UNRISD United Nations Research Institute for Social Development

CONFERENCE NEWS

The Need to Rethink Development Economics

Report of the UNRISD Conference
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Contents

This conference, a joint undertaking of UNRISD and the Ford Foundation, brought together 29 social scientists, mainly economists and activists, from developing and industrialized countries to exchange ideas on an alternative to the neoliberal approach to development issues. Participants shared views on how economics can serve to empower the South and on how to revive development economics—not as a deviant branch of mainstream economics, but as a discipline whose role is to address the vital problems that developing countries typically face. UNRISD has embarked on a research project on Social Policy in a Development Context and is thus keenly interested in what is happening in the various fields of development studies.

Conference participants prepared short papers on the following themes, which structured their discussions during the meeting:

- the decline of development economics;
- current intellectual trends;
- new challenges;
- regional perspectives; and
- strategies and future activities.

This report is based on both oral presentations and written contributions. The conference papers and participants are listed at the end of this report.

THEME ONE
The Decline of Development Economics

In their exchanges during the first session, conference participants analysed the reasons for the demise of development economics during the late 1970s and the 1980s. This provided the background for their subsequent discussions of why its revival is currently being urged or contemplated.

The crisis of Keynesianism

Up until the 1970s, problems of welfare and unemployment in developed countries, and those of poverty and underdevelopment in developing ones, were interpreted through the lenses of Keynesian economics and "development economics", respectively. The presentations by Jayati Ghosh, Thandika Mkandawire, C.P. Chandrasekhar and Erinç Yeldan served to remind participants of the central tenets and preoccupations of development economics. In his background paper, Mkandawire argued that although there were few analytical commonalities between the Keynesian doctrine and that of development economics, the two approaches shared both critical views of neoclassical economic theory and acceptance of state intervention. They also had in common the assertion that the economy described by neoclassical economists was a "special case", and there were many other economies that could be "stylized" by entirely different models because they were characterized by different structural features. Furthermore, they shared the view that the state could play an important role in addressing these structural features, which often resulted in "market failures". Both were motivated by the need to solve policy problems through theoretical modelling that was based on the real experiences of economies trapped in a particular equilibrium (unemployment or underdevelopment) from which they had to be extricated.

Development was understood as self-sustaining growth accompanied and driven by structural change in patterns of production and consumption, and technological upgrading. It involved social, political and institutional modernization leading to widespread improvement in the human condition. Both Keynesian economics and development economics proposed that markets were by no means benign, and that state intervention and public action were prerequisites for full employment and development. The task of development economics included helping to define both the role of the state and the nature of public action in the pursuit of particular goals in specific contexts. This led the discipline to define a terrain of its own, separate from economics. Development economics, argued Chandrasekhar, was concerned with understanding specific structures, global and national, generated by the process of integration of economies with varying initial conditions into the world capitalist system. It was interested in analysing the mechanisms by which those structures constrained the process of development, and with deriving from that analysis the policy options available to address the adverse consequence of integration. Several participants highlighted the wide range of strategies devised and pursued in different countries. And in retrospect, they claimed, the policies produced what was a "Golden Age" of capitalism in quite a large number of developing countries, at least when compared with the anaemic growth rates of the 1980s and 1990s.

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The oil crisis, "stagflation" and subsequent indebtedness of developing countries severely tested the models and theories that had underpinned welfare and development policies. This led to a resurgence of neoliberalism, which called for reining in the state and greater reliance on the market. Given the perceived affinity of development economics with Keynesian economics, it is perhaps not surprising that the neoclassical counterrevolution and the ascendancy of monetarism in advanced industrial countries led also to the rejection of development economics in the South.

From the perspective of neoliberal economists, development economics falsely denied the universality of rational economic behaviour and, by focusing on market failure, opened the door to dirigisme. For some, the whole enterprise of development economics was a futile one, and the dirigisme associated with it was squarely blamed for poor economic performance. For example, the failure of import substitution industrialization in a number of countries (often as a result of failures to move toward more competitive structures, and to respond to external pressures) was blamed on the interventionism associated with development economics.

