

Economists and Power at the World Bank

Humberto Campodónico, DESCO

Our dream is a world free of poverty.

World Bank

If you torture statistical data long enough, they will confess.

Anonymous

In this article, we will discuss some of the conflicts existing between the different economic approaches within multilateral organizations, such as the World Bank (WB) and, to a lesser degree, the International Monetary Fund (IMF). Evidently, the analysis will have to be confined to issues that we consider most important.

Economists have various facets. When economists are academics, in other words, when they dedicate themselves to teaching and research, they have the freedom to fully express their points of view. Things can be different when they work for the government or for a multilateral organization. The reason is simple: economics is not a pure and exact science as are physics, chemistry and mathematics. Economics is a social science, since it is ultimately the study of economic relations between people, and therefore its conclusions have direct implications in people's lives.

It is precisely why there is not only one but various schools of thought in economics. Each places the emphasis on different elements, and discussions between schools have been one of the most important characteristics in the history of economic thought. For example, since its emergence at the end of the twenties, the Keynes school has thoroughly questioned the assumption that capitalist economy is in a general state of equilibrium, or whether it leans towards it naturally. For Keynes, the capitalist economy could be in a state of equilibrium without the full employment of factors (capital and labor), the state's intervention becoming

necessary to increase demand, which would have a multiplying effect leading to the full employment of factors, as sought.

This essential discussion between distinct schools of economics was overshadowed by the rise of neoliberal economic discourse, started in the mid-seventies and prevalent as the dominant trend in the eighties. Economic policies under Reagan, Thatcher and Kohl clearly illustrated this. The fall of the Soviet Union in 1991 accentuated the hegemony. Fukuyama's statements in "The End of History" were supposedly the last word in the debate: There is no political system other than western-style parliamentary democracy. And no possible economic system other than the neoliberal economy, which advocates the unrestricted validity of the laws of offer and demand in a free-market economy. These ideas perfectly suited the interests of multinational, industrial, commercial and financial businesses, which, while relying on the latest technological innovation, aggressively promoted globalization, i.e. free access to every market on the planet.

Economic trends at the World Bank

Roughly two trends of economic thought have been present at the WB since the early nineties. One of them is the neoliberal school of thought, which adheres to the principles of the Washington Consensus (WC) ^[1]. To its proponents, economic growth by itself will bring on development, social wellbeing and the eradication of poverty by means of the market's invisible hand. The other suggests that economic growth on its own does not necessarily lead to the achievement of these goals, which is why exogenous policy, by directly attacking poverty and income distribution problems, is indispensable. This school of thought does not object to the economic premise of the first; rather, it says that, until the market's invisible hand starts to operate, there is a social cost that is very hard on the poor. This is why there must be policy specifically aimed at them until the "flow" trickles, sooner rather than later,

Economists and Power at the World Bank

not only to those on top, but to the whole of society.

The first school of thought has actually always been the decisive one, as opposed to the second. Macroeconomic stabilization (balanced budget, low inflation) and loans designed to implement structural reforms with WC neoliberal content have indisputably remained at the core of WB policy in the nineties. Loans for infrastructure, promotion of human capital (health, education) and increased social spending on poverty alleviation policy come in second place and as long as they do not interfere with the above^[2].

Notwithstanding, since 1990 the WB has stated, in its public discourse, that its main priority was to fight poverty. This came with important reforms to ensure freer access to the Bank's information and civil society's part in some loans granted by the Bank^[3]. For example, in the early nineties, a working group of NGOs and the Bank was formed and joined by NGOs worldwide. Later on, the WB established that its Country Assistance Strategy (CAS) documents, normally prepared strictly among WB employees and the countries' governments, would now be the object of consultation with civil society organizations in order to gather their opinions, and then published to inform the entire country^[4].

In 1998, new WB President, James Wolfensohn^[5], stressed this orientation by proclaiming that the WC had come to an end at the Summit of the Americas, in Santiago^[6]: But by the end of the day and a half, there was a general belief that the Washington Consensus is over, that we now need a new Santiago Consensus. That, yes, it is crucial to have economic growth and it is crucial to adhere to policies which are tried and true in terms of balance, in terms of equilibrium, in terms of monetary and fiscal policy. But the real issues as we go forward, are the issues of equity and social justice. The real issues are the issues of inclusion. The real issues are how can you deal with poverty within the framework of environmental sustainability, with inclusive and sustainable programs, with participation, and with results that can make a big enough

difference. And if any of you get time to read the Santiago Consensus, you will see that there is very little talk of the agenda items that dominated ABCDE ten years ago. The agenda has moved on. (James Wolfensohn, Annual Conference on Development Economics, Washington, 21/4/98).

