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From Washington Consensus to Inclusive Growth: The Continuing Relevance of Pro-Poor Policy Alternatives[1]

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Abstract

This paper reviews the debates about growth poverty and inequality, arguing that they have tended to revolve around the question of whether market-led growth is sufficient to eliminate poverty and reduce inequality or whether deliberate policies are necessary because the impact of growth may be insufficient or even lead to perverse outcomes. It also charts the degenerating outcomes of some of these debates, especially the recent rollback of pro-poor growth (PPG) policies and the emergence of the inclusive growth (IG) paradigm. Third, it examines the weaknesses of IG, and argues that these are best confronted through a broader and more ambitious statement of the pro-poor goals - specifically, through a pro-poor development strategy (PPS). PPS is theoretically more resilient than PPG, and it offers a more cogent set of macroeconomic policy recommendations to address growth, poverty and inequality than IG.

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Introduction

Between the late 1950s and the early 1970s, the dominant views about the relationship between economic growth, poverty and inequality tended to draw on the Kuznets (1955) and Solow (1956) models. They suggested that the distribution of income tends to deteriorate in the early stages of growth only to improve spontaneously at a later stage, and that initial country differences in per capita income levels would be eroded through the equalisation of marginal returns to the factors of production. Direct state intervention in the process of development and World Bank support for large-scale infrastructural and capital-building projects contributed to expectations that capitalist economies could deliver growth, international convergence and the elimination of poverty as rapidly as their socialist rivals.

In the mid-1970s, many observers agreed that these hopes were misplaced: most poor countries were failing to converge with the rich 'core' of the world economy, and the distribution of income was deteriorating steadily in several countries.[2] It was difficult to spot any signs that equality-generating processes would eventually prevail either in the global economy, or within most developing countries. The ensuing debates about these failures of development were, inevitably, heavily influenced by the ongoing economic controversies in the rich countries, in this case, between Keynesianism and monetarism. While the former tended to argue that improvements in distribution required deliberate policies of redistribution, the latter claimed that the inefficiencies due to state intervention would inevitably grind any process of rapid growth to a halt.

The rise of monetarism and new classical economics, between the mid-1970s and the late 1980s, helped to shift the expectations of development and poverty alleviation towards the trickle-down of the dividends of growth, which would accrue from the conscientious application of Washington consensus (WC)-type economic policies. The clear failure of this strategy by the start of the 1990s, the rise of new institutional economics (NIE), and growing pressure on the World Bank and the IMF by developing country governments, international organisations (including some UN agencies), NGOs, universities and activists compelled the mainstream and the international financial institutions (IFIs) to address the problems of inequality and poverty reduction explicitly once again. During the 1990s and early 2000s, the mainstream approach - now split between the WC and the post-Washington consensus (PWC) - gradually lost ground to the emerging pro-poor alternatives. This shift in the terms of the debate was nowhere more evident than in the global commitment to the millenium

development goals (MDGs) after 2000. However, the pendulum swung back again in the late 2000s, with a sophisticated attempt by the mainstream to recapture the theoretical, if not moral, high ground with the notion of 'inclusive growth' (IG).

This paper has three main aims. First, it reviews the debates about growth poverty and inequality, arguing that they have tended to revolve around the question of whether market-led growth is sufficient to eliminate poverty and reduce inequality (because it automatically trickles down to the poor) or, alternatively, whether deliberate policies (including the redistribution of assets and/or income) are necessary because the impact of growth may be insufficient or even lead to perverse outcomes (see Heltberg 2004, p.81).

Second, it charts the degenerating outcomes of some of these debates, especially the recent rollback of the pro-poor growth (PPG) alternative by the mainstream's emerging IG paradigm. It is claimed that debates about growth, poverty and distribution have tended to revolve around non-mainstream critiques of the suitability of conventional policy prescriptions (whether they are informed by the neoclassical synthesis, the WC or the PWC). The difficulty, here, is that the alternative policies have tended to be defined in opposition to the mainstream, rather than around a positive platform drawing upon heterodox economic principles. Consequently, each oscillation of the mainstream, either because of internal developments or even in response to non-mainstream critiques, destabilises the alternative views - at least until a new mainstream consensus emerges, and the dissenting views can reassemble in opposition to it.

Third, it examines the weaknesses of IG, and argues that these are best confronted through a *broader* and *more ambitious* statement of the pro-poor goals - specifically, through the outline of a pro-poor development strategy (PPS). It is claimed that PPS is theoretically more resilient than PPG, and it offers a more cogent set of macroeconomic policy recommendations to address growth, poverty and inequality than IG.

This paper has four sections. The first reviews the rise of the WC, its internal transformations through the PWC, and the factors leading to the introduction of external debt relief initiatives, especially HIPC. The second summarises the pro-poor policy alternatives which have emerged since the 1990s, in order to outline a comprehensive package of macroeconomic policies which may be contrasted to those policies favoured by the mainstream. The third traces the degeneration of the pro-poor debates of the 1990s and early 2000s and the

emergence of the World Bank's IG paradigm. This section also offers a critique of IG from the pro-poor viewpoint. The fourth argues that the conventional pro-poor critique of the mainstream is insufficient, and a broader pro-poor development strategy is necessary to overcome continuing poverty and deeply ingrained inequality in the poor countries. This section examines two complementary aspects of PRS, the economic policies needed to achieve their stated aims, and the political conditions for the success of this strategy. The fifth section concludes this study.

1 - From Washington Consensus to PRSPs

This section reviews the progression of mainstream development policies, from the pre-Washington consensus (pre-WC) period, in the late 1960s and early 1970s, to the HIPC initiative in the early 2000s. The review focuses on the mainstream debates between more and less pro-poor views, and between more and less interventionist approaches to economic policy in the poor countries. This review is organised around five sub-sections, approximately in chronological order, starting with the pre-WC, and reviewing the WC, the critiques which it received from within and outside the mainstream, and the debates around the post-Washington consensus (PWC) and the HIPC initiative.

1.1 - Pre-Washington Consensus Poverty Debates

The pre-WC period is most closely associated with Robert McNamara's Presidency at the World Bank (1968-81). At the level of rhetoric, this period is attached to anti-communism in a context where the Soviet and Chinese models seemed to offer an alternative to the developing countries in the wake of widespread decolonisation and intense left activity in almost every continent. The notion of development within this orthodoxy was linked to modernisation and underpinned by Keynesianism, structuralism and an elementary version of welfarism. Methodologically, development economics was both highly inductive and historical in content, grasping the idea that development involved a transition through modernisation to the ideal-type of advanced capitalism, most notably represented by the five stages of economic growth popularised by Rostow (1960) (see Fine and Saad-Filho 2010).

Development policy was perceived to require state co-ordination of large-scale investment projects, including public ownership of key sectors, if necessary, in order to provide the economic infrastructure required for private sector-led industrialisation. This 'big push'

approach was presumably essential to deliver rapid growth, employment creation, macroeconomic stability and a sustainable balance of payments, which, in turn, should reduce poverty through a process of trickle-down. In other words, poverty reduction was the *indirect* outcome of growth. By the same token, some increase in inequality was probably unavoidable in the early phase of development, and this should support the required capital accumulation, as was suggested by the Keynesian argument that the rich have a higher marginal propensity to save than the poor.

Unsurprisingly, the pre-WC was heavily contested. Indicative was the strength of radical alternatives in scholarship, even against an orthodoxy that now seems disconcertingly progressive by comparison to that of today. This confrontation was especially prominent in the various forms of dependency theory, which promoted the view that development and underdevelopment constitute two sides of the same coin, and that autonomous development was contingent upon a socialist alternative (see Cardoso and Faletto 1979, Kay 1989, ch.5, and Saad-Filho 2005).

The debate around competing development strategies was fuelled by the realisation that rapid growth during the 1960s and early 1970s was accompanied by continuing poverty and rising inequality in many countries aligned with the West. These outcomes were surprising, given the expectations of international convergence following the diminishing returns to capital incorporated by the Solow (1956) model, and the spontaneous reduction of domestic inequality through the processes of structural change and labour mobility in a dual economy, suggested by Lewis (1954) and Kuznets (1955) (see Bigsten and Levin 2004, pp.254, 258). These regressive outcomes, and the proliferation of right-wing military regimes across the so-called 'Third World', were in sharp contrast with the achievements of the rich countries under the postwar Keynesian-social democratic consensus, and the economic successes of those countries moving towards the Soviet and Chinese alternatives.

The Latin American experience loomed large in these exchanges. In particular, the Brazilian census of 1970 demonstrated the deterioration of the country's already heavily concentrated distribution of income and wealth even after four decades of rapid growth, and regardless of the country's recent 'economic miracle'. In contrast, there were concrete improvements in Chile, but only through political mobilisations accommodated by increasingly progressive administrations. Expectations of the imminent abolition of mass starvation were also disappointed, despite the first shots of the Green Revolution in South Asia, and there was an

increasing realisation that the poor remained highly vulnerable, despite sustained economic growth around the world.

In 1974, Hollis Chenery, the World Bank's vice president for development policy, published *Redistribution with Growth* (Chenery et al 1974), in collaboration with the Institute for Development Studies at the University of Sussex. This study expressed a growing scepticism with the Bank's strategy of supporting 'big push' growth projects, while expecting market processes to address the problems of poverty and inequality spontaneously (see McKinley 2009, pp.15-16). The book argued that, since the rich control the majority of national income, their own income growth would determine the national growth rate; consequently, strategies of growth maximisation would always be biased towards the rich (e.g., including lower taxes, wage restraint and low inflation policies, all of which disproportionately favour the rich). A new growth strategy supporting the poor should be based on the redistribution of investment, especially by the public sector ('investment in the poor'). The goal should be to shift the distribution of income and productive assets gradually, as the economy expands. In order to avoid the political opposition of the rich, there was no suggestion of redistribution of productive assets or stocks of wealth. In sum, redistribution should smoothly follow (rapid) growth, bypass political conflicts, and avoid any radical transformations of the state or the international economy.

Redistribution with Growth triggered a review of the World Bank's emphasis on capital-intensive development and the maximisation of the investible surplus, because of their concentrating implications and perceived inability to generate sufficient employment growth. The Bank's new priorities should turn towards the promotion of labour-intensive industries and the provision of education and infrastructure for the poor, especially in small-scale agriculture (now deemed to be at least as productive as large farms), and through transfers of land and other productive assets to the poor. These policy priorities should be supported by improvements to labour and other markets directly bearing upon the welfare and productive capacities of the poor, especially the markets for credit, health, education, and basic productive services.

Shifts in the global economy did not give these policy priorities enough time to bed in. On the one hand, poor countries were increasingly caught up in the international debt crisis, which consumed resources that could have been deployed to support the Bank's strategy of redistribution with growth. On the other hand, the economics profession shifted towards the

right with the rise of monetarism and its direct descendants, supply-side and new classical economics. These radical strands of the mainstream acquired canonical status after the consolidation of neoliberalism as policy orthodoxy in the US, the UK and elsewhere during the 1980s (see Milonakis and Fine 2009 and Fine and Milonakis 2009). In development economics, concerns with rent-seeking and corruption became increasingly prominent, and they placed the responsibility for the persistence of poverty squarely on the poor countries themselves, mainly because of their unwillingness to follow the precepts of the 'correct' economic theory. In this context, the scope for redistributive policies was increasingly diminished.

1.2 - The Washington Consensus

The WC emerged in the late 1970s and early 1980s as a dramatic right-wing reaction against the perceived weaknesses of the pre-WC developmentalist consensus. Rhetorically, the WC involved a heavy attachment to a universalist neoliberal ideology, with absolute commitment to the free market and the presumption of the state as a source of both inefficiency and corruption, not least through rent-seeking (for a clear statement, see Krueger 1974). At the level of scholarship, the WC suppressed the old development economics as a separate and respected field within the discipline and imposed, instead, a rigid adherence to the deductive and formal methods of neoclassical economics which, presumably, could be applied directly to the problems of the poor countries (see Jomo and Fine 2006).

