REVIEW ESSAYS

AFTER THE WASHINGTON CONSENSUS

The Limits to Democratization and Development in Latin America*

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AFTER THE CONSENSUS: RESTARTING GROWTH AND REFORM IN LATIN AMERICA. Edited by Pedro-Pablo Kuczynski and John Williamson. (Washington, DC: Institute for International Economics, 2003. Pp. 373.)

THE POLITICAL ECONOMY OF EMERGING MARKETS: ACTORS, INSTITUTIONS AND FINANCIAL CRISES IN LATIN AMERICA. By Javier Santiso. (New York: Palgrave, 2003. Pp. 255. $59.95 cloth.)

SILENT REVOLUTION: THE RISE AND CRISIS OF MARKET ECONOMICS IN LATIN AMERICA. By Duncan Green. (New York: Monthly Review Press, 2003. Pp. 299. $22.00 paper.)

ECONOMIC PERFORMANCE UNDER DEMOCRATIC REGIMES IN LATIN AMERICA IN THE TWENTY-FIRST CENTURY. By Lowell S. Gustafson and Satya R. Pattnayak. (Lewiston, NY: Edwin Mellen Press, 2003. Pp. 229. $109.95 cloth.)

Roughly two decades into the "dual-transition" of democratization and neoliberal economic reforms, neither process looks particularly robust. A large number of Latin American regimes appear stuck in a

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limbo of neither really regressing nor really progressing from the status of relatively limited, disappointing democracies (with a small number clearly regressing). The economic reform process has also yielded disappointing results, performing well below the promises and expectations of its early advocates. Although economic reforms made some important contributions, particularly the virtual elimination of inflation throughout the region, economic performance has weakened dramatically in recent years. Perhaps not surprisingly, the political base for continued economic reforms also appears to be shrinking in a number of countries in the region.

In many respects, this disappointing set of results does not come as a shock. While many were optimistic about democratization and economic reforms early on, skeptics and cautionary analyses abounded regarding both processes. Poverty, inequality, corruption, weak rule of law, weak institutions, clientelism, risk aversion among domestic capitalists, inadequate financial markets (especially for small business), external constraints, as well as undemocratic attitudes and behaviors all figure among the underlying problems that undermine efforts to promote democracy or economic development. These problems are well known and have been thoroughly discussed. As a result, the literature on Latin America abounds with excellent studies and diagnoses of a wide array of aspects of the democratization and economic development process. But, we still do not seem to have a strong explanation for why this complex of problems persists—and has persisted for so long—in Latin America. We don't have a consensus on what has gone wrong in recent years (or even agreement on the extent to which things have gone wrong) and we certainly have little agreement as to where Latin American governments can or should go from here.[1]

The four books under review here offer different perspectives on the question of what has happened over the past two decades, whether the issue is too much or not enough neoliberalism, and how neoliberal economics reforms interact with democratic rule. They do not provide conclusive answers, and for the most part do not claim to do so. They do offer four alternative, intriguing insights into the nature of the problems confronting the region in recent years. They also highlight in important ways the limitations of our current understanding of the twin challenges of promoting economic development and stabilizing/deepening democracy.

Fifteen years after the elaboration of the Washington Consensus, John Williamson and Pedro-Pablo Kuczynski return in *After the Consensus*

1. For example, see the debate on neoliberalism between Evelyne Huber and Fred Solt, "Successes and Failures of Neoliberalism," and David Walton, "Neoliberalism in Latin America: Good, Bad, or Incomplete," in *Latin American Research Review* 39 (3): 150–164 and 165–183 (2004).

with a reflection on the performance of the neoliberal reform agenda. This new volume grew explicitly out of concern about Latin America's stagnating economic performance (xi) and a desire to both establish the causes of this decline as well as make recommendations for restarting growth. Needless to say, as key intellectual architects of neoliberal reforms, the editors do not conclude that neoliberalism is the source of the problem. In the opening pages, the editors quickly defend the Washington Consensus from the charge of bearing principal responsibility. For one, they note that Chile's performance has remained strong despite poor performance virtually everywhere else in the region. Thus, any explanation for the performance failings in the rest of Latin America need to also account for the success of Chile—something wholesale criticisms of neoliberal reforms can't and don't do. In fact, several chapters document significant improvements in economic performance on a range of social and health indicators. In short, the period of neoliberal reform has witnessed a set of improvements that do not square easily with some of the criticisms of the reform agenda.

