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## RECLAIMING DEVELOPMENT FROM THE WASHINGTON CONSENSUS

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### Abstract

This paper summarizes our new book, *Reclaiming Development: An Alternative Economic Policy Manual* [Chang and Grabel, 2004]. It begins from the premise that the view that there is no alternative to neo-liberal economic policies in developing countries is fundamentally and dangerously incorrect. The "no alternative" dictum has commonly been associated with popularizations (and arguably, misinterpretations) of Williamson's original statement of the "Washington Consensus." We demonstrate that feasible alternatives to neo-liberal policies exist that can promote rapid economic development that is equitable, stable and sustainable. Some of these are proposals for strategies not yet adopted. But many others have already proven their worth in practice across the globe. We offer them in order to shatter the idea that there is no alternative, and to contribute to the vigorous campaign now underway across the globe to "*Reclaim Development*."

Keywords: Washington consensus; alternative development policies; neo-liberal policy

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## 1. RECLAIMING DEVELOPMENT FROM THE WASHINGTON CONSENSUS

“There is no alternative.” This is the famous pronouncement by former British Prime Minister Margaret Thatcher when she was faced with widespread opposition to her program of radical neo-liberal reform during the 1980s. Thatcher’s dictum captures the triumphalism, hubris and closed-mindedness with which the neo-liberal orthodoxy (or “market fundamentalism” as Williamson [this issue] terms it) has dominated discussions of economic policy around the world during the last quarter of a century.

This paper summarizes our new book, *Reclaiming Development: An Alternative Economic Policy Manual* [Chang and Grabel, 2004]. It begins from the premise that the view that there is no alternative to neo-liberal economic policies in developing countries is fundamentally and dangerously incorrect.<sup>1</sup> As we demonstrate in great detail throughout the book, feasible alternatives to neo-liberal policies exist that can promote rapid economic development that is equitable, stable and sustainable. Some of these are proposals for strategies not yet adopted. But many others have already proven their worth in practice across the globe. We offer them in order to shatter the idea that there is no alternative, and to contribute to the vigorous campaign now underway across the globe to “*Reclaim Development*.”

The timing of both our book and this *JPKE* symposium on the Washington Consensus is propitious for three reasons. First, there is now abundant and increasing evidence that the economic policies associated with the neo-liberal agenda have failed to achieve their chief goals, and that the cost of this failure has been serious harm in the developing world. Second, there is a great deal of historical and current evidence that there are multiple routes to development. Indeed, most of the policies used by successful countries run counter to the policies advocated by neo-liberal economists today. Third, in the face of such evidence, some of those most closely associated with the Washington Consensus (and with neo-liberal policies, more broadly) have recently attempted to modify their position. The most notable examples include the much-cited IMF study cautioning against premature capital account opening [Prasad et al., 2003] and recent work by John Williamson, who coined the term, the Washington Consensus.<sup>2</sup>

We are, of course, encouraged by these recent efforts to rethink development policy. In particular, we are pleased that recent research by the IMF now recognizes, albeit some seven decades after John Maynard Keynes, that unrestrained flows of liquid international capital can lead to speculative bubbles and financial crises. We are also encouraged by acknowledgement, six or so decades after Karl Polanyi, that institutions, governance and distribution matter. But these insights, and this point bears emphasis, have not altered the content of Washington’s policy advice to developing countries in fundamental and practical ways.

In our view, this updated Washington Consensus--or what Harvard University economist Dani Rodrik [2002] aptly calls the “Augmented Washington Consensus”--seeks to save the core tenets of the original program from embarrassment and refutation by modifying a few of its less central policy prescriptions. For example, Kuczynski and Williamson [2003] emphasize that they do not reject the original Washington Consensus; they state that “the way forward is to complete, correct, and complement the reforms of a decade ago, not to reverse them” [2003: p. 18]. Indeed, the new thinking reaffirms and even extends the neo-liberal character of the original Washington Consensus in several

important policy domains, such as the increased attention that is paid to the promotion of labour market flexibility and the commitment to privatization.

This paper, and the book by Chang and Grabel [2004] on which it draws, seeks to provide real alternatives to the (original, augmented, or updated) Washington Consensus. Our goal is to “Reclaim Development” from the neo-liberal orthodoxy that has dominated discussions of development policy during the last quarter of a century.

