



Initiative for Policy Dialogue



# *El Consenso de Buenos Aires*

*Una Nueva Agenda para America Latina  
Quince Años Después del Consenso de Washington*

*Buenos Aires, 23 de Agosto de 2005*

**TOWARDS A POST *WASHINGTON*  
CONSENSUS CONSENSUS  
AND  
POLICIES MOVING FORWARD**

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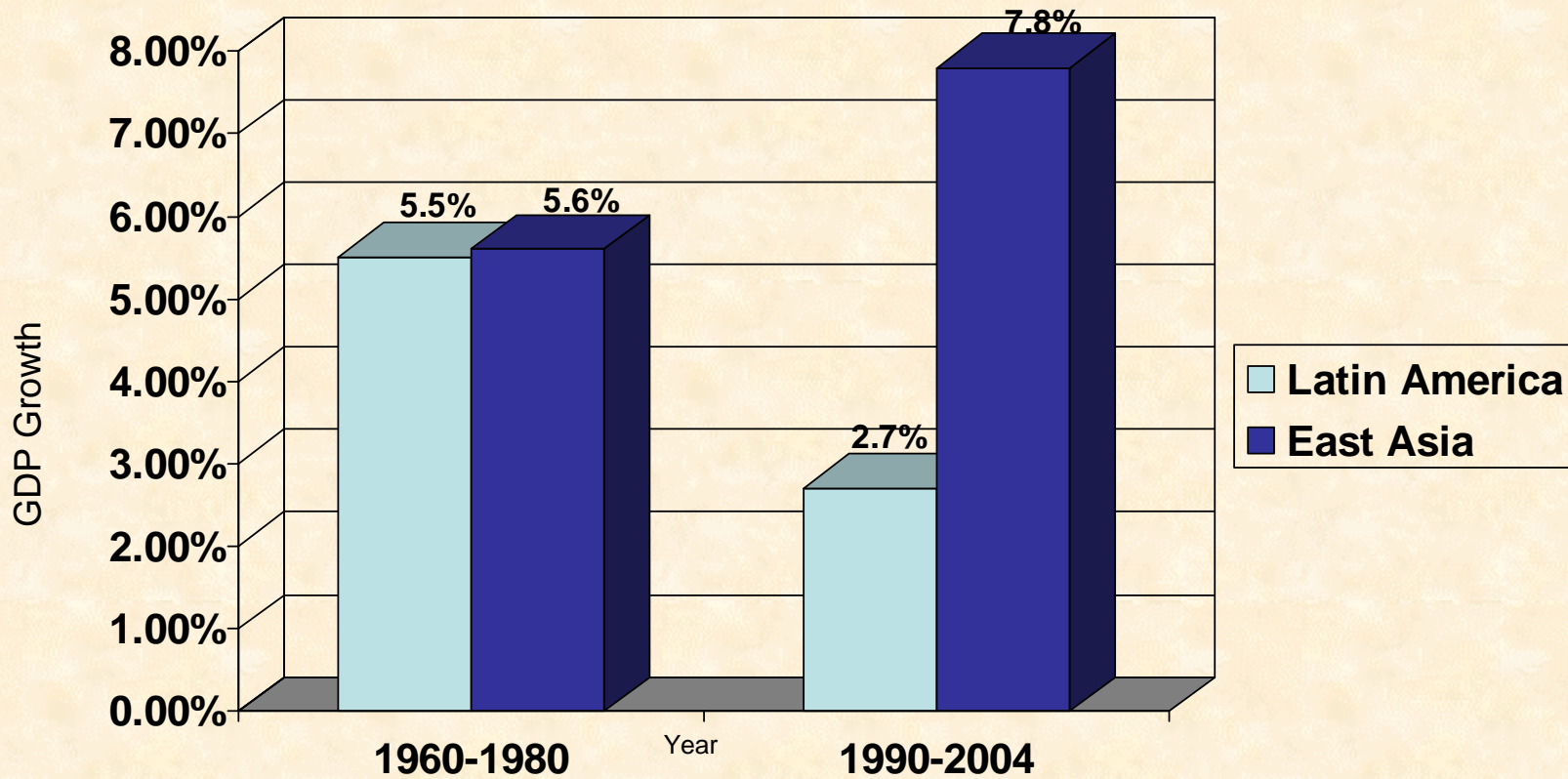
# GLOBAL CONSENSUS ABOUT THE WASHINGTON CONSENSUS

- The Washington Consensus has proved neither necessary nor sufficient for successful development
  - *Even if each of its policies made sense for particular countries at particular times*
- Any future consensus cannot be made *just in Washington*
- Any new framework must provide better and greater adaptation to the circumstances of the countries involved