So, what does account for the limitations of the region's performance? Overall, the editors argue that responsibility for the poor performance of Latin American economies rests partly on poor policy decisions, partly on the incomplete implementation of the original reform agenda, and partly on the need to move beyond the original Washington Consensus into the second generation of reforms. The volume features a series of uniformly interesting and enlightening chapters analyzing different aspects of the reform agenda including social policy, education policy, fiscal policy, monetary policy, trade policy, and labor-market policy. Based on the analyses and recommendations of these chapters, the editors outline a series of recommendations grouped in four "agendas."

The first and second agendas are not particularly surprising. The first is to "crisis-proof" Latin American economies—i.e., take steps to reduce the economy's vulnerability to crisis. None of the recommendations is particularly novel, although many of them are clearly good ideas. For example, suggestions about improving prudential regulation of the banking system, creating stabilization funds, and building reserves in good times have been widely discussed and are already in practice in some developed countries.[2] The second agenda is to actually complete the first-generation reforms of the original Washington Consensus. In particular, the editors point out that labor-market reforms have lagged well behind other areas of reform, such as trade liberalization or privatization.

2. See for example, Sylvia Maxfield, "Alternatives to Cope with Financial Instability." In, Ana Margheritis, ed., *Latin American Democracies in the New Global Economy*. Miami: University of Miami, North-South Center Press, 2003.

But, the real value-added of the book lies in the discussion of the third and fourth agendas: passing second-generation reforms and addressing issues of income distribution and the social sector. The recommendations arise directly out of the detailed analyses of specific policy areas in the substantive chapters. Each chapter provides an overview of the policy reforms in that area, an assessment of the accomplishments and weaknesses of the policy reforms, and a set of recommendations for further reform. The substantive chapters address square on the issue of "too much" or "too little" neoliberal reform and not surprisingly generate more complex and nuanced answers than the editors' summation would suggest.

For example, despite some strong claims of immiseration and dismantling of citizenship from some critics,[3] Nancy Birdsall and Miguel Székely (chapter 3) argue that neoliberal reforms have neither hurt nor helped the poor. In fact, they argue that the recovery of some fiscal health in a number of Latin American countries helped reinvigorate public spending on health and education. The authors argue, however, that social policy "band-aids" are not the answer. Instead, real welfare improvements come from an overarching set of policies that strengthen the economy and increase workers' productivity. Another nuanced example is the discussion of labor-market policies, in which Jaime Saavedra (chapter 9) demonstrates that the impact of neoliberal reforms varied considerably across cases and over time. For the most part, wages and employment levels rose when there was economic growth and did not when there was not. Overall, however, neoliberal reforms did have important negative consequences in the labor market, particularly a decline in manufacturing jobs, a rise in the informal sector, and in general inadequate creation of high-quality jobs. Despite these limits of neoliberal reform, Saavedra makes a forceful case for the need to complete the reform process by tracing the impact of extensive labor regulations on incentives for employers to move into informality or to find expediencies that increase flexibility in the formal market. Needless to say, such maneuvers come at the ultimate expense of wages and employment in the formal economy.

At a minimum, then, the value of the book lies in its review and analysis of the performance of neoliberal policies and in demonstrating that it is too simple to denounce such policies as inherently wrong or entirely responsible for the misery and poverty in Latin America. The specific recommendations for policy reforms that come out of each chapter provide a thought-provoking and interesting collection that are

3. For example, Carlos Vilas makes a powerful statement to that effect in "Inequality and the Dismantling of Citizenship in Latin America." *NACLA Report on the Americas* May/June 1997.

