individual capitals. On the other hand, by overemphasising the role of competition it fall to the naïve belief that simply the spontaneous action of individual capitals will suffice to return the capitalist economy to another 'golden era' of accumulation. However, there exist significant contradictions between individual and collective capitalist interests and for this reason the role of the state, as a 'collective capitalist', is necessary. Furthermore, the width and the depth of the capitalist restructuring required to surpass the structural crisis necessitates much more than the spontaneous action of the market forces. This is another reason why the state is required as a commanding centre, which will guide, motivate and correct the market.

These inabilities lie at the heart of the failures of neo-liberalism and of the Washington Consensus. Tantamount to that is the renewed emphasis—either by its supporters or by its mainstream critics—on the role of institutions. For these reasons both neo-liberalism and the Washington Consensus are virtually dated in the beginning of the 21st century and the search began for their successors. Social-liberalist trends appear as such a successor and the post-Washington Consensus is part of them. Their main trust is that they represent a rupture within the continuum of neo-liberalism. They built upon its successes but also strive to correct its deficiencies. Thus a new role for the state-headquarter is researched and also, in the face of serious social upheavals, a more sophisticated form of attacks on and compromises with the working class and the other popular classes.

However, this new emerging orthodoxy has its own deficiencies and, in the cases of the post-Washington Consensus, the radical critique is very accurate on that. In analytical terms, its critique against the Washington Consensus correctly pinpoints its non-social character and its inability to grasp the socio-political dimensions of the development process. However, this defect cannot be repaired by simply adding a role for the state and the institutions to combat market imperfections caused by informational asymmetries and conceived on the basis of methodological individualism. The socio-political dimensions of the development problem are far wider, cannot be grasped properly even by 'socialised' versions of methodological individualism and require more radical and rigorous instruments than simple institution-building. In a sense, where the Washington Consensus creates (or

expands) markets—and in some cases where this cannot be done it creates quasi-markets by imposing private-sector modes of operation—the post-Washington Consensus attempts to create quasi-societies as complements to the markets. It neglects that it is social and class interests that create institutional frameworks and rules—and sometimes even markets. Furthermore, the division in different social and class interests is not the result of more or less fleeting informational asymmetries but of more fundamental and deep-rooted socio-political factors. For all these reasons and despite the valiant critique of its proponent against its predecessor, it seems that the most that the post-Washington Consensus can offer is a compromise with the former. This is probably bound to produce similar dismal results with the Washington Consensus regarding the development process. The only area where it may have a limited success is in a form of *gatopardismo*—to borrow from Lucino Visconti's famous film: everything in the system has to be changed in order for the system to remain unchanged.

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