Roy Culpeper suggested that the decline of central planning in Eastern Europe and the former Soviet Union also served to further strengthen the case against development planning and interventionism in general. In contrast, Vladimir Popov suggested that the opposite might actually be true. By the time central planning collapsed, development economics was already in decline. Moreover, the experience of the East Asian Tigers could have been used to bolster the case for development economics, if it had been presented as evidence of success of the policies associated with that paradigm. The reason why neoliberal economics became so popular during transition in the former Soviet Union and Eastern Europe, he asserted, was precisely because development economics was in decline. Had development economics offered enlightening approaches to policy and development issues at the beginning of transition, the process would probably have looked different. Ninety per cent of all the policies implemented during transition were neoliberal "shock therapy". The current interest in development economics in the former Soviet Union and Eastern Europe thus stems, in part, from the fact that the neoliberal doctrine, as applied and tested in transition economies, has yielded poor results. This is a complete failure not of development economics but of conventional economics.

Aside from the attribution of the causes of the crisis of the 1970s and 1980s to policy errors and the ideological ascendance of neoliberalism in the leading countries and financial institutions of the Organisation for Economic Co-operation and Development, the demise of development economics also had a lot to do with a widely accepted interpretation of the development experience of the postwar period. Up until 1997, the spectacular economic performance of the East Asian Tigers stood in stark contrast to the poor performance of most countries in Latin America, Asia and Africa, and the transition economies. As with all successes, their admirable performance elicited many claims of paternity. The neoclassical counter-revolution claimed that their success was evidence of the wisdom of relying on market forces. In contrast, the "lost decades" of much of Africa and Latin America were attributed to "development planning", which distorted prices and led to slower growth. Indeed, through what participants termed a rather tendentious reading of the countries' historical record and economic policies, the successes of the quintessential developmental states were cited as evidence against development economics.

Globalization

A number of participants pointed to globalization as a major force against some of the central tenets of development economics. One interesting feature of Keynes's thought was its contribution to "embedded liberalism", which involved open international financial and trade structures and unilateral intervention in pursuit of national-level goals such as full employment and social stability. This international order not only created space for the welfare states, but also permitted the emergence of "developmental states" through a wide range of policy instruments—the protection of domestic markets via the control of capital flows and credit rationing, for example. A salient feature of globalization has been the ascendance of finance capital. This has had enormous implications for states' capacities to pursue their domestic agendas, as well as for economic theorizing itself.

Yeldan attributed the demise of development economics to financial market liberalization and the growing dominance of finance over industry. Kamal Malhotra noted that finance had transformed the very nature of foreign direct investment into acquisitions in developing countries, whereas in the North, it largely reflects mergers. This manifestation of finance is not productive. In terms of policy, Machiko Nissanke pointed out that, generally, the International Monetary Fund (IMF) and the World Bank have forced nation-states to manage their economies within the particular parameters that have resulted from the way globalization has evolved. In many cases, this has meant that certain policy instruments successfully used in the past are now either off-limits or ineffective. Kari Polanyi Levitt remarked that the high mobility of finance capital was reminiscent of the nineteenth century gold standard, which had made it impossible for countries to pursue independent monetary and fiscal policies. Then as now, this order was ultimately deflationary in its thrust, and thus contrary to the expansionary imperatives of development.

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The process of globalization and the collapse of the Bretton Woods financial architecture have increased economic volatility. This exposed a fundamental weakness of development economics: its inattention to the short-term problems of stabilization. As a result, the field of macroeconomics has been dominated by precisely such preoccupations—but this has often been at the cost of concern with long-term economic growth and development. Thus the mainstream understanding of "sound" macroeconomic policy entails contractionary monetary policy, fiscal austerity and deflation. Significantly, these policies are "sound" *within the particular global financial order that they contributed to creating.*

During this discussion, K.S. Jomo introduced the idea that the way in which words and meanings are appropriated by different discourses may be dangerous. Some substitute the word "globalization" for the word "imperialism", for example, and this can be disempowering and deceptive. First, "globalization" usurps "internationalism" by allowing the latter word to be captured by neoliberals. Second, it prevents criticism of imperialism and incorporation of liberal perspectives in the critique. In making this argument, Jomo reminded participants that a century ago, the first comprehensive critique of imperialism was actually made by the English liberal John Hobson, who signalized that the dynamism of capitalism was pushing it in the direction of concentration (monopoly) and, eventually, imperialism. Such an approach today would challenge the claims of neoliberals about globalization and liberalization because much of what is being done in their name is actually anti-liberal, in that nineteenth-century sense.