very much worth reading and thinking about. But, the chapters also highlight one of the central limits to the Washington Consensus (rounds 1 and 2). In virtually all of the substantive chapters, the analysis and recommendations point to deeply rooted societal problems that are not easily diagnosed, nor easily resolved. For example, Birdsall and Székely call for policies that empower workers by increasing their productivity—their only real tradable asset. Yet, how and why governments can overcome generations of highly exclusionary practices and instead work to implement policies that empower traditionally marginalized groups is not at all clear. The dilemma is captured in the conclusion to the chapter on education by Laurence Wolff and Claudio de Moura Castro (chapter 8), in which the authors conclude by noting that there are no shortcuts or magic bullets in education. Instead, "progress in education, far from being an autonomous process, depends greatly on policies inducing equity-based growth and on political stability" (208). This sounds like it is very probably true—the problem is that after decades of political and economic analysis of Latin America, we seem to be no closer to knowing how exactly one goes about achieving that result.

To their credit, the editors try to anticipate this, as well as a number of other plausible criticisms. In some instances their response is well taken and in others it is almost dismissive. The type of criticism noted above is probably the one the editors take most seriously. They observe that the set of recommendations developed in the book are enormously detailed and complex and therefore implementing the full agenda is an impossibly complicated task. Instead, they concede that governments will have to make decisions about how to sequence policy reforms. Similarly, they concede that their agenda is oriented toward sustainable development over the medium to long term, but does not identify a path out of the current crises afflicting many countries in the region. Figuring out that path and the correct sequence of reforms, they argue, is for other scholars to examine.

On one level, this is a fair response, yet on another level it reveals a serious limitation of the "After the Washington Consensus" agenda. As others have observed already about the "expanded Washington Consensus" agenda, many, if not most, of the recommendations in this volume are to establish new institutions or improve on existing institutions to make Latin American political economies function more like those of developed countries. So, for example, the editors recommend that Latin American governments improve their prudential regulation of banking systems or increase the independence of the judiciary. These are certainly fine recommendations, but they are not terribly helpful in the absence of any realistic plan for getting there.

The limits to these recommendations have two sources. The first is that policy recommendations calling for new institutions or improving existing institutions present several problems in the Latin American context. A large number of analyses in economics and political science have focused on problems that derive from poor institutional design or from the absence of key institutions. The underlying assumption in all of these analyses is that if the institution is correctly designed, then the incentives will produce the correct behavior and as a result the desired policy/performance outcome as well. In some instances that may be true: Saavedra's discussion of the perverse effects of labor-market rules makes that clear (although critics may legitimately point out that labor-market regulations are frequently and easily evaded in many countries and contexts).

But even well-designed formal institutions may not have the expected effects. As Guillermo O'Donnell reminded us with reference to democratic consolidation, informal institutions/practices may subvert formal institutions, significantly altering the resulting incentives and related outcomes.[4] In other words, no matter how clearly one specifies the formal rules, people may not behave the way we expect or want them to. We may not agree on what explains the behavior—culture, class, education, social networks, power dynamics, etc.—but we can point to numerous instances in which the behavior on the ground deviates in important ways from the model of how it is supposed to work. So, for example, it has been hard to link the abundant literature on political institutions to policy outcomes in a systematic way. Similarly, in the study of privatization and regulation there appear to be many gaps between what is supposed to happen in newly privatized and regulated sectors and what really does happen. Thus, calls for creating new or improving on existing institutions may have little value if we have little confidence that they will function as intended.

A second area of difficulty is that we still don't really understand the underlying social dynamics that limit the progress of democracy and the extent of economic development. Latin America has experienced important changes in a number of areas, but in other important ways it seems to be barely moving. The rule of law remains fragile in most countries, and downright illusory in many cases. Marginalization, exclusion, and extreme inequality seem to be permanent fixtures of Latin American societies and disappointingly impervious to the widespread emergence of competitive electoral politics. Corruption and pervasive clientelism also seem essentially impervious to change. The ability of elites to protect themselves and to subvert formal rules and practices to preserve themselves at the expense of the rest of society seem highly

4. Guillermo O'Donnell, *Counterpoints: Selected Essays on Authoritarianism and Democratization.* Notre Dame: University of Notre Dame Press, 1999.

resistant to democratic forms of politics and liberal economic policies as well. In short, the underlying societal dynamics needed to support many of the recommendations offered do not appear to be forthcoming. If that is the case, then many of the prescriptions will be inadequate simply because actors will behave in ways that undermine the intent of the reforms or prevent their implementation in the first instance. If our models of development do not adequately account for behavior, then they will not perform well either as explanations or as prescriptions.

