Winners and Losers:

The Politics of Participation in Economic Policy Reform

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I. INTRODUCTION

The challenge of constituency management is at the heart of the politics of economic growth and democratic governance, as Bill Clinton no doubt reflected recently while presenting his "fast-track" treaty authorization goals to AFL-CIO members at their annual convention. All governments need constituencies and coalitions of support in order to govern, and they need feedback from constituents in order to make and modify economic policies. At the same time, economic reform creates winners and losers, fragments old coalitions, and limits democratic governments' traditional abilities to reward supporters. Resolving these challenges is the ongoing business of democratic governance.

From the government's side, constituencies are a mixed blessing.[1] Coalitions of various interests are critical for supplying the support democratic leaders need to get their reforms through the legislative process and to maintain reforms during implementation. Yet constituency demands may derail reforms that would be in the long-run public interest. Interest groups frequently possess the technical knowledge required to make some kinds of reform feasible. Yet government-interest group relationships that are too close create the danger of "capture" where agencies begin to identify more closely with special interests than the public interest. Interest groups articulate the needs of important societal groups, supply a generalized demand for more effective governance, and provide channels for negotiation and mediation between their constituencies and government. But they can also "radicalize and promote conflict" (Nelson, 1994, 150).

It is still believed by many that authoritarian governance is necessary for growth in low income countries; democracy can wait. This idea was reinforced in the 1980s with the phenomenal economic success of the four East Asian NICs, all of which began as authoritarian regimes. However, the idea that authoritarian regimes in general have growth-enhancing advantages over democracies has been shattered by research that demonstrates conclusively that there is no clear relationship between regime type and economic growth, or between regime type and success at stabilization or adjustment (Remmer 1990; Devarajan and Lindenberg 1993; Limongi and Przeworski 1997; Alesina and Perotti 1996).

Democracies don't always produce the best economic policies, and they don't necessarily do a better job than authoritarian regimes, but both new and established democracies are quite capable of growing their economies and of implementing the difficult economic reforms that are supposed to establish a more supportive environment for growth. In fact, Devarajan and Lindenberg (1993) found that in developing countries during the 1980s, established democracies performed better than authoritarian regimes *and* new democracies on stabilization and growth measures.[2] While democracies appear to be no better and no worse than authoritarian regimes at producing growth, growth may be critical for *sustaining* democracy in poorer nations. Recent research by Limongi and Przeworski showed that over time, poor countries with *growing* economies were more likely to remain democratic than poor or even middle-income countries suffering economic decline (1997, 167-169).

Given the wide variation in democracies and in nondemocracies, it is clear that the more important questions center on the quality of leadership and the capacity of government agencies, the relations between governments and their societies, and the processes that connect government decisions and policy implementation to affected groups. This paper explores the current state of knowledge about the role of interest groups and constituencies in economic policy reform. It begins by exploring the different kinds of reform, the political implications of stage and reform type, and the different kinds of interests. The next section examines some of the typical political problems presented by reforms, and the tension between autonomy and participation. The fourth section outlines some of the factors that affect the ability of groups to affect the policy process, and describes some of the ways in which reforms can be made more participatory and more sustainable at the same time. The final section addresses the role of foreign aid in this process.

II. WHAT REFORMS? WHAT CONSTITUENCIES?

During the first part of this century, the developing world relied heavily on exports of agricultural commodities and raw materials, and these were the groups with the most political influence. When most developing countries selected import-substitution industrialization strategies in the 1950s and 1960s, new coalitions formed around policies of cheap food and cheap credit, overvalued exchange rates, high formal sector wages, job security, public employment guarantees for university graduates, and protectionism. Backed by buoyant international commodity prices and the Keynesian consensus that governments facing unemployment problems ought to stimulate demand through government spending, governments were, for a time, able to avoid the hard choices between consumption and investment. The crash of commodity prices, international recession, the debt crisis, and the drying up of external finance forced countries to reexamine their development policy mix. More recently, the collapse of the Soviet Union's socialist model forced a similar reexamination in Eastern Europe. This is the setting within which countries are undergoing economic reform today.

What Reforms?

Economic reforms vary on a number of dimensions: purpose, ease of implementation, and the importance to their success of correct timing and/or sequencing. In general, the purpose of reform and the timing of reform affect the scope and desirability of participation. Some policy changes can be done through a "stroke of the pen": devaluation, raising interest rates, or decontrolling fixed prices. Others require much more complex negotiations and institutional changes. For example, privatization may require legislation to clarify and secure private property rights, capital markets, a methodology for assessing enterprise assets and liabilities, provisions for worker retraining, and so on. Reforms also have time dimensions. Any reform has a decision phase, and an implementation phase, and the political management of each phase may differ for good reasons. Sequencing may also matter. Reforms can be attempted all at once (shock treatment) or gradually, following some sequence dictated through an uneasy balance of economic theory and political feasibility. These sequences can cover successive stages of economic liberalization (McKinnon 1993) or choices about whether to liberalize the economy first, and then the polity (as in China or Chile in the 1980s) or to have democracy first, and then liberalization (as in Costa Rica or India) or both simultaneously (as in Russia).