We begin the paper by presenting and rejecting the six major “Development Myths” that are used to justify the neo-liberal policies that have been pursued with such disastrous results in the developing world during the last quarter of a century. Next we provide an array of concrete policy options that are superior to their neo-liberal counterparts.<sup>3</sup> For reasons of space, in this paper we can only present a handful of policy options within four distinct domains of economic policy. Interested readers should refer to our book, which discusses a much wider range of policy domains and provides theoretical, historical and empirical support for policy alternatives. We emphasize at the outset that we present these policy alternatives in the spirit of pluralism and humility. We do not share the hubris of neo-liberals, and therefore do not argue that there is an ideal, single set of “good” policies. We hope that our work serves as an antidote to the defeatism and fatalism found among many opponents of neo-liberalism who find it difficult to challenge these policies, believing that there are no credible alternatives.

## **2. THE MYTHS BEHIND THE CONSENSUS**

Advocating alternative development policies requires of us that we first articulate and reject what we term the six main “Development Myths.” These myths form the basis of conventional wisdom regarding the types of economic policies and institutions that are both appropriate and feasible for developing countries today. We will not go into much detail here for reasons of space, but rather will highlight the grounds on which we reject each of the myths.<sup>4</sup>

### ***2.a. Myth #1: Neo-liberal policy has succeeded over the past twenty-five years, while other regimes have failed.***

The reality is that neo-liberalism has not even promoted the economic growth that is supposed to be its primary achievement.<sup>5</sup> Average annual per capita income growth in developing countries slowed from 3% during the interventionist era of 1960-80 to 1.5% during 1980-2000. Indeed, the median rate of per capita GDP growth in developing countries over the last two decades was zero. Most disturbing is the fact that the poorest developing countries (defined as countries with per capita GDP from \$375-\$1,121) went from a modest 1.9% rate of per capita GDP growth during the interventionist 1960s-80s to a *decline* of 0.5% per year during the neo-liberal era. All told, countries at every level of per capita GDP performed worse on average during the neo-liberal era than in the two preceding decades.

Even these dismal statistics underestimate the failure of neo-liberalism. Growth rates in developing countries over the last two decades or so have been buttressed by the acceleration of economic growth in the two largest developing economies, namely China and India—countries that in no sense followed the neo-liberal formula. Moreover, the growth failures of neo-liberalism mean that it cannot even compensate for the other costs and dislocation that it introduces. These include an increased propensity to financial

crisis; increased inequality (both within and among nations); reductions in living standards; and an increase in the power of speculators and external actors (such as the IMF) in political decision-making.

***2.b. Myth #2: Today's wealthy countries achieved success through the free market.***

An impartial reading of the historical record indicates that today's industrialised countries pioneered and relied upon myriad interventionist industrial, trade and financial policies in the early and often in the later stages of their own development (for details, see chs. 7-11 of Chang and Grabel [2004] and Chang [2002]). Moreover, well-designed programs of intervention explain most success stories in the developing world over the past half century. Indeed, the performance of developing countries during the interventionist era was not only impressive in an absolute sense, but also relative to the performance of today's industrialised countries at a comparable stage in their development.

This is not to say that state intervention always works. There are cases where state intervention failed spectacularly. But when we look at the most dramatic success stories, the record clearly shows that development success is strongly related to interventionism of different kinds. Indeed, except for the case of Hong Kong, the East Asian "miracle" was engineered by activist "developmental states" that aggressively promoted economic development and financial stability (see Woo-Cumings [1999]). China and India have also developed successfully via strong state direction of economic affairs.

***2.c. Myth #3: While state-led development policies may have met with partial success in some countries in the past, today's global economy dictates that only neo-liberal regimes can succeed.***

The argument that the competitive pressures fostered by globalisation make it necessary for all countries to converge on the same neo-liberal economic model is contradicted by evidence of continuing institutional and policy divergence across national borders—a divergence that has confounded those analysts who associate globalization with convergence (Chang and Grabel, 2004: chs. 5, 7-11; see also Berger and Dore [1996]). This institutional heterogeneity is apparent among wealthy countries today. But we find it also in the developing world.