Joseph Stiglitz's arrival and departure

A year earlier, in 1997, Wolfensohn had named Joseph Stiglitz – a recognized economist who came from a long-established academic tradition in the US – as the WB's Chief Economist and Senior Vice-President^[7]. Stiglitz's most original contributions sprang from a novel branch of economics called "Information Economy". Stiglitz developed a series of arguments highlighting the limits of the neoliberal model^[8] in achieving poverty mitigation objectives, including new approaches to "development" processes and goals.

With Stiglitz, the ideological hegemony of the neoliberal trend began to be questioned, giving a boost to those who held that economic growth is not enough to achieve development^[9]. Talk of second-generation reforms, the need to strengthen democracy and decentralize, strong and efficient institutions and greater promotion of human capital started to be heard at that time.

As long as Wolfensohn's and Stiglitz's discourse was limited to so-called Developing Countries, the orthodox neoliberal establishment (IMF and US Treasury), let them work for the most part, issuing isolated criticism from time to time. Things started to change in July 1997, at the beginning of the Asian crisis, which threatened to expand to the entire international financial system. The IMF, along with the US government and the European Union, implemented a series of rescue packages for Asian economies, as well as economic programs involving over US\$ 117,000 million, including US\$ 37,000 from the IMF and US\$ 14,000 million from the WB. Evidently, the amounts were far from negligible.

Economists and Power at the World Bank

From the end of 1997, but mostly in 1998, Stiglitz began expressing direct opposition to the IMF's economic programs in Asian countries (see text in the box), which put an end to the establishment's tolerance. Discussing Developing Countries' problems is one thing, as they only represent 20% of the world's GDP; but getting involved in the problems of the planet's wealthiest 20% and the international financial system is quite another.

Rescue package to three Asian countries, July 7 1998 in US\$ billions				
Engagements(1)				
Country	IMF	Multilaterals (2)	Bilaterals	Total
Korea	20.9	14	23.3	58.2
Indonesia	11.2	10	21.1	42.3
Thailand	4	2.7	10.5	17.2
TOTAL	36.1	26.7	54.9	117.7

- (1) Does not include IMF engagements for the Philippines
 (2) World Bank and Asian Development Bank

Stiglitz's criticism toward IMF policies in March 1998

It seems that many of the factors identified as contributors to East Asian economies' current problems are strikingly similar to the explanations previously put forward for their success. Strong financial markets, which were able to mobilize huge flows of savings and allocate them remarkably efficiently, have turned into weak financial markets, which are blamed for their current problems. Addressing information problems in an effective way, including business-government coordination, were considered a hallmark of these economies' success; but this coordination is now viewed as political cronyism and lack of transparency is viewed as one of the main failings. Openness to international markets was hailed as one of the grounds of their success, yet insistence on eliminating barriers in capital and trade flows is an important ingredient in many of the IMF programs. Macro-stability including low inflation was agreed to be one of the key ingredients of the East Asian economies' remarkable

performance, yet the Korea IMF program included a provision requiring the establishment of an independent central bank whose sole focus was price stability. Promoting competition, especially through export-oriented policies was hailed as one of the central pillars of their stellar performance, yet lack of competition in the business conglomerates is seen as one of critical failings.

We seem to be ignoring the fact that this is a single crisis against a record of thirty years of remarkable growth. Although a significant setback, the current turmoil does not seem likely to permanently reverse the gains of the past quarter century. We are unjustifiably treating the occurrence of a crisis as compelling evidence of a fundamentally malfunctioning economy. No economy since the beginning of capitalism has escaped fluctuations. The historical record, in fact, shows that East Asia has had less such fluctuations than other parts of the world -- hardly evidence of a striking vulnerability in the economies. In the last three decades, Indonesia and Thailand have not had a single year of negative growth, and Korea and Malaysia have only had one each. In contrast, the United States and United Kingdom have had 6 years each of negative growth over the same period. History also suggests that, over the long run, East Asian governments' investment strategies were reasonably successful.

(Redefining the Role of the State, What should it do? How Should it Do it? And How should these decisions be made?, Presented on the Tenth Anniversary of MITI Research Institute, Tokyo, March 17, 1998).

The confrontation reached an unbearable stage for the "establishment", particularly for Lawrence "Larry" Summers, Treasury Secretary since 1996, and considered an "enfant terrible" of economics^[10]. Annoyed by Stiglitz's criticism, "Larry" (who has also been the WB's Chief Economist from 1991 to 1993) suggested to Wolfensohn that his next 5-year term at the Bank (2000 to 2005) would be in "greater harmony" with the US government, the Bank's main member with 19% of its capital, if he fired

Economists and Power at the World Bank

Stiglitz^[11]. Stiglitz had to resign from his position of Chief Economist at the end of 1999.