So, how do we derive better prescriptions and more satisfactory explanations? The answers almost certainly lie somewhere in between neoliberals and their critics and probably need both more frequent debate and discussion as well as more policy experimentation. Unfortunately, the editors' tone seems poorly disposed towards dialogue. Both the editors and some of the authors dismiss criticisms from outside of their methodological and epistemological framework as "not serious." But even "serious" critics, like Dani Rodrik, Joseph Stiglitz, or Paul Krugman, are not engaged in the book either. In fact, the editors even ignore the more nuanced suggestions of some of the substantive chapters. For example, Roberto Bouzas and Saúl Keifman (chapter 7) write that the unexpectedly (for neoliberals) poor benefits deriving from trade liberalization point to the need for more interventionist government policy to promote development and specifically identify industrial policy as an appropriate form of intervention. The editors, however, dismiss industrial policy as a bad idea except in cases where private firms are strong enough to ignore what they view as typically bad advice of the government.

The lack of interest in engaging their critics highlights the extent to which neoliberalism is more than a simple set of policy prescriptions that some economists and policy-makers champion. Instead, it is arguably a political program with its adherents working to maintain a hegemonic position, intellectually and in policy circles. This obviously is not a new charge. For example, Judith Teichman uses "policy network" analysis to trace how politically influential networks of senior policy makers, academics, and business leaders insulated themselves politically while implementing neoliberal reforms without transparency or accountability.[5]

In *The Political Economy of Emerging Markets,* Javier Santiso adds to our understanding of neoliberalism as an ideology with an impressive analysis of the way financial markets really function. Santiso combines anthropological, sociological, and economic analysis to understand how actors behave within financial markets and the consequences that

5. Judith Teichman, *The Politics of Freeing Markets in Latin America: Chile, Argentina, and Mexico.* Chapel Hill: University of North Carolina Press, 2001.

result from that behavior. Santiso's extensive background as a financial consultant gives him a rare combination of academic analytical tools and an insider's view of the world he studies. The result is a sophisticated account of why the world of neoliberalism is so insular and the ways that neoliberals intentionally and unintentionally cut off both policy alternatives and even debate about them. The analysis builds on work on financial markets by scholars like Dani Rodrik and Sylvia Maxfield and extends beyond them.

This is a very nuanced account, but in brief, there are two factors that drive behavior in financial markets. One of them is time, or more precisely the extremely short time horizons in which decisions are made, and the other is beliefs and/or credibility. Financial managers are required to make decisions relatively quickly, but they swim in a vast ocean of pertinent information that is produced and disseminated rapidly. The result is that a number of potentially perverse shorthand methods are used to parse through this wealth of data. This includes focusing on a limited number of indicators, following a limited number of financial news agencies such as Bloomberg (which then become, in effect, market makers), and imitating each other's behavior. In what Santiso refers to as a "confidence game," financial actors all figure out what to do by imitating each other and establish their own credibility by doing what everybody else is doing. Although players in emerging markets may have different characteristics, different strategies, different attitudes toward risk, etc., they are all players in a world with their "own rituals, beliefs, and symbols"—a place where anthropology meets economics (5). Unfortunately, another characteristic of this world is that its elites on Wall Street and in international agencies, notably the International Monetary Fund, only talk to each other and only listen to each other (Santiso establishes this point with some careful sociological investigative work identifying the networks of financial insiders with a level of detail and care reminiscent of Peter Evans' *Dependent Development*).[6] Of course, the beliefs of these elites become the consensus views, which then constrain all other financial actors, even if they have evidence that contradicts the prevailing opinion. Furthermore, emerging-market political leaders are required to play the confidence game, issuing the correct rhetorical and policy signals in order to maintain credibility among those whose views make markets. In the final analysis, the unintentional and intentional limits on information close off discussion of alternative development policies and help provoke financial crises from which market actors ultimately do not really learn.

6. Peter Evans, *Dependent Development: The Alliance of Multinational, State and Local Capital in Brazil*. Princeton: Princeton University Press, 1979.