Larger and/or richer developing countries--especially China, India, Taiwan, and Malaysia--have also managed to maintain non-neoliberal policy regimes. To be sure, smaller and/or poorer developing countries confront more severe restrictions on their policy autonomy. But even these countries may enjoy greater policy autonomy than is generally recognized. Chile is an example of a developing country that pursued a generally neo-liberal path in the 1990s, but nevertheless managed to maintain a rather stringent regime of capital controls [see Grabel, 2003a; Chang and Grabel, 2004:ch. 9].

Neo-liberal globalisation is but one form of globalisation. Different policy choices (particularly, in relation to trade and financial policies) can create a form of globalisation that would not be so damaging to living standards and growth prospects in developing countries. It is the neo-liberal form of globalisation that is being promoted so aggressively today—and not globalisation itself--that is chiefly responsible for the poor economic performance and the deterioration of living standards in so many countries.

***2.d. Myth #4: Developing countries need the discipline imposed by international institutions and by politically-independent domestic institutions (such as independent central banks) in order to keep them honest.***

The neo-liberal view of the inherent corruption and/or incompetence of the government has done much to generate—rather than simply reveal—a virulent distrust and denigration of the government and public officials. The historical record shows that state intervention has played an essential, positive role in the development process. Moreover, placing policy-making authority in the hands of unelected technocrats runs counter to the principles of democracy, accountability and transparency. Evidence also shows that this strategy does not even improve long-term economic performance [for evidence, see Chang and Grabel, 2004: ch.11].

***2.e. Myth #5: The East Asian model of development cannot be replicated in whole or in part because its success depended on the unique historical, political and cultural conditions of the region. In contrast, the Anglo-American model is universally applicable and sustainable.***

Arguments that emphasize the role of unique internal and external factors in the success of the East Asian model range from exaggerated to incorrect. Most of today's wealthy countries utilised an economic model that is far closer to the East Asian model than it is to the contemporary Anglo-American model. Moreover, the specious special conditions argument could just as easily be invoked to explain the economic success of the USA and the UK. Indeed, the success of the Anglo-American model depends on specific institutional and regulatory preconditions. Absent these prerequisites, the Anglo-American model cannot function properly.

***2.f. Myth #6: The Anglo-American model of capitalism represents the ideal that all developing countries should seek to replicate.***

The American triumphalism that solidified during the economic boom of the 1990s is based on wishful thinking rather than on a careful, objective analysis. There are many reasons to reject claims for the superiority of US capitalism, particularly in regards to its performance during the 1990s (and since). Even the most strident advocates must acknowledge that US economic performance during this period was not very impressive compared to previous booms. Moreover, many other industrialised countries performed as well or even better than the USA during this period. Finally, other Anglo-American economies also fared poorly during the 1990s. The case for exporting the Anglo-American model to the developing world is, in a word, under-whelming.

### **3. DEVELOPMENT POLICY OPTIONS BEYOND THE WASHINGTON CONSENSUS**

The heart of our book presents a discussion of alternative economic policies for development. While this discussion is not exhaustive, we do focus on those policy domains where new thinking is most urgently needed, and where there exists sound and feasible alternatives to the neo-liberal policies that have been promoted so forcefully over the last two decades.

We look specifically at policies toward trade and industry, privatisation and intellectual property rights, international private capital flows, domestic financial

regulation, and macroeconomic policies and institutions (namely, currency and exchange rate policy, central banking and monetary policy, and policy toward government revenue and expenditure). In each case, we explain why the neo-liberal policy recommendations in these domains have failed, often with disastrous consequences for developing countries. We then counterpose an array of alternative policies that can promote faster economic development than can neo-liberalism, while ensuring that the development that is promoted is equitable, stable and sustainable. For reasons of space, we present in what follows examples of policy alternatives in four policy domains.<sup>6</sup>

### ***3.a. Policy options with regard to domestic financial regulation***

We argue that domestic financial regulation in developing countries should be guided by one fundamental consideration: the financial system should provide finance in adequate quantities and at appropriate prices for investment projects that are central to sustainable, stable and equitable development. All financial reforms should be evaluated against the extent to which they contribute to this aim. We submit that the most important way in which the financial system can serve appropriate economic development is through the provision of long-term finance as it is necessary to the success and viability of most projects that are central to economic development (such as investment in infrastructure and the promotion of infant industries). Any proposed financial reform should be evaluated based on its ability to contribute to the provision of long-term finance, a characteristic that James Tobin [1984] called “functional efficiency.”