The WC comprised four elements. First, the hegemony of modern neoclassical theory within development economics. At the microeconomic level, neoclassical theory assumes that the market is efficient and the state is inefficient. It naturally follows that the market rather than the state should address such economic problems of development as industrial growth, international competitivity and employment creation. At the macroeconomic level, this approach presumes that the world economy is characterised by capital mobility and the relentless advance of 'globalisation'. Although they offer the possibility of rapid growth through the attraction of foreign productive and financial capital, this can be achieved only if domestic policies conform to the short-term interests of the (financial) markets – otherwise capital will be driven elsewhere. Finally, and given the priority of monetary over fiscal policy as traditional (neoclassical synthesis) Keynesianism was sidelined, the interest rates became the most important economic policy tool. Presumably, the 'correct' interest rates could deliver balance of payments equilibrium, low inflation, sustainable levels of consumption and

investment, improved allocation of resources and, therefore, high growth rates in the long term.

Second, for the pre-WC the main reason why poor countries remain poor is because they lack capital (machines, infrastructure and money). Development is seen as a process of systemic transformation through modernisation and industrialisation driven by domestic consumption and domestically financed capital accumulation. In contrast, for the WC countries are poor because of misconceived state intervention, corruption, inefficiency and misguided economic incentives. Development is the inevitable outcome of a set of 'appropriate' incentives and outward-looking neoclassical economic policies, including fiscal restraint, privatisation, the abolition of government intervention on prices, labour market 'flexibility', and trade, financial and capital account liberalisation. There is very little specification of what the end-state would look like but, presumably, all countries would eventually look like the United States.

Third, the WC justification for the virtues of the market was supported both by the neo-Austrianism associated with Friedrich von Hayek and the general equilibrium theory of mainstream economics, which is based on neoclassical orthodoxy and is absolutely intolerant of alternatives. Interestingly, these are logically incompatible with one another, with the former emphasising the inventive and transformative subjectivity of the individual and the spontaneous emergence of an increasingly efficient order through market processes, while the latter focuses on the efficiency properties of a static equilibrium achieved entirely in the logical domain, on the basis of unchanging individuals, resources and technologies (see Fine and Saad-Filho 2010). Despite these (mutually incompatible) libertarian streaks, even the most ardent supporter of freedom of the individual in general, and through the market in particular, agrees that those freedoms can be guaranteed only through state provision of, and coercion for, a core set of functions and institutions. These range over fiscal and monetary policy to law and order and property rights, through to military intervention to secure the 'market economy' when this becomes necessary. Unsurprisingly, then, WC policies are often associated with authoritarianism, while their declarations of support for political democracy are hedged and conditional in practice (Chile serves as a classic illustration; see Barber 1995, Bresnahan 2003 and Saad-Filho 2007). While the WC claimed to be leaving as much as possible to the market, this is better seen as rebuilding the state to intervene on a discretionary basis, systematically to promote the expansion of a globalising and heavily financialised capitalism.

Fourth, under the WC the World Bank set the agenda for the study of development, with the Bank and the IMF imposing the standards of orthodoxy within development economics itself, and enforcing the relevant policies through the conditionalities imposed on poor countries facing balance of payments, fiscal or financial crises.

It is apparent that this combination of policies, regulations and incentives is designed to reduce the economic role of state institutions, and transfer to the (financial) markets control over the allocation of economic resources, including the levels of investment and consumption, the allocation of investment funds, the composition of output and employment, and the selection of the country's competitive advantages. In these circumstances, poverty alleviation cannot be a priority except rhetorically and, even then, distributive aspirations were tempered by 'recognition' of their alleged growth-reducing and inefficiency-generating impact. Significantly, with the WC states lost much of their capacity to select, implement and monitor distributive and welfare policies because of legislative changes, redundancies, salary reductions, and departmental reorganisations. Because of these overlapping pressures, the improvement of the lot of the poor under the WC would have to depend upon the vicissitudes of trickle-down.

The conditionalities through which WC policies were imposed in the poor and post-Socialist countries went far beyond the core monetary and fiscal macroeconomic policies (in the case of the IMF) and the sector-specific, micro and financial policies (for the World Bank) that were accepted in the pre-WC period. An expanding set of policy areas were claimed by the IFIs in the 1980s, including pricing policy, the ownership of productive and financial enterprises, market structures and regulation, public sector management, and political and economic governance (see UNCTAD 2002, pp.16-17). The widening scope of policy conditionality was justified by the need to avoid moral hazard and adverse selection, and the hope of securing better institutions and improved governance, which would provide credibility to the policy reforms and demonstrate government commitment to the policy changes. At a further remove, the endogenous growth literature suggested that economic convergence was not inevitable, as was implied by the Solow model but, rather, conditional on 'good policies' and sound investment decisions which could be secured only by market friendly governments (see Bigsten and Levin 2004, p.255).

1.3 - Critiques of the Washington Consensus

In the late 1980s and 1990s, the hegemony of the mainstream came under attack both in academia and in the emerging social movements, with two complementary approaches to the fore. The first was inspired by the notion of the developmental state (see Fine 2006). With particular emphasis upon industrial policy, the notion of a developmental state was perceived to apply to the successful industrialisations in the East Asian newly industrialising countries (NICs), with Japan as the classic precursor, followed by the four ‘tigers’ (South Korea, Taiwan, Singapore and Hong Kong) in the 1960s and 1970s. These were followed, in turn, by Malaysia, Thailand, Indonesia, China and Vietnam. In all these cases, it was found that the state had violated the main tenets of the WC through protectionism, directed finance, and other major departures from the free market.

The second criticism of the WC focused upon the notion of ‘adjustment with a human face’. Irrespective of the questionable merits of the WC in bringing stability and growth, the adverse impact of WC policies on those in, or on the borders of, poverty was highlighted by a growing literature departing from the findings in Cornia, Jolly and Stewart (1987). They documented the human costs of the crisis, showed that poverty was rising in the ‘adjusting’ countries, and demonstrated the tendency of the adjustment costs to fall on the most vulnerable.[3] The WC stood accused of being at least oblivious to the disproportionate burden of the poor in processes of adjustment and stabilisation. It was also criticised for tolerating, and even promoting, rising inequality as a way of reducing the fiscal burden on the state and of enhancing the scope for introduction of market incentives in everything from health and education to agriculture and to the workings of urban labour markets (see Chang 2003 and Chang and Grabel 2004).

The mounting opposition to the WC dovetailed with the growing evidence of the 1980s as a ‘lost decade’ for development across the portfolio of policies and countries that were subject to adjustment through conditionalities imposed by the World Bank and the IMF. It did not escape the critics’ attention that there was no evidence of a correlation between the application of one-size-fits-all structural adjustment programmes and progress in development or poverty alleviation. It also became evident that WC policies are not self-correcting, with failure often leading to the *intensification* of the conditionalities under even closer supervision by the IMF, the World Bank, the US Treasury Department and many aid agencies.

The World Bank sought to defend itself through questionable appeals to the empirical evidence, selective reference to the occasional if invariably temporary star performers, and the argument that the problem was not with the policies but with their insufficient implementation, opening the way to subsequent discourses around corruption, good governance and the like, invariably shifting the blame to the underperforming countries themselves (see UNCTAD 2002, p.5). This effort culminated in the publication of a major report on the East Asian NICs (World Bank 1993), arguing that government intervention had been extensive but had only succeeded because it had been along the lines of what the market would have done had it been working perfectly – and, in any case, the East Asian experience was not replicable elsewhere. The implausible claims were received with a mixture of astonishment and derision, and the World Bank's report was soon buried (see Wade 1996).

The critics focused on three shortcomings of the WC (see, for example, Buira 2003, Fine and Stoneman 1996 and Pender 2001). The first is conceptual. The neoliberal faith on markets contradicts even neoclassical theory, since the second best analysis of Lipsey and Lancaster shows that, if an economy departs from the perfectly competitive ideal on several counts, the removal of one imperfection may not make it more efficient. Therefore, each policy reform ought to be evaluated independently and justified on its own merits. Closely related to this point, while WC advocates invariably calculate the costs of state intervention in order to press the case for market reforms, they systematically ignore the cost of the neoliberal policies. These include the loss of dynamic benefits because of lower growth rates, the social and economic costs of high unemployment, foreign currency waste in (liberalised) imports of luxury goods and capital flight, and the negative impact of the contraction of the manufacturing base which invariably follows the reforms. There are, also, unresolvable sequencing problems with WC policies, leading to endless debates between proponents of a 'big bang' approach and advocates of gradualism - and, among the latter, to different suggestions of how to order the policies of liberalisation or, alternatively, pragmatism in suggesting that the adjustment programmes should do what is politically feasible at each point in time. These debates were significant not only because they revealed weaknesses in the mainstream case for policy reform, but also because they were, necessarily, based on the high cost of sequencing errors in different countries.

The second concerns the implementation of WC policies. It was easily demonstrated that the WC reforms introduce mutually reinforcing policies that destroy jobs and traditional industries that are defined, often *ex post*, as being inefficient. The depressive impact of their

elimination is rarely compensated by the rapid development of new industries, leading to structural unemployment, greater poverty and marginalisation, the disarticulation of existing production chains, and a more fragile balance of payments. Moreover, WC policies systematically favour large domestic and foreign (financial) capital at the expense of smaller capitals and the workers. The ensuing transfer of resources to the rich, and the growth slowdown triggered by the neoliberal obsession with very low inflation rates, has led to higher unemployment, wage stagnation and concentration of income in virtually every country (see Milanovic 2002). WC-inspired economic deregulation reduces the degree of co-ordination of economic activity and state policy-making capacity, and precludes the use of industrial policy instruments for the implementation of socially determined priorities. For example, it can be difficult to reduce production costs through the optimisation of the country's transport network if its ownership is fragmented between competing firms. Finally, 'market freedom', including volatile capital flows to poor countries, increases economic uncertainty and volatility and facilitates the onset of financial and balance of payments crises, including those in Mexico (1994-95), East Asia (1996-98), Russia (1998), Brazil (1999) and Turkey and Argentina (2001).

In other words, WC policies focus inordinately on short-term stabilisation while undercutting the basis for long-term growth. This can lock fragile economies into a *stabilisation trap*, including very low inflation, low investment, low growth rates and high unemployment. Stabilisation traps can also induce a deterioration of the distribution of income either directly (because of the job losses and the greater rewards to finance through high interest rates) or indirectly (because the economic stagnation reduces the resources available for poverty reduction policies). The cumulative reduction of investment and growth undercuts the economy's potential output, leading to persistent economic underperformance *regardless of the full utilisation of the existing capital stock*. In turn, the declining growth rate of the capital stock will raise the rates of unemployment and underemployment, at least until emigration or the demographic transition catch up with the economic transition. A stabilisation trap will also reduce the economy's capacity to accommodate high growth rates in the future, because inflation and balance of payments pressures will become binding at lower GDP growth rates. Rao (2002) hints at this problem when he argues that:

> [E]xcessive fiscal deficit reduction and monetary restraint causes growth to be policy-constrained i.e., growth is demand-constrained but demand is itself policy-constrained.

> Thus, orthodox stabilization aims to promote growth with stability but ends up compressing investment.

The third criticism concerns the interface between economics and politics. The closely related transitions to neoliberalism and to democracy in several countries in the South and in Eastern Europe have introduced a tension in policy formulation, through the deployment of democratic and supposedly *inclusive* political systems to enforce *exclusionary* economic policies. These policies demand a state hostile to the majority, even though a democratic state should be responsive to majority pressures.