Ravi Kanbur's departure

In 1990, the same year the term "Washington Consensus" was coined, the WB dedicated its World Development Report^[12] (WDR) to the issue of poverty. This document established the Bank's theoretical and practical concepts for the nineties. The WB is preparing a new WDR on the same issue for the year 2000, which also deals with the globalization process under way. In May 1998, the WB entrusted British economist Ravi Kanbur with the responsibility of the 2000 RWD. A Cambridge graduate in economics and holder of a Ph.D. from Oxford^[13], he had been a Bank employee since 1987. The website of Cornell University, where he is currently on leave, displays his résumé. It says that his work covers conceptual, empirical and policy analysis, with a particular interest in bridging rigorous analysis and practical economic policy development.

In June of that year, a few months after Stiglitz's departure, Kanbur resigned from his position as WDR Head. According to the Financial Times of London, Bank staff said Mr. Kanbur's emphasis on income redistribution brought him into conflict with other economists at the Bank, who argued that the promotion of economic growth through market liberalization was the most effective weapon in combating poverty^[14]

Criticism from Kanbur's followers pointed, once again, to the now familiar Larry Summers:

"In a move which exposes a deep intellectual rift at the heart of the Washington-based institution, Ravi Kanbur, a highly respected development economist, quit amid claims that the US treasury secretary Larry Summers is seeking to rewrite this year's World Development Report to make it less radical".^[15]

For Lisa Jordan of the Bank Information Center, a Washington-based NGO,

"Kanbur left his job because the institution's top-level authorities could not stand his

points of view on a necessary balance between growth and equity. An attempt was made to keep him, but it failed. The Treasury Department and the United Kingdom issued bitter comments on one of his last drafts, and that is what left him out in the cold, for two reasons: 1) one of the main members was pressuring him, and 2) President Wolfensohn did not defend him. Furthermore, a Bank economist, David Dollar, published an article, titled: "Growth is good for the poor", which stressed that economic growth is more important than any other factor, such as equity. Kanbur felt that these articles, which were direct attacks on his WDR work, had important backing".

As for WB employees, they denied there had been pressures to make Kanbur leave, insisting that the rest of the team preparing WDR 2000 had continued in their positions and that Nora Lustig, a renowned Mexican/Argentinean economist, had replaced their outgoing boss.

When it is published this September, the WDR 2000 will reveal who was right. But a few things are already clear: the WB's swing to the right and its discarding Stiglitz's concepts, all in favor of multinational companies, who felt ill at ease with criticism towards globalization: Development campaigners consulted on the report earlier this year reacted with dismay to the news.

"Kevin Watkins, senior policy adviser at Oxfam, said the resignation marked 'the ultimate triumph for the Neanderthal tendency within the World Bank', which threatens to bring the development debate 20 years back in time, when free-market fundamentalism strongly discredited the World Bank"¹⁶.

Relations between economists and multilateral organizations could be characterized as follows: WB intellectuals have their quota of power (at least on the theoretical plane and as far as policies for Developing Countries are concerned) as long as their discourse does not interfere with the central interests of its main

Economists and Power at the World Bank

member, the US, and of financial capital and multinational companies.

A second conclusion could be that, as the financial crisis heightens by means of the globalization process under way, positions occupied by the non-orthodox at the WB are disappearing, and neoliberal economists, who cringed for most of the nineties (once again, let us emphasize that this was on the theoretical plane; they did maintain their preeminence in the practice), are aggressively reintroducing their theoretical approaches, with the support of the establishment's hard core: the US Treasury Department and the IMF.

Many civil society organizations, including NGOs, which have taken part in the discussions opened by the WB in the nineties, are reviewing their approaches, as they believe that these discussions are not achieving the objectives they set out. This reflection, fueled by growing international mobilization among civil society and NGOs, rejects the globalization process headed by multinationals, through expressing the need for democratic globalization. Demonstrations against World Trade Organization policies in Seattle, in December 1999, and during the spring meeting of the IMF and the World Bank in Washington in April of this year, have been the most important expressions of this process. In any case, we find ourselves, without a doubt, in a new period.

Email: humberto@desco.org.pe

^[1]“In 1990, a group of Latin American and Caribbean policy makers, representatives of international agencies and members of academics and “think tank” communities participated in a conference sponsored by the Institute for International Economics in Washington. Their purpose was to evaluate the progress achieved by LAC countries in promoting economic policy reforms following the debt crisis of the 1980's. At the conclusion of the group's deliberations, John Williamson wrote that “Washington” (at least as represented by those attending) had reached a substantial

degree of consensus regarding 10 policy instruments” (World Bank, *Beyond the Washington Consensus*, Institutions matter, Washington, 1999).

These instruments consist in the opening, liberalization and deregulation of all markets, as well as the state's withdrawal from any businesslike activity, and privatization of public companies.