In much of the world, the first generation of reforms -- stabilization -- was focused more on the less complex if still highly politicized decisions necessary to achieve macroeconomic stability in the wake of the debt crisis. These reforms generally included devaluation, and improved control over the fiscal deficit and money supply, and liberalization of trade, interest rates, and most prices. The second generation of reforms involves more microeconomic and institutional restructuring as well as additional liberalization: financial sector deregulation, tax reform, labor market reforms, export promotion measures, and social security system reform (Naím 1994). Although many governments and their advisers resist the delays and possible dilution that accompany participation in first generation (stabilization) reforms, consultation and negotiation over things like public and private sector wages can in many cases improve the sustainability of fiscal and monetary discipline. Second generation reforms require greater technical capacity, capacity which may be more easily found outside of government. Feedback and inputs from stakeholders can frequently improve the design and implementation of second generation reforms.

Stakeholders

Stakeholders are the individuals and groups whose interests are affected by a given policy. One of the primary tasks of democratic governance is coalition management: building and managing alliances of key stakeholders, partners whose support reinforces the leadership's ability to push forward its policy agendas (Waterbury, 1989, 39). Potential domestic coalition members, stakeholders and constituencies include organized labor; the urban informal or "popular" sector; the middle class; professionals like lawyers or physicians; business; farmers; the intelligentsia (including students); and state actors: policy elites or technocrats, public enterprise managers, and the military. Many stakeholders are located in civil society, but a significant number are also located within the state itself. International aid agencies clearly also become stakeholders as they join the policy circle with their own agendas and resources of funds and information. Individual stakeholders and interest groups vary in size and political clout, in their interest in becoming "partners" as opposed to fighting change, and in the extent of their losses and gains from reform.

The stakeholders that hold "veto power" in economic reform are often lumped into "business" and "labor" but this may obscure the very real differences within as well as between these groups. For example, business interests can easily be divided along several axes: those oriented toward exports and those toward import-substitution, or those relying on liquid assets (finance and banking) and those relying on fixed assets (Frieden 1991). Reforms are likely to affect these interests differently. Take devaluation for example. Export-oriented businesses and farmers, and those who find employment in the export sector benefit, while the costs are borne by uncompetitive import-substitution industries and their workers, and all those who consume imported goods.

Typically, traditional chambers of commerce and industry associations have been dominated by interests opposed to economic liberalization: large scale farmers that benefit from tractor service and fertilizer subsidies, and import-substitution industrialists opposed to reductions in protection. Yet in many cases, business associations wary of liberalization are nonetheless supportive of stabilization, with its promise of greater predictability, since foreign exchange shortages and inflation play havoc with a business's ability to plan. For example, MAN, the Manufacturers Association of Nigeria, supported the 1985 stabilization plan, but fought the 1986 trade liberalization. Their participation led to trade "liberalization" that lowered tariffs overall, but imposed a record number of new import bans.

III. POLITICS AND POLICY REFORM: WHAT DO WE THINK WE KNOW?

Economic policy reform is a highly political process, affected by state capacity, international pressures, domestic interests, and the institutional legacies of previous choices. Policy-makers must walk a fine line between insulation/autonomy and participation. Reform choices involve trade-offs: suppressing high inflation ultimately benefits almost everyone but speculators, yet the instruments used almost inevitably provoke recessions, with wide-spread lay-offs and bankruptcies. Trade liberalization benefits exporters and consumers, but since trade taxes are generally among the easiest to collect, trade liberalization often worsens fiscal deficits.

Democratic decision-making presents specific challenges to economic management. Thailand's present crisis was caused in part by the refusal of its democratic leadership to consider de-linking the baht from the dollar, its legislature bickering over how to address the problem of bank insolvency, and a general refusal to either raise taxes or cut spending. Several weeks before the crisis, the finance minister resigned in frustration "over the political obstacles to fiscal discipline" (Economist). On the other hand, the two countries with the strongest and most stable economic growth in Africa are also two of its oldest and most stable democracies: Botswana and Mauritius. The happy synergy USAID is seeking between economic growth and democracy is contingent on many factors, not least among them, *virtú* and *fortuna*.

Political Problems Associated with Reforms

Many of the political problems associated with reforms can be grouped into three categories: distributive problems, collective action problems, and principal-agent problems (Haggard 1994b, Bates 1993, Waterbury 1993).

Distributive Problems and Inequality. Distributive problems might better be termed "redistributive problems." Markets are good at efficiency, not equity. Policy change intentionally redistributes income and resources from some groups (losers) to others (winners). Often, the losing groups have considerable political clout, either through their close ties to the political class, or their ability to disrupt business as usual through strikes and protest. Electoral cycles give the hardiest democratic reformers pause as they contemplate raising taxes on the middle class, cutting subsidies on urban staples, or freezing public sector wages. These distributive problems have a temporal aspect. In the short term, as with raising taxes and cutting spending to address a fiscal deficit or raising interest rates and cutting credit to repress demand, the pain of reform is widespread, while the benefits of a more healthy economy take time to materialize.

Distributive problems are exacerbated by the tendency of many kinds of reform to produce increases in inequality. This tendency has many possible sources. One is the fact that stabilization tends to reduce real wages and increase the returns to capital (devaluation drives down the relative value of labor, recession breeds unemployment, collapse of external finance cuts the supply of capital while higher interest rates raise its return). New taxes and subsidy cuts introduced for fiscal balance tend to be regressive: value-added taxes, reductions in food subsidies, and public transport fare hikes fall relatively more heavily on low income people.