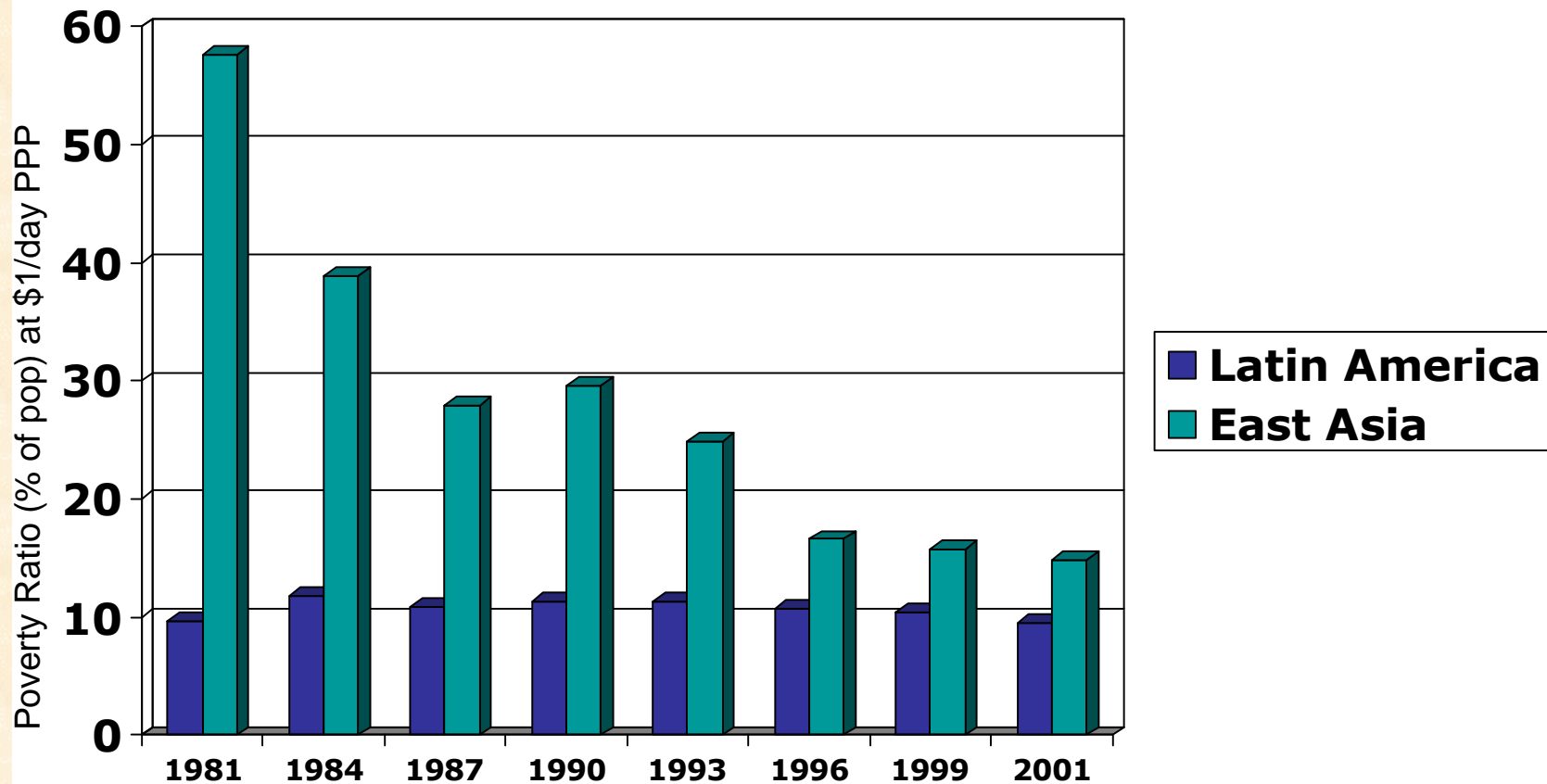
# **GLOBAL CONSENSUS ABOUT THE WASHINGTON CONSENSUS**

- It produced limited growth
- Often associated with high levels of instability
- Undermining of social safety nets
- Benefits of what growth was produced was not equitably shared