The goal of finance in the service of development and the performance criteria of functional efficiency can be operationalized in a number of ways. Government influence over the price and direction of bank lending to key sectors was central to industrial development in Continental Europe, East Asia (especially Japan), and a number of other developing countries (e.g., Brazil). Government influence over loan allocation may also involve the establishment of lending targets at the sectoral level that are imposed on private, quasi-private or publicly-controlled banks. Alternatively, the government can use the tax system to influence bank lending. Tax incentives can encourage banks to lend to strategic firms or sectors. A system of lending targets or tax credits can ensure that bank lending supports certain social and economic goals. Specialized lending institutions can also be established to serve particular goals. These might include developing certain ‘strategic’ industries, encouraging female and/or minority entrepreneurship, supporting the development of small- and medium-sized businesses, or promoting the development of new technologies.

Another means of ensuring the provision of stable, long-term finance to particular sectors/firms is through the creation of development banks that specialize in long-term financing. Development banks can be publicly financed and managed as in Brazil and Korea, or can be privately financed as in the case of German industrial banks. It is also conceivable that these banks could be organized as a public-private hybrid, and could raise capital on international markets and even from private sources. Development banks are the institutional counterpart of the industrial policies and public investment programs that are critical to late development, as the experiences of several countries suggest. Evidence shows that development banks and other specialized banks can be managed and regulated effectively. The challenges of effectively managing these institutions are

neither greater nor lesser than those associated with managing private banks in a liberalised environment.<sup>7</sup>

A system of variable asset-based reserve requirements for financial firms (discussed in Palley [2000]) can also serve development goals. Variable asset-based reserve requirements provide regulators with a means to affect the mix of financial assets that financial institutions hold. Variable reserve requirements may be used to target sectoral imbalances involving over-investment in some sectors and under-investment in others. In this way, the financial system may be put in service of industrial policy goals. A system of variable asset-based reserves can also reduce the risk of financial crisis by allowing regulators to deflate bubbles in particular asset markets as they emerge and before they culminate in financial crisis.

Policymakers may wish to embark eventually on a limited program of domestic financial liberalisation, particularly once the country's initial industrialization and growth objectives are attained. In this connection, a few things need to be considered.

First, the success of liberalised financial markets depends on numerous prerequisites, many of which are not met in developing countries and cannot be transplanted easily. The financial history of industrialised countries also shows that a sound financial and regulatory infrastructure cannot be created overnight [Chang, 2002, ch. 3, for details].

Second, policymakers should adopt a cautious stance on liberalization in the sense that they liberalise only when the benefits are unambiguous and cannot be reasonably achieved through any other means. For example, liberalised capital markets have provided a greater volume of finance to “start-up” enterprises than have more regulated systems. But this does not mean that financial liberalisation is the only way to ensure the provision of finance to these enterprises. Public investment, lending targets, tax credits, specialized lending institutions and variable asset-based reserves may all be used instead.

Finally, we argue that particular caution is warranted in two areas: the promotion of stock markets (where they do not exist or where they are thin) and off-balance sheet activities such as derivatives. *If* stock markets are to be promoted at all, significant resources must be committed to minimizing their risks, narrowing the scope of their operation, and in ensuring that other segments of the financial system serve developmental objectives. Off-balance sheet activities are even more problematic, given their non-transparent nature and the high degree of risk introduced by them.<sup>8</sup> We argue that accordingly these activities have no place in developing countries.

### ***3.b. Policy options with regard to foreign bank borrowing***

It would be of significant benefit were policymakers to enforce strict ceilings on the volume of new foreign loans that can be incurred by domestic borrowers. Ceilings might involve strict limits on the allowable ratio of foreign to total loans, or might mandate that each firm can finance only a certain percentage of its projects with foreign loans that have a certain maturity and/or locational profile. Alternatively, restrictions on foreign borrowing could be deployed dynamically and temporarily as circumstances warrant, following what Grabel [2003b, 2004] has termed the “trip wire-speed bump” approach to managing financial risks.