Another source of inequality is the fact that those with access to resources and information can take advantage of the opportunities created by reforms more easily. Partial reforms create gaps quickly filled by speculators with money to gamble. Many Nigerian speculators became very rich when the government liberalized the banking system, but kept the exchange rate tightly controlled and highly overvalued (Lewis and Stein 1996). Indeed, in much of the former Soviet Union, people with greater access to power and information -- managers of state-owned enterprises and other bureaucrats -- make up much of the new private sector. Their unequal access was the antithesis of a level playing field for entrepreneurs. Finally, in most instances the first risk-takers to respond to successful reforms face little competition and can earn a high rate of very visible profits while most are still struggling with unpaid wages and the loss of the welfare state.

Increases in inequality can have serious implications for sustainable reforms, for growth, and for democracy. Research conducted over the past decade by Jeffry Sachs, Manual Pastor, Alberto Alesina and others suggests that countries with more equal income distribution may be better able to avoid severe macroeconomic imbalances in the first place (Sachs 1985; Pastor and Dymski 1990, 128). Other research has found a positive relationship between lower levels of inequality and rates of growth (World Bank 1991; Alesina and Perotti 1996). Finally, growing inequality may put democracy at risk, particularly if the large majority, suffering hardships while a minority flaunt their sometimes ill-acquired gains, blame democracy and the market for their problems (Nelson 1994, 24). It is perhaps for reasons like this that Chile's business class was prepared to agree to a temporary surtax to fund redistributive social programs as the country moved back to democracy in the late 1980s.

Collective Action Problems. The second set of problems, collective action problems, center on the difficulties of getting individuals to join in cooperative action for the public good. In general, collective action is difficult when the benefits of collective action are non-exclusive, available to all, while the costs are felt only by those who join in the collective action (Olson 1965). This creates incentives for individuals to try to "free ride" in the hope that others will incur those costs. If most individuals act on the strong incentive to be a "free rider", actions that would benefit the group as a whole won't be taken. Take fiscal discipline, for example (Haggard 1994b). Congressional representatives would benefit collectively from being able to cut spending as per their campaign promises, but individual politicians benefit from increases in the "pork-barrel" spending going to their districts. This set of problems also arises because winners and losers have different incentives for collective action. Losers from reforms have clear incentives to struggle to maintain or return to the status quo, even when society as a whole would be better off under reforms. Conversely, the costs of reform come immediately, while benefits are slow to emerge. This makes it difficult for potential winners to have the incentive to organize to support reforms.

Principal-Agent Problems and Credibility. Finally, principal-agent problems also abound in policy reform, and these are related to the issue of credibility. Principal-agent problems relate to the difficulties principals have in monitoring and enforcing compliance by their agents, due to the lack of full information or the absence of appropriate instruments. "Principal" and "agent" are relative terms and are used to describe relationships where one party sets tasks, and the other carries them out. In policy reform, one set of principals and agents are voters and politicians: voters and other constituents are principals, with politicians being their agents. Within government, politicians are principals and the bureaucrats their agents, and so on.

One of the reasons for the extensive use of controls in developing countries is the expectation by principals that agents will abuse their position for their own gain, unless they are tightly controlled. Deregulation requires adequate information for monitoring and the capacity to enforce the remaining rules. Likewise, voters have few instruments other than exit and voice for ensuring that politicians carry out election promises. Yet politicians have an incentive to promise more than they can deliver in order to be elected. Promising without delivering creates credibility problems, and if economic actors don't believe in the credibility of reformers, they are likely to take a wait and see position when policy changes (Rodrik 1989).

Policy Styles

One of the earlier studies of the politics of economic reform was entitled *Fragile Coalitions* (Nelson 1989), a telling reminder of both the importance and the difficulty of building constituency support for economic reform. These difficulties arise because of the distributive, collective action, and principal-agent problems described above, but also because reformers need different strategies and tactics for different stages and types of reforms. The need to build consensus and the need to exercise decisive leadership may work at cross-purposes. Finally, as reforms progress, they generally affect the capacity of interest groups to affect the policy process, often in unpredictable ways.

Given these political challenges, policy styles employed by democratic states vary sharply in their degree of participation and/or delegation (Haggard 1994b; Bresser Pereira *et al* 1993). Policy styles include extensive use of executive decrees, insulated technocracies, passive voting by legislative majorities, negotiation and coalition formation in active legislatures, and corporatism or concertation with the formal input of social groups outside the legislature, generally business associations and labor unions.

Some democratic leaders make extensive use of executive decrees to cut through the tangle of legislative politics. For example, in its first year the reformist Aquino government in the Philippines made economic policy largely by issuing presidential decrees (Haggard and Kaufman 1989, 72). Yet decrees, easily delivered, can also be easily reversed, posing credibility problems. Decrees also purposively circumvent the democratic decision-making process. Some governments rely on insulated "change teams" to shape and implement policies, groups of technocrats in the executive branch, out of the direct reach of legislators and interest groups (Waterbury 1989; Williamson 1994; Grindle 1996). Some governments manipulate the electoral rules or processes to ensure a legislative majority, giving their party a mandate, while others rely on negotiation and coalition formation to pass and implement reforms. Finally, governments can institutionalize a consultation process through corporatism or concertation, or a variety of less formal mechanisms that bring representatives of the major societal interests to the policy table. All of these mechanisms may come into play at various times, depending on the stage of reform and the nature of the interest group.