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The political context and academic currents

The political and ideological context in which theoretical positions thrive or fail is significant. Jeff Faux pointed out that the triumph of neoliberalism is part of a wider conservative political agenda. As noted earlier, the 1970s saw important ideological shifts in the industrialized countries that challenged the welfare state and the Keynesian thinking that had been a counterpart of development economics. So, Diane Elson asked, why had the demise of Keynesianism elicited so little political response in developed countries? Part of the response might emerge if macroeconomic analysis were united with class analysis in a more complex way, to look at the interests promoting market opening. This linked to social policies, as the redesign of many such policies had led to the emergence of a new rentier class (through private pensions and private health insurance, for example). The prospect of many workers profiting from the financial markets through privatization may have been one reason for the success of Thatcherism and privatization in the United Kingdom.

Following up on Elson's remarks, Jomo underscored the importance of understanding the popular bases for Reaganism and Thatcherism, and also for globalization and liberalization. Political shifts in which neoliberal-conservative forces assumed power in the United States, Germany and the United Kingdom had immediate effects on how the Bretton Woods institutions (BWIs) operated. He also recalled that in the 1970s there were some tentative North-South coalitions—best reflected, perhaps, in the Brandt Commission and in debates on a new international economic order. In his paper, Faux also emphasized the need for global politics to accompany the global economy. And Brian van Arkadie referred in his paper to the "euthanasia" of social democracy, which ceded a lot of intellectual ground to the new doctrines. Both participants suggested that anti-statism among the political left in the United States—a result of protests against the Viet Nam War—might also have played a part in discrediting an active role for the state. They asserted that some of the most trenchant criticism of state activism came from the political left. These discussions emphasized the political underpinnings, left and right, for policy shifts and academic debates.

Other participants suggested that the top-down nature of policy making in both welfare and developmental states was another reason for their decline. Adebayo Olukoshi argued that the authoritarianism of the top-down approach became increasingly problematic for many people, as did its neglect of the connection between states and citizens. In other words, statist development strategies were deemed guilty by association with authoritarian governance structures in some contexts, making them unattractive to the many emerging social movements associated with the trend toward democratization.

Franklin Serrano did not fully share the view that this top-down nature was a major reason for decline. The welfare state in the North and developmentalism in the South, he contended, were mainly sanctioned by strategic Cold War fears and were the conquest of the working classes and other social movements. The end of the Cold War undercut the political basis of these policy regimes.

Ghosh suggested that one of the main weaknesses of development economics was that, at a fundamental level, it was not "political economy"—in the sense of politics of the evolutionary interaction between states and markets. Politics determines both government actions and the outcomes of markets, and those processes in turn alter politics. Development economics missed this symbiotic relationship between politics and economics, and the fact that economics is about politics.

Elson asked participants to again consider the autonomous intellectual practices that commanded such public interest in and support of neoclassical economics. This paradigm combined two persuasive kinds of rhetoric. One was scientific, as seen in its self-definition as scientific and, therefore, rigorous theory. The other was about choice and efficiency. While one can question whether the theoretical framework was truly scientific, and how efficiency is defined in its models, such characteristics are highly valued by the public. In rethinking development economics, therefore, it will be necessary to take on board questions of analytical rigour and public concerns about the efficient use of resources.

The seduction of the natural sciences and the use of quantitative methods in economics suggested that development economics, with its more descriptive formulation, lacked rigour. Or, as Jomo noted, development economics was not seen as positive but rather as normative economics, and hence not scientific. Joseph Lim suggested that interdisciplinarity rendered development economics indistinguishable from sociology, psychology and other "soft" social sciences, tarnishing its image and segregating it from true, scientific, analytical (neoclassical) economics. In this sense, then, development economics may have contributed to its own demise by eschewing techniques of analytical rigour. The more realistic characterization of developing economies by the pioneers of development economics was not simply neoclassical models devoid of all empirical realism. What was required was rigorous theory firmly based on realistic characterization of developing economies.

Other reasons for the demise of development economics also emerged from the discussions: postmodernist disdain of "history as a reality"; identification of the development discourse with the "modernist" enlightenment project; allegations that developmentalism was manipulative discourse deployed by developed countries and local elites; and its failure to fully integrate the real concerns represented by new social movements (such as the women's and environment movements).

Theme Two
Current Intellectual Trends: Why the New Interest in Development Economics?

