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MARKET-BASED STRUCTURAL ECONOMIC REFORM:

A Review of the Literature

Prepared for

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INTRODUCTION AND OVERVIEW

The shift toward market-oriented economic policies evident in many parts of the developing world and Eastern Europe since the mid-1980s has sparked an outpouring of articles, monographs and books on the subject. This growing body of literature spans all the major academic disciplines related to international development--economics, political science, public policy and administration, international finance and even health and social development. Many thoughtful analyses of the structural reform phenomenon in the developing world and Eastern Europe have begun to appear in the popular and business press as well. What follows is a survey of the English language literature on market-based policy reform in the context of the developing world and centrally planned economies.

The process of identifying and choosing the most relevant works on the structural reform subject began with an extensive data base search. A total of eight data bases were tapped: PAIS International, Dissertation Abstracts Online, Foreign Trade and Economic Abstracts, Academic Index, Economic Literature Index, Trade and Industry Index, National Newspaper Index and the Washington Post Index. To maximize comprehensiveness, a parallel title identification effort was launched, using references and bibliographies of the core structural reform authors as well as World Bank and IMF catalogues as sources. Combined, these efforts produced rich results. More than 160 titles directly related to the structural reform topic were identified and many of these were scanned in abstract form early on in the process.

For reasons of time and budget, the roster of review material had to be significantly narrowed down. The study team set a target number of 60 works to be reviewed. It was decided that two-thirds of the total would be general works on structural economic reform and related issues. The remaining one-third would deal with reform in the context of Africa, Asia, Eastern Europe and Latin America. This basic mix, it was felt, would assure in-depth coverage of the economic and policy issues and, at the same time, provide real-world insights into region-specific issues as well as problems that cropped up at the implementation level.

The final selection of works for review was governed by such factors as the prominence of the author, the nature of the publisher (all World Bank publications were considered particularly carefully), the perceived weight of the subject matter and finally, the actual content of the work. Also, the target list represented works that were written in the last five years. Special efforts were made to include a sampling of works that challenged the conventional thinking and offered credible policy alternatives. Regrettably, the project team was unable to include several valuable works that could not be accessed in time to be included in this study.

Structural Economic Reform: The State of the Literature

Perhaps the most compelling evidence of the continued evolution of thinking and writing on the subject of structural economic reform is the fact that a clear revisionist or reactionary school of thought has yet to appear to seriously challenge the dominance of the so-called "new orthodoxy." Indeed, while the subject seems to have cooled off a bit in Western Europe and the U.S., structural reform remains a very hot issue throughout much of the developing world, Eastern Europe and the Soviet Union.

Declaring the existence of a consensus among serious thinkers on any subject is always a treacherous endeavor and it is even more so when the subject is economic development and the thinkers come from all corners of the world and represent such diverse institutions as academia, government, business, think tanks and multilateral institutions. Beyond the most general and unassailable economic development goals (e.g., rising per capita income and maximizing efficiency), points of broad-based agreement are hard to identify. Increasingly, however, it is now possible to say that there exists, in broad terms, general recognition of the value of market forces in the organization of a national economy.

Although not to the complete exclusion of alternative viewpoints, this literature review is focused heavily on the "new orthodoxy," which is linked closely with the World Bank, and other mainstream viewpoints. This new orthodoxy represents, in important respects, an evolution beyond the external adjustment orientation, associated with the IMF and which focused on the obtaining of narrow macroeconomic targets while ignoring broader structural issues.

Among the key findings of the literature review were the following:

- Government and markets. That government has an important role to play in furthering economic development is just about unquestioned. Where reasonable people differ is over the nature of that role. At the very least, there is broad agreement that developing countries should be involved in creating and upgrading factors--especially skilled human resources, economic information and infrastructure--in order to maximize their nations' competitive advantage in world markets. The consensus begins to break down when the discussion turns to the economic role of the state.

- Export-oriented growth. Based on recent studies showing superior economic growth results for export promotion (EP) over import substitution (IS) approaches, mainstreamers come down heavily in favor of export-oriented growth. They tend to be critical, however, of trade distorting policies such as export subsidies or special concessions. As such, they define export orientation as the absence of policies that discourage exporting. Key pro-export elements are import liberalization and a competitive exchange rate.

  Not all critics of the export-oriented strategy subscribe to import substitution as an alternative tack. But many fear a new wave of protectionism in the industrial world in response to any massive rise in developing country exports.

- Reform timing. It is unanimously held that timing is key to successful structural reform. Elections and government changeovers present particularly important opportunities for new economic programs. For some regimes, honeymoons are one-shot opportunities for reform. Related to the timing issue is the need for strong political support. Despite the political sensitivity of many reform policies, regimes can and should attempt to build constituencies behind reform programs.

- Reform sequencing. The literature is not at all in agreement on the proper sequencing of reforms, although the importance of the issue is not all questioned. There seems to be fairly wide recognition of the need to achieve basic external stability before undertaking a reform program. Probably a majority of mainstream thinkers (among them Anne Krueger and Michael Bruno) believe that liberalization of the current account should almost always precede the liberalization of the capital account. Sebastian Edwards is among those who believe the opposite, provided, however, that shadow prices can be established to guide allocation of resources prior to liberalizing trade. Jeffrey Sachs, meanwhile, stresses the need for fiscal reform first, as a means of stemming inflationary pressures.

- Privatization. Mainstream writers view the sale of state-owned enterprises to the private sector as an important component of structural reform, but one that has been overemphasized in the formulation of reform programs. Some warn that selling off or liquidating state enterprises should come later in the reform process, to avoid political problems that could jeopardize the broader reform effort. Nearly all warn against replacing a state enterprise with a private sector monopoly. In many instances, privatization is meant as a broader reform movement that encompasses simulated privatization (introducing market forces into state company operations), deregulation and franchising out public sector services to private operators.

- The lessons from East Asia. The literature is highly skeptical of the notion of East Asian development as an economic model for the developing world, given the very different social, cultural and economic histories involved. However, there is wide agreement that the region's development history offers important policy lessons. The new orthodox thinkers stress East Asia's successful outward-oriented development approach. Many others, however, attribute that region's economic success to effective government intervention and industrial planning. They continue to recommend a similar approach for the developing world, but one that is adapted to local conditions and changed global circumstances.

The special case of Sub-Saharan Africa. There seems to be a consensus that the severe underdevelopment and poverty of Sub-Saharan Africa warrants a more gradualist approach to structural reform in which basic human needs receive clear priority. (Such needs are laid out in the U.N.-sponsored *Adjustment with a Human Face* collection.) At the same time, many of the more mainstream writers argue convincingly that the right structural reforms (especially price liberalization) will actually alleviate poverty by redistributing wealth from the urban to the rural sectors. Nearly all agree that Sub-Saharan Africa, more than any other region, is in desperate need of ongoing external assistance and that reform cannot be sustained without it.

The market revolution in Eastern Europe. The literature very clearly understands the unique challenges and difficulties facing Eastern Europe and the Soviet Union on the road to economic reform. Creating market economies virtually from scratch will be a monumental task. So will be the tasks of engendering an efficient work ethic and an entrepreneurial spirit where none presently exists. A vitally important issue that needs to be further explored is whether significant market-oriented reforms can take place in the absence of private property. Also, unlike the other regions, there are no success stories for Eastern European reformers to follow. The structural reform policy priorities for Eastern Europe will be different. The sale of state companies, for example, may not be advisable until the real value of such assets can be ascertained.

Prospects for sustained structural reform. A sense of concern underlies the discussion over the future of structural economic reform. Few hold that the new thinking represents a change in ideology; most believe that policymakers in the developing world are embracing market-based policies for very practical reasons and in the absence of viable alternative policies. In short, politicians and policymakers are looking to market forces to help correct severe economic distortions and restore growth. Without positive results, however, the next shift in thinking is likely to be back toward state intervention. Destabilizing exogenous shocks such as the oil price hikes of the 1970s and early 1980s could seriously undermine structural reform progress. Even in the absence of new shocks, many writers question whether Latin America's debt overhang will permit (Brady Plan relief or not) sufficiently robust growth for reform programs to be sustained. Finally, more than a few writers emphasize the importance of parallel structural reform in the ~~developing~~ world--especially with respect to market access for developing country exports.

The Direction of the Literature

Case studies of market-based reform programs will doubtless be on the rise as countries progress further along the reform path. These will be welcomed additions to the more theoretical aspects of the literature dealing with issues such as reform timing and sequencing. Interest in the political economy of reform does not appear to be waning. Hopefully, future case studies will shed light on winning tactics for garnering political support behind potentially unpopular programs. The successful use of tripartite negotiations involving government, labor and business sectors in, for example, Mexico would seem to deserve a closer examination. Also, Chile's highly regarded reform efforts will doubtless be revisited in light of the nation's recent return to civilian rule.