Interest Groups and Economic Reform

Interest groups, as Joan Nelson has remarked, are "Janus-faced" (1994, 150). Seen from one perspective, interest groups are part of the fundamental core of democratic practice, the bedrock of civil society. Exercising "voice" and forming alliances with other compatible organizations, interest group competition leads to sustainable policies that reflect the core concerns of a nation's citizens. From another perspective, interest groups create a politics of rent-seeking. Interest group pressure at its worst produces disastrous policies like the Smoot-Hawley tariff of 1930 and may ultimately, as Mancur Olson (1982) has warned, lead to "sclerosis" of the body politic, a break-down of government's ability to make decisions.

Likewise, many who write about or practice economic policy-making regard interest groups as a cause for concern. Most studies of economic performance in East Asia point out that region's phenomenal growth was put in place during an earlier period of exclusionary policy-making, featuring the repression of labor and opposition parties and the close control of business.

The widespread assumption that policy-makers need to be protected from interest group pressure also shows up in research on actual practice (Bates and Krueger 1993; Williamson 1993). Haggard and Webb found in their research that "in every successful reform effort, politicians delegated decision making authority to units within the government who were insulated from routine bureaucratic processes, from legislative and interest group pressures, and even from executive pressures (Haggard and Webb 1994, 13). Joan Nelson suggests a more nuanced view: insulation may be useful to get reforms underway, but "may be less helpful, or even dysfunctional" while reforms are being consolidated (1993, 438).

Excluding important social groups from policy negotiations can have severe implications for democracy and for the sustainability of reforms. Former Brazilian finance minister Luiz Carlos Bresser Pereira and his co-authors warn that while delegating reform to insulated technocracies may speed the process of reform decision-making and implementation, "if democracy is not to be undermined as a consequence of economic reforms, the representative organizations and institutions must participate actively in the formulation and implementation of the reform program, even if this participation weakens the logic of the economic program or increases its cost" (1993, 10). Furthermore, a more inclusionary approach involving consultation with affected groups can affect the sustainability of reforms and may improve the prospects for the design and implementation of growth-supporting policies. Jeffry Frieden's 1991 analysis of the economic reform in Latin America pointed out that when "important interest groups were left out of negotiations, they disrupted the implementation of whatever decisions were made" (252).

Europe's Social Democracies. The literature on social democracies in Europe reinforces this point of view. Europe's small social democracies -- Denmark, Switzerland, Belgium, the Netherlands, Sweden and Austria -- have better records than many large industrial states in maintaining both economic openness and harmonious labor relations. Peter Katzenstein (1986) has argued that the system rests on the *strength* of economic interest groups, particularly unions, and their formal inclusion as partners in the coordination of economic policy: "interest groups participate in the formulation and implementation of policies that go beyond their specific sectoral interests to include such broad political objectives as full employment, economic stability and growth, or the modernization of industry" (92). While the reasons for the success of democratic corporatism in Europe may be historically specific, other cases also suggest a pattern where strong unions linked to strong ruling parties are better able to implement economic adjustment policies, presumably because strong unions can better guarantee their members' compliance with agreements, and because strong party ties make for mutual interest in fairness and stability, ultimately generating greater trust (Bates 1993b, 33; Heller 1996).

Embedded Autonomy in Asia. Recently, research from East and Southeast Asia suggests that the successful growth policies implemented in those countries stem not from policy-makers acting in authoritarian isolation, but rather from the complex "embedded autonomy" and "deliberation councils" that facilitated feedback and exchange between government technocrats and business (Evans 1995, Doner 1993, World Bank 1993). In this view, the strong, meritocratic bureaucracies in Korea, Taiwan, and other East Asian developmental states are *not* insulated from society, but are instead "embedded in a concrete set of social ties" that bind them to industrial groups, providing "institutionalized channels for the continual negotiation and renegotiation of goals and policies" (Evans 1995, 12). This embeddedness, together with the internal cohesion of the bureaucracies themselves, enables them to avoid "capture" and instead use these ties to make more informed policy decisions. Increasingly, governments are realizing that long-term economic management is more effective with regularized consultation between interest groups and government officials (Haggard and Kaufman 1995).

Ownership and Credibility. Finally, greater participation by affected social groups in policy formation and implementation is likely to boost two elements found to be associated with successful reform: ownership and credibility. Research by John Johnson and Sulaiman Wasty (1993) at the World Bank found that "borrower ownership" of reforms was strongly associated with the success of adjustment programs, and that the most significant factor influencing the degree of borrower ownership was the nature of public-sector/private-sector relations and the political influence of interest groups. In a similar vein, other research has indicated that weak long-term growth is strongly associated with lack of political credibility (Brunetti and Weder 1994 in Nelson 1994, 176). If reforms have been negotiated with affected groups, then it is more likely that they will "own" the reforms and also see them as more sustainable, and therefore more credible.