1.4 - The Post-Washington Consensus

Discontent with WC policies has spread since the 1990s, with disquiet reaching even some Washington institutions. The IMF has continued to stress the supposed virtues of the reforms, and to blame the poor countries for their own reform failures. For example, former IMF Acting Managing Director Anne Krueger (2004) claimed that:

> There can be no doubt about the good intentions of many economic policymakers … But appearances can be deceptive. In some cases, tough commitments were made without a full understanding of what was involved. In other cases, the commitment was only skin-deep: rhetoric seen as alternative to real reform, or at least as a way of buying time. Public opposition to policies that have painful implications for some sections of the population can also weaken political resolve … [T]here have been two main problems. One was insufficiently ambitious reform - especially with regard to labor markets. Not aiming high enough at the outset is almost certain to mean that the outcome will be seriously disappointing … The second problem was lack of follow-through for those reforms that were adopted. It is hardly surprising that policymakers prefer to avoid politically difficult decisions - and prefer to do the minimum necessary by way of unpopular reform. But this inevitably damages the prospects for success.

The implication of the IMF view is that countries must ‘do more of the same, and do it well’ (Rodrik 2006, p.977). In contrast, the World Bank has looked more carefully at the implications of the East Asian growth experiences, recognising their association with the distribution of income and assets, mass education and, especially, with state guidance of investment.

The World Bank's shift away from the neoliberal orthodoxy became evident after the appointment of Joseph Stiglitz as its chief economist, in 1997. Stiglitz is one of the main proponents of the new institutional economics (NIE), and he used his position to promote a post-Washington consensus (see, for example, Stiglitz 1998). Although he was ejected from the Bank in 1999 (see below), Stiglitz's views remain highly influential, as was demonstrated by his Nobel Prize for economics in 2001 and his high-profile interventions in development debates.[4]

The intellectual thrust of the PWC has been to shift the analytical focus away from the neoclassical emphasis on competition and the virtues of (perfect) markets, and towards the institutional setting of economic activity, the significance of market imperfections, and the potential outcomes of differences or changes in institutions. The PWC rejects the WC for its antipathy to state intervention, and questions the conventional stabilisation policies for their adverse short- and long-term impacts.

The PWC can provide a more nuanced understanding of economic development (see Harriss et al 1995). For example, the PWC acknowledges that at the core of the development process lies a profound shift in social relations, the distribution of property rights, work patterns, urbanisation, family structures, and so on, for which an analysis limited to macroeconomic aggregates is both insufficient and potentially misleading. This conclusion vindicates some of the political economy critiques of the WC. For NIE and the PWC, poor countries fail to grow because of misguided regulation of economic activity, ill-defined property rights and other institutional constraints. Policy-wise, the rhetoric of the PWC is comparatively state-friendly but in a limited and piecemeal way, with intervention only justified on a case-by-case basis, should it be demonstrable by mainstream criteria that narrow economic benefits would most likely accrue. Despite its obvious limitations, the PWC offers a rationale for discretionary intervention across a much wider range of economic and social policy than the WC. However, it remains fundamentally pro-market, favouring a poorly examined deepening of 'globalisation' but, presumably, with a human face and guiding hand.

For proponents of the PWC, this shift represents a distinct break with the WC, as they associate neoliberalism narrowly with the WC and the dogmatic belief in the virtues of the free market. Nevertheless, the PWC tends to exaggerate the contrast with the traditional WC concerns, allowing Stiglitz stridently to protest policies imposed by the IMF on Russia and

South Korea, in particular, which triggered his enforced departure from office at the World Bank (see for example, Wade 2002). In contrast, critics claim that the PWC is essentially the WC (and the continuation of neoliberalism itself) by other means, and that the most significant policy difference between them is in the PWC's more careful approach to the liberalisation of capital flows. In particular, there is a significant set of shared principles between them, including reductionism, methodological individualism, utilitarianism and the dogmatic presumption that exchange is part of human nature rather than being an aspect of society, as well as the virtues of 'sound' macroeconomic policy and maximal, though not exclusive, reliance upon (global) market forces (see Marangos 2007, 2008, Saad-Filho 2003, and Williamson 2007).

Despite these similarities, PWC discourse emphasises heavily the importance of appropriate institutions for growth. 'Getting the institutions right' has sometimes been exaggerated to the point of becoming a mantra, just like 'getting the prices right' was the mantra of the WC (see Rodrik 2006, pp.979-80). However, this is severely limited at three levels. First, the literature has been unable to establish strong links between any modality of institutional design and long-term economic performance. Second, the institutional reforms demanded by the PWC are rarely new, and the World Bank has intimated poor countries to improve the investment climate, invest in infrastructure and the agricultural sector and educate girls for several decades. Third, even if these relationships could be demonstrated the implications would be disabling for the poor countries, because institutions are historically determined, contextually specific and rigid over time, suggesting that poor countries with weak institutions would be unable to rapidly implement institutional reforms leading to 'development':

> In the limit, the obsession with comprehensive institutional reform leads to a policy agenda that is hopelessly ambitious and virtually impossible to fulfill. Telling poor countries in Africa or Latin America that they have to set their sights on the best-practice institutions of the United States or Sweden is like telling them that the only way to develop is to become developed - hardly useful policy advice! Furthermore, there is something inherently unfalsifiable about this advice. So open-ended is the agenda that even the most ambitious institutional reform efforts can be faulted ex post for having left something out (Rodrik 2006, p.980).

In terms of macroeconomic policy reforms the PWC is either a dead-end or, alternatively, simply a more palatable path towards the WC (as is suggested, respectively, by Rodrik 2006

and by Fine, Lapavitsas and Pincus 2001). The picture is slightly more ambiguous in terms of poverty reduction policies, where the PWC recognises that growth may not automatically trickle-down to the poor and adjustment policies may have a disproportionate impact on the vulnerable. Therefore, 'spontaneous' market processes may need to be supplemented by state provision of education, health and other services, as well as safety nets and targeted benefits (see UNCTAD 2002, pp.4-5).

The emergence of the PWC is best seen as deriving from trends within economic orthodoxy. The market imperfection economics on which it is based, especially the appeal to the notion that individual agents are imperfectly coordinated by the market alone, can explain everything from corruption through to civil war and aid-effectiveness by reference either to narrow economic motives or to arbitrary addition of other motives and factors. Thus, despite what appears to be a radical shift from the WC to the PWC, upon closer analysis the PWC only represents a limited break from it, as is demonstrated by the PWC commitment to mainstream economics despite its overt rejection of the neoliberal free market ideology and one-size-fits-all WC policies. The outcome of these developments within the orthodoxy was the *augmentation* of WC policy reforms by the PWC, with reference to a long but imprecise list of 'second generation' reforms, pithily summarised by Rodrik (2006, p.978): 'The precise enumeration of these requisite institutional reforms depends on who is talking and when, and often the list seems to extend to whatever it is that the reformers may not have had a chance to do'. Nevertheless, Rodrik offers one possible rendition of these PWC, or 'augmented' WC reforms (see Table 1).

Table 1: The Post-Washington Consensus

WC	**PWC (Original WC plus:)**
Secure property rights	Anti-corruption
Deregulation	Corporate governance
Fiscal discipline	Independent central bank and IT
Tax reform	Financial codes and standards
Privatisation	Flexible labour markets
Reorientation of public expenditures	WTO agreements
Financial liberalisation	'Prudent' capital account opening
Trade liberalisation	Non-intermediate exchange rate regimes
Openness to FDI	Social safety nets
Unified and competitive exchange rates	Targeted poverty reduction

Source: Rodrik (2006, p.978).

These policy recommendations have been called 'enhanced conditionality' and, after some hesitation, they have been welcomed even by the IMF:

> In the past decade or so, we have come to realize that economic stability has to encompass a much wider range of factors than had previously recognized. There has to be fiscal and debt sustainability, of course. But sound governance - at the national and corporate level; effective and respected institutions; a well-established legal system; recognition of, and protection for, property rights; a well-functioning financial sector: these are all vital ingredients for lasting economic success … I include labor markets in this list. To reduce poverty, faster growth in poor countries has to bring employment growth: but rigid markets often prevent that (Krueger 2004).

The accretion of conditionalities and policy reforms by the IFIs reveals their continuing attachment to a conception of development as the natural outcome of shifting, but unambiguously 'correct', policies imposed from above, and implemented under external guidance. Paradoxically, the expansion of conditionality has been compatible with an *increase* in the legitimacy of these policies as they have been embraced, within limits, even by some of their erstwhile critics, perhaps because of their rhetorical concessions and the partial recognition of the imperative of poverty alleviation.

1.5 - HIPC and PRS

During the 1990s the limitations of conventional economic strategies and programmes increasingly forced the Washington institutions into the defensive. The Heavily Indebted Poor Country Initiatives (HIPC-1 and HIPC-2) were developed by the IMF and the World Bank in order to recover the policy initiative and demonstrate the compatibility of conventional macroeconomic policies with external debt relief and pro-poor outcomes, symbolised by the MDGs.[5] In terms of policy formulation and implementation, the most important innovation of HIPC is the requirement that countries should submit poverty reduction strategy papers (PRSPs, later PRS) as a key requirement for debt relief.

It was rapidly noticed (see, for example, Cling et al 2002, and UNCTAD 2002) that HIPC presumes that the main weakness of the structural adjustment policies was that they were not nationally owned and not well implemented. Therefore, the changes introduced by the IMF and the World Bank focus on the process of policy formulation rather than the content of the policies: in effect, HIPC has been used an instrument to make countries internalise the norms of the Washington institutions:

> The emphasis on ownership and participation might thus be perceived as having the objective of mobilizing greater popular and political support for the conventional adjustment and stabilization policies, rather than of giving recipient countries greater autonomy in designing their stabilization policies and development strategies (UNCTAD 2002, p.6).

These processual and discursive changes generated a tension between the country need to present a façade of 'ownership' based on a costly participatory process, while making sure that their PRS arrives at the policies expected by the Fund and the Bank, without which no debt relief would be forthcoming. Other limitations of HIPC were also identified, including the fact that up to 40 per cent of the 'forgiven' debt was actually non-performing. Consequently, a considerable part of the relief granted under HIPC has been an accounting exercise to clean up the books, but that has not freed up resources for poverty alleviation. In effect, some of the poorest countries in the world, with a total population of around 600m, half of which living on less than one dollar a day, have been asked to jump through difficult hoops in order to plead for scant amounts of relief - around US$75bn in face value, or 6 per cent of the 2006 stock of the long-term public external debt of developing countries (relief is limited to debt contracted before 2003). This situation has not improved significantly after the Multilateral Debt Relief Initiative (MDRI), introduced at the G8 meeting in Gleneagles, in 2005:

> Data on the face value of debt can give a misleading impression on the actual change in the value of external debt of developing countries. Part of the reduction in external debt was due to debt relief under the HIPC initiative. However, some of the cancelled debt had a present value which was well below its face value. Focusing on the net present value of debt shows a smaller decline in public external debt (5 versus 10 percentage points). In fact, debt relief under the HIPC Initiative has not been fully successful in achieving long-term debt sustainability. According to the 2007 HIPC and MDRI Status of Implementation Report, more than half of the post-completion point countries are still considered as having either a moderate or a high risk of debt distress and only 10 out 22 post-completion point countries have graduated to the low risk category … The evidence summarized above points to the fact that it would be wrong to claim, as it is often done, that developing countries no longer have an external debt problem (Panizza 2008, p.3).

The limitations on debt relief imposed by the developed countries and the IFIs stand in sharp contrast with the vastly larger sums disbursed instantly and, largely, unconditionally, to support the Western banks during the global crisis unfolding since 2008. A much bolder approach is needed to remove the debt overhang crippling the poorest countries in the world and, simultaneously, to free them from the mainstream identikit of policies imposed externally, and enforced by stringent conditionalities. Despite these ethical and economic imperatives, the IMF and the World Bank remain wedded to - essentially - the same macroeconomic strategies attempted in the past, plus limited poverty relief programmes. This is insufficient to address the severe problems of mass poverty in most countries.