Economic liberalization efforts in Africa will be assessed on the basis of social welfare factors, and still more alternative approaches to reform will be offered and discussed. Eastern Europe and the Soviet Union, where reform programs are for the most part just getting under way, will generate massive scholarly interest in the progress and problems of market-based reforms in these centrally planned economies. The consequences of heavy export dependency are certain to be explored further in the context of Korea, Hong Kong and Taiwan in the 1990s. Finally, the Latin American-focused literature will continue to debate the proper mix of policies needed to simultaneously "get prices right," fight inflation, service debt and boost exports--while keeping the democrats in the palaces and the generals in the barracks.

STRUCTURAL ECONOMIC REFORM: GENERAL WORKS

Adelman, Irma. "Beyond Export-Led Growth." World Development 12, September 1984.

This article is a critique of manufacturing export-led growth as a model development strategy for LDCs in the late 1980s and early 1990s. Most LDCs, the author maintains, are unlikely to be able to break into international markets for nontraditional exports at a time of relatively slow industrial country growth and limited demand for LDC nontraditionals. An alternative strategy is offered: an agricultural-demand-led industrialization (ADLI) program. The author insists that ADLI is not anti-export in essence. It is a strategy that puts agriculture at the center and yet spurs industrialization by expanding internal demand for intermediate and consumer goods produced by domestic industry. Using a computable general equilibrium (CGE) model of a small, low-income, semi-industrial, open economy, the author compares the relative merits of ADLI and export-led industrialization. She finds that ADLI generates the same rate of industrialization as does export-led growth but leads to a higher employment rate, better income distribution, a stronger balance-of-payments, less poverty and higher per capita income growth than export-led growth.

Alam, Shahid M. "Anatomy of Corruption: An Approach to the Political Economy of Underdevelopment." American Journal of Economics and Sociology 48, October 1989.

The author attempts to discredit functionalist theories on the controversial subject of the economic effects of corruption in developing countries. Furthermore, he argues that corruption represents a barrier to economic progress. The author analyzes two claims on the economic effects of corruption. First, he investigates the connection between market corruption and improved allocative efficiency, and second, he examines the relationship between corruption and capital formation. With the former, the author attempts to show that corruption actually eliminates the most efficient producers and prevents market forces from weeding out the most inefficient. For the latter, the author's point is that corruption is more likely to reduce investment and savings than to encourage capital formation. In addition, the author examines the political effects of corruption and concludes that it has a negative impact on political integration inasmuch as corruption serves primarily to enrich the dominant ruling elite.

Bates, Robert. "The Reality of Structural Adjustment: A Sceptical Appraisal." Structural Adjustment & Agriculture: Theory and Practice in Africa and Latin America. Simon Commander, ed. London: Overseas Development Institute, 1989.

In this critical overview of structural adjustment issues, the author questions whether, especially in the African agricultural context, the intent of structural adjustment policies is really to promote private capital formation. Rather, he says, the intent is to restore the health of governments "by bringing their policies back into line with current economic realities." An implication of this would be that many of the programs and policies advocated in the name of structural reform will have no real effect on the political or economic status quo. Despite this reality, the pursuit of true structural reform is a worthy one. The proper sequencing of economic reforms depends heavily on conditions in the reforming country. For developing country politicians, the best sequence of reforms must take into account the need to build a constituency around the reform program, while deflecting the political opposition. Since political conditions differ significantly from country to country, there can be no real "best" sequence for reform policies.

Balassa, Bela. "Adjustment in Socialist and Private Market Economies." Journal of Comparative Economics10, 1986.

This article examines the policies that were formulated by socialist and newly industrializing private market economies (NICs) in response to external shocks during 1974-1976 and 1979-1981. To their apparent detriment, the inward-oriented NICs and socialist countries relied heavily on foreign borrowing during these periods. Furthermore, the inward-oriented economies' incentive system amounted to an anti-export bias, which was further aggravated by overvalued exchange rates in some cases. In contrast, the author argues that "output-increasing polices" (mainly export promotion and import substitution) resulted in higher economic growth rates for the outward-oriented NICs that adopted them, despite harsher shock effects overall. Other policy decisions that worked to the benefit of the outward-oriented NICs include: greater rationality in the choice of public investments and encouragement of higher domestic savings rates via positive real interest rates and relatively low budget deficits.

Bauer, P.T. Reality and Rhetoric, Studies in the Economics of Development. Cambridge, MA: Harvard University Press, 1984.

The author argues that the "extension of the range of choice of people as consumers and producers" is one of the most important means and ends of economic development. Through a series of case studies he seeks to demonstrate that development policies that ignore or seek to circumvent the interests and desires of the individuals within the economy do not succeed. The cases he uses are almost entirely drawn from African and Asian experiences in low income countries. Market forces are presented as being highly effective at shaping and directing economic behavior in these low income economies. Historical examples of such economic behavior include peasant farmers in Africa and Asia responding very rapidly and successfully to changing market opportunities. When government monopolies and buying cartels replaced market forces, both the farmers' income and the national income suffered. The emphasis in this analysis is on the nature and importance of the productive, wealth-generating role of the segment of the population that is the least "Westernized" politically and economically.

Bhagwati, Jagdish N. "Rethinking Trade Strategy." Development Strategies Reconsidered. John P. Lewis and Valeriana Kallab, eds. New Brunswick: Transaction Books, 1986.

This article is a thoughtful and balanced rethinking of the export promotion (EP) versus import substitution (IS) debate in the context of the adjustment-weary 1980s. The author, a long-time proponent of EP strategies, reviews the evidence and concludes that most developing countries that failed to shift from IS to EP "lost out on the opportunity for an impressive economic performance that the growing postwar economy liberally provided." An extended IS period would be an acceptable means of promoting industrialization only for "primitive" economies, with a limited industrial base and an export base dominated by non-manufactures. In general, however, the author reiterates his view that EP (which he defines simply as the elimination of any bias against exports) is the superior policy course on the basis of economic growth, allocative efficiency and demand for labor, among other factors. He vigorously attacks the view that world markets cannot absorb developing country exports or are too potentially protectionist to make massive changes to EP policies viable on a global basis. Embracing EP policies would not turn most countries into a Korea or Taiwan.

Bienen, Henry and John Waterbury. "The Political Economy of Privatization in Developing Countries." World Development, May 1989.

The authors draw on a variety of historical examples--ranging from Japan in the 1930s to Turkey in the 1960s--to warn that some developing countries could revert back to state-led growth in response to extreme changes in economic events, good or bad. The authors highlight some key regional differences in political economies that greatly influence the outcome of privatization campaigns. In Sub-Saharan Africa, for example, regime discontinuity has led to an acute preoccupation with maintaining political power. This represents a serious obstacle to privatization. In Latin America, entrenched domestic economic interests are often satisfied with gaining political control over state companies and will therefore not pressure ruling regimes to cede ownership.

Blejer, Mario and Silvia Sagari. "The Structure of the Banking Sector and the Sequence of Financial Liberalization." Economic Reform and Stabilization in Latin America. Michael Connolly and Claudio Gonzalez-Vega, eds. New York: Praeger, 1987.

This paper seeks to understand the impact of financial liberalization policies on the banking sector in a small, developing economy. External financial liberalization is defined as the opening up of domestic financial markets to international capital flows, the removal of exchange controls and the elimination of barriers to entry of foreign banks. Internal liberalization refers to elimination of domestic credit controls, interest rate ceilings and differential reserve requirements, among other restrictions. Assessing recent experiences in the Southern Cone, the authors identify a number of problems associated with rapid and simultaneous liberalization of internal and external financial systems. Owing to typically heavy domestic bank regulation, government intervention and a lack of competition in the banking sector, the authors argue that internal financial liberalization should, in most cases, precede external liberalization. Without time to adjust to new market pressures, local financial institutions would be ill-equipped to compete with new foreign competition. Massive bank failures could result and thus undermine future competitive conditions in the financial market undergoing liberalization.

Boskin, Michael J. and Charles E. McLure, Jr., eds. World Tax Reform: Case Studies of Developed and Developing Countries. San Francisco: International Center for Economic Growth, 1990.

This survey covers tax reform efforts in a diverse group of countries, north and south. The editors assert that tax reduction has been the most important manifestation of the reform movement during the 1980s decade, as lower rates attenuate the adverse incentive effects of taxation on work effort, saving and investment. Another salient development has been the decline in tax incentives, which are viewed as encouraging rent-seeking behavior. In their conclusion, the editors note the growing acceptance of consumption-based taxation on the part of economists and business interests. Colombia, Mexico, Sweden, the U.K. and the U.S. are among the countries to have considered such a move, but none has yet to do so.