V. STRUCTURING PARTICIPATION AND COALITION MANAGEMENT

Possibilities for participation in economic reform are contingent on several factors, including the type of reform and the stage of reform, timing, the condition of the economy and the position of the actor(s) in it, characteristics of the groups themselves, and the institutional structure of politics.

Reform Characteristics

Reforms vary in the opportunities they present either for participation, or for resistance. "Stroke of the pen" macroeconomic reforms such as devaluation or raising interest rates offer low scope for participation, although wage rates and price levels are often subject to negotiation. In a democracy, levels of taxation and of government spending (and thus the level of the fiscal deficit) are also typically subject to societal pressures, negotiation, and compromise as the government budget is developed. Pressures here generally develop through existing channels of lobbying and political exchange. Restructuring reforms, such as financial sector deregulation, trade liberalization, privatization, export promotion and public sector reform, require feedback, information, consultation, and coalition-building between government and interest groups in order to enhance their feasibility and political sustainability. These reforms are more likely to remain ongoing efforts where the kind of "embedded autonomy" found in East Asia has a useful place.

Timing

Timing also matters in the management of participation. The impact of a strong external shock such as Thailand experienced recently with its delayed devaluation may shake political rigidities up enough to enable constructive compromises. In democracies, the timing of electoral cycles is also a factor in establishing an environment for compromise. Painful reforms may face less opposition and be more sustainable if implemented during the "honeymoon" immediately after an election, as Peru's Fujimori and Argentina's Menem found.

Condition of the Economy and Position of the Interest Group

The condition of the economy and the position of an actor within the economy also affect the role it can play in policy reform. Country-specific patterns of societal interests explain much of the ease or difficulty with which countries can adjust their development strategies. Institutions inherited from the colonial period, natural resource endowments, and the legacies of development strategies of the 1960s and 1970s produced particular patterns of economic interests in developing countries. As the first oil shock hit in the mid-1970s, for example, Zambia's pattern of high dependence on large-scale, rigid, state-owned copper mines with well-organized mining unions created a different pattern of interests which made it inherently more difficult to adjust than did the interests created by Taiwan's or Korea's pattern (then) of predominantly small and medium-sized, export-oriented firms, with highly decentralized, firm-specific unions (Shafer 1994). These structural differences should be understood by those who would blame reform difficulties solely on "lack of political will." Likewise, businesses and unions in a dynamic sector are more likely to see opportunities for mutual gain than those caught in a dying sector, with each side trying to shift more of the losses onto the other. Finally, for various reasons, business interests generally have more channels of access to government, including informal channels, and don't need to rely on their business associations to represent their views and needs the way that union members rely on their unions. This also means that individual members of business associations have more opportunities to carve out special deals that allow them to maintain privileged positions.

Institutions

The institutional structures of the political system affect the ways in which interests are represented, the linkages between state and social groups, and the modes of consultation. Political parties in some countries have institutionalized close relations with social groups, much as Britain's Labour Party is linked to labor federations in the U.K. and the Greens in Germany are linked to environmental groups. Party systems that tend to generate coalition governments also tend to be more open to consultation, since parties need to reach out to sometimes diverse interests in order to build and maintain ruling coalitions. Countries vary in the extent to which they have cabinet-level technocratic policy agencies, or insulated institutions like the U.S. Federal Reserve Board that keep some areas of policy-making relatively immune to outside pressures. In corporatist systems, widespread in Latin America, the institutionalization of consultation gives "peak associations" of select societal interests (farmers, labor, business, and so on) a direct role in policy-making processes, for which they give up their ability to act independently of the government. Mexico, until very recently, was a good example of corporatist policy-making, but so, too, are the small, social democratic states of Europe. Less formally, tripartite commissions limited to governments, and peak associations of labor and business, provide periodic formal opportunities to reach agreement on some of the key parameters of the economy, particulary wages and other prices. Many former British colonies share this institutional feature. Finally, in countries where knowledge of specific policy issues is widespread in both government and society, policy networks made up of think tanks, academics, and practitioners bring government and informed interests together to establish formal and informal policy recommendations.

Group Characteristics

Finally, groups' ability to influence reforms is also affected by the characteristics of the particular groups: size, degree of fragmentation, capacity and representativeness. As the collective action problems outlined above suggest, people with common interests don't automatically become a pressure group: they need selective incentives (collective action benefits from which "free riders" can be excluded), compulsion, or institutional arrangements that facilitate organization (Olson 1965). Second, it is easier for small groups to organize themselves to act collectively than large groups. Therefore, in general, small, well-organized groups like formal-sector manufacturers have advantages over scattered, informal sector producers. Large-scale, organized commercial farmers have more of a voice than peasant farmers. The recent rise in non-governmental organizations (NGOs) speaking on behalf of weakly organized social groups has ameliorated some of these structural disadvantages, but NGOs -- particularly international NGOs -- face their own problems of legitimacy and accountability in claiming to represent groups that are not organized and have not elected them as representatives.

The degree of fragmentation of a group also affects its relative power: countries like Chile that have relatively strong, unified, disciplined labor movements are more likely to see labor with a place at the bargaining table than countries like Thailand, where labor is weak and divided. Unified movements are also more able to deliver credible commitments to respect bargains and pacts negotiated over economic reforms, as in the European social democracies. On the other hand, fragmentation and competition in an interest area, as in politics, may offer more opportunities for militant tactics and extremist views hostile to compromise as leaders compete for members (Nelson 1994, 174).