Taxes can also be used to discourage domestic borrowers from incurring foreign debt obligations (as in Chile and Colombia during much of the 1990s, see Grabel 2003a).

Domestic borrowers might pay a fee to the government or the central bank equal to a certain percentage of any foreign loan undertaken. Loans that involve a locational or maturity mismatch would incur a higher surcharge. Alternatively, the surcharge might vary based on the level of external indebtedness of the particular borrower involved, such that borrowers who already hold large foreign loan obligations face higher surcharges than do less-indebted borrowers. Another strategy might involve varying the surcharge according to the type of activity that was being financed by foreign loans. For instance, borrowers might be eligible for a partial rebate on foreign loan surcharges when loans are used to finance export-oriented production.

Careful management of the allocation of foreign debt can ensure that it is used for productive, developmental purposes. Prior to financial liberalisation in the 1990s, many governments in East and Southeast Asia tightly coordinated allocation and access to foreign loans. Policymakers in China and India today continue such practices [for details, see Epstein, Grabel and Jomo KS, 2003].

Economic reforms that increase the pool of domestic finance could replace at least some of the finance that is forgone by restrictions on foreign borrowing. In this connection, measures that restrict the exit options of domestic savers and businesses would increase the pool of capital available domestically (since so much of it is presently lost to flight). The coordination of industrial policy and domestic financial regulation can also ensure that domestic firms have access to capital that is generated domestically (on industrial policy, see Chang and Grabel, 2004:ch.7). Tax reform is yet another means of increasing the domestic resource base (see below). More generally, many of the economic policy reforms that we discuss throughout the book are intended to generate higher levels of investment and economic growth. If these reforms are successful, the economy in the medium- to long-term will generate new resources that can be used to finance additional investment.

### ***3.c. Policy options with regard to foreign direct investment***

Governments in developing countries should maximize the potential for FDI to promote economic, and especially industrial, development by creating employment, increasing living standards, promoting the transfer of knowledge and technology. The historical and empirical record reveals that there are many different paths for achieving this aim [Chang, 1998; Chang & Green, 2003]. The ability to manage FDI and other TNC activities depends on several factors, such as the host country's relative bargaining position (which itself may depend on country size), the technological nature of the industry, and the importance of the particular firm or industry in the government's overall national development vision.

FDI policy stands the best chance of achieving developmental objectives if it is firmly tied to national development and/or industrial policy plans. Countries like Korea and Taiwan are known to have used strict regulation on FDI in most industries, while also taking a very liberal attitude towards FDI in others. This mixture of restrictive and liberal policies was possible because the governments developed a clear FDI strategy that differentiated among industries. The recent experiences of Singapore and Costa Rica show that policymakers can target the attraction of particular types of FDI (or even target particular firms) as a central part of their industrial or development strategy (as discussed in Chang and Grabel [2004:ch.7]).



The precise strategy toward FDI should depend on the nature of the FDI that is being sought, the country's endowments, and the goals of the country's industrial policy regime. Some countries, especially the poorest ones, may have rather narrow goals for FDI, seeking only an infusion of foreign capital that will increase employment (under any terms) and foreign exchange earnings. The garment industry, shoe production, and toy manufacture often function in this limited, but in some cases, economically important capacity. In such cases, it may be acceptable--or even important--that the country maintain a relatively liberal attitude toward FDI because the industries are seen strictly as a "cash cow." Many countries have established export-processing zones for the purpose of attracting FDI to these types of industries. However, it should be noted that cash cow industries tend to be "dead ends" in the long run. Therefore policymakers need to devise a strategy to reinvest the export earnings generated by such industries in order to generate new industrial (and exporting) capabilities.

In some countries and in some industries, the government may find it necessary to induce foreign investors to undertake expensive investments in capital equipment and technology. These types of foreign investments can sometimes be a precondition for using the country's natural resources because the technology necessary to exploit them is not always available domestically. In this context it may be necessary to adopt an FDI strategy for this sector that is attractive to foreign investors, but which nevertheless allows the host country to extract the largest possible "rent" from their own natural resources. Carefully structured joint-operating agreements have worked well in some countries.