Bradford, Colin I. "East Asian Models: Myths and Lessons." **Development Strategies Reconsidered.** **John P. Lewis and Valeriana Kallab, eds. New Brunswick: Transaction Books, 1986.**

The author argues against using the cases of Hong Kong, Singapore, Taiwan, and Korea as a singular model for economic development. The stylized version of the East Asian model, with its outward-orientation, market-determined prices and export promotion based on internal liberalization, does not, in fact, reflect the reality of those nations' development experience. Sectoral priorities and industrial policies, the author asserts, "have been essential ingredients in the East Asian success stories." What distinguishes the East Asian development experiences is not the dominance of market forces, free enterprise and internal liberalization but "effective, highly interactive relationships" between the public and private sectors . . . " One of the keys to these successful relationships is the national economic policy; it embodies common public and private goals and commitments. The lesson from East Asia's economic development is "messier" than the conventional wisdom would allow. Yet, the East Asian examples do suggest the importance of future development policies that fuse structurally oriented development and macroeconomic policies.

Bruno, Michael. "Opening Up: Liberalization with Stabilization." **The Open Economy: Tools for Policymakers in Developing Countries.** **Rudiger Dornbusch and F. Leslie C.H. Helmers, eds. Oxford: Oxford University Press, 1988.**

Economic liberalization efforts undertaken during periods of macroeconomic disequilibrium present special challenges to policymakers. One very important reason is that the speed of adjustment in various markets (commodity, financial, etc.) differs. Rapid trade liberalization, the author suggests, may be preferable to gradual reform for reasons of credibility and long-term efficiency. Financial liberalization, on the other hand, should be approached cautiously since potentially destabilizing changes (e.g., rapid appreciation in the real exchange rate) may occur instantaneously. The author argues strongly that the liberalization of trade should always precede the opening up of capital markets. Argentina and Chile could possibly have avoided foreign exchange crises at various times during the 1980s if they had followed this prescription. But there are no guaranteed recipes for success. In the early 1980s, Chile did things in the correct order and still suffered a foreign exchange crisis (partly as a result of an expansionary wage policy).

Center for International Private Enterprise (CIPE). "Market-Oriented Paths to Economic Growth: Lessons of the 1980s." **Summary of Findings.** **CIPE, 1989.**

A product of CIPE's February 15, 1989 conference on structural economic reform, this document is a less than encouraging assessment of market-oriented progress across the developing world. In Africa, such reform efforts appear widespread, but actual results thus far are limited (and to a large extent concentrated in agriculture). Latin America's shift toward democratic rule has not greatly accelerated the structural reform process in that region's key markets; the pattern of nonsustained, "stop-and-go" policies continues to undermine longer-term reform goals. South Asia's reforms are described as generally mild, with little impact on the essentially statist thrust of economic policy. The clearest success stories are those of East Asia's "four tigers." Conference participants offered different views on the key growth ingredients in East Asia--whether market-oriented reforms or timely government intervention was responsible.

Chu, Ke-young. "External Shocks and Fiscal Adjustment in Developing Countries: Recent Experiences." **<u>Fiscal Policy, Stabilization, and Growth in Developing Countries.</u>** **Mario I. Blejer and Ke-young, eds. Washington D.C.: International Monetary Fund, 1989.**

This paper seeks to provide empirical support for the argument that much of the fiscal instability experienced by developing countries is largely the result of external shocks. The argument rests on the assertion that in most developing countries the tax base and the ability to collect revenues are such that foreign trade either directly or indirectly provides the main source of government revenue. Thus the government's income can fluctuate significantly due to shifts in the country's trade position. Empirical evidence suggests that this has in fact been the case, and that countries that anticipated such shocks were better able to deal with their own fiscal problems.

Crook, Clive. "Poor Man's Burden: A Survey of the Third World." **<u>The Economist</u>, September 23-29, 1990.**

More than simply analyzing the "lost decade" of the 1980s, this superbly written (and ambitious) feature by <u>The Economist</u>'s economics editor chronicles the entire postwar development experience of the LDCs. The author argues that the inward-looking/import substitution policies that were in vogue from the 1950s to the 1970s--especially in Latin America and Africa--failed to create a foundation for sustained, balanced economic growth. A highlight of the survey is a series of graphics and tables based on World Bank data demonstrating superior overall economic performance for countries that have pursued market-based policies, particularly with respect to prices, interest rates and trade. Considering the whole range of structural reform policy options, what matters most, he says, is outward-looking trade policies. The author takes issue with the notion that import restrictions and heavy export incentives policies made South Korea a fast-growing dynamic exporter. Instead, says the author, South Korea's record in the 1980s shows that the nation countered a moderate and declining degree of domestic protection with just enough export promotion to achieve broad neutrality.

De Soto, Hernando. **<u>The Other Path: The Invisible Revolution in the Third World</u>.** **New York: Harper & Row, 1989.**

This widely read and highly acclaimed book is an important addition to the literature on structural reform. Peru is the subject for the author's empirical research of this country's informal sector, and his findings are invaluable to understanding the existence and growth of the sector in Peru and in other underdeveloped countries. A key aspect of the author's analysis is that the informal sector has endured because of the mercantilist structures of the political economy; these structures have distorted the functioning of the market, with the result being broad and unreasonable laws that benefit only privileged interest groups. The author and his affiliated organization Instituto Libertad y Democracia (ILD) have unveiled the entrepreneurial and democratic spirit of the participants in the informal sector and offer evidence which says that these individuals are forced away from the formal sector because of its unbearable regulations and high costs of entry. The author believes that the cumbersome and inadequate legal framework in Peru is a barrier to the productive development and operation of the market. In accordance with other research on this topic, "The Other Path" reveals the informal sector as a symptom, and specifically a symptom of "institutional dysfunction." The informal sector is also a solution for illustrating and explaining the causes of underdevelopment.

Devarajan, Shantayanan and Dani Rodrik. "Trade Liberalization in Developing Countries: Do Imperfect Competition and Scale Economies Matter?" American Economic Review, May 1989.

The authors examine the roles of imperfect competition and scale economies in a general equilibrium model of a developing country--Cameroon. They analyze the impacts of trade liberalization under two sets of conditions: oligopolistic market structure in some sectors and oligopoly combined with economies of scale. They conclude that imperfect competition and scale economies do indeed matter. Interestingly, trade liberalization is found to work to the disadvantage of cash crops and to the benefit of selected manufacturing sectors, especially intermediate producers and food processing firms, which are observed as responding to liberalization by boosting output.

Dornbusch, Rudiger. "Overvaluation and Trade Balance." The Open Economy: Tools for Policymakers in Developing Countries. Rudiger Dornbusch and F. Leslie C.H. Helmers, eds. Oxford: Oxford University Press, 1988.

This article dissects the problem of overvaluation, with respect to the balance of payments of developing countries. Not only does overvaluation make imports artificially cheap, it also reduces the external competitiveness of a country. Victims of this process are domestic production, employment and fiscal revenue. The author's strong case for a realistic, market-driven exchange rate is not carried to the extreme--that is, fully flexible exchanges are not prescribed, especially for developing countries, among other reasons because of the potentially destabilizing actions of speculators. At the same time, real exchange rates should not be allowed to appreciate, even during export windfall years. Undervaluation, which maximizes a country's external competitiveness and often results in large trade surpluses, poses no acute risks but over time could slow growth by discouraging domestic savings and investment.

Douglas, Roger. "The Politics of Successful Structural Reform." The Wall Street Journal, January 17, 1990.

New Zealand's recent success with structural economic reform is the subject of this article, which was written by a former member of that government's policymaking team. In contrast to the gradualist positions frequently espoused by developing country analysts, the author prescribes an aggressive approach to structural reform. For effective structural reform, the author suggests the following: electing quality politicians to establish the right policies; implementing reform policies in "quantum leaps" ("advancing a step at a time will give the interest groups time to mobilize and restrain the reform"); reforming at a rapid pace ("it is impossible to move too fast"); maintaining momentum to keep the government at the forefront of the economic policy debate; and keeping the public informed throughout all stages of the reform process.

Edwards, Sebastian. "On the Sequencing of Structural Reforms." OECD Department of Economics and Statistics. OECD Working Paper No. 70, September 1989.

The author details the debate in the literature regarding the sequencing of structural economic reforms--whether current account liberalization should precede capital account liberalization or vice versa. A framework is then developed to test the validity of each proposition. The results indicate that capital market distortions are more welfare-reducing than trade distortions and therefore should be reformed first. This is true, however, only when shadow prices can be established to appropriately guide allocation of resources until the tradeable sectors of the economy can be reformed. The author also looks at the debate between reform and stabilization and draws the conclusion that the degree of macroeconomic distortion should determine the degree to which stabilization must take precedence over structural reform programs. Finally, the author also argues forcefully that credibility and consistency are key to the successful implementation of any reform program. The absence of credibility, the author asserts, is equivalent to a distortion itself.

Frischtak, Claudio R. "Competition Policies for Industrializing Countries." Policy and Research Series 7. Washington, D.C.: The World Bank, 1989.