^[2] This is in qualitative, not quantitative, terms since the amount of money of structural adjustment loans is normally lower than that going to the other loans mentioned.

^[3] Civil society's participation mainly consisted of implementing and executing, but not designing loan-related projects. For a detailed analysis of the Bank's reform agenda and civil society's participation, see *El Banco Mundial y la sociedad civil: Nuevas formas de financiamiento internacional*, FLACSO, Buenos Aires, 1997 and *Luces y Sombras de una nueva relación: El BID, el Banco Mundial y la sociedad civil*, FLACSO, Buenos Aires, 2000. Both books were compiled by Diana Tussie. On the Peruvian case, see the papers we authored in this book.

^[4] In Peru, the WB consulted with civil society in preparing the 1998 CAS. However, due to the government's refusal to publish it, the degree to which civil society's contribution was actually included or not remains unknown since the document has never been made public.

^[5] Named in 1995. Before taking on this position, he had been President and Executive Director of James D. Wolfensohn Inc., his own investment fund, created in 1981. He had previously worked as a directing member of Salomon Brothers, and Executive Vice-President and Managing Director of Schroders Ltd., London. He has also been Managing Director of Darling & Co. of Australia.

^[6] To some, the Santiago Consensus could also be called the New Washington Consensus. See Brendan Martin, *New leaf or fig leaf?*, *The Challenge of the New Washington Consensus*, Bretton Woods Project, London, 2000.

Economists and Power at the World Bank

^[7] Stiglitz has been a professor at Stanford, Princeton, Yale and Oxford. He has also held prominent positions in public administration: he has been Head of President Clinton's Economic Advisors Committee.

^[8] For example, Stiglitz refers to the limits of commercial opening: "Consider an example that is particularly relevant in a time of globalization. As one who supports lowering trade barriers, I am nonetheless dismayed to note that all too often ardent free-trade advocates cavalierly dismiss the opponents, including those who stand to lose by free trade, and refer to them as "special interests" trying to protect their existing "rents". But among those hurt by trade reforms will be many who will lose their jobs; if the economy is suffering under an unemployment rate of 10% or more, there is a great risk of extended unemployment. And if the society lacks an adequate safety net, the unemployed worker risks true impoverishment, with disastrous effects on the lives of all family members. What is of concern to the worker is not just his loss of "rents", but the loss of his family's livelihood. Those experts who are not disciplined by having to be accountable to the citizenry too often ignore this. Inclusive processes make it more likely that these legitimate concerns will be addressed. In this way, they can ensure greater equality, and even allow more efficient outcomes – given that the loss in output from extended periods of unemployment may far outweigh the losses associated with the inefficient use of resources (Participation and Development Perspectives from the Comprehensive Development Paradigm, Remarks at the International Conference on Democracy, Market Economy and Development, Seoul, Korea, February 27, 1999).

^[9] "The expectation however, was not only that globalization and the "first generation" reforms would raise economic growth rates, but that they also would significantly reduce poverty and inequality. Indeed, capital inflows and export growth were expected to promote the development of labor-intensive sectors. This has not occurred. To be sure, the reforms have produced a decline in poverty rates, but this

development seems to be more a consequence of the decline in inflation rates and modest growth, rather than of the distributive consequences of trade and financial liberalization (World Bank, *Beyond the Washington Consensus*, Institutions matter, Washington, 1999).

^[10] Summers received the John Bates Clark medal, awarded to the best economist under 40 years old. He also won the Alan Waterman prize, from the National Science Foundation. He has been a professor at Harvard and MIT. According to TIME: "Summers, the Harvard academic everyone knows as the "Kissinger of economics" is totally pragmatic, at times irritatingly ambitious, but his intellect never ceases to amaze (...) 'Larry has an outstanding virtue: his intelligence', explains Greenspan. 'As opposed to people who are intelligent and think they are, he recognizes the possibility that many of his ideas could be wrong. This feature is very rare. The academic model's structure is too simplistic to explain how all this works. And Larry had enough intelligence to quickly understand this'" (*Los mosqueteros de la economía*, 11/02/99).

^[11] We borrowed this argument from the Brendan Martin document cited above, p. 3.

^[12] The WDR, published annually by the World Bank, is a synthesis of its reflections, analysis and proposals on issues relating to Third World countries' development. It greatly influences governments, the academic community, civil society and NGOs worldwide.

^[13] Kanbur has been a professor at Warwick, Oxford, Cambridge, Essex and Princeton. From 1989 to 1997, he was a member of the WB's staff. He has received the Quality Scientific Research Award from the American Agricultural Economy Association.

^[14] Financial Times, 15/6/2000.

^[15] The Guardian, London, 15/6/2000.

^[16] The Guardian, *ibid*.