2 - The Pro-Poor Alternative

This section reviews a pro-poor alternative to the (P)WC, focusing on a comprehensive and reasonably ambitious package of macroeconomic policies aiming to shift not only the distribution of income and assets (which could be a one-off process) but, primarily, supporting the transformation in the engine of growth towards the consolidation of a more equitable society. The argument is structured around three sub-sections. The first examines the assumptions underpinning the pro-poor approach; the second describes the pro-poor macroeconomic policies, focusing on investment and productivity growth, fiscal policy and public investment, balance of payments and exchange rate policies, and financial policies. The third focuses on the social policies required as part of the pro-poor approach.

2.1 - The Pro-Poor Approach

The (P)WC was increasingly criticised in the 1990s and early 2000s because of its theoretical inconsistencies, close association with weak macroeconomic performance and recurrent crises in the poor countries, and regressive shifts in the distribution of power, income and wealth. There was also a growing realisation that conventional policies thwart the achievement of pro-poor outcomes, including the MDG (see Jomo and Fine 2006, Milanovic 2002 and 2003, and Weller and Hersh 2004). These criticisms were tempered by realisation that, in order to counter the argument that the (P)WC is the only game in town, it is necessary to offer an alternative framework for macroeconomic policy in the poor countries.

The pro-poor policy framework emerged in the early 2000s, drawing upon the heterodox macroeconomic traditions (especially the Post-Keynesian, Institutionalist, Evolutionary,

Kaleckian and Marxian schools), and closely related critiques of the mainstream drawing on the structuralist, developmentalist and other critical approaches to development economics.[6] Some of these traditions had found space to thrive within UNDP, UNCTAD, ECLAC, WIDER and other UN agencies, in some NGOs and in academia. Pro-poor development strategies draw upon them to offer a compelling case for economic policies focusing on the basic needs of the poor and the improvement of the distribution of income, wealth and power in the poor countries. These policies can contribute to the achievement of democratic and distributive economic outcomes in poor countries. This can be done optimally through a combination of rapid, sustainable and employment-intensive growth, and the redistribution of income and assets.

Pro-poor development strategies are based on four principles. First, *mass poverty is the most important problem facing the developing countries, and its elimination should be their governments' main priority*.[7] For the mainstream, poverty is created by social exclusion, defined as segregation from market processes either through market failures or through the imposition of limitations to voluntary exchange, and it is measured by the inability to reach arbitrary expenditure lines, for example US$1 or US$2 a day. This viewpoint defines markets unproblematically as creators of wealth, and market integration as the main force for economic growth and poverty reduction in all circumstances.

This is misleading, because it decontextualises poverty and obscures its sources and processes of reproduction. In minimally complex capitalist economies, poverty can *persist* because of the lack of markets, jobs and opportunities for the productive deployment of existing resources (a 'Smithian poverty trap'). Alternatively, poverty may be *created* by the form of integration into the dominant mode of social and economic reproduction (a 'Marxian poverty trap'). In the latter case, insufficient income is not merely a *symptom* of poverty but, more significantly, one of the *implications* of the structural inequalities constituting the economic system (for a similar approach, see Bracking 2004, Bush 2004 and Weeks et al. 2002, pp. 12–14).

'Modern' forms of economic and social integration can create wealth, for example, by providing expanded opportunities for market access. They can also - simultaneously - dispossess poor peasants, e.g., through rural development projects, deskill urban workers or destroy jobs through technological change or policy shifts, for example trade or exchange rate policy reforms. These poverty-generating policies and processes can also impose upon the

poor labour regimes associated with high exploitation, low incomes and precarious living standards. These include badly paid wage labour, child labour, bonded labour, slavery, volatile modalities of market dependence under a low productivity regime, and insecure and inadequately paid self-employment. The degrading implications of 'modern' forms of social reproduction can be aggravated by environmental and other forms of vulnerability, which invariably affect the poor disproportionately (see, for example, Davis 2000 and 2006).

Conventional definitions of poverty, limited to the inability to reach an arbitrary level of income, cannot distinguish between Smithian and Marxian poverty-generating processes, and they tend to suggest that 'more growth' eliminates poverty spontaneously. Pro-poor approaches are different. They are informed a detailed understanding of the structures and processes of economic reproduction and by a nuanced perception of the operations of labour and commodity markets, and they recognise that these structures and processes can create *and* eliminate poverty simultaneously. Pro-poor approaches also recognise that markets and other economic and social structures are vehicles for the exercise of economic and political power. Consequently, eliminating the structures of reproduction of poverty amid wealth is primarily a political (rather than technical) process, requiring structural reforms to remove the systemic inequalities of access to, and control over, labour, economic resources and political power.

Second, *pro-poor growth must benefit the poor more than the rich*. In other words, *growth is pro-poor when it reduces relative as well as absolute poverty* (see section 3.1, McKinley 2003, Roy and Weeks 2003 and Wignaraja et al 2009). Traditionally, as was shown in section 1.1, growth and equity were perceived to be negatively correlated at least in the early stages of growth, which was often used to validate the implementation of regressive policies in the poor countries. This claim was challenged by studies of the empirical evidence and by alternative accounts of the East Asian experience, suggesting that greater equity supported rapid growth in these countries.

This debate is informative, but it contributes only marginally to the case for pro-poor strategies. In the pro-poor framework, economic policies are not selected in order to maximise growth, equity is not an instrument for the achievement of rapid growth, and there is no presumption that there is a stable trade-off between growth and equity which can be exploited for policy purposes. Although rapid growth can generate additional resources to achieve pro-poor outcomes, recognition that growth can also generate poverty and inequality suggests that the impact of growth on poverty is maximised, and trade-offs are bypassed, when the *process*

of growth directly addresses both Smithian poverty (conventionally, 'the rising tide lifts all boats') and Marxian poverty (which requires policy steering).[8] Conversely, if country's macroeconomic strategy fosters stagnation and the reproduction of poverty, targeted social programmes and exiguous safety nets are insufficient to reverse the trend. In sum:

> Poverty reduction cannot be an afterthought; it cannot be a subsidiary goal to be achieved indirectly or tackled through auxiliary social policies. Instead poverty has to be viewed as the central outcome of the economic system and hence to be redressed by changes in economic system itself (WESS 2010a, p.8).

In order to do this, it is essential to:

> forge consistency between the macroeconomic framework and the national poverty reduction strategy. This is usually interpreted as a 'one-way' consistency, in which the anti-poverty strategy has to adjust to a fixed and rigid macroeconomic framework. However, both should be jointly determined to serve the overriding objective of poverty reduction (UNDP 2002, p.1).

The relationship between development strategies and poverty elimination suggests, first, that poverty reduction works best if technologies and the economic structure are geared towards producing goods and services for the poor, with labour-intensive technologies, and employing skilled and relatively well-paid workers. Second, investment in productive assets and in health and education, rather than the expansion of unproductive activities such as finance or speculation in real estate, are essential to build economic resilience. Third, reductions in poverty and in inequality can be mutually supporting; for example, because greater equality expands the markets for labour-intensive non-traded goods and services, allowing the producers and the sellers to reap economies of scale (see section 2.2). Fourth, the case for pro-poor economic policies is based both on the intrinsic value of economic equity and its potential contribution for democracy and human rights (see Sengupta 2004), and on their potential to eliminate poverty and material deprivation faster than any other combination of policies. In this strategy, GDP growth, inflation control, high investment, low public debt and other conventional parameters of economic 'success' are not the most important goals of government policy. Instead, they are *instruments* for the elimination of mass poverty and the achievement of secure, sustainable, equitable and empowering human development.

Third, *improvements in distribution and social welfare should be pursued directly*. These improvements should not be conditional on trickle-down, and they must be unambiguous across a broad spectrum of measures of welfare and distribution. Changes in the initial distribution of income and wealth (for example, through land reform, universal education and training and the introduction of pensions and other entitlements funded by progressive taxation) can promote several pro-poor objectives simultaneously. These distributional shifts can be achieved only through public policy. In addition to those *ex ante* distributive shifts, the process of income generation needs to be transformed in order to benefit the poor disproportionately. Possible changes include the deployment of industrial policy instruments to support strategic activities, aggressive employment generation programmes, and incentives for wage increases for low-skilled workers.[9]

Macroeconomic stability is a significant constraint to the achievement of pro-poor outcomes. Stability includes intertemporal fiscal and balance of payments equilibrium, real exchange rate stability and the minimisation of inflation and macroeconomic volatility. As was indicated above, these are not objectives in themselves. However, stability provides a supporting environment for the implementation of pro-poor policies. For example, inflation can redistribute income towards the rich, exchange rate volatility can render industries uncompetitive, and balance of payments crises can limit essential imports; moreover, expectations of instability can erode the support for the government's pro-poor strategy.

In order to minimise the scope for these destabilising outcomes, the macroeconomic limits of government policy should not be defined precisely in advance. While the pro-poor goals should be described in detail and achieved within a given time frame, the optimal policy stance with respect to macroeconomic stability is *constructive ambiguity*. Stability must be pursued because of its instrumental value, but listing a set of arbitrary restrictions on government action (such as maximum inflation rates, fiscal deficits or exchange rates) alongside the pro-poor targets undermines policy implementation because it signals that the government is only conditionally committed to its pro-poor goals. For example, what should the government do if inflation marginally exceeds the announced target? Which commitments should be prioritised - the maximum inflation rate or the pro-poor income, housing and health programmes? The answer depends on the nature of the macroeconomic imbalances and the political circumstances. This does not imply that stability is unimportant, but recognises that it has costs. The preservation of stability should not become an objective in itself or an excuse

to undermine the pro-poor programme; and the distribution of the costs of stabilisation should support, rather than undermine, the achievement of pro-poor outcomes.

Fourth, *pro-poor strategies must be nested within democratic political processes.* Distributive policies disconnected from political democracy are populist: they are selected and implemented arbitrarily, and they tend to be poorly monitored and disembedded from the social groups directly concerned with their success. These are not merely process failures, but symptoms of political flaws and strategic vulnerabilities in the distributive project. In the absence of supporting mass intervention, e.g., through participatory budgeting, there is no way to ascertain the social priorities, gauge the intensity of support for conflicting goals, select between alternative uses for the available resource, and evaluate the performance of the pro-poor programme (see Wignaraja et al 2009, pp.xv, 4). Democratic accountability also increases the resilience of the distributive project, making it less vulnerable to political shifts within the state apparatus either because of changes of government (which may or may not take place by constitutional means) or through backroom negotiations between the economic and political elites. In sum, a pro-poor democratic institutional framework is essential for an effective, legitimate and durable pro-poor development strategy.

2.2 - Pro-Poor Economic Policies

In order to maximise its distributive and poverty-alleviating impact, growth should focus on two complementary areas. First, *sectors that directly benefit the poor*, especially those generating income and employment for the poor and producing goods and services consumed primarily by the poor, for example, small-scale agriculture, construction and the informal sector (see section 2.1).[10] Second, growth should *relax the balance of payments constraint*. These outcomes should be pursued through the selective adoption of macroeconomic policies 'pursuing: a) low external indebtedness (public and private); b) competitive exchange rate regimes; c) countercyclical fiscal policies; d) rising tax/GDP ratios, and e) sustained investment in public goods' (WESS 2010b, pp.2-3).

These policy priorities should be funded primarily by domestic sources, because foreign savings and investment tend to be volatile, difficult to target, and they are often inimical to pro-poor objectives; for example, foreign investors often produce luxury goods and services rather than basic consumer goods and manufacturing inputs. Raising the necessary resources domestically will require a concerted effort, since the savings in poor countries tend to be

insufficient to support ambitious pro-poor development programmes. Tax revenues will normally need to rise to help to fund these programmes (see below). It will also be necessary to set up or expand long-term public-private savings initiatives (such as development banks, as in Brazil and Chile) in order to fund infrastructure, housing, education and training programmes, pensions and other costly pro-poor projects. In very poor countries, the savings potentially available domestically may be insufficient to permit the achievement of MDGs and other pro-poor goals even under the best combination of policies. In this case, pro-poor growth is likely to require foreign aid, other unrequited transfers (such as workers' remittances) and large-scale debt forgiveness.