The creation of a competitive environment is the most effective way for developing countries to stimulate modernization and structural change. But the least-developed countries must take other steps--i.e., build up their industrial endowments, markets and institutions--before competition can be fully used as an effective industrial policy tool. This does not mean that competition-producing policies should be postponed indefinitely; the author asserts that countries should stimulate competition at the same time that they are building up industrial endowments. Competition is required if countries are to move beyond the initial stages of industrial development. Japan and the successful East Asian countries are held up as examples of countries that have achieved high levels of technological and managerial maturity via competition in home and foreign markets.

The proper sequencing of competition policy reforms is important. It is not crucial for regulatory reform to precede export development and trade liberalization. However, all three policy moves, the author argues, must be launched jointly or within a year or two of each other. Otherwise, rapid import liberalization, for example, could result in a negative supply response. In general, policymakers need to provide a structure of incentives and the right institutional setting to stimulate entry and competition in high-priority sectors. Owing to natural entry barriers existing in foreign markets (e.g., protectionism, lack of marketing know-how, etc.), a temporary pro-export policy bias is sometimes justified. Encouraging specific companies or industries via incentives is risky, unless clearly done on a temporary basis, with specific goals in mind.

Ghatak, Subrata and Derek Deadman. "Money, Prices and Stabilization Policies in Some Developing Countries." Applied Economics 21, 1989.

The "right" adjustment moves for a developing nation may be insufficient to bring about price and payments stability. Even the most conservative fiscal policies can be undermined by severe external shocks, such as the oil price hikes of the 1970s and 1980s. Examining the case of Thailand, for example, the authors attribute rising inflation to the oil price increase, not higher government spending. In environments of rising inflation in which government spending and money supply indicators are unchanged, the authors question what they call traditional IMF prescriptions centering on money supply reduction. Also, while they do detect a positive relationship between higher interest rates and savings levels, the overall impact is not always significant.

Haggard, Stephan and Robert R. Kaufman. "Economic Adjustment in New Democracies." Fragile Coalitions: The Politics of Economic Adjustment. Joan Nelson, ed. Washington, D.C.: Overseas Development Council, 1989.

Dictators in developing countries have no better economic reform records than their democrat counterparts. A close examination of policymaking in 25 developing countries in the 1978-1986 period shows virtually no differences between continuous democratic regimes (e.g., Venezuela and India) and continuous authoritarian regimes (e.g., Mexico and Zambia). But the authors also observe that countries experiencing democratic transitions (e.g., Brazil and Turkey) appear to be more expansionist than countries in either of the other two categories, especially with respect to government spending and growth of central bank credit. Significant differences in policy performance appear between regimes undergoing democratic transitions. Economic conditions existing at the time of the political changeover help explain some of these differences. The authors urge creditors to allow for "policy experimentation" on the part of debtor countries undergoing reform. Wage and price controls may, for example, help break inertial inflation. External assistance from creditors and donors is important, but should be made conditional upon policy reform. Adjustment programs should be designed and timed to maximize the use of political "honeymoons" of new regimes.

Hamilton, Clive. "The Irrelevance of Economic Liberalization in the Third World." World Development 17, 1989.

The author takes issue with the argument that, in the developing world context, government intervention stifles entrepreneurial initiative and profitable activities. For social, cultural and developmental reasons, the adversarial government-business relationship that exists in the West is largely absent in the developing world (and in Japan for that matter). The bureaucracy is much more closely intertwined with business. Government regulation is seen as much less of a constraint. In fact, it is viewed as an agent that supports private capital formation. The nature of the government-business relationship combined with the economic leadership role that the state traditionally plays in developing countries renders economic liberalization dangerous. The author suggests that the West's interest in penetrating developing world markets may render its liberalization promotion activities self-serving.

Hemming, Richard and Ali M. Mansoor. "Is Privatization the Answer?" Finance and Development, January 1988.

This is an informative and helpful review of the most important arguments in favor of public enterprise and government intervention in the developing country context. The authors assert that in the case of public utilities, public ownership may be the preferred means of achieving efficiency when alternative forms of regulation are too complex and costly for developing country governments to undertake. At the same time, they suggest that the problem of ownership and control of "natural" monopolies might best be handled by the awarding of franchises on a competitive basis. Examples provided include contracting out services such as street cleaning and garbage collection. The economic grounds for privatization are more apparent than real, they say. The key is combining privatization efforts with broader liberalization policies, especially trade liberalization.

Krueger, Anne O. "Government Failures in Development." The Journal of Economic Perspectives 4, 1990.

This author suggests that research in development economics should direct its attention to the causes, nature and effect of "government failures" in developing countries. She points out that past development economists turned to government intervention in the economy to make up for "market failures" which were believed to be severe in undeveloped countries and a major roadblock for development. Much of the government action that has been taken in developing countries has not only failed to deal with the "market failures" but has in fact actively hindered development. Some of these policies were pursued for the personal gain of individuals in power, and others may have been simply well intentioned but misguided. The net result, whatever the cause, the author terms a "government failure." Much research has been done in other areas of economics on defining the object functions and constraints on political actors. Development economics, it is argued, would benefit from a similar effort.

Krueger, Anne O. "Problems of Liberalization." World Economic Growth, Arnold C. Harberger, ed. San Francisco: Institute for Contemporary Studies, 1984.

Economic liberalization often takes place in a crisis atmosphere marked by skyrocketing inflation, acute external disequilibrium and a mounting government budget deficit. This reality makes the design and implementation of reform programs exceedingly difficult. The author observes that trade liberalization programs have frequently been undermined by antiinflation efforts. Policy prioritization, as well as implementation timing, are key factors, since "total liberalization is generally unfeasible." Local economic circumstances and the structure of the targeted economy need to be taken into account in assessing the short-term costs and welfare benefits of various policy options. In the foreign trade market, controls are more costly the smaller the size of the domestic market. Similarly, producer price controls in agriculture tend to be more costly for poorer countries since a higher share of GDP is based in farming. With respect to labor and financial markets, the Asian Tigers are credited with having successfully combined free labor markets and liberalized trade with regulated financial markets. The author concludes with the assertion that optimal dismantling of controls must involve current-account transactions, agriculture pricing and the domestic labor and capital markets. Capital market reform should be delayed for an unspecified period.

Maddock, Nicholas. "Privatizing Agriculture: Policy Options in Developing Countries." Food Policy, November 1987.

This article evaluates the conditions behind, and options for, the privatization of state-owned enterprises (SOEs) in the agricultural sector of developing countries. On account of limited government activity in direct agricultural production, there may not be as many opportunities for reducing government involvement in this sector as there are in the industrial or infrastructure sectors. Also, developing country governments control a relatively small amount of land holdings. The greatest possibilities for privatization rest in the institutions that service the farm sector--e.g., state marketing organizations. Removing control from these bureaucratic and loss-making entities will increase efficiency in the marketing and distribution of agricultural goods both within and outside the domestic economy. Privatization possibilities also exist for state-run input supply companies (e.g., fertilizer suppliers). Overall, the author concludes that government involvement in the farm sector will remain sizeable, even where privatization takes place. Government involvement will be especially strong in countries where noncommercial objectives (e.g., food security, low food prices, etc.) are sought.

Nelson, Joan, ed. "The Politics of Pro-Poor Adjustment." Fragile Coalitions: The Politics of Economic Adjustment. Washington, D.C.: Overseas Development Council, 1989.

Much of the resistance to economic adjustment measures in developing countries is unrelated to the poor. Rather, opposition typically arises from politically muscular groups such as the middle class, domestic capitalists, and organized labor. The urban middle deciles of populations in countries such as Mexico have witnessed the greatest decline in living standards under adjustment conditions. These groups represent the greatest political threat to structural reform. Specially targeted pro-poor relief measures, such as food subsidies, can relieve suffering and promote social justice, but without strengthening the ruling regime significantly. Frequently, political expedience dictates that regimes expand subsidies to satisfy the less-needy middle sectors. The author argues that withdrawing of benefits from the middle class should be gradual and "accompanied by painstaking explanation and dialogue" as well as timed to coincide with political events that might cushion the impact or divert attention. Timing should also take into account other needed adjustment measures.

Organization for Economic Cooperation and Development. "Progress in Structural Reform." Supplement to OECD Economic Outlook 47, OECD, 1990.

This report provides an overview of economic reform progress in the OECD nations, as well as highlights of progress and problems in each of the 24 member nations. As an OECD document, this study clearly does not focus on developing country problems. It does, however, provide broader insights into the structural reform issues as they are being played out in the industrialized world. The greatest progress is seen in sectors where there exists a high degree of interdependence on the part of member nations--liberalizing financial markets and reforming investment, taxation and competition policies. In contrast, the OECD as a whole has made "comparatively little progress" in liberalizing trade and agricultural policies.

Pfeffermann, Guy P. and Andrea Madarassy. "Trends in Private Investment in Thirty Developing Countries." IFC Discussion Paper No. 6. Washington, D.C.: The World Bank, 1989.