This is a valuable and important book. Some of the basic ideas, such as the fact that financial markets constrain policy makers or that market actors have different investment strategies, are not necessarily new. But Santiso has generated real value-added in the excellent anthropological detective work he has performed and the way that he shows how very short-time horizons, information overflow, and the need to establish or protect credibility interact. That financial markets exhibit a herd-like quality is also not a new idea, but Santiso has provided a powerful account for why and how it happens.

Santiso ends his provocative work in a chapter entitled "A Bias for Hope" in honor of Albert Hirschman to whom the book is dedicated. But from my perspective, it is not really a hopeful book. One of the central dilemmas running through the book is the tension between the extreme short-term considerations of financial markets and the long-term interests/concerns of states and state actors. In part, Santiso's hope lies in the fact that market actors are willing to make charitable donations to support long-term horizon endeavors (especially education) and that markets forget easily and renew lending relatively quickly to countries that experienced crises (and even to countries that default on their debt as Argentina is demonstrating). But, this is a slim bias for hope against the overwhelming reality of the confidence game and the very considerable constraints it places on emerging markets' policy makers. In particular, it makes it clear why little policy experimentation is tolerated in the developing world and why financial market elites, such as the developers of the Washington Agenda, do not engage in discussions that question the neoliberal "consensus."

This lack of willingness to engage their critics is genuinely unfortunate because, as Duncan Green points out, regardless of the aggregate statistics, the reality of neoliberal reform on the ground in Latin America is pretty bad and even the aggregate statistics are uneven. *Silent Revolution* (2nd edition) stands out for a number of considerable strengths. Green, a policy analyst for CAFOD (Catholic Agency for Overseas Development) presents a strong—and even at times angry—critique of neoliberal reforms. But one of the book's strengths is Green's willingness to take seriously both neoliberalism's criticism of import-substitution-industrialization (ISI) as well as neoliberalism's policy prescriptions. In other words, it is not a knee-jerk rejection of the Washington Consensus. Furthermore, it is a thoughtful, thorough, and fair critique, even if the Washington Consensus crowd might dismiss it as not being "serious" work.

Generally speaking, Green does not offer arguments that will feel new to most critics of neoliberalism. The book documents the dislocations associated with trade liberalization and privatization, the inadequacies of export promotion as a strategy, and the environmental costs of neoliberal reform. It also chronicles how international and domestic neoliberals came to occupy hegemonic positions and the consequences of neoliberal reforms for democratic politics. The book does several things so well that it is a real contribution, even to somebody familiar with the general arguments and sympathetic to the ideological orientation. It is a wonderful mix of non-technical explanation of neoliberal policy prescriptions, fair evaluation of the problems these solutions are trying to fix (i.e., Green does not suggest that ISI would or did solve these problems any better), and thorough evaluation of the evidence of neoliberal policy. He is remarkably effective in providing anecdotes that illustrate the points he is trying to make and then tying them seamlessly to larger presentations of data and other evidence. Finally, he complements Santiso by documenting ways in which IMF and World Bank officials actively bury evidence that conflicts with their policy preferences and diagnostic beliefs (especially 67–68), thus adding to the picture of how the neoliberal community intentionally closes off discussions of alternatives.

Where Green perhaps falls short are two key places that neoliberals hold up in defense of their views. First, Green does not really ask and probably is not methodologically equipped to ask what is the real impact of neoliberal reforms versus other possible causes. Thus, Washington Consensus advocates suggest, quite legitimately, that neoliberal reforms are blamed for many problems that they did not cause and that might have gotten worse in the absence of reforms. The second problem lies with Green's discussion of alternative paths in the concluding substantive chapter. Like other critiques of neoliberalism that come readily to mind, the criticisms and reappraisals are more persuasive than the proposed solutions. In Green's case, the hope lies with CEPAL and NGOs that proffer policies more focused on equality, promotion of domestic industry and national savings, and a more active role for the state through public policy. Unfortunately, as is too often the case, the specific proposals are relatively vague. They include references to success stories in East Asia, idealistic sounding policy goals (like promoting equality) with little suggestion of how governments really do it, and various twists on neoliberal policies that promise essentially "neoliberalism with a human face" (211). In short, Green has done an excellent job portraying the limitations of neoliberal reforms, but in the end does not have a convincing alternative to propose in its place.