In some cases, the government may seek to promote certain industries as part of an industrial policy plan aimed at creating long-run international competitiveness in some realm. At the early stages this might necessitate a major injection of new technology and capital, a circumstance that necessitates TNC participation. In this type of situation, it is important for the national government to negotiate with TNCs over technology transfer and to prevent TNCs from imposing restrictions on export and R&D. These matters were rather well negotiated in the cases of the Chinese auto industry and the Korean fast train project in the mid-1990s.

Finally, in those cases where the country is reasonably close to achieving international competitiveness in a particular industry, it may be necessary to exclude TNCs altogether. This is especially important where the domestic market is small. This restriction may be necessary so that local firms have the greatest possible opportunity to develop their competitive advantage.

The main point is that there is no single appropriate strategy for all types of FDI and TNCs and for all types of countries. Each industry serves different functions in the greater scheme of industrial development. Policies towards FDI and TNCs must be tailored to the particular conditions of each industry and each country. FDI and TNC policy must be dynamic so that policy evolves as internal and external conditions change.

Of course, it is one thing to say that countries should use TNCs in a strategic manner, and it is another to say that they can actually do so. Developing countries that are extremely poor, small or poorly endowed with natural resources hold far less bargaining power than countries with better "initial conditions." This is especially the case because poorly endowed countries are often most attractive to precisely those industries where capital mobility is highest (such as garment production).

On the other hand, many developing countries do have some bargaining power, at least in relation to some industries. Some countries offer the prospect of a large and/or rapidly growing domestic market. Examples of such countries are China, India, Brazil, and the rapidly growing East Asian countries. A large and/or rapidly growing market is particularly important in industries where transportation costs are relatively high and/or where proximity to the desired market is important.

Another element of bargaining power that is possessed by some countries is the presence of a well-educated, well-trained workforce (relative to its wage level). Notably, the formerly and presently Communist countries of Eastern Europe, Vietnam, and China, are best situated in this regard thanks, somewhat paradoxically, to their Communist legacies.

Location is another advantage possessed by some developing countries. Countries that have the locational (and legal) advantage of easy access to large markets with rich consumers are also well situated to negotiate with some foreign investors. The bargaining power of Mexico is increased by its proximity to the USA (and its NAFTA membership), and that of the Central European countries (such as the Czech and Slovak Republics, Poland, and Hungary) is enhanced by their proximity to Western European countries and their recent EU membership. The possession of rare, strategic or otherwise valuable mineral and other natural resources also enhances bargaining power.

Needless to say, a developing country will be in the best position to exercise its bargaining power if its economy is on solid footing in the first place. In this connection, it is important to pursue appropriate economic policies in the many realms that are discussed throughout part III of our book. It is also critical to have a government that is internally coherent and is politically and administratively capable of exercising its bargaining power vis-à-vis foreign investors and other actors.

### ***3.d. Policies options with regard to government revenue and expenditure***

The obsession with fiscal restraint (and even more so, with budget balance) is clearly inappropriate in the context of economies that have vast social ills and low (or even negative) rates of economic growth. Developing countries cannot afford excessive fiscal restraint and have no reason to focus on budget balance as a key policy objective in itself.

Cross-country and historical experience show that strategic, well-designed and well-managed programs of public expenditure are critical to the promotion of economic growth, investment and the alleviation of important social problems. Studies find that growth is strongly correlated with public investment in transportation and communications, and expenditures on health services and primary education promote growth while reducing poverty [Easterly and Rebelo, 1993]. The experience of numerous industrialised countries—let alone the East Asian NICs--underscores the importance of government expenditure on industry, agriculture, infrastructure, and social and educational programs.

Clearly, a program of growth-promoting public investment and ameliorative social expenditure must be tied to the generation of additional tax revenue and the reduction in tax evasion. There are several avenues that policymakers might consider in this regard.

A first avenue for increasing tax revenues involves carefully examining the revenue implications of economic policy changes, such as trade and financial liberalisation [Toye,

2000; Khattry and Rao, 2002]. For instance, the tax holidays granted to TNCs (especially in export-processing zones) deserve serious examination in light of their costs to the tax base. Recent research suggests that companies invest where growth prospects, the human resource base and other conditions are propitious—not where taxes are low.