Groups also differ in the degree to which they are truly representative, the degree to which they have internal accountability, and their capacity to propose alternative programs, as opposed to simply reacting (Nelson 1994). When governments are trying in good faith to consult with non-governmental groups they may easily face many groups claiming to represent important stakeholders. Some groups -- unions, in many cases -- attain representative status through closed shop legislation and elections, but without institutions like these to legitimize a group's claim to be representative, there is often no easy way to determine which groups ought to be sitting at the table. A different problem is posed by the corporatist practice in many Francophone and some Latin American countries of parastatal chambers of commerce with mandatory membership, sanctioned and frequently funded by the state, and given quasi-official duties of business representation and internal "policing" much like the American Medical Association in the United States. Close relations can lead to more effective communication and representation -- however, if such organizations have an official monopoly, the danger arises that corporatist chambers will come to see their interests as more closely aligned with government, than with their members.

VI. MANAGING PARTICIPATORY POLICY REFORM

Building and maintaining the "fragile coalitions" necessary to support economic policy reform under democratic governance entails a mixture of incentives and compensation, education, capacity building for governments, political parties, and interest groups, channels for communication, and political sequencing.

Incentives and compensation

John Waterbury argues that leaders use three kinds of rewards to manage their relations with their constituencies: incentives directed at winners to boost their ability to accelerate the resumption of growth; compensation for losers, to ameliorate their pain and protests; and the "rents" and "pork" necessary to maintain the support of voters and patrons. He observes that "Donors, creditors, and economic advisors approve of the first, do not always understand the logic of the second, and condemn the third. It is in fact the design and disbursement of compensatory payments that is crucial to transitional periods in coalition management (Waterbury 1989, 41).

Losers have considerable power to disrupt reforms, through riots, strikes, and "exits" like black market activity and capital flight. The most powerful coalition opposing reform is frequently organized labor combined with the urban popular sector. Increases in inequality falling on these two groups may threaten both democracy and long-term growth prospects. But targeted compensation and protections may also assist countries to respond more flexibly to shifts in the global economy. Research on social democracies suggests that higher levels of worker protection are correlated with lower levels of trade protection (Muñoz 1994; Bates, Brock and Tiefenthaler 1991). Generally, these social protections were located at the level of society (unemployment insurance, worker relocation and retraining mechanisms) rather than at the firm level (job guarantees). These social protections can also strengthen democracy. In Bolivia, the decentralization of safety net benefits not only offered employment and resources to those hurt by the reforms, helping to maintain the course of reform, but also went some way toward building support for the democratic system from people who were frequently receiving their first state assistance (Graham 1994).

While the costs of reform hit almost immediately, the benefits are uncertain and slow in coming, making it hard for winners to know who they are, or to organize to support reform-minded coalitions. This makes it all the more important to design and sequence reforms so that winners are more clearly aware of their benefits. Targeting specific social services such as public transport or electricity, for visible improvement may help urban areas gain confidence that the reforms will work (Nelson). Sometimes immediate proceeds from reforms can be transferred directly to compensate losers: Mexico was able to channel some of the gains from privatization directly into its safety net program (Graham, 1994). Winners can be created. The Czech program of privatization relied on transferable vouchers that were distributed among citizens, giving them an immediate interest in supporting the reforms. Although it may seem inequitable to channel additional resources toward winners of economic reforms, temporary subsidies and other measures to assist farmers and others in their export efforts may make the gains from reform more visible, more quickly (Nelson). In Mauritius's successful adjustment, funding from the World Bank helped compensate losers and accelerate gains to winners (Bräutigam forthcoming). Small farmers were given assistance to diversify from sugar to exports of tea, cut flowers, and other agricultural products, while unemployed graduates enjoyed a program that gave out unsecured loans of 50,000 rupees to start small businesses in the Export Processing Zones.

Public Education and Communication

Efforts by governments, political parties, and interest groups to educate and inform constituencies may also ease the course of reform. Public education and communication might take the form of economic literacy campaigns, advertisements, speeches, town meetings, and so on. In 1976, the Italian Communist Party sent a million workers through evening economics courses that explained why austerity was necessary (Bresser Pereira *et al* 1993, 12, n. 9). Skillful use of the media to give public explanations and communicate the reasons for reforms creates transparency, is low cost, and may make reforms more sustainable. In Zambia, the Kuanda government was forced to beat a retreat after its unilateral decision to raise the price of maize meal sparked riots and a coup attempt. Several years later the democratically-elected Chiluba government spent time explaining why the maize price needed to be raised, and there was little protest when the new price took effect. Peru's decision to remove subsidies from gasoline went into effect after extensive efforts from the finance minister to communicate the reasons for the August 1990 stabilization effort. Despite a 3000 percent hike in the price, there were no public protests (Graham 1994, 7-8). As Poland implemented its successful "shock treatment" reforms, the popular Minister of Labor made frequent appearances on television to guide citizens through the rationale for each step of the reforms (Sullivan 1990).