# UNDER WASHINGTON CONSENSUS LATIN AMERICAN GROWTH PLUMMETED

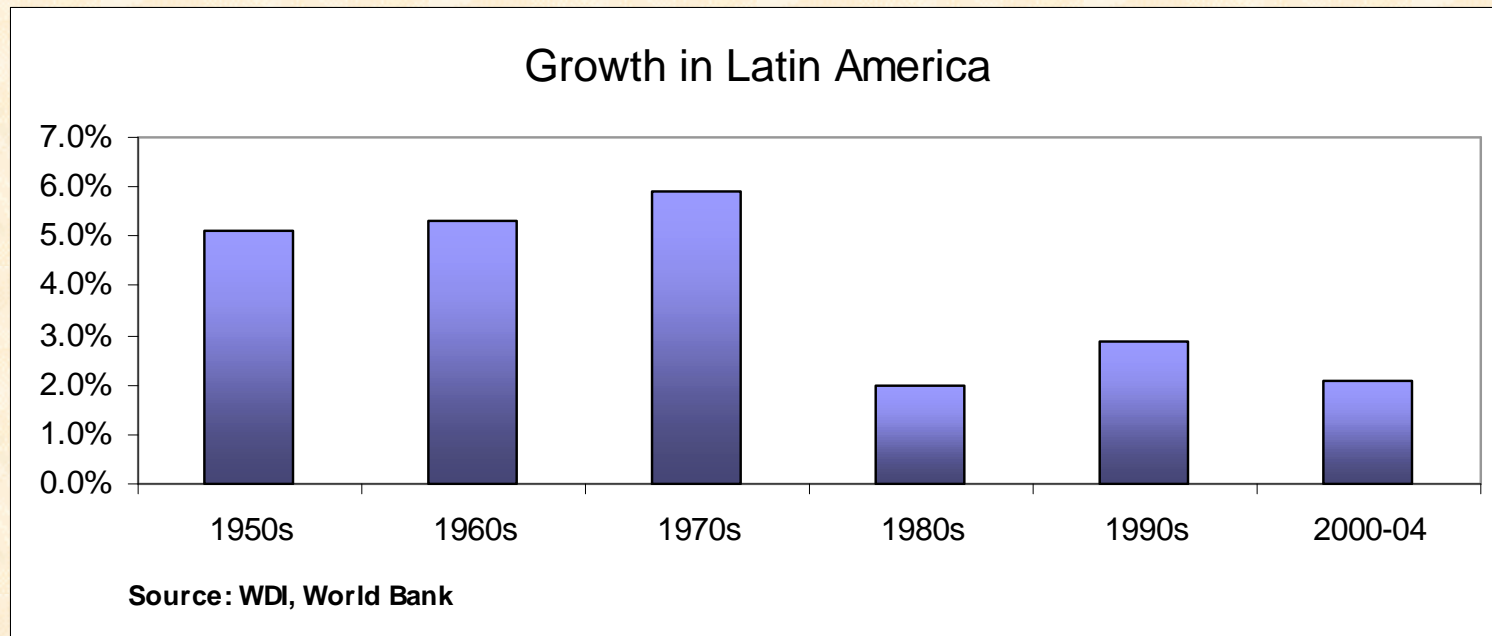


# POVERTY IN LATIN AMERICA HAS NOT DECLINED...



Source: World Development Indicators, the World Bank

# ... AND GROWTH RATES HAVE BEEN VOLATILE



# **GLOBAL CONSENSUS ABOUT THE WASHINGTON CONSENSUS**

- Need to focus on broader objectives
  - And our measures of success have to adjust accordingly
- And more instruments
- There are trade-offs
  - Which cannot be left to technocrats
  - Especially from outside the country



# **BEWARE OF WASHINGTON CONSENSUS *PLUS***

- Lip-service to issues of distribution
  - better safety nets
  - or improved female education
- Emphasis on second generation of reforms
  - Items left off in earlier agenda
    - In particular about governance issues
- Step in the right direction
- But does not deal with fundamental inadequacies in the current approach

# **ELEMENTS OF THE POST *WASHINGTON* CONSENSUS CONSENSUS**

*Economic policy is supposed to enhance the living standards of the vast majority of the citizens*

- Importance of equity
- Importance of employment
- Balanced role of government and market

# IMPORTANCE OF EQUITY

- Equity is an “end” in itself
  - GDP a bad measure of success
    - GDP can increase even as the country gets poorer
      - Latin American debt
      - Resource depletion, environmental degradation
      - Better to focus on NNP
      - Even better to take account of liabilities
- There can be rich countries with poor people
  - Better to focus on median income
  - Median household income in the US is declining, even as GDP increases
- Equity promotes growth and even efficiency
  - Better use of human resources
  - Social and political sustainability

# IMPORTANCE OF EQUITY

- Markets by themselves do not produce social justice, an equitable distribution of income
- Modern theories emphasize that equality and efficiency *cannot* be separated
  - Agency theory
  - The arguments for land reform
    - Sharecropping attenuates incentives just as taxes do
- Trickle down economics does not work
- Failures of Washington consensus not surprising: Equality issue not even considered

# IMPORTANCE OF EMPLOYMENT

- Lack of employment greatest waste of economic resources
- Full employment most important social policy
  - Better than any safety net
  - With all kinds of social consequences