This survey of investment trends over 1970-1988 for 30 developing countries confirms that private investment has been on the rise in recent years. One interpretation of this finding is that the fruits of structural economic reform are beginning to show in the developing world. The authors' research reveals that public investment's share of total investment has been falling since the advent of the debt crisis in the early 1980s. At the same time, private investment, after reaching its low point around 1985-1986 (an average 9.6 percent of GDP versus 12.9 percent in the 1970-1979 period), has begun to recover. One important finding, drawn from periods when public investment was increasing rapidly, was the observed absence of a "crowding-out effect." That is, private investment does not appear to have been discouraged by higher levels of state investment spending.

Pinstrup-Anderson, Per. "The Impact of Macroeconomic Adjustment: Food Security and Nutrition." Structural Adjustment & Agriculture: Theory and Practice in Africa and Latin America. Simon Commander, ed. London: Overseas Development Institute, 1989.

Explicit considerations of the short-term effects of macroeconomic adjustment on the poor are crucial, both to avoid human suffering and to ensure long-term political stability and economic growth. While acknowledging the lack of hard empirical evidence, the author observes some indications of nutritional decline in select African and Latin American countries that corresponds with periods of macroeconomic adjustment policies. To limit the possibility of negative nutritional effects, the author recommends the following policy modifications: extending stabilization periods over longer time periods; a greater emphasis on supply expansion and less attention to demand contraction; a selective removal of market and institutional distortions in the economy rather than "a single-minded pressure for market liberalization"; boosting the capacity of the poor to generate income; and measures to enhance the productivity of the self-employed in the informal sector.

Porter, Michael E. The Competitive Advantage of Nations. New York: The Free Press, 1990.

Although the primary foci of this massive work are the industrialized and newly industrialized countries, there is no shortage of relevant material for the developing world and Eastern Europe. Chapter 12 ("Government Policy") is particularly rich in its balanced assessment of the proper role for government in creating and upgrading factors. Governments should ensure the existence of skilled human resources, basic scientific knowledge, economic information and infrastructure. But governments should limit their efforts at factor creation in these generalized areas. By involving themselves in creating specialized factors, they run the risk of creating the wrong factors at the wrong time.

The author asserts that direct subsidies represent the wrong kind of government intervention and do not help build true competitive advantage. Subsidies delay industrial adjustment and innovation. Tax incentives are generally preferable because they force firms to undertake only those projects in which they see the prospect of an economic return. The author acknowledges the potential value of devaluations for nations in the relatively early stages of competitive development (which are factor- or investment-driven), but warns against overdependence on price competition, which rarely leads to long-term productivity growth. He also warns against an overreliance on foreign direct investment which he says may doom a developing nation to be factor-driven. In contrast, indigenous companies tend to upgrade competitive advantage beyond basic factors.

Sachs, Jeffrey D. "External Debt and Macroeconomic Performance in Latin America and East Asia." Brookings Papers on Economic Activity, Volume 2, 1985.

The author tackles the question of why East Asia's economic record is so far superior to that of Latin America's. His assessment of the available data leads him to rule out the following popular explanations: that Latin America was worse hit by the external shocks of the early 1980s or that Latin America simply overborrowed. Backing the earlier works of Bela Balassa and Anne Krueger, he concludes that the most important differences center on trade regimes and exchange rate management. That is, the divergence occurred because (1) exports grew more rapidly in Asia than in Latin America, and (2) Asian exchanges were kept sufficiently competitive to encourage exports and avert destabilizing capital flight.

The foundations for both export promotion and import substitution policies are political. The former policy preference tends to favor rural interests, especially in agriculture. Import substitution, in contrast, by shielding the domestic manufacturing sector and thus protecting jobs, is an urban-based strategy. The relative strength of urban groups in Latin America has, until very recently, meant a heavy import-substitution bias. In South Asia, meanwhile, the relative strength of rural groups has resulted in notably stronger pro-export policies. Latin America's failure to boost exports has exacerbated its debt burden and forced growth-stunting reductions in imports.

Sachs, Jeffrey D. "Trade and Exchange Rate Policies in Growth-Oriented Adjustment Programs." Growth-Oriented Adjustment Programs. Vittorio Corbo, Morris Goldstein and Mohsin Khan, eds. Washington, D.C.: International Monetary Fund and The World Bank, 1987.

This is a sharply critical assessment of the outward-oriented or "new orthodoxy" school of development thinking with respect to its applicability to developing countries suffering severe external debt burdens. The success stories of East Asia are inappropriate models for developing countries today. Japan, Korea and Taiwan all solved their macroeconomic problems before embarking on export-led development programs. The author contends that the economic crises in the Latin American Southern Cone in the 1970s are proof of "the conflicting requirements of stabilization and liberalization." In addition, the East Asian example sheds light on the distinction between export promotion and liberalization policies. The East Asian experience suggests that export promotion policies might best be pursued by a *dirigiste* government, "and even in the presence of tight import controls and tight regulations in the capital markets." Also, in contrast to Latin America, the relative equality of income in East Asia has allowed governments there to concentrate on promoting efficiency.

Macroeconomic stabilization should precede any dramatic shift to liberalization. The author argues that pro-export policies can be pursued successfully by interventionist governments and without across-the-board import liberalization. But redressing fiscal imbalances, which feed inflation, is crucial to the reform process. Without this, exchange rate reform and trade liberalization will not achieve their intended goals. "Shock" programs may be acceptable as temporary measures to end high inflations but they are not without complications. The author concludes by saying that the centrality of the fiscal crisis in Latin America will necessitate greater amounts of debt relief.

Schumacher, Dieter. "The Market Economy: No Panacea for Developing Countries." Intereconomics 21, 1986.

This article analyzes some empirical studies that formed the basis for the development policy debate centering on whether the market economy is more successful in the developing world than central planning. These German studies attempted to show a connection between the type of economic system, from strongly market-oriented to strongly socialist, in a country and its development performance during the 1970s. Average results for groups of developing countries were determined from socioeconomic indicators. Although the studies concluded that developing countries classified as market economies generally obtained higher economic growth, the author questions the meaningfulness of these results. The exclusion of very low income countries and countries undergoing political change from the study would show no significant difference in average growth between the two groups of economic systems. The author concludes that a free-market structure is not always the answer. Rather, it is how an economic system is organized, governed, and how effectively resources are directed that are the key to an economy's success.

Shirley, Mary. "The Experience with Privatization." Finance and Development, September 1988.

Privatization should not be viewed as an end in itself but rather as a means to a broader end. Reviewing the World Bank's research into privatization campaigns in 37 developing countries, the author identifies the most common problems and obstacles to such efforts. Among these are the tendency to reward buyers of state companies with market-distorting incentives; underdeveloped capital markets, which make it difficult for would-be buyers to raise capital; high short-run social costs (e.g., unemployment) and the inadequate administrative capacity on the part of privatizing regimes. One valuable recommendation offered is to limit the potentially high social costs of privatization by partially compensating, for example, laid-off workers, with the proceeds of the asset sale.

Shirley, Mary. "The Reform of State-Owned Enterprises: Lessons from World Bank Lending." Policy and Research Series 4. Washington, D.C.: The World Bank, 1989.

Between 1978 and 1988 the World Bank funded some 122 projects aimed at reforming state-owned enterprises. This study is based on the results of those operations. The basis of World Bank activity in this area is that all enterprises, public or private, function most efficiently when they strive to maximize profits in a competitive market. Management must be autonomous in the sense that it has the administrative capacity to respond to market signals. Efficiency dictates that bankruptcy must be a consequence of a failure to compete. Since operating conditions for many state companies in the developing world are very different from this, the bank often recommends privatization. At the same time, the bank urges a cautious, gradualist and coordinated approach to privatization in, for example, Sub-Saharan Africa, where state companies frequently play a dominant role in the economy. Among the pitfalls of public enterprise reform are the following: the ignoring of the underpricing of state company outputs; the promotion of trade liberalization without preparing state companies for new competitive pressures and government injection of new equity into failing state enterprises.

Stewart, Frances. "Alternative Macro Policies, Meso Policies, and Vulnerable Groups." Adjustment With a Human Face, Volume 1. Giovanni Andrea Cornia, Richard Jolly and Frances Stewart, eds., 1987.

This article focuses on the design of macro policy adjustment strategies that will best protect the vulnerable groups of a society. Growth-oriented adjustment is the basis for the macro policies' design and is necessary to halt the decline in per capita income. Three mechanisms for economic growth are discussed: improving employment and wage levels, improving the supplies of food, and increasing taxable capacity. The author discusses the need for a high level of external finance and/or an ability to defer payments on existing debts to ensure growth-oriented adjustment in developing countries. In choosing economic policies, it is suggested that governments focus on: (a) policies that are directed at influencing macro aggregates in the economy; (b) policies that influence the allocation of income and resources ("meso" policies); and (c) policy reforms and institutional changes that will improve the performance of existing policies and encourage participation of the vulnerable population groups.