The extra legitimacy of a democratic government may be necessary for explanations and public education to work. For example, the military government in Nigeria mounted an extensive campaign to educate the public about the costs of maintaining subsidized fuel prices (then at pennies per liter), but when the subsidies were consequently reduced, strong protests made it clear that the public distrusted the military government's ability to channel the gains of higher prices toward the public good.

Capacity-Building

In order for consensus-building and persuasion to move beyond legislative debates and public education conducted through the media, both governments and stakeholder groups need to develop technical and analytical capacity, while stakeholder groups in particular need to strengthen their ability to have their voice heard. Frequently, few groups outside of the finance ministry have a strong understanding of the reasons why economic reform are necessary. Weak understanding of economics limits the ability of interest groups to analyze reforms proactively and present constructive critiques or alternative approaches. This generally includes reporters and editors in the media, which can limit the media's effectiveness as a forum for debate, even with press freedom. Political parties frequently conduct campaigns based on personalities, not issues. Shifting to an issues-based politics requires stronger internal ability to analyze policy issues, supplemented by access to think-tanks and university institutes. In Ghana, the donor-supported Institute of Economic Affairs (IEA), an independent think-tank and advocacy group, provides independent analysis of economic policy reforms pending before the legislature, focusing in particular on how the proposed reforms would affect business. The IEA's efforts have apparently raised the quality of discussion and served to better inform a wide range of stakeholders (Scribner 1997, 35).

Likewise, political liberalization means that many voices have the opportunity to speak, and it takes good organization and funds to ensure that the spectrum of voices making it to the ear of policy-makers expands beyond a narrow assortment of well-funded business groups. Newspaper and other media advertisements, the production and distribution of position papers, lobbying campaigns, newsletters and public relations materials, and public forums all cost money. Lacking funds and public relations savvy, women's groups, small farmers' associations, informal traders, and small manufacturers are less likely to get their issues on the policy agenda. External sources of funding have sometimes helped these groups strengthen their demand-making capacity in ways that help ensure that their concerns get on the policy reformers' agenda. Here, donors need to be careful to allow groups their own voice. A good example of how this can be done is the approach taken by the USAID-sponsored West Africa Enterprise Network. The facilitators working with the Network consciously refrained from suggesting which policies Network members should work on, limiting their involvement to the provision of tools and training (Crosby 1996, 1413; Brinkerhoff 1996, 1464).

The final critical area for capacity building lies within government (Grindle 1996; Bräutigam 1992, 1996). The more governments can limit their reliance on patronage and maintain integrity, accountability, transparency, and professionalism, the better their chances of avoiding capture by special interests, while being able to legitimize the insulation of policy-making in key areas like monetary policy.

Mechanisms for Consultation

Capacity is of little use without transparent channels of access and mechanisms for consultation. Democracies embody constituency consultation primarily through the electoral and lobbying processes, but there are many other mechanisms for formalizing communication: regular meetings of tripartite commissions of labor, capital and government, task forces that bring experts from government and society together to make recommendations about policy issues, government attendance at associations' annual meetings and conferences, public hearings, action-planning workshops, even focus-groups and town meetings. No matter what the forum, non-governmental participants need free access to economic information in order to make their participation meaningful.

Channels for consultation were actively used in the East Asian cases: President Park Chung Hee instituted and "religiously attended" regular National Export Promotion Meetings including ministers, business association representatives, bureaucrats, and firm executives, to strategize about export policy, hear the problems of firms, and get their feedback on policy initiatives (Haggard 1990, 71). Labor was denied equivalent access, a fact which probably helped build the high degree of intransigent militance among unions in democratic Korea. Countries that have been democratic for longer tend to have more well-developed mechanisms for openly bringing dissenting views into the decision-making process. Botswana's semi-corporatist democracy regularly uses traditional community meetings called "kgotlas" as opportunities for public consultation. In Costa Rica, when the government announced it planned to sharply reduce agricultural subsidies, farmers took to the streets to demonstrate against the cuts. The government responded by establishing six commissions so that all interested parties could "explore all dimensions of the planned changes" (Nelson 1990, 209). Democratic Mauritius took more than four years and many formal meetings to negotiate and build a domestic consensus among sugar workers, small, medium, and large-scale sugar cane farmers, cane processors, and other interests on the framework for its World Bank-supported sugar sector restructuring (Bräutigam forthcoming). In contrast, insulated technocrats in Mexico City designed the wide-reaching reform of Mexico's Ejido Law, affecting the lives of the majority of the rural poor, with no consultation with the affected people. The 1994 Chiapas uprising represented in part the "feedback" of those people.

Some examples exist of new democracies developing effective mechanisms for consultation over economic policy. The Uganda National Forum, established in 1992 to create a mechanism for dialogue between politicians, senior government officials and representatives from the Uganda Manufacturers Association (UMA), has established four sectoral working groups on investment and exports, finance, human resources and capacity, and tax policy "that meet on a regular basis and produce recommendations and feedback on policy decisions to the President's Economic Council" (Crosby 1996, 1409). Given that Uganda is currently regarded as one of the most successful reformers in Africa, it is likely that this process of engagement has contributed to the sustainability of reforms, perhaps along the lines of the "embedded autonomy" found in the East Asian model. Also like the East Asian model, Uganda's consultation process brings government together with the more powerful manufacturing interests, but the 80,000 members of the National Organization of Trade Unions, and the 1000 members of the Small Scale Industries Association lack equivalent access to the President's Economic Council. The long-run impact of this exclusion remains to be seen.