Investment and Productivity Growth

The selection of investment priorities should recognise that, while investment is the driving force of growth, growth is *also* the driving force of investment because rapid and sustained growth generates the demand that makes individual investment projects viable. Conversely, low investment not only weakens growth but also complicates the task of reallocating resources towards pro-poor sectors.

Resources should be available for the expansion of labour-intensive sectors producing non-tradables, such as small-scale agriculture, the construction industry, repair workshops and services industries, which produce food and industrial inputs, have a significant employment-generating potential, and train entrants to the labour markets. Infrastructure sectors, including electricity generation, water and sewerage provision, rural roads and irrigation facilities will invariably need to expand in the poor countries, which will require state funding and may benefit from public works programmes. In most poor countries it is especially important to support the development of agriculture and its linkages with other economic sectors, because of their economic importance and the fact that large numbers of poor people live in rural areas. The poor countries can draw upon the Chinese, Indonesian and Vietnamese strategies between the 1970s and the 1990s, as they attempt to raise agricultural productivity, boost the links between agriculture, manufacturing industry and other dynamic activities, and increase the output of exportable goods simultaneously. In order to do this, it may be necessary to reform the land tenure systems and invest in better technology and in physical and social infrastructure, for example, seeds and fertilisers, crop selection, irrigation, storage and transportation facilities and so on. These programmes can be funded by a combination of taxation and targeted credit by state-owned and private financial institutions.

In addition to these essential, but mostly low productivity investment priorities, pro-poor programmes should also aim to incorporate selected high-productivity projects, because these can open new export opportunities and they require the development of chains of related activities that will expand growth and employment in other areas of the economy. They also demand a skilled workforce, which can transfer their expertise to other sectors when they change jobs or if they open small businesses. These workers will be better paid than the average, which will raise the aspirations of the workers employed elsewhere in the economy. Finally, more productive firms can set high standards of workplace safety and security that will facilitate the regulation and eventually the elimination of unsafe and degrading working conditions in other sectors.

These favourable outcomes are neither necessary nor automatic. High productivity gives firms the scope to grow and improve pay and conditions, rather than press for wage cuts or labour-shedding whenever they are hit by demand pressures. However, the market does not always spontaneously generate exports, internalise value chains, pay salaries commensurate with productivity or deliver adequate health and safety standards in the workplace. State regulation, incentives and trade union intervention are essential to achieve these outcomes. Regulation should make it difficult for firms to increase profitability by cutting wages, arbitrarily extending the working day or bypassing health and safety rules. Productivity growth and better working conditions can also be promoted by legislation raising the minimum wage and reducing wage dispersion and offering tax and other incentives for firms investing in priority sectors, introducing new technologies and paying high wages. These policies can be partly funded by progressive income taxes and social security contributions (see Onaran and Stockhammer 2002, and Taylor 1988).

Fiscal Policy and Public Investment

Fiscal policy is a powerful macroeconomic policy tool.[11] The (P)WC claims that the size of the public sector should be kept to a minimum, however defined, because low taxes, limited regulation and low levels of public spending will increase the scope for private sector activity, which should drive economic growth. In contrast, pro-poor strategies require the public sector to induce, regulate and sustain the process of growth, target resources into priority sectors and preserve macroeconomic stability.

Public expenditures and, in particular, public investment can boost aggregate demand, loosen the supply constraints on long-term growth and support the reallocation of resources towards poverty reduction goals, especially in economies operating below potential. Although the mainstream insists that public investment crowds out, and is less efficient than, private investment, empirical studies offer no firm evidence supporting this claim. Quite the contrary: a significant body of research indicates that public investment can *crowd in* private investment in upstream and downstream sectors such as those which supply inputs and consumables, cleaning, maintenance and security services, trading and finance, workforce training, and so on. Public investment can also support private investment and output growth if it expands the physical infrastructure (roads, ports and airports, water, sewerage and irrigation systems, electricity generating capacity and transmission lines, and so on), boosts labour productivity (through public education and training programmes, public transport or public health provision), or fosters private savings.

Historical evidence shows, first, that public investment has played an essential role fostering growth and reducing poverty in several dynamic economies in East Asia, Latin America and elsewhere and, second, that when public investment falters aggregate profits decline, reducing the incentives (and the resources available) for private investment (see McKinley 2003). Public investment can also support quality foreign investment. For example, Roy and Weeks (2003, p. 24) note that:

> two [Asian] countries with the strongest public investment programmes, China and Vietnam, also had the highest rates of growth. Both countries attracted large inflows of foreign direct investment, suggesting that, at least, major public investments did not discourage such inflows and may have facilitated them.

In order to finance the required public investment programmes poor country governments must jettison the restrictive fiscal policy stance imposed by (P)WC policies. This will not necessarily be inflationary; in spite of the mainstream claims to the contrary, there is no strong relationship between fiscal deficits and inflation (see Fischer, Sahay and Végh 2002, pp. 876–7). Public investment programmes can be deficit-financed if the economy is operating below capacity, if the balance of payments constraint is not binding, and if the deficits can be financed in a sustainable manner (for example, if the additional public sector debt can be paid off by the tax revenues generated by future growth). In these cases, public deficits should have

no inflationary impact. However, if the government needs to monetise its deficit on a regular basis, perhaps because the financial markets are insufficiently developed, the expansion of demand must be regulated because of its potential implications for inflation, the exchange rate, and the balance of payments.

The growth-supporting fiscal policies required by pro-poor development strategies will be sustainable only if the tax system is modernised and the tax base is expanded. It is simply impossible to finance the necessary initiatives with tax rates much lower than 20 per cent of GDP, as is commonly the case in poor countries (see MacEwan 2003, UNCTAD 2002, p.27, and Vandemoortele 2004). Tax revenues play a fundamental role in the mobilisation of resources for the allocative, distributive, growth and stabilisation functions of the state in poor countries, especially in the light of their weak financial systems (see below) and the vulnerability of aid flows. There is scope for raising tax revenues in most poor countries and, simultaneously, to redistribute income. These reforms require the enforcement of the existing tax laws and the reduction or elimination of the deductions, exemptions and loopholes favouring the well-off. It will also normally be necessary to increase the existing tax rates, to tax wealth and large or second properties in rural and urban areas, and to tax interest income, capital gains, financial transactions and international capital flows. Experience shows that the most important constraint to the expansion of the tax base in the developing countries is not poverty or the lack of managerial capacity to apply the law; it is primarily the lack of political will to confront domestic pressures for the preservation of inequitable privileges, threats of capital flight, and attempts at non-compliance with the law.

Balance of Payments and Exchange Rate Policy

The currencies of poor countries are not international means of circulation or reserve value, and they do not serve as units of account for international transactions. These limitations impose a balance of payments constraint on these countries (Thirlwall 2003). The balance of payments constraint is probably 'the single most important constraint on capital accumulation and growth' in poor countries (UNCTAD 2002, p.32). It can trigger exchange rate crises, inflation, unemployment and other destabilising processes, with serious consequences for the poor. Rich countries also have a balance of payments constraint, but it is more flexible and supply bottlenecks can usually be bypassed through imports, often funded by capital flows attracted through movements in the interest rates.

The balance of payments constraint includes two types of restrictions, on trade (the current account) and on capital flows (the capital and financial account). WC programmes almost invariably recommend the liberalisation of imports in order to foster competition and productivity growth, economic reforms to shift resources towards the economy's (presumably given) comparative advantages, and incentives for capital inflows in order to attract foreign savings (see Jomo and Fine 2006). These policies are not conducive to macroeconomic stability or to the welfare of the poor. Foreign trade and financial policies should be part of a pro-poor industrial strategy fostering productivity growth and the development of domestic production capability in selected areas. An alternative set of policies, compatible with macroeconomic stability and pro-poor outcomes, is sketched below.

The first element is the promotion of exports. Export growth can give an important contribution to productivity growth because it exposes producers to the stringent test of competition in foreign markets (Chang 1994). Export growth is also essential for the generation of trade surpluses and the accumulation of foreign currency reserves, which is essential to minimise balance of payments vulnerability and macroeconomic volatility. Export growth requires a competitive and stable real exchange rate (see below), as well as coordinated industrial policy initiatives to develop the country's competitive advantages in strategically important sectors (see Amsden 1997 and 2001, and Chang 2003). The promotion of domestic industries requires government involvement in the complex task of 'picking winners', which has been addressed successfully by several East Asian and Latin American countries (see Agosín and Tussie 1993, and Gereffi and Wyman 1990).

The second element of this pro-poor trade policy framework is the management of the country's import restrictions. In spite of mainstream myths to the contrary, 'openness and trade integration, either separately or together, do *not* have a measurable impact on long-run growth' (Weller and Hersh 2004, p.492). Imports should be liberalised cautiously and selectively because of their potentially adverse impact on the poor and on strategically significant sectors. First, the gains from trade can be concentrated in enclaves, or they can raise the returns for skills or assets that are beyond the reach of the poor, increasing income and wealth inequality. Second, liberalisation can increase predatory competition, reducing economic growth and the wages and the employment opportunities of the poor. Third, subsidised exports from the rich countries (grain, sugar, cotton, fruit, meat and dairy products) can undermine the viability of small-scale agriculture and the livelihoods of millions of rural poor:

> continued protectionism in agriculture constitutes perhaps the most important external impediment to resource mobilization in many developing countries in Africa, where this sector could provide considerable 'vent for surplus' needed to generate resources for creating jobs in industry (UNCTAD 2002, pp.7-8).

In their study of openness, Weller and Hersh (2004 pp. 499–500) conclude that:

> the income shares of the poor are lower in countries with deregulated current and capital accounts compared to more regulated ones. This is not because trade is directly harmful for the poor but because of the institutional design under which trade is conducted ... [T]he short-term adverse effects of current and capital account deregulation on the income shares of the poor are not offset by faster income growth in the long-run, which could raise the possibility of faster income growth for the poor ... [because] liberalization has no robust impact on growth rates. But ... trade may have a beneficial effect on the income shares of the poor in the short-run in a regulated environment. ... [In sum,] countries where trade and capital flows [are] regulated ... do best for the poor.

Pro-poor strategies also require the regulation of the capital and financial account of the balance of payments. Capital account liberalisation can be destabilising for four reasons. First, liberalisation fosters the accumulation of foreign debt, especially by the banks, promotes speculative inflows that can finance consumption rather than investment, facilitates capital flight and increases the country's vulnerability to balance of payments crises:

> the boom-bust cycles associated with rapid entry and exit of capital under open capital account regimes tend to deepen poverty not only by undermining investment and growth, but also by leading to regressive income distribution. Surges in capital inflows often lead to a deviation of key macroeconomic aggregates such as savings, investment, fiscal and external balances, exchange rates, employment and wages from their longer-term, sustainable levels. The rapid exit of capital and financial crises, on the other hand, tend to lead to overshooting in the opposite direction. The recovery process, which restores aggregate income to pre-crisis levels, generally results in a different configuration of key macroeconomic variables from those previously prevailing, often resulting in large shifts in income distribution and heightened poverty, which can be

> corrected only after many years of growth … Reduced incomes and employment in organized and informal labour markets are the main social conduit of the adverse impact of financial crises on poverty and equality (UNCTAD 2002, p.33).

Second, pro-poor strategies require monetary policy autonomy, which is severely curtailed by financial liberalisation. Third, pro-poor strategies require the state to direct investment and other resource flows to growth-promoting and poverty-reducing objectives, which may conflict with the short-term interests of the financial sector. Fourth, and more prosaically, capital controls are needed to curb tax evasion, since the tax rates required to fund pro-poor programmes will be higher than abroad. The adverse implications of capital account liberalisation are especially damaging for the poor:

> The link between capital flows and incomes of the poor arises from a greater probability of financial crises in a liberalized environment. More capital flows, especially short-term portfolio flows, are often associated with a greater chance of financial crises ... [T]he burdens of financial crisis are disproportionately borne by a country's poor ... Although high-income earners are more likely to hold financial assets and hence to be hurt by a crisis through declining asset values, low-income earners may be more likely to be affected by declining demand as unemployment rises ... [A]t the same time that economic crises increase the need for well-functioning social safety nets, unfettered capital flows limit governments' abilities to design policies to help the poor when they need it most - in the middle of a crisis. The poor are the first to lose under such fiscal contractions, and the last to gain when crises subside and fiscal spending expands (Weller and Hersh 2004, pp.478–9).