All told, reading the three books leaves it hard to avoid certain conclusions. First, neoliberalism is not the culprit its critics made it out to be, but it is also not the savior its advocates sold it as. As a consequence, we need considerably more policy experimentation than is occurring generally in Latin America. But, one obvious problem is that financial markets for a variety of reasons appear unwilling to finance policy experimentation, and Latin American governments don't have alternative sources of funding. In fact, the actors who form the core of the Washington Consensus advocates are even reluctant to engage in "serious" discussions of alternatives. Instead, they offer a dizzying array of policy recommendations with little consideration for their political, institutional, or behavioral feasibility. The end result is deeply disappointing: in order to develop, developing countries must look and act like developed countries. But, there is no real prospect of looking and acting like developed countries until we understand better the political and social reasons why Latin American countries don't and can't look and act that way.

The question of how to explain the underlying societal limits to democratization and how they relate to economic development is the subject of Lowell Gustafson and Satya Pattnayak's *Economic Performance under Democratic Regimes in Latin America in the Twenty-First Century*. This eclectic and uneven volume examines various aspects of democratic and economic performance, mixing reviews of historical antecedents of democracy, broad cultural comparisons, broad political-economy comparisons, as well as case studies of Central America, Argentina, Chile and Mexico. Such a mix makes it difficult to pull out specific overarching themes or conclusions, and that is a central limitation of the volume. Some interesting observations do emerge, however.

One of them comes from Imtiaz Hussain's comparison of Latin America and East and Southeast Asia. He advocates a return to a study of political culture and in particular offers a provocative reflection on the process of socializing the norms of democratic culture. Hussain points out that this phase of democratic consolidation

> deals with the intangibles rather than the tangibles, it does not have an endpoint nor display any significant thresholds of change; it takes inordinate time, receives less analytical treatment, and is given even less theoretical significance. Yet, this phase may hold the answer to the million-dollar question posed in the first phase by the institutional/consolidation school: Why is democracy not sinking in? (42)

Ultimately, Hussain's inquiry bears a lot in common with straightforward modernization theory (including looking at the size of the middle class, and looking at social capabilities, here defined as indicators like media subscriptions, possession of radios and TVs, newspaper subscription, etc.). But it is not satisfying as a solution to the "million-dollar" question.

Another interesting set of observations comes from Satya Pattnayak's examination of the relationship between economic liberalization, democratization, and the role of the state. Pattnayak uses Freedom House scores to assess the relationship between democracy and a variety of economic and policy indicators. The findings are interesting, although the limited sample permits only tentative, suggestive observations rather than firm conclusions. Pattnayak observes that in general the Latin American countries with the highest freedom scores had higher growth rates, higher rates of export growth, and lower current account deficits. In addition, free states had higher rates of social spending, lower levels of inequality, and, over the 1990s, reduced poverty more effectively than less-free states. For Pattnayak, the state is a crucial mediating force between economic liberalization and democratization: an effective and active state is critical for satisfying the performance needs of the population and thereby enhancing the legitimacy of democratic rule.

Of course, it is hard to know which way the causal arrow flows in the set of relationships described by Pattnayak. Lower levels of poverty and inequality and higher levels of social spending may be functions of higher freedom scores, or it may be the reverse. Economic growth may drive all of the political and social indicators. But Pattnayak's essay also raises the possibility that neoliberal reforms are not inherently undemocratic. Rather, they appear undemocratic when they are introduced in societies that are already only weakly democratic in the first instance. If that is the case, then some of the deepest concerns of critics like Duncan Green may result more from the "intangibles" of the million-dollar question than from the inherent limitation of neoliberalism. If that is the case, then it is also possible that market-oriented reforms perform better in those countries that are more democratic and therefore already look and act more like developed countries. This possibility, of course, returns us to the million-dollar question of why is democracy—and economic development—not sinking in. Alas, the four books under review do not answer this question, but they are informed, informative, and insightful and they highlight the need to think about the larger picture.