Political Sequencing

Finally, reforms need to be designed and implemented with specific attention to political, not just economic, sustainability. Sequencing reforms to take into account the problem of building constituency support may dictate different sequencing than might economic theory. For example, trade liberalization before exports have become strong means that governments must attack the interests of import-substituting industrialists, while running the risks that cheaper imports without a rapid export response will put heavy pressure on their balance of payments, while reducing their revenues from tariffs and straining their efforts at fiscal stability. Governments might better turn attention first, as East Asia did, to institutional and leadership changes designed to promote exports within the existing illiberal trade policy framework (Rodrik 1990). Once exports grow and exporters are strengthened, they become a solid constituency that can support the government in later efforts to liberalize trade (Milner 1988).

VII. THE ROLE OF FOREIGN AID

"If success means resuming growth under democratic conditions," a recent study concluded, "the evidence for successful recipes turns out to be much thinner than for disasters" (Bresser Pereira *et al* 1993, 200). Under democratic governance, policy reform is a continual, iterative process of decisions implemented, reversed, reconsidered, re-implemented. Given the highly political nature of economic reform, and the uncertainty about the direct growth implications of many liberalization recommendations, donors need to maintain a certain modesty and caution in their interventions. There is a lot that we simply don't know about the relationship between economic growth and democracy. With that caveat, this final section considers some of the implications for USAID programming.

1. Economic reformers need to be able to communicate with and (often) compensate losers. Evidence suggests that even difficult macroeconomic reforms can be tolerated with patience when governments make an effort to explain and communicate the need for reforms, their purpose, and the ways in which the government will help the population to adjust.

Democratic governments have an advantage here, since their higher degree of legitimacy helps win the confidence of constituencies. However, it is also widely recognized now that reform is a long-term process that creates many losers along the way, and that social programs and safety nets are important for reform sustainability. Safety nets serve a political purpose by compensating losers, but they also buffer the impact of rising inequality, a dangerous trend that threatens both democracy and growth. And although donors don't like it, governments need to have some degree of pork, patronage, rents, and spoils to maintain political support for their initiatives.

2. Political sustainability may require reform sequences that are out of step with current orthodoxy. Economic efficiency and political feasibility are unlikely to always coincide. Furthermore, a policy environment that is stable, even if not of the highest efficiency, is probably more important for investment and thus growth than policies that are of optimal efficiency, but unsustainable politically (Rodrik 1990, 738). Investors value predictability highly when making medium and long-term investment decisions. Consider again the fact that the East Asian NICs had their highest growth rates between 1965 and 1985, when all their economies were characterized by highly controlled interest and exchange rates, state-owned enterprises, and protection. Donors might exercise more modesty and caution regarding the content and details of economic reforms. It is more important to support an overall commitment to reform than to ensure that a country takes a given set of measures at a particular time (Nelson 1986, 72).

3. Policies and programs that create winners before creating losers, or that deliberately accelerate the gains to winners, ease the task of creating constituencies for reform. China's leaders decided twenty years ago to allow the creation of a vigorous private sector and strong, export-oriented enclaves. Trade liberalization has barely begun, and only this year has the government begun to privatize the problematic, but powerful, state-owned enterprises. The decision to create winners first means millions of stakeholders in support of a market-oriented system. Likewise, introducing competition into an economy by building incentives for import-substituting firms to shift capital into exports rather than allowing across-the-board trade liberalization, a strategy followed in Mauritius, creates constituents who are more likely to support later liberalization efforts.

4. Democratic "embeddedness" and consultation are more time-consuming and require deliberate capacity-building and construction of mechanisms of interaction. Donors who sought to work with teams of technocrats in an insulated enclave of the executive branch now face a policy making process that has been widened to include all kinds of stakeholders. Although messier and more time-consuming, an approach that brings key stakeholders together in negotiating reforms keeps decision-makers in touch with the needs, expectations, and likely objections of the actors whose behavior they hope to influence through policy reform. Donors can assist in speeding this social learning process through helping groups gain exposure to "best practice" in other countries, and through helping build their ability to analyze the costs and benefits and feasibility of various alternative policies. Many of the programs USAID is supporting through the National Endowment of Democracy and the Center for International

Private Enterprise appear to be doing this, however, for the long term strength of democracy it is particularly important not to exclude labor representatives from the learning and consensus building that goes on in these broader policy circles.

5. Donors should exercise caution when tempted to throw their support behind particular constituencies or coalitions. USAID faces a certain dilemma in the fact that certain stakeholders are more friendly to USAID's positions on policy reform than others. The temptation is to act to empower those stakeholders. This can backfire. As Tony Killick (1989, 64) warns, "The danger is that donors will use their muscle in ways which have political consequences which they are not in a position to anticipate and whose risks will have to be borne by others." A more neutral stance by donors, offering general capacity building, information, education, and informed analysis may be critical for success, as well as for supporting local ownership of reforms.

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NOTES

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1.Thanks to Larry Cooley for this trenchant observation.

2.Interestingly, one measure of democracy, medium and high levels of civil and political liberties, was itself not strongly associated with higher GDP growth rates (Devarajan and Lindenberg 1993).