Several forms of capital control have been used recently by such diverse countries as Chile, Japan, Malaysia, South Korea and Sweden.[12] In these countries,

> The use of controls has not resulted in interruptions of economic growth; on the contrary, when controls have been removed, as in Mexico in the early 1990s and in East Asia in the late 1990s, financial crises and severe economic downturns have been the result ... Whatever form they take, *controls over the movement of funds across a country's borders are a necessary part of any general program of economic change*; without such controls, a government

> cedes the regulation of its economy to international market forces, which often means the forces of large internationally operating firms and powerful governments of other countries (MacEwan 2003, p.6).

Capital controls can include restrictions on foreign currency bank accounts and on currency transfers; taxes or administrative limits on outflows of direct and portfolio investment; restrictions on foreign payments for 'technical assistance' between connected firms; non-interest bearing 'quarantines' on investment inflows; controls on foreign borrowing, and multiple exchange rates determined by the priority of each type of investment. Managing these controls will burden the monetary authorities, but this task is not beyond the capabilities of most central banks. The most significant obstacle to capital controls is not technical: it is political.

The choice involved in establishing a pro-poor exchange rate regime is relatively straightforward. The basic alternatives are fixed exchange rates (including currency boards), adjustable pegs or managed floating (free floating regimes are too unstable to be considered seriously). In order to preserve macroeconomic stability, small poor countries with highly concentrated trade patterns and countries where currency substitution is advanced may be forced to adopt fixed exchange rate systems. This is far from ideal, because supporting an arbitrary peg inevitably reduces the scope for pro-poor monetary policy initiatives, but it may be unavoidable in the short-term. In this case, pro-poor fiscal policy becomes even more important. Other countries may enjoy additional degrees of freedom to adopt a managed floating exchange rate regime or, even better, an adjustable peg, which maximises the scope for monetary policy discretion.

Whatever the exchange rate regime, it must be managed carefully. Although overvaluation can offer immediate benefits through cheaper imports and lower inflation, pro-poor strategies should normally avoid 'exchange rate populism'. Currency overvaluation can have destructive implications for domestic production and employment, and it can induce consumption and asset bubbles that may be difficult to neutralise. Experience suggests that export growth and the expansion of employment are more easily obtained with selective import protection, export incentives, capital controls and a moderately *undervalued* exchange rate.[13] This may be achieved in different ways, including a relatively low peg (if this is relevant), expansionary monetary policies, the taxation and regulation of currency trading, capital controls and regular intervention in the currency markets.

Financial Policy

The financial sector centralises the key sources of capital in the economy: it mediates between savers and investors, between taxpayers and the state, and it plays an essential role in the transactions between the economy and the rest of the world. Two principles should inform the choice of pro-poor financial policies. First, experiences of domestic financial liberalisation have often been destabilising, and failed to increase the resources available for investment, the quality of investment or the GDP growth rate.[14] Moreover, liberalisation has often led to excessively high interest rates, bouts of speculation with foreign assets, excessive buildup of external and domestic debt, and unwarranted threats of instability should the government fail to abide by the financial market criteria of economic 'prudence'. The potential influence of the financial sector, and the destabilising impact of financial crises, make it essential to impose regulations to make financial sector operations compatible with the government's pro-poor strategy. These regulations are relevant regardless of the ownership structure of the financial institutions (e.g., whether they are state- or privately-owned and, in the latter case, whether the dominant interests are domestic or foreign).

Second, fashionable suggestions that poor country financial institutions should prioritise microcredit and microfinance initiatives should be rejected. On the one hand, there is no evidence that even a large number of individual success stories adds up to a successful pro-poor development strategy. On the other hand, experience shows that microfinance uses scarce savings to support the informalisation of the production structure and the dismantling of labour market structures, leading to the disordered multiplication of such unproductive activities as street trading, petty food sales, kiosks, as well as subsistence production. Their funding crowds out larger-scale projects which can support the development of productivity-enhancing technologies, the creation of quality jobs and the generation of essential backward and forward linkages. Although microfinance can generate immediate benefits to the poor, it fosters a macroeconomic spiral of disarticulation, fragility and cumulative decline which is incompatible with pro-poor outcomes.

2.3 - Pro-Poor Social Policies

Pro-poor development strategies require the integration of macroeconomic and social policy in order to protect the poor and improve social welfare. Mainstream economists generally claim that 'trickle-down' and targeted social programmes are sufficient to deliver benefits for the poor at low cost. However, the contractionary policies associated with (P)WC strategies can overwhelm these compensatory programmes, which become a tool of *poverty management*, rather than poverty elimination. Targeted social programmes are expensive to run and tend to miss out many potential claimants. They are also prone to corruption, and allocation is always arbitrary at the margin. Vandemoortele (2004, p. 12) rightly observes:

> Narrowly targeted programmes are increasingly prescribed for reasons of efficiency and cost savings – for they claim to minimise leakage to the non-poor ... As far as basic services are concerned, narrow targeting can have huge hidden costs. They result from the fact that it is often difficult to identify the poor and to reach them because the non-poor - most of whom remain 'near-poor' - seldom fail to capture a large part of subsidies destined for more destitute people. Also, administering narrowly targeted programmes is at least twice as costly as running untargeted ones. In addition, the poor must frequently document eligibility - which involves expenses such as bus fares, apart from the social stigma they generate. Such out-of-pocket costs can be a real obstacle. Most importantly, however, is the fact that once the non-poor cease to have a stake in narrowly targeted programmes, the political commitment to sustain their scope and quality is at risk. The voice of the poor alone is usually too weak to maintain strong public support.

In order to maximise their impact, pro-poor social programmes should be universal. They should also prioritise the provision of public goods and the social wage, rather than monetary handouts. Social programmes including the provision public education, training, public health, housing, water and sanitation, parks and public amenities, environmental preservation, food security, and affordable clothing, shoes and public transportation can have relatively low managerial costs and they improve the standard of living of the poor directly:

> These programs meet people's basic needs, contributing to the reduction of poverty and to the equalization of the income distribution; they thus generate

> immediate benefits. Many of these programs ... contribute to people's productivity, laying a foundation for more successful, long-term economic expansion. The production process to create and operate social programs is often labor intensive, and thus their implementation tends to use the resource most abundant in low and middle income countries and, which is to say the same thing, tends to be employment-creating … Often these programs can be shaped in ways that directly and indirectly contribute to the development of democratic participation, which is valuable in itself and strengthens the foundation of change (MacEwan 2003, pp. 6–7).

In many countries, the administrative infrastructure required by these universal public goods programmes is already in place, or it can be created relatively cheaply. Public goods and social wage programmes can also be rolled out gradually (e.g., one product or service at a time, and they can be limited to selected regions), making them simple and cost-effective. In spite of their universal coverage, they can incorporate several advantages of targeted programmes, which may be called 'smart targeting': they are *universal* because they are available to all, and they are *targeted* because distinct social groups will be affected differently by each project or initiative. For example, in India and Brazil heavily subsidised food stores and 'popular restaurants' are open to all; yet, they target the poor through their selection of products for sale (staple foods only) and the limited availability of the outlets (which operate only in poor areas). The non-poor exclude themselves voluntarily: a middle-class Indian will not drive into a slum to purchase ordinary rice, while her Brazilian counterpart will never eat pork and beans in the company of her social inferiors, however cheap it may be. Obviously, the precise balance between the targeted and universal aspects of the provision of public and wage goods depends on policy decisions about access and the nature of each project.

Cash transfers are generally less desirable than public and wage goods programmes except for emergency support to very poor groups and long-term assistance to dependent children, the elderly, and the chronically sick and disabled, who have few alternative sources of income. Cash transfers are limited for cost, efficiency and equity reasons. First, it is usually cheaper to provide public goods centrally through state provision rather than privately, via cash transfers (unless the domestic financial system is relatively sophisticated and bank cards are widely used). The managerial costs of these programmes tend to be lower, their quality is more uniform and, as long as provision is controlled democratically, corruption is more easily

avoided. Second, cash transfers are a form of targeting, which is relatively inefficient.[15] Third, cash transfers imply that social welfare is determined by the individual capacity to purchase private goods, rather than the availability of public goods. These transfers foster the commodification of social life and the development of competition, which conflicts with the social solidarity engendered by the pro-poor strategy. In contrast, public goods and social wage programmes ensure the provision of key goods and services to all, contribute to the de-commodification of social exchange and foster the development of community relations.

All social programmes are expensive to run, and the budgetary limitations prevailing in poor countries should not be underestimated. However, these programmes can have a significant redistributive impact. They can also contribute to the achievement of other pro-poor goals; for example, they can create employment in deprived areas, they can be plugged into regional development programmes through the creation of markets for local produce, and they can be linked to the expansion of infrastructure, for example, through public works initiatives. In spite of these advantages, limited funding is likely to pose severe difficulties, especially in very poor countries. In general, these programmes should be funded by taxation or, exceptionally, foreign aid. Cost-sharing and user fees can be unfair and inefficient, and they should normally be avoided.[16]

3 - The Emergence of 'Inclusive Growth'

In the late 1990s, growing recognition that (P)WC strategies were not leading to significant improvements in macroeconomic performance or contributing to the rapid elimination of poverty fuelled interest in pro-poor alternatives. Pressure on the (P)WC increased with mass campaigns such as Jubilee 2000, and after the Asian, Russian, Brazilian, Argentine, Turkish and other crises in the developing countries, the collapse of the dot.com bubble, the disappointing outcomes of HIPC, and the unimpressive performance of the poor countries in the early 2000s. These pressures, symbolised by the approval of the MDGs and the continuing campaign for the cancellation of the external debt of the poor countries, made it impossible for the mainstream to deny the centrality of poverty reduction in any development strategy.

The reaction of the mainstream was two-fold. First, the World Bank quietly withdrew its most unrealistic claims about the conventional policies. The Bank's discourse - and, in some measure, also the IMF's - gradually incorporated humility, eclecticism, and several Institutionalist, Evolutionary and other heterodox insights about the effectiveness of industrial

and distributive policy, which had been rejected completely only a few years before. Second, considerable efforts were devoted to the search for mainstream alternatives to the emerging pro-poor framework. Section 3.1 reviews the pro-poor policy debates; section 3.2 summarises the policy turnaround at the World Bank, and sections 3.3 and 3.4 examine the new 'inclusive growth' (IG) paradigm emerging at the Bank since the mid-2000s. Section 3.5 offers a pro-poor critique of IG.

3.1 - The Pro-Poor Policy Debates

In the late 1990s the mainstream was compelled to admit that poverty reduction and redistribution were not spontaneous by-products of growth, the correction of macroeconomic imbalances or improvements in policies and governance; instead, poverty had to be addressed directly through a dedicated set of economic and social policy tools. The IMF and the World Bank were also forced to confront claims that inequality is harmful to growth because it leads to political and economic instability and, in extreme cases, to political violence and civil war.

The shift in the terms of the debate was accompanied by a significant broadening of the concept of poverty in World Bank documents, drawing upon the debates around the Human Development Index in the early 1990s (see, for example McGillivray and White 1993 and Srinivasan 1994). Symptomatically, the World Development Report (WDR) 1990 defined poverty around income levels, and suggested that pro-poor policies should promote labour-intensive sectors, exchange rate management, countercyclical fiscal policies, social safety nets, education for girls and microfinance. The WDR 2000 expanded the concept of poverty to include assets and vulnerability, and the poverty-reduction tools encompassed conventional macroeconomic policies, capital controls, social funds, workfare programmes and early warning systems. The WDR 2006 went even further than that, accepting from the start that equity has intrinsic value - however, the remainder of the report focuses on the much narrower relationship between equity and growth, with equity being narrowly defined as 'equality of opportunity', rather than in terms of outcomes: 'This report recognizes the intrinsic value of equity but aims primarily to document how a focus on equity matters for long-run development' (World Bank 2006, p.4).