In the 1990s, there was a revival of interest in development economics—or at least in its paradigmatic preoccupations—as illustrated, for example, by the publication of a number of new textbooks on the subject. Conference participants identified and discussed several reasons for the resurgence of interest in development economics.

The collapse of the Washington Consensus

The most immediate reason for the renewed interest in development economics today, participants agreed, was the failure of the Washington Consensus that underpinned the structural adjustment programmes of

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the BWIs. Growth rates in the era of liberalization were almost everywhere lower than in the era of developmentalism. In addition, the persistence of poverty—even in countries that were hailed as success stories by the BWIs—clearly suggested that the framework was not able to address this crucial aspect of structural change. Indeed, given their focus on stabilization and static allocative efficiency, and their deflationary bias, adjustment programmes have failed to induce the kinds of structural changes associated with development. In addition, the Asian financial crisis of 1997 and the standard prescriptions of the BWIs raised questions about the appropriateness of the Washington Consensus to address problems of stabilization. The Asian crisis also underscored the importance of external factors to developing countries, including those whose fiscal policies were not characterized by profligacy and whose trade balances were sound. Earlier, the debacles of "instant capitalism" in the countries of the former Soviet Union and Eastern Europe had exposed the essentially dogmatic nature of neoliberalism's one-size-fits-all prescriptions.

The rehabilitation of the state

In a number of developing countries, authoritarian political regimes lent credence to the focus of the Washington Consensus on policy reforms that reduced the role of government. By the mid-1990s, however, the tarnished image of the state had begun to take on a new lustre. Transitions from authoritarian rule toward democracy served to improve the status of governments as national institutions. Many actors, including civil society and donors, were increasingly willing to engage with these democratically elected governments. In addition, the success of the "developmental state" in East Asia and the emergence of new democracies combined in new thinking about "democratic, developmental states". Furthermore, there was a growing realization—even among those of neoliberal predisposition—that market liberalization required a capable state to secure property and to provide regulation that would ensure competition. Calls from within the BWIs themselves for going "beyond the Washington Consensus" toward "second generation reforms", and for "reinvigorating the state's capability" all pointed up the need to return to the concern for development for which a wide range of scholars and institutions had been arguing. The World Bank also began calling for "comprehensive development frameworks", the components of which were reminiscent of the "development planning" previously associated with development economics.

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Intellectual and theoretical changes

As participants had noted in their earlier discussions, development economics had been founded on the recognition of the pervasiveness in developing countries of "market failures" due to imperfect information, increasing returns to scale, structural rigidity, and so forth. The models informing adjustment policies perfunctorily acknowledged these failures, but then proceeded to make policy recommendations as if all market distortions were caused by state intervention. Yet major theoretical advances in the discipline of economics have proposed that failures were not peculiar only to developing countries, but rather features of any real economy. As a result, the key assumptions of development economics—about markets, and about the need for collective action to address some of the co-ordination problems engendered by market imperfections—were increasingly acknowledged by theoreticians as being entirely appropriate. And yet this acknowledgement had few concrete implications for policy making.

Indeed, in his contribution to the conference, Joseph Stiglitz raised the following anomaly: whereas much cutting-edge theoretical work in developed countries centred on problems of imperfect information, new industrial organization and the effects of imperfect competition—and many insights drawn from observing developing countries were part of this corpus of knowledge (for example, agency theory, screening models and efficiency wage theory)—in the same period the master in development economics was the Washington Consensus, which ignored these considerations despite their even greater importance to developing countries. By something tantamount to legerdemain, neoclassical economists did away with these problems by simply assuming diminishing returns and perfect information.

Renee Prendergast intervened, suggesting a number of possible explanations for this anomaly. One is that the market failure literature suggests "multiple equilibria", which undermines simple rule-based intervention by suggesting that effective analysis is specific to institutional and cultural factors at a specific place and time. This immediately rules out the one-size-fits-all prescriptions favoured by international organizations. Another, more fundamental, explanation is that market failure implies room for selective state intervention, which goes against the ideological and intellectual predisposition of most economists, some of whom have been persuaded that "government failure" is always worse than market failure.

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Alexandre Rands Barros claimed that "new growth theories"—which point to increasing returns and externalities as potential engines of growth and development—have also contributed to the revitalized interest in development economics. Some proponents of these theories stress the role of investment in public infrastructure, and in strengthened institutions, as important determinants and potential sources of externalities. Other theorists are, however, sceptical of public investment, given the complex issues raised by these models—including the prospects of rent-seeking and "capture" of policies by interest groups. The latter group is wary of public ownership and planning, and instead proposes institutional arrangements that mimic the market.