# BALANCED ROLE OF GOVERNMENT AND MARKET

Market failures endemic even in developing countries

- Whenever information is imperfect or markets incomplete
- Whenever technology is "endogenous"
- When competition is imperfect

Reason that "invisible hand" is often invisible because it's not there

Important role of government in

- Promoting and regulating markets
- Providing institutional and physical infrastructure
- Promoting education, innovation and technology
- Promoting equity and employment

# MORE THAN THEORY

- The ideas are not just of academic importance, but are of relevance to every major aspect of public policy—even affecting technical issues like how we measure success (GDP, green GDP, median income) and measure budget deficits
- What we measure affects what we eventually do

## **Accounting Distortions:**

- IMF accounting practices continue to put a roadblock in the way of market based land redistribution
- Accounting practices can “force” privatizations

# **MICRO-ECONOMIC POLICIES**

## Importance of finance

- Keeping lending rates down
- And making finance available
- Creating financial institutions
- And regulating them
  - CRA, Branching requirements



# **MICRO-ECONOMIC POLICIES**

## **Importance of competition policy**

- Necessary if markets are to yield their benefits, e.g. low prices
- Even necessary to have high levels of innovation
- New challenges with emergence of global monopolies

# MICRO-ECONOMIC POLICIES

## Importance of technology

- Market based industrial policies can work
  - Every successful country, including the US, uses them
- Appropriate intellectual properties structure
  - Not based on the US
  - Which is not even best for the US
  - Bit reflects interests of special interests

# MICRO-ECONOMIC POLICIES

## Corporate governance - managing the market

- There is an especial need for a legal structure to ensure that corporations act in broader interests, not just in the interests of the managers
- Conflicts of interest - abuses so apparent in U.S. during the roaring 90s (private sector corruption was pervasive)
  - At great cost to economy before and after bubble
  - Issues of equal or greater relevance in developing countries

# TAX POLICY

- Important to engage in as much ex-ante redistribution as possible (e.g. through better education)
- But there will still be need for ex-post redistribution
  - V.A.T. does not do this
  - Must be accompanied by other redistributive taxes
  - Often not the case in developing countries
  - And in most developing countries, V.A.T. is not even an efficient tax

# MACROPOLICY

## Importance of balanced emphasis on growth, employment and inflation

- Focusing on *lending* rates and credit availability
- On Competitive exchange rates
- On maintaining low unemployment and high growth
- Fiscal policies to stimulate growth and full employment
  - *But aware of consequences of deficits and debt*
  - *Moderate borrowing with low debt can yield high returns*
- Aware of distributive and growth consequences of stability policies

# INFLATION

- General agreement that high/hyperinflation has high costs to economy
- But evidence of effect of low inflation less clear; at least for some countries (U.S.)
  - No significant adverse effect on growth; high interest rates to fight inflation do have adverse effect on growth
  - No inflation momentum
  - Limited costs of disinflation
  - Adverse distributional effects of high interests to fight inflation far greater than adverse distributional effects of slight increases in inflation

# BEYOND WASHINGTON CONSENSUS

- Cannot separate out economics from politics and society
- Societal consequences of economic policies
  - Erosion of social capital
  - Alienation
- Intertwining of economics and politics

# INTERTWINING OF ECONOMICS AND POLITICS

- In Russia, system of privatization, liberalization, high interest rates undermined demand for rule of law
  - Created incentives for asset stripping rather than wealth creation
  - And created a political demand for legal structure that facilitated that
- Campaign contributions shape economic agenda
  - Evident in U.S. in energy bill, bankruptcy laws
  - Even in resistance to accounting reforms



# A POLITICAL AGENDA

- Democracy means more than periodic elections
- Requires citizens to know what their government is doing
  - Freedom of information acts/right to know laws
- Citizens right to know can be affected by lack of media diversity
  - More important than concentration of economic power
  - Important that there is contestability
  - Media concentration and distorted information has become an increasing problem around the world, even in democracies

# A POLITICAL AGENDA

- Incentives matter—
  - Those who give campaign contributions expect a return
  - And generally they get it
  - It means that laws are, in effect, put up to “auction”
- Need to have campaign finance reform
  - Public funding of campaigns
  - Using public airwaves

# CONCLUDING REMARKS

- Development is possible, but clearly not easy
- Equitable, sustainable and democratic development may even be more difficult
- Policies do matter
- The intellectual framework for thinking about policies provided by the Washington Consensus was badly flawed
- **There are other frameworks**
  - **More rooted in economic theory**
  - **And historical experience**
  - **Which, at least in other countries, have worked better**
    - **Faster, more sustainable growth**
    - **More equitably shared**
- **These provide the basis of the *Post Washington Consensus* Consensus**