A second avenue involves reducing the opportunities for tax evasion by wealthy individuals via capital flight and by domestic and foreign corporations (via ‘transfer pricing’ and other practices). Capital controls that are supported by foreign banks and multilateral institutions could reduce capital flight, and thereby reduce its effect on the tax base.

A third avenue for increasing tax revenues involves redesigning the value-added tax (VAT) so that income taxes are replaced with a *progressive* VAT that exempts purchases of basic needs and wage goods and imposes a heavy tax on the purchase of luxury goods [Toye, 2000]. Evidence shows that VAT systems are more “revenue productive” than are income-based tax systems because they are more difficult to evade. The greater revenue productivity could go a long way towards reducing the constraints on public expenditure that stem from difficulties with tax collection in developing countries.

A fourth avenue for raising revenue involves introducing taxes on speculative activities, including short-term currency and stock trading and short-term international private capital flows. National tax authorities could collect taxes on stock transfers and on short-term international capital flows, though it should be noted that such taxes are relevant only to middle-income developing countries where stock markets are sufficiently deep and where international private capital inflows are significant [Grabel, 2003c]. International bodies, such as the UN, could collect taxes on currency speculation and redistribute the proceeds of such taxes to developing countries (or use them to finance important global development programs) [Nissanke, 2003].

#### **4. OBSTACLES AND OPPORTUNITIES FOR RECLAIMING DEVELOPMENT**

We have demonstrated that a number of alternative economic policies are available that can generate more rapid, equitable, stable and sustainable development than has been achieved by neo-liberal policies over the last twenty-five years. The appropriateness of any particular policy depends on specific national conditions, such as resource endowments, the scarcity of foreign exchange, proximity to key markets, social and political conditions, etc.. Through this work we hope to have challenged the triumphalism that has surrounded the neo-liberal agenda.

Unlike many aspects of the neo-liberal policy agenda, the alternative economic policies that we articulate have a sound basis in economic theory (see also the essays in Chang ed. [2003]). Moreover, in most cases, they are supported by historical evidence relating to the development strategies and trajectories of today’s wealthy countries and/or by the recent experience of several developing countries. Of course, no track record can be invoked in support of some of our policies that are more innovative or experimental in nature. But we maintain that the vast challenges facing developing countries today make it all the more important that policymakers think more creatively about policy options.

We are well aware that some might respond to this work by arguing that the changing rules of the global economy over the last quarter of a century have made some of the alternative policies that we discuss difficult (or even impossible) to implement in developing countries. The skeptical reader would rightly invoke the pressures that

emanate from the IMF, the World Bank and the WTO, various international agreements (such as free trade agreements), donor governments, private international lenders, and the portfolio investors. We certainly do not deny the severe constraints that these actors have introduced in the developing world. *However, we maintain that it is both fatalistic and incorrect to act as if this power and influence are absolute and unyielding.* If so, then surely there is little hope for today's developing countries.

It is imperative that advocates of alternative economic policies do not take the rules of the current global environment as fixed. It is always possible, and is certainly necessary, to re-write the global rules. This is not easy, especially in a world dominated by an increasingly unilateralist US government. However, re-writing the rules should not be seen as an impossible task. By now, long-standing critics of neo-liberal policy in the developing world (and elsewhere) have a vast arsenal of evidence to support their case against this failed policy regime. We are encouraged by the number and strength of new cross-border social movements opposed to neo-liberal, corporate-led globalisation and anti-democratic multilateral institutions and agreements. We certainly hope that our work contributes to the conversation among policymakers and activists about positive and practical alternatives to neo-liberal policy.

At the present juncture, long-standing critics of neo-liberal policy may find that they share some common ground with those who have recently become disillusioned with aspects of the neo-liberal agenda. For example, it is now fairly uncontroversial that developing economies should not liberalize highly liquid international capital flows; that privatisation programs should not simply transfer resources from one group of insiders to another; and that preventing tax evasion is at least as important as expenditure reduction in the face of budget deficits. These areas of agreement can and should be exploited in discussions of policy whenever possible.