Taylor, Lance. Varieties of Stabilization Experience. Oxford: Clarendon Press, 1988.

The World Institute for Development Economics Research (WIDER) in Helsinki sponsored studies of 18 developing countries undergoing economic stabilization programs. The Taylor work is an overview and analysis of the results of those studies. It also is a critique of orthodox IMF and World Bank stabilization prescriptions and "heterodox" shock programs fashioned by countries such as Brazil and Peru in the 1980s. The author observes that the outcome of orthodox stabilization programs has ranged from moderately successful (Colombia) to disastrous (Chile in the early 1980s). Nor have heterodox approaches proved significantly more successful at promoting stability and growth. The shortcoming of this work is its preoccupation with stabilization failures and its lack of attention to market-oriented reform policies. The author is, generally speaking, critical of the long-term effects of liberalization policies in the developing country context.

Van de Walle, Nicolas. "Privatization in Developing Countries: A Review of the Issues." World Development, May 1989.

This is a brief but sophisticated overview of key privatization issues. The article is especially rich in its identification of the main political and implementation constraints related to privatization. The author observes that governments sometimes agree to sell off state assets to avoid having to implement broader (and more politically difficult) liberalization measures. Moreover, the buyers of these assets are sometimes granted market-distorting privileges in the form of tariff protection, tax incentives and monopoly privileges. Among the author's findings are that market inefficiencies are more a result of government regulation and market structure than they are a function of ownership. Thus, privatization's effects "are likely to be modest in the absence of other reforms."

Waterbury, John. "The Political Management of Economic Adjustment and Reform." Fragile Coalitions: The Politics of Economic Adjustment. Joan Nelson, ed. Washington, D.C.: Overseas Development Council, 1989.

An essential task for policymakers in the process of implementing structural economic reforms is coalition management. Regimes must understand how the reform process will impact various components of its coalition and avoid injuring the interests of all coalition members simultaneously. On the basis of his analysis of Pakistan and six Middle East countries, the author argues in favor of spreading the burden of adjustment over time. High impact measures such as devaluation, wage de-indexation and subsidy withdrawal should not be attempted at the same time. Coalitions should not be intentionally weakened. In fact, early on, the political leadership should take steps to attract or retain constituents. Some key tactics are incentives to key economic leaders, compensation for the highly disadvantaged and rents for spoils to state officials and private sector allies.

Weede, Erich. "The Impact of Democracy on Economic Growth: Some Evidence from Cross-National Analysis." Kyklos 36, 1983.

The author considers the compatibility of democratic government and economic growth in the developing country context. Much of the economic development literature has focused on the tension between the two goals and indeed several respected analysts have supplied convincing evidence that authoritarian rule tends to promote economic growth while democracy tends to retard it. Using cross-national and cross-sectional multiple regression analysis of data from the 1960s and 1970s on some 70 countries, and including nonpolitical determinants of economic growth as control variables, the author finds that "the overall effect of political democracy on economic growth is negative, but very weak." A fairly strong and negative impact of democracy on growth can be demonstrated--but only for a minority of nations where state intervention in the economy is extreme (i.e., government revenue exceeds 20 percent of GDP). Elsewhere, the author finds no relationship at all. Thus, these findings suggest that it is not democracy alone, but the combination of democracy and heavy state intervention that compromises economic growth.

The World Bank. World Development Report 1990. Oxford University Press, 1990.

The Bank's commitment to promoting structural economic reform is reflected in its 1990 development report, the theme of which is poverty. Particularly important is the chapter, "The 1980s: Shocks, Responses and the Poor." Based on the experiences of a diverse group of developing countries, the Bank makes a case for swift action on fundamental reform policies growth (e.g., price adjustment and fiscal reform) in conjunction with carefully applied policies, such as social service transfers, which moderate demand contraction during the adjustment period. Removing exchange rate and price distortions will help, rather than hurt, the poor, by raising returns to agriculture, which will boost rural incomes. (Rural areas account for 80 percent of Sub-Saharan poverty.) Sub-Saharan Africa presents unique challenges because of the region's severe poverty and the governments' inability to further restrain expenditures. As the case of Ghana shows, structural reform must be accompanied by foreign aid infusions for investment and consumption to recover.

Another key observation is developing country policymakers' need to build coalitions in support of structural reform programs--a difficult task given the short-run social costs typically involved. Many East Asian countries built powerful reform constituencies, but under relatively favorable initial conditions. Crises can strengthen overall support for policy change by creating new hope for the economically disadvantaged and weakening the influence of antireform interest groups.

Regional Studies

Africa

Bartlett, Bruce. "The State and the Market in Sub-Saharan Africa." World Economy, September, 1989.

This is an examination of the pre-colonial, colonial, and "decolonialized" African economies. The author ventures that it is statism, not colonialism per se, which has constrained the development of capitalism in Sub-Saharan Africa. Pre-colonial Africa exhibited some elements of a capitalist economy, but social customs were most often a barrier to a truly free and voluntary market. The author suggests that the colonial experience, with its strong government intervention, left African leaders with the impression that private enterprise was a form of imperialistic control. Although they thought socialism would move their countries away from colonial economic policies, the author attempts to show how the leaders' new socialist policies were just a continuance of state control over the economy. It is pointed out that agricultural marketing boards, which were established by the colonial governments, continued to exist after decolonization. Control over agricultural prices and other factors--the creation of state-owned enterprises, the evolution of the informal economy, heavy taxation, and the rise of Africa's immense foreign debt--produced Africa's current economic woes. African governments have started to recognize socialism's negative economic impact and are attempting to alter policies, and thus, according to the author, there is potential for the development of the private sector.

Gordon, David F. and Ernest J. Wilson. **<u>Workshop on Economic Reform in Africa</u>. The Center for Research on Economic Development at the University of Michigan, December 1989.**

This report is based on the "Workshop on Economic Reform in Africa" held in Nairobi, Kenya, July 18-20, 1989. Among the key findings were the following: the evidence thus far on the success of structural economic reform in Africa is ambiguous at best. Efforts have not been under way long enough, nor have they been steady or vigorous enough. Also, the poor African results suggest that external factors have not been sufficiently factored into performance evaluations of reform efforts. A guiding principle for future African reform should be the need to minimize the social cost of reform. The workshop participants thought fiscal reform a precondition to the success of other reforms, especially since, for example, a typical devaluation leads to higher import tax revenues and higher debt interest charges. Fiscal reform also gives rise to a desirable redirection of resources, public to private. Other reforms that participants thought needed greater attention included employment policies, capacity utilization and portfolio management of ongoing projects and programs.

Green, Reginald Herbold. "Articulating Stabilisation Programmes and Structural Adjustment." <u>Structural Adjustment & Agriculture: Theory and Practice in Africa and Latin America</u>.

The author identifies and assesses the main points of conflict between IMF stabilization prescriptions and agricultural development objectives in the Sub-Saharan Africa context. In a general sense, agriculture requires a micro or sectoral perspective, and the payoff for farm development policies is long-term. In contrast, the IMF is concerned with macro policy measures and its vista is clearly short-term. The author identifies two specific problems related to the Fund's macro model, which is based heavily on prices. One, the macro model does not factor in real variables. Therefore, an agriculture model cannot be easily integrated into it. Two, none of the variables in an extended sectoral model can be quantified with any precision (except nominal prices). The author suggests alternative agricultural adjustment strategies that he claims are consistent with bottom-line IMF objectives but that are not, as Fund programs frequently are, destabilizing.

Gulhati, Ravi. "The Political Economy of Reform in Sub-Saharan Africa." <u>Economic Development Institute Seminar Report No. 8</u>. Washington D.C.: The World Bank, 1988.

This report is a summary of two World Bank workshops on Sub-Saharan Africa economic reform. The meetings, which were held in late 1986, brought together development professionals and scholars to discuss issues related to economic reform in the African context. Among the key findings to emerge were the following: the participants agreed that the region's economic crisis was a product of both exogenous shocks and policy failures. However, the relative weight of these factors varied significantly across countries. The existence of high levels of economic distortions was not a reliable predictor of intense reform programs. Nor did the participants discern a relationship between reform intensity and type of political regime. Referring to previous research by P. Cleaves, the author of this report identifies five important reform factors: the higher degree of complexity of the desired change, the lower the chance of success; incremental change enjoys a better chance of success in that it reduces the amount of information required and the risk of error; changes involving many actors are more difficult than those affecting fewer actors; multiple or unclear goals complicate reform implementation; and, finally, the longer the time frame for policy implementation, the greater the difficulty of implementation.

Helleiner, G. K. "Outward Orientation, Import Instability and African Economic Growth: An Empirical Investigation." Theory and Reality in Development. Sanjaya Lall and Frances Stewart, eds. New York: St. Martin's Press, 1986.