The debates around the relationship between growth and inequality in the early and mid-2000s tended to focus on the *concept* of pro-poor growth. Take, for example, the key exchanges between Nanak Kakwani (see Kakwani, Khandker and Son 2004 and Kakwani and

Pernia 2000) and Martin Ravaillon (see Ravallion 2004 and Ravaillon and Chen 2003, and DFID 2004; for an overview of the debate and additional references, see Besley and Cord 2007, and McKinley 2009).

Kakwani departed from the definition of PPG in section 2.1, in which the incomes of the poor grow faster than those of the non-poor (alternatively, in PPG the income share of the poor increases, or poverty falls faster than it would have if all incomes had grown at the same rate). In contrast, Ravallion focused on the *absolute* improvement of the living standards of the poor, regardless of changes in inequality. For example, Ravaillon stressed the pro-poor implications of growth in China because of the significant reduction of absolute poverty, despite the worsening inequality in the country (McKinley 2009, pp.5-6). Kakwani rejected Ravaillon's definition of PPG because it is too elastic, incorporating most growth processes in history; in turn, Ravaillon criticised Kakwani for the alleged inconsistency of his definition of PPG.[17]

Debates around the definition of PPG were heavily influenced by parallel exchanges about the relationship between growth and equity.[18] On the one hand, Deininger and Squire (1998) attempted to test the Kuznets hypothesis using land distribution as a proxy for asset inequality, and concluded that high inequality is bad for growth (see Bigsten and Levin 2004, p.259), while Birdsall and Londono (1997) claimed that - given assset inequality - income inequality does not improve growth outcomes (see World Bank 2009, p.6).

On the other hand, Dollar and Kraay (2004) famously suggested that growth is, on average, distribution neutral: 'growth-enhancing policies and institutions tend to benefit the poor - and everyone else in society - equiproportionately' (p.30; for a similar claim, see Ravaillon and Chen 1997). Their conclusion triggered a wide-ranging controversy about methodology and policies, focusing on Dollar and Kraay's suggestion that although 'policy interventions … [to] raise the share of income captured by the poorest in society … [may improve] the lot of poor people in some countries and under some circumstances, we are unable to uncover any evidence that they systematically raise the share of income of the poorest in our large crosscountry sample' (p.32). Consequently, while the effect of targeted interventions is both uncertain and weak, growth can *certainly* improve the welfare of the poor. It follows that attempts to shift the income distribution are largely a diversion, and the provision of 'standard growth-enhancing policies' ('private property rights, stability, and openness', p.57) leads to optimal outcomes both for the rich and the poor.

Despite their somewhat grandiose claims, Dollar and Kraay's work can be read, much more simply, as merely confirming that 'empirical evidence ... consistently indicates that size distributions of income are quite stable, in the absence of radical changes in institutions and political power' (Rao 2002, p.7). In other words, shifts in distribution must be pursued *deliberately* through public policy; moreover, a more equal distribution of income does *not* necessarily impair growth performance.

The search for a general relationship between growth and distribution had destructive implications for PPG, because it implicitly attributed an *instrumental* value to equity - that is, instead of being good in itself, equity was seen as a tool to accelerate the reduction of poverty, on a par with other poverty-reducing tools, especially growth (McKinley 2009, p.10). Once it was reduced to this, the PPG debate rapidly collapsed. For, although growth is logically independent from equity, faster growth generally benefits everyone (despite its differential impact upon distinct social groups, regions, professions, skill levels, genders, age groups, and so on). In contrast with the virtual certainty of improvements in the *absolute* condition of the poor through faster growth, and plausible warnings that the pursuit of equality can generate political tensions and damage economic efficiency, the pro-poor camp only managed to respond that improvements in equality could *also* be good for everyone (if they led to faster growth), or that 'too much' inequality (however defined) may trigger political instability. These lame responses helped the debate to converge around the terms of a presumed trade-off between rising equality (benefitting the poor relative to the rich) and faster growth (benefitting everyone). Over time,

> the definitions of Kakwani and Ravallion have become more similar. They have tended to reach agreement on the ultimate goal of maximizing the reduction of poverty. And for this goal, they have tended to agree that both faster growth (implying *absolute* improvements) and greater equity (implying *relative* improvements) should be priorities … how to combine the two means now appears to be primarily a pragmatic issue for both researchers … The underlying conceptual problem … is that the Kakwani and Ravallion definitions of [pro-poor growth] have, indeed, converged towards a common pragmatism. In other words, they have chosen to mix and match both means, i.e., faster growth and greater equity, in order to maximize the impact on poverty. How exactly the impact is achieved is of secondary concern (McKinley 2009, pp.6, 9).

The logical consequence of the collapse of the PPG debate is that *all* growth is, presumably, 'good', and different types of growth can be distinguished only to the extent that they are more or less 'poverty-reducing'; in other words, we should be indifferent to the combination of growth and equity in any development strategy - the point is how rapidly it can reduce absolute poverty.

3.2 - Policy Turnaround at the World Bank

Internal developments at the World Bank, including its retreat from the WC, and the appointment and subsequent ejection of Joseph Stiglitz, destabilised the Bank's views on development and equity, and contributed to an increasing fragmentation of the Bank's approach to development policy. In 2005 the Bank published *Economic Growth in the 1990s: Learning from a Decade of Reform* (World Bank 2005) and, in 2008, a committee of prominent economists and leaders of successful economies assembled in the Bank-sponsored Commission on Growth and Development (CGD)[19] published *The Growth Report: Strategies for Sustained Growth and Inclusive Development* (CGD 2008). These documents and complementary papers, especially Besley and Cord (2007), stand in sharp contrast with conventional presentations of the (P)WC (see section 1.4). They pointedly avoid blueprints for development and emphasise, instead, the virtues of experience, selective reforms, eclecticism, experimentation, the middle-ground and learning-by-doing. For example, 'policy making will need to be patient, pragmatic, and experimental' (CGD 2008, p.15).

These lessons from experience include, first, recognition that there *was* an economic collapse in the transition countries of the former Soviet Bloc, that sub-Saharan African countries have *failed* to take-off despite significant policy reforms, aid and debt forgiveness, and that there *were* recurrent financial and balance of payments crises across the developing world. The Bank also admits that most poor and middle-income countries have failed to match their growth performance in the pre-reform period (e.g., since 1930 in Latin America, and since 1950 in East Asia and sub-Saharan Africa). The reports also acknowledge that rapid growth in China and India has been responsible for most poverty reduction in the world during the last generation; they also note, in passing, that these countries did not follow conventional policies. While *Economic Growth in the 1990s* avoids tackling this disjunction head-on, the CGD includes representatives from both countries.

Second, the reports recognise that the mainstream has tended to exaggerate the advantages of small governments:

> In recent decades governments were advised to 'stabilize, privatize and liberalize.' There is merit in what lies behind this injunction … But we believe this prescription defines the role of government too narrowly. Just because governments are sometimes clumsy and sometimes errant, does not mean they should be written out of the script. On the contrary, as the economy grows and develops, active, pragmatic governments have crucial roles to play (CGD 2008, p.5).

Third, there has been too much emphasis on rules over discretion in government behaviour:

> There are certainly times and places in which avoidance of mistakes is the first priority and rigid rules can be essential for this purpose. However, these rules can become counterproductive if applied too strictly for too long (CGD 2008, p.54).

Fourth, the reforms should not be overambitious, both because this is politically impractical, and because it may be inadvisable even on theoretical grounds:

> An important insight from this stream of research is that numerous distortions exist at any time in a given country, and that some are more important than others. Moreover, as posited in the theory of the second best, it can actually be *welfare reducing* to institute reforms that remove some distortions as long as other distortions remain, which is the case in all real economies (World Bank 2009, p. 7).

In sum, the conventional reforms were too obsessed with deadweight losses and the efficiency gains to be gained through their elimination, and they tended to overlook the dynamic forces underpinning the growth process (Rodrik 2006, p.976).

Fifth, economic policy is necessarily contextual:

> A coherent growth strategy will … set priorities, deciding where to devote a government's energies and resources. These choices are extremely important. They should also be country- and context-specific, responding to widely varying initial

> conditions. This report cannot therefore set priorities for policy makers. It can only identify the policies that need attention (CGD 2008, p.5).

Therefore, the goal of the Bank reports is to 'offer a framework that should help policy makers create a growth strategy of their own' (CGD (2008, p.2).[20] Pragmatism is essential:

> We … refrain from offering policy makers a recipe, or growth strategy, to follow. This is because no single recipe exists. Timing and circumstance will determine how the ingredients should be combined, in what quantities, and in what sequence … Wedded to the goal of high growth, governments should be pragmatic in their pursuit of it. Orthodoxies apply only so far … If there were just one valid growth doctrine, we are confident we would have found it (CGD 2008, pp.4, 16).

For example, trade openness can be achieved through lower import tariffs, duty drawbacks, export subsidies, special economic zones, export processing zones, and so on (Rodrik 2006, p.976), and infrastructure provision for the expansion of markets can mean very different things in Indonesia and Bolivia. Similarly, improving incentives for private sector investment may require improving property rights in one country, and reforming the financial sector in another.

3.3 - New Policies for Rapid and Pro-Poor Growth

Having cleared the conceptual ground, and despite their claims to the contrary, the World Bank reports proceed to offer a fairly detailed picture of the 'correct' menu of economic policies. The reports depart from a wholly conventional list of ambitions, including a stable macroeconomic environment, fiscal responsibility, price stability, improving the investment climate, strengthening property rights, regulatory improvements to lower transaction costs, high savings and investment rates, transparent markets taking responsibility for resource allocation, greater access to infrastructure, improved mobility of resources, particularly labor, openness to trade, strategic integration with the world economy, and capable, credible and effective government committed to growth.[21]

Distributive concerns are noticeably absent from this sprawling list of aims, with two exceptions. First, the CGD is concerned that inequality might trigger political instability: 'in the early stages of growth, there is a natural tendency for income gaps to widen. Governments

should seek to contain this inequality … Otherwise, the economy's progress may be jeopardized by divisive politics, protest, and even violent conflict' (CGD 2008, p.7). Second, and drawing on the pro-poor debates reviewed in section 3.1, the Bank recognises that large inequalities can slow down the translation of growth into reductions in absolute poverty (Besley and Cord 2007, p.1). In other words, the Bank's reports focus almost *entirely* on the absolute improvement of the conditions of the poor, without any consideration of 'active' distributional policies. In this case, growth is both necessary and sufficient:

> We focused on sustained growth, not because it is the final goal, but because sustained growth enables and is essential for things that people care about: poverty reduction, productive employment, education, health, and the opportunity to be creative … Growth is not an end in itself. But it makes it possible to achieve other important objectives of individuals and societies. It can spare people en masse from poverty and drudgery. Nothing else ever has. It also creates the resources to support health care, education, and the other Millennium Development Goals to which the world has committed itself (CGD 2008, pp.x, 1).

Growth policies include, first, a competitive environment:

> Growth entails a structural transformation of the economy … This transformation is the result of competitive pressure. Governments committed to growth must therefore liberalize product markets, allowing new, more productive firms to enter and obsolete firms to exit. They must also create room to maneuver in the labor market, so that new industries can quickly create jobs and workers can move freely to fill them (CGD 2008, p.6).

Second, government commitment to growth (rather than simply the absence of government):

> Successful cases [of sustained growth] share a … characteristic: an increasingly capable, credible, and committed government. Growth at such a quick pace, over such a long period, requires strong political leadership. Policy makers have to choose a growth strategy, communicate their goals to the public, and convince people that the future rewards are worth the effort, thrift, and economic upheaval … Such leadership requires patience, a long planning horizon, and an unwavering focus on the goal of inclusive growth (CGD 2008, p.3; see also p.30).