Prendergast pursued the discussion of increasing returns. They provided the theoretical underpinnings for the kinds of selective industrial policies pursued by countries such as the Republic of Korea, she suggested. If one accepts the hypothesis that comparative advantage flows from specialization, it follows that through careful selection and targeting of investment, a country can build comparative advantage in particular domains. But the timing of intervention is quite important, and it is very difficult to be prescriptive in advance. In order to make proper judgements about the kinds of support that are likely to be effective, policy makers must have in-depth knowledge of all economic sectors. Yet when an economy is trapped in low-level equilibrium, or when new economic activities are undertaken, substantial policy interventions are often required.

She cautioned, however, that intervention was becoming increasingly difficult—in terms of timing, selectivity and the cost of failure. While the literature on increasing returns opens up spaces where intervention can be valuable, *appropriate* intervention places significant demands on the capacity of policy makers. Information requirements are extremely high, especially given the nature of the international climate for industrialization. The Republic of Korea became internationally competitive in industry by simultaneously protecting its home markets and encouraging firms to meet export targets. The current global trade regime, overseen by the World Trade Organization (WTO), would make it very difficult for other developing countries to adopt such selective policies. Opportunities for developing countries to learn by doing are being squeezed by the nature and requirements of such international institutions.

Theme Three
New Challenges for Development Economics

If the revival of development economics is to be meaningful, the new circumstances in which it might take place must be carefully considered. This new context poses both new and old questions. In her remarks, Gita Sen reminded participants that rethinking development economics was not the same thing as resuscitating it. There were many fundamental weaknesses in earlier versions that should not be glossed over in simple criticism of neoliberalism, and there are new phenomena and understandings to be taken into account. A major weakness of development economics in the past was its inability to integrate the rich insights of development studies writ large. More recent debates on development economics have paid insufficient attention to changes in forms of accumulation over the last three decades. Specifically, thinkers have yet to come to grips with the implications of the information and biological technology revolutions for accumulation and the labour process. And they have not yet addressed the transformation or erosion of certain social pacts—between workers and employers, states and citizens, countries of the North and of the South—that underpinned economic development following the Second World War. Understanding these processes and relations is essential if new policy frameworks are to be built on stable foundations.

Democracy and the role of the state

According to Lim, development economics is not only about policies, but also about the institutions, governance structures, patterns of class formation and power structures needed for the design and implementation of those policies. This implies that there is a need for different types of political and structural analysis at the national and international levels. Several participants noted that one of the criticisms of development economics was its failure to specify institutions and governance structures. One feature of current normative and political discourse on the role of the state insists on democracy and human rights. Many developmental states in the past were authoritarian. They had been sanctioned by development economics, which tended to argue that, because of the sacrifices it imposed on the population at large (in terms of postponed consumption or greater inequality), development required authoritarian regimes that would make hard decisions unencumbered by politics.

Malhotra argued that reviving and rethinking the developmental activist state did not mean going back to old notions of the role of the state. It did mean, however, trying to see how one could support an activist state that created space for a plurality of organizations from civil society to the market. Along the same lines, Olukoshi contended (in extending the discus-

intellectual fears about interventionism—ranging from the fear of authoritarianism to that of wrong macroeconomic policies—now need to be squarely addressed. For South Africa, where a nationalist interventionist project was pursued by a racist regime, state interventionism has become virtually taboo, he explained. Ritu Sharma questioned whether developmental states were everywhere politically feasible. How can one be sure that those who are on the government side in developing countries, the investor class, will be responsible developmental activists?

Macroeconomic analysis should contribute to a democratic process of policy deliberation. However, as Elson noted, the possibility of determining macroeconomic policy through an open social dialogue—in which different interests can exercise voice and in which entitlement failure can be explicitly brought into view—is often foreclosed not by the technical requirements of macroeconomic policy, but by fear of preemptive exercise of the "exit" option by financial capital and institutions. Their ability to exit rather than join in a policy dialogue is a result of the openness of financial markets. Fears that the wrong signals will unsettle volatile investor sentiments will mute debates. It is difficult to conduct a policy dialogue when some of the key players have no stake in the outcome

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