The discussion surrounding export orientation in African countries is the subject of this article. The advice to be more "outward-oriented" is borne out of economic development theories that hold that increased exports are instrumental in accelerating economic growth. The author analyzes empirical and econometric research and concludes that the effects of external instability had a profound impact on Africa's ability to implement outward-oriented policies. The author discusses the global recession of 1979-1982 and the international lending institution's reaction to Africa's credit problem. The major conclusions are that Africa's interaction with the global economy in the 1960s and 1970s showed that it is more important to stabilize import volumes than to increase exports. Furthermore, the region would have benefitted greatly from receiving increased international liquidity to tide countries over during acute balance-of-payments stress.

Wilson, Ernest J. "Privatization in Africa: Domestic Origins, Current Status & Future Scenarios." Issue 16, 1988.

This article addresses the much debated topic of privatization in Africa, where it is struggling against well-established views on the need for economic nationalism, redistribution and heavy state intervention. Privatization, according to the author, offers a valuable opportunity in social science to examine the relationship between the public and private sectors. Buttressed by policies that promote deregulation and greater market competition, privatization can help African governments revitalize their economies. Three scenarios are presented on the possible role of privatization in the future of African economies: (1) privatization as a permanent goal of reform, which is necessary to correct the failures of excessive state intervention; (2) privatization as a function of economic forces and business cycles--widely espoused in the current austerity but probably deemphasized as economic conditions improve; and (3) privatization as an economic policy tool, which represents a temporary interruption of longer-term, politically driven economic policy.

The author offers the following observations, which are drawn from actual cases of privatization: support for privatization in an African nation requires an ample local business class, politicians who are willing to take the risk of alienating important constituencies who are opposed to economic reform, and manageable ethnic and racial strife; privatization appears to be the most effective in small to medium-sized firms; and a change in ownership may not be as important as the quality of management appointed to run the newly privatized enterprise.

Asia

Amsden, Alice H. "East Asia's Challenge to Standard Economics." The American Prospect, Summer 1990.

This article champions the interventionist policies of the East Asian economies as a model for success that may be adoptable by other developing nations and one that deserves consideration from free-market advocates of the developed world. Highlights of the author's arguments for recognition of the East Asian paradigm include the governments' effective distortion of market prices (i.e., setting a negative interest rate for preferred borrowers) to stimulate investment and trade and their high degree of control over industry (i.e., allocating subsidies for only those firms that meet government-determined performance standards). Neither of these techniques is consistent with market-based reform, yet resulted in a surge of industrial growth for East Asian countries. The author suggests that transferring the methods that worked well for South Korea and Taiwan to other developing countries warrants examination; however, the corresponding economic distortions that occurred as a result of government intervention must be investigated as well.

Gill, David. "Privatization: Opportunities for Financial Market Development." Privatization and Structural Adjustment in the Arab Countries. Said El-Naggar, ed. Washington: The International Monetary Fund, 1989.

Since the main benefits of privatization relate to efficiency factors, the author argues that the transfer of public assets to private hands will only be effective if management can be assured of independence from the state. He asserts that a strong and efficient financial market is essential for privatization of enterprise management and control, as well as ownership. Depending on the setting, privatization itself can create favorable conditions for equity market reforms. With respect to financial market conditions in the Arab countries, privatization might ease budgetary constraints as well as enhance private sector resource allocation--i.e., making risk capital returns more attractive than interest-bearing deposits. There exist strong social and cultural biases against small minority shareholders in the Arab world, however. Furthermore, nonbank financial institutions (e.g., pension funds) are not as developed as they are, for example, in many middle-income and developing countries. The creation of a strong institutional investor base in the Arab world is therefore essential for successful privatization.

Streeten, Paul, ed. Beyond Adjustment: The Asian Experience. Washington, D.C.: International Monetary Fund, 1988.

The bulk of this work is papers from a 1986 conference jointly sponsored by the IMF and the Indian Council for Research on International Economic Relations. Among the salient conclusions were the need for critical assessment of the practical implications of comparative advantage doctrine in the developing country context. While the doctrine holds, for example, that comparative advantages (and disadvantages) are translated into absolute price advantages (and disadvantages), the mechanism does not always work. Massive speculation and other factors can undermine the process. More fundamentally, comparative advantage should no longer be regarded as a static notion. It is changing continually, in many ways in response to research and development expenditures.

In trade policy, it was noted that periods of import substitution often precede export phases. (This is true for firms as well as countries.) However, both import substitution and export promotion must be efficient. Investment decisions, for manufacturing and agriculture alike, must be made on the basis of future prices and market opportunities. Investment strategies must strive to allow for switching between domestic- and export-driven market strategies, depending on market signals. Trade liberalization programs must be designed with fundamental national characteristics in mind. Finally, the observation was made that Korea and Taiwan's export success was due to a significant extent to efficient government intervention.

Westphal, Larry E. "Industrial Policy in an Export-Propelled Economy: Lessons from South Korea's Experience." The Journal of Economic Perspectives **4, 1990.**

The author argues that economic intervention by the Korean government has contributed to rapid achievement of international competitiveness in a number of industries. He also argues that Korea's performance owes much to the government's focus on international competitiveness and on its reliance on free-market institutions to provide for flexibility in resource allocation. The government's intervention was most effective when it targeted only a few industries based on their expected profitability in international markets. Of equal importance, however, was the fact that the government also allowed private initiative to exploit export opportunities in areas not targeted by the government. Where the government targeted an industry, the objective was to attain international competitiveness within an explicit medium-term time horizon. This targeting was least successful when the government failed to do sufficient research required to evaluate the opportunity, when it failed to reevaluate a decision in the face of changes in the global markets, and when the choice of too many targets overextended the country's scarce and specialized technical and entrepreneurial talents. Politically, these policies were pursued by an "economically enlightened dictatorship" which was wil'ing and able to force highly successful private individuals "to employ their wealth in socially productive development activities."

Eastern Europe

Cochrane, Nancy J. and Miles J. Lambert. "Eastern European Agriculture: Pressures for Reform in the Eighties." Pressures for Reform in the East European Economies, Volume 1, Study Papers Submitted to the Joint Economic Committee of the United States Congress. **Washington, D.C.: U.S. Government Printing Office, 1989.**

Agricultural reform in Eastern Europe will yield quicker benefits than reform of industrial enterprises because agricultural enterprises generally require less time and investment to alter the structure of production. The authors hold that the existence of significant private ownership in Eastern Europe--even in rigidly centralized countries such as Romania--could further speed the reform process. Other factors clearly will inhibit the reform movement: the sector's subordinate role to industry, the subsequent strict regulation of farm prices and agricultural trade and official resistance to more extensive private agriculture.

There are two distinct approaches to Eastern European farm reform. The so-called "Bulgarian Model" involves higher farm autonomy and greater productivity incentives but still holds producers hostage to official planning dictates. The Hungarian Model, in contrast, provides considerably greater autonomy at the farm level, especially with respect to supplier choices, investment decisions and pricing. Reforms undertaken in the 1980s have yielded results, seen in the significant rise in the private sector's shares of meat, fruit and vegetable production throughout the region. Countries such as Hungary that need hard currency to service their foreign debts will explore foreign trade opportunities (especially with the European Community) more aggressively.

Fureng, Dong. "Development Theory and Problems of Socialist Developing Economies." The State of Development Economics: Progress and Perspectives. Gustav Ranis and T. Paul Schultz, eds. New York: Basil Blackwell Inc., 1988.

Development theory in socialist developing countries has been largely based on the concept of socialist public ownership. In agriculture, this has had disastrous consequences since peasants tended to consume or sell off seed and livestock rather than turn them over to the commune, and once established, the peasants had no personal interest in maintaining the resources or improving their yield. Socialist enterprises in cities tended to operate under "soft budget constraints" in which losses were subsidized, profits were taxed away, and bankruptcy was nonexistent. In addition, the strategy placed its primary emphasis on heavy industry, national self-sufficiency, and high rates of growth rather than meeting basic consumer needs. As a result, the economies experienced chronic shortages of consumer goods, serious disproportion in resource allocation, and retardation of technological development.

In 1979, China began shifting its development objectives. Primary emphasis was placed on meeting basic needs, balancing the development of all sectors of the economy, and opening up to the outside world. In seeking these objectives, China experimented with long-term leases and outright enterprise sales as a means of relinking the risks and returns of an enterprise to its workers and management. Wholesale relationships between enterprises have been simplified. Financing is no longer freely allocated by the state but instead is loaned out through a banking system. Overall economic performance has improved with these reforms, but they have also resulted in a widening of income gaps and increased unemployment, both of which may be socially destabilizing.

Hardt, John P. and Sheila N. Heslin. "Measuring and Interpreting Economic Performance." Pressures for Reform in the East European Economies, Volume 1, Study Papers Submitted to the Joint Economic Committee, Congress of the United States. Washington, D.C.: U.S. Government Printing Office, 1989.