Moreover, it is equally important to acknowledge that many of the alternative policies that we discuss can be employed *even without radical changes in the global environment*. A great many of the policies that we discuss in our book have been employed successfully (and without penalty from international investors or lenders) in the recent past or are still in use today in some countries. For example, many (although not all) of the strategies toward investment and financial flows that we discuss are not specifically prohibited by the IMF today. It is also the case that a country's policymakers may find it possible to combine neo-liberal policy in some part of the economy with alternative policies in other domains. For instance, policymakers in small, poor countries might establish a free-trade zone that welcomes unregulated FDI in certain industries in order to earn foreign exchange, while simultaneously pursuing restrictive policies over FDI in other sectors of the economy (such as requiring domestic sourcing of inputs or technology transfer) in order to promote technological advance.

Policymakers across developing countries can also work collectively to increase their ability to pursue alternative economic policies. In this connection, regionalism and/or bilateral economic agreements among developing countries can be an important way to increase bargaining power vis-à-vis external actors, especially in the case of very poor and/or very small countries [DeMartino, 1999]. Moreover, policy coordination across developing countries might reduce the costs and risks of policy experimentation. For instance, the coordinated use of capital controls might reduce financial instability with the effect of increasing capital flows to all developing countries [Gabel, 2003a]. In

this connection, larger developing countries that have had positive experience with alternative policies have an important leadership role to play in advocating for new regimes.

The hope for more rapid, equitable, stable and sustainable development has been too long deferred by economists and policymakers who are so wedded to the neo-liberal orthodoxy that they can neither imagine nor countenance any alternative. They have pursued the neo-liberal agenda with extraordinary single-mindedness and even hubris. The effect has been devastating: in the wake of the neo-liberal experiment, we find extraordinary misery, inequality and despair on a scale unknown in recent human history.

Fortunately, Margaret Thatcher was wrong. There are alternatives—an abundance of alternatives, in fact—that can deliver a more desirable form of economic development. We have presented some of these alternatives here, in hopes of solidifying this claim.

The need to “Reclaim Development” has never been more pressing. We offer our work as a small contribution to that task.

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### Endnotes

<sup>1</sup> The "no alternative" dictum has commonly been associated with popularizations (and arguably, misinterpretations) of Williamson's [1990] original statement of the "Washington Consensus." See his paper [this issue] for discussion of what he means by the Washington Consensus and what he sees as the distinction between this term and neo-liberal policies.

<sup>2</sup> Williamson [1990] is the original statement; modifications to the original work appear in Kuczynski and Williamson [2003] and in his article in this issue.

<sup>3</sup> We agree with Williamson that it is critical that national policymakers in developing countries are informed about policy options, and that it is not within our charge to "tell countries exactly which reforms are needed, or most urgent, or how they should be done...[t]hose are tasks for national policymakers, whom we aim to assist, but not absolve from thinking..." [this issue, p. 14]. However, unlike Williamson, we are certain that there are numerous feasible and desirable alternatives to neo-liberal policy [cf. Kuczynski and Williamson, 2003: p. 18]. In this connection, we note the transparent rhetorical maneuver to insulate his new work from criticism by dismissing his detractors as relics from the "old left [Williamson, this issue, p. 13]. In contrast to Williamson, we are appreciative of the critiques of neo-liberalism that have emanated from the left—but we note that many of the most powerful critiques that have emerged in recent years have come from economist that even Williamson would have to recognize as entirely "respectable." We note finally the close-mindedness reflected in his statement that it is a matter of "intellectual apartheid" to claim that the needs of developing countries are such that they call for different policies than do OECD countries [Williamson, this issue, p. 13]. It bears notice that this sentiment is also incorrect in terms of what it presumes about industrialized countries and what it infers from this presumption about the developing world.

<sup>4</sup> The intellectual foundation and rejection of each of myth (along with requisite citations to the literature) appear in chs.1-6 of our book.

<sup>5</sup> Data in this and the next paragraph are from Weisbrot et al. [2001].

<sup>6</sup> See part III of our book for discussion of the theoretical, empirical and historical foundations of these and other alternative policies.

<sup>7</sup> Moreover, as Singh and Weisse [1998] argue, the resources used to create a liberalized financial system would be better spent in ensuring the appropriate and sound operation of a financial system that operates in the service of development.



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<sup>8</sup> See Dodd [2002] for discussion of transparency and other aspects of prudential financial regulation vis-à-vis derivatives in developing economies.