Eastern European systems of statistical measurement evolved in an environment of centralized decisionmaking, where private citizens did not play a role in decisionmaking and thus had no obvious need for information. Published data, as a result, tended to be used to achieve policy objectives rather than portray reality. Accurate and reliable statistical information is, of course, a basic component of effective decisionmaking, but it is also a basic component in performance evaluation. Many of the disastrous policy decisions and ill-founded investment projects of the 1970s may be traced to the unreliable information and the resulting inaccurate analysis. Credible statistical reform, including open publication of accurate, nonpoliticized data, is a key element in the domestic economic reforms now taking place in these countries.

Hardt, John P. and Richard F. Kaufman. Introduction to Pressures for Reform in the East European Economies, Volume 1, Study Papers Submitted to the Joint Economic Committee of the United States Congress. Washington, D.C.: U.S. Government Printing Office, 1989.

The authors discuss two types of reform options for Eastern Europe: equivocal reform and comprehensive reform. The former type is marked by gradual, step-by-step movements typically aimed at addressing specific problems. Comprehensive reform, on the other hand, is "systemic," involving fundamental changes across economic, military and social spheres. Comprehensive reforms will give Eastern Europe the best shot at achieving long-term growth and competitiveness in global markets.

But attempts at such massive shifts from planned to market-oriented economies will engender sizeable adjustment problems, among them: resistance from government and party elites and enterprise managers threatened by a loss of power; inflation resulting from price control and subsidy withdrawals; interruption of agricultural and industrial production during modernization phases; and unemployment and general political resistance as the bureaucracy shrinks and overstaffed enterprises are privatized.

Hinds, Manuel. "Issues in the Introduction of Market Forces in Eastern European Socialist Economies." (Mimeo.)

The author raises the question, "Can market-oriented reforms achieve their intended goals without extensive private ownership of production?" His answer is no. Without ownership reform, changes such as decentralization and price liberalization would move Eastern Europe toward a model that has failed in practice in Yugoslavia, which suffers from the core problems associated with central planning--insufficient investment of savings, overstaffing, toleration of loss-making enterprises and heavy enterprise indebtedness. Markets, the author insists, cannot function efficiently if private ownership is not predominant. For Eastern European countries attempting to achieve structural reform, the implications of this analysis are not encouraging. Current reform programs, which focus on decentralization, enterprise self-management, worker incentives and price reform, but do not alter the socialist structure of ownership, will ultimately fail. There is no viable half-way strategy. Prescriptions for enterprise and financial system reforms appear in the annexes of this paper.

Vacic, Aleksandar M. "Current and Prospective Economic Reforms." Economic Reforms in the European Centrally Planned Economies. New York: United Nations, 1989.

Surveying the economic reform experience of Eastern European countries in the 1980s, the author identifies a common set of problems that need to be addressed if lasting change is to take place. First, the problems at hand are often poorly diagnosed and, as a result, the proposed solutions are poorly designed and frequently off-target. Second, owing to the degree of distortions existing in their economies, Eastern European countries have been ill-prepared to deal with, for example, the relaxation of traditional economic management systems--e.g., mandatory planning indicators, state procurement, price controls, and subsidies. Consequently, reform proposals are either diluted or extended over longer time periods. Both of these impede the economic reform process. Third, the results of reform often lag behind expectations, in part because of a lack of realism but sometimes as a result of unfavorable exogenous factors. Fourth, while social and political tensions are a natural product of the reform movement, they can be attenuated by effective policy timing and coordination. Finally, economic reforms require corresponding adjustments in legislative and political systems. Bureaucracies, too, must be reformed and obstructive bureaucrats removed.

Van Brabant, Jozef and Paul Marer. "Reform and Membership of the Planned Economies in GATT, the IMF, and the World Bank." Pressures for Reform in the East European Economies, Volume 2, Study Papers Submitted to the Joint Economic Committee, Congress of the United States. Washington, D.C.: U. S. Government Printing Office, 1989.

Since the late 1950s there has been growing interest among the centrally planned economies (CPEs) in active participation in GATT. Requests by CPEs for association have been handled on a case-by-case basis, with no attempt to develop a comprehensive GATT program for CPEs. As a result, CPEs within GATT have tended to have a "second-class" status, consisting mainly of three elements: (1) stringent special provisions, such as quantity restrictions, designed to allow regular GATT members to insulate their economies from the CPEs; (2) import commitments, such as those accepted by Poland and Romania, which would be met by retaliation if not fulfilled; and (3) special restrictions in the CPEs trade with the U.S. The CPEs have generally been more reluctant to join the IMF since membership has stricter requirements, and have generally only joined after establishing membership in GATT. Economic reforms, increased internal openness, and reduced geopolitical tensions all make membership more attractive today. Membership may also be attractive to the extent that it provides outside support and pressure for difficult internal reforms.

The authors suggest that CPE membership in the international economic organization should be conditional on specific economic reforms within the CPEs. These include a granting of growing autonomy to producers and traders, the establishment of close links between internal prices and international prices, and an agreed-upon timetable for currency convertibility.

Wolf, Thomas A. "Reform, Inflation, and Adjustment in Planned Economics." Finance and Development, March 1990.

Structural economic reform programs in planned economies are frequently accompanied by acute price pressures and large current account deficits, according to the author. But both inflation and a nation's external situation are functions of macroeconomic policy, not economic reform per se. The sequencing of reforms may have a significant bearing on macroeconomic policy. Inflationary pressures may increase, for example, if rising retail prices are not checked by other policy liberalization measures--especially those moves that promote greater competition among producers. Financial discipline is characterized as the central requirement for market-oriented reform, as it reduces the possibilities for bargaining over financial relief and preferential credits; encourages the growth of private sector activities; facilitates more flexible and rapid resource allocation; establishes the basis for stable and uniform fiscal policies and paves the way for a truly independent banking system.

Latin America

Fishlow, Albert. "The Latin American State." The Journal of Economic Perspectives 4, 1990.

The author argues that recent changes in Latin American government policies in the development area are due to the convergence of two significantly different political trends. One is a market-oriented movement, which seeks to place as many public functions as possible into the private sector. The other strongly supports government involvement in the economy but, in the face of massive government deficits, recognizes the necessity of a new approach. Of the two, the latter has stronger and deeper political support. Recent economic emergencies, however, are forcing the recognition that the state is too large and too weak. The sought-after new strategy must increase public revenues and reduce expenditures. A financially sound state is expected to guarantee economic growth by allowing for increased public investment in infrastructure and public services--both prerequisites of private capital formation. State divestiture is thus viewed as a means of improving state involvement in future economic development.

Glade, William P. "Privatization in Rent-Seeking Societies." World Development, May 1989.

This article analyzes the dynamics and effects of rent-seeking behavior during privatization campaigns in four Latin American countries--Mexico, Chile, Brazil and Argentina. Traditionally, in all these nations, rent "has been distributed lavishly to buy political support." Privatization and economic liberalization in general thus represents clear threats to the political equilibrium. Chile, owing to the authoritarian features of the Pinochet dictatorship, proved most adept at reducing the economic role of the state. Mexico, in the last few years, has moved aggressively toward economic liberalization, but is now dealing with the social and political fallout resulting from the steady destruction of the old system. Of particular interest is the author's identification of privatization variants: semi-privatization (partial sale of state shares in an enterprise), simulated privatization (application of market-type performance criteria to state firms), and peripheral privatization (contracting out of public sector activities on a competitive basis).

Williamson, John. The Progress of Policy Reform in Latin America. Washington, D.C.: The Institute for International Economics, January 1990.

Based on the findings of a November 1989 IIE conference, this work examines ten key market-based policy reform areas and assesses the extent to which 10 reform-oriented Latin American countries have committed themselves to market-based policies. The reform categories are fiscal discipline; public spending priorities; tax reform; financial liberalization; competitive exchange rate; trade liberalization; foreign direct investment; privatization and deregulation. The findings show moderate to substantial reform in the 10 countries studied, with the most positive results evident in trade liberalization, fiscal discipline and tax reform. Bolivia, Chile and Mexico emerge as the top reformers.

Looking at the results of policy implementation across countries, the data do not supply proof that a switch to market-based policies has yet boosted economic growth in Latin America. There is, however, significant evidence that a few of the countries that have had substantial reform programs in place but had yet to take off (e.g., Mexico) were in fact on the verge of resuming growth. The author concludes that the transition to the "new realism" of market-based policies is still Latin America's best bet for renewed growth and development. He allows that circumstances may sometimes justify short-term measures such as heterodox shock plans, a stable exchange rate or even dollarization. Strong prescriptions for "Washington"--defined as the IMF, World Bank, the IDB and the U.S. government--are supplied at the conclusion. One of the most compelling of these is the need, in the absence of significant inflows of new investment capital, for sustained external support to strengthen the liberalization process.