Third, public sector investment in infrastructure and the creation of physical and human capital (including roads, ports, airports, power, telecommunications, health and education, especially for girls):

> No country has sustained rapid growth without also keeping up impressive rates of public investment … Far from crowding out private investment, this spending crowds it in. It paves the way for new industries to emerge and raises the return to any private venture that benefits from healthy, educated workers, passable roads, and reliable electricity (CGD 2008, pp.5-6; see also p.36).

Fourth, labour market (de)regulation, especially in order to support the expansion of the formal labour market:

> Labor market regulations … can restrict formal labor markets and the market access of poor workers. In India states with 'pro-worker' legislation recorded lower growth rates and less efficiency in reducing poverty. By contrast, Indonesia's high degree of labor market flexibility during the Suharto years promoted formal employment and labor-intensive growth. But since the 1997 Asian financial crisis, minimum wage increases prompted by union activity have left almost all employment growth to the informal sector, at wages below those in the formal sector (Besley and Cord 2007, p.17).[22]

Fifth, employment and labour productivity growth are central for growth as well as poverty alleviation: '*Employment growth* generates new jobs and income for the individual … while *productivity growth* has the potential to lift the wages of those employed and the returns to the self-employed' (World Bank 2009, p.11).

Sixth, international integration:

> The open world economy … offers developing countries a deep, elastic market for their exports … [and it] allows fast-growing economies to import ideas, technologies, and know-how from the rest of the world. One conduit for this knowledge is foreign direct investment … another is foreign education … Sustainable, high growth is catch-up growth. And the global economy is the essential resource (CGD 2008, p.2; see also p.22).

Seventh, exchange rate management in order to maintain export competitiveness. This is advantageous because it is relatively simple to implement, and it is neutral between economic sectors (CGD 2008, p.50).

Eighth, capital account liberalisation, in order to lower the cost of capital. However, liberalisation should be gradual both because foreign saving is an imperfect substitute for domestic saving (CGD 2008, p.3), and because excessively rapid liberalisation introduces unnecessary risks (p.57). Capital controls should be imposed if necessary.[23]

Ninth, social safety nets - not primarily for pro-poor reasons, but instrumentally:

> governments should … establish social safety nets - which provide a source of income to people between jobs - and ensure uninterrupted access to basic services. These policies are both ethical and practical. Without them, popular support for a growth strategy will quickly erode (CGD 2008, p.6).

These safety nets should be circumscribed, because:

> transfer schemes cannot be an answer in the long run and can be problematic also in the short run. In poor countries such schemes can impose significant burdens on already stretched budgets, and it is theoretically impossible to reduce poverty through redistribution in countries where average income falls below US$ 700 per year … even in developed countries, redistribution schemes cannot be the only response to rising poverty rates in certain segments of the population' (World Bank 2009, p.2).

Tenth, there must be political support for any set of policy reforms: 'Technical solutions should only be considered technically correct if they are also politically supportable' (World Bank 2008, Annex 1, p.8).

The pro-poor implications of growth derive both from faster growth and from the emphasis on policies addressing the specific constraints faced by the poor:

> policy makers who seek to accelerate growth in the incomes of poor people and thus reduce overall poverty levels would be well advised to implement policies that enable

> their countries to achieve a faster rate of overall growth. A successful pro-poor growth strategy would thus need to have, at its core, measures for sustained and rapid economic growth … These ingredients - good policies, stability, and public goods - were essential in facilitating private initiatives and investments among the non-poor and especially the poor (Besley and Cord 2007, p.19).

Implementation of these policy recommendations requires a selective, strategic and sequenced focus on the binding constraints on growth at each point in time. As Rodrik (2006, p.982) starkly put it,

> Policy reforms of the (Augmented) Washington Consensus type are ineffective because there is nothing that ensures that they are closely targeted on what may be the most important constraints blocking economic growth. The trick is to find those areas where reform will yield the greatest return. Otherwise, policymakers are condemned to a spray-gun approach: they shoot their reform gun on as many potential targets as possible, hoping that some will turn out to be the ones they are really after. A successful growth strategy, by contrast, begins by identifying the most binding constraints.

Similarly, for the CGD (2008, p.33):

> A list of ingredients is not a recipe, and our list does not constitute a growth strategy. We identify possible constraints on the economy's performance. A fully fledged growth strategy would identify which of these constraints demands immediate attention and which can be deferred (CGD 2008, p.33).

The World Bank is increasingly committed to this 'growth diagnostics' approach, having held at least one workshop on the issue, in mid-2008, to:

> share emerging findings and lessons from World Bank and DFID [UK Department for International Development] case studies on the linkages between growth analysis/diagnostics and work on governance and political economy issues … The workshop highlighted the need to shift from growth diagnostics (identifying the constraints to growth) to growth 'therapeutics' … finding policy solutions that are politically feasible and can be implemented [and] [i]dentifying "good enough" institutional arrangements likely to deliver growth (World Bank 2008, p.1).

The Bank has high hopes for its new approach, expecting large and rapid payoffs:

> There are important lessons to learn from this approach including that development policy is country-specific, may involve just a few reforms that can be optimally sequenced to relax binding constraints, and it may lead to large positive welfare impacts (World Bank 2009, p. 9).

3.4 - Inclusive Growth

The collapse of the PPG debates, combined with the new (but firmly neoclassical) growth framework developed by the World Bank and its associates, including DFID, have provided the conditions for the emergence of the *inclusive growth* (IG) paradigm in the late 2000s. This paradigm stresses the importance of growth for poverty reduction, admits that a wide range of policy combinations can deliver these outcomes, and aims to select the appropriate policies through 'growth diagnostics':

> Inclusive growth refers *both* to the pace and pattern of growth, which are considered interlinked, and therefore in need to be addressed together … Traditionally, poverty and growth analyses have been done separately. This paper describes the conceptual elements for an analytical strategy aimed to integrate these two strands of analyses, and to identify and prioritize the country-specific constraints to sustained and inclusive growth … Encouraging broad-based and inclusive growth does *not* imply a return to government-sponsored industrial policies, but instead puts the emphasis on policies that remove constraints to growth and create a level playing field for investment (World Bank 2009, pp.1-2).

Therefore, '[t]he inclusive growth approach takes a longer term perspective … The goal is to identify a bundle of binding constraints rather than the binding constraint, and then sequence these constraints to maximize inclusive growth in a country' (World Bank 2009, p. 12). For the World Bank, IG is *broader* than pro-poor growth:

> Rapid … growth is unquestionably necessary for substantial poverty reduction, but for this growth to be sustainable in the long run, it should be *broad-based* across sectors, and *inclusive* of the large part of the country's labor force … [T]he pro-poor approach is

> mainly interested in the welfare of the poor while inclusive growth is concerned with opportunities for the majority of the labor force, poor and middle-class alike (World Bank 2009, p.1).

Inclusiveness is understood in the sense of the WDR 2006 (see section 3.1), that is, focusing on equality of opportunity 'in terms of access to markets, resources, and unbiased regulatory environment for businesses and individuals' (World Bank 2009, p.2). This is essential for instrumental reasons, since 'systematic inequality of opportunity [is] "toxic" as it will derail the growth process through political channels or conflict' (ibid.).

Unsurprisingly,

> The inclusive growth definition is in line with the absolute definition of pro-poor growth, but not the relative definition. Under the *absolute* definition, growth is considered to be pro-poor as long as poor people benefit in absolute terms … In contrast, in the *relative* definition, growth is 'pro-poor' if and only if the incomes of poor people grow faster than those of the population as a whole, i.e., inequality declines. However, while absolute pro-poor growth can be the result of direct income redistribution schemes, for growth to be inclusive, productivity must be improved and new employment opportunities created. In short, inclusive growth is about raising the pace of growth and enlarging the size of the economy, while leveling the playing field for investment and increasing productive employment opportunities … [IG] focuses on productive employment rather than income redistribution … IG is typically fueled by market-driven sources of growth with the government playing a facilitating role (World Bank 2009, pp.3-4).

Finally, and to remove any remaining doubts about the close similarity between IG and older World Bank strategies,

> in countries starting at a very low income level and low growth, an inclusive growth approach would be very close to an approach for speeding up the pace of growth, as the main focus should be on getting the fundamentals for growth right [because a] high pace of growth over extended periods of time is a necessary, and often the main contributing factor in reducing poverty as found by a sizable body of literature (World Bank 2009, p.5).

3.5 - A Pro-Poor Assessment of Inclusive Growth

The World Bank's shift towards growth diagnostics and the identification of constraints to (inclusive) growth, which should be addressed sequentially, replicates the debates about the 'order of liberalisation' in the 1980s, after the collapse of the first wave of radical reforms in Latin America, and the debates about the speed of transition in the former Soviet bloc.[24] In both cases, essentially the same package of WC policies was offered, with only the order and speed of implementation being open to debate, regardless of the persistent underperformance and repeated crises in the adjusting countries. Even after the transition to the PWC, the Bank's policies were always presented as a package which may be sequenced, but should not be jettisoned. Interestingly, both WC and PWC economic policies were presumably identified *deductively*, starting from the 'best' economic theory (whether straight neoclassical or NIE).

The new IG paradigm is different in two respects: first, the 'correct' policies are, supposedly, drawn up *inductively* from successful growth experiences around the world. This is a way to incorporate carefully selected insights from the developmental state debates, as if they were merely practical truths. Second, and despite this logical reversal towards empiricism, table 2 shows that IG policies are *essentially identical* to the PWC, *plus a government-led push for growth*. In other words, the World Bank has conceded *nothing* of substance either on the content of its preferred policies or on the primacy of growth (rather than distribution) to improve the lot of the poor, with lip service only being paid to the need for distribution.

Table 2: From the Washington Consensus to Inclusive Growth

Original WC	PWC (Original WC plus:)	IG (PWC plus:)
Secure property rights	Anti-corruption	Competitive environment
Deregulation	Corporate governance	Government commitment to growth
Fiscal discipline	Independent central bank and IT	'Good policies'
Tax reform	Financial codes and standards	Public sector investment
Privatisation	Flexible labour markets	Labour market deregulation
Reorientation of public expenditures	WTO agreements	Employment and productivity growth
Financial liberalisation	'Prudent' capital account opening	International integration
Trade liberalisation	Non-intermediate exchange rate regimes	Exchange rate management
Openness to FDI	Social safety nets	'Prudent' capital account opening
Unified and competitive exchange rates	Targeted poverty reduction	Social safety nets

Source: Table 1 and section 3.4.

These striking conclusions suggest six limitations to the IG paradigm. First, the World Bank's refusal to admit that it provided misleading advice to its clients, and that its policies fostered stabilisation traps, is self-defeating because it dilutes the policy differences between IG, the PWC and the original WC. The Bank's avoidance of responsibility for its actions is morally

questionable. It is also inconsistent with the Bank's new emphasis on the constraints under which policy decisions take place and must be implemented. For these constraints must include the conditionalities imposed by the IFIs, buttressed by the carrots of refinance, aid and debt relief, and by punishingly large sticks in cases of non-compliance.[25] Although the World Bank does not currently claim the laurels in every case of success (it is merely happy to welcome the relevant 'leaders' in the CGD), the Bank continues to devolve responsibility for failure to the poor and transition countries themselves: apparently, if some have succeeded, those who haven't only have themselves to blame.[26] Unless the World Bank accepts its share of responsibility for the economic underperformance of the poor countries, its claims to have - finally - nailed down the 'correct' principles for economic policy will ring hollow.[27]

Second, IG presumes that countries fail through either ignorance of the 'correct' policies (which, incongruously, the Bank itself seems to have only just discovered) or through deviousness (e.g., because of corruption or rent-seeking behaviour). However, it is equally plausible that countries could fail because their preferred policies could not be implemented due to currency or balance of payments crises, insufficient aid, lack of market access, domestic or external debt overhang, conditionalities, or immiserising growth.

Third, IG does not address the limitations of previous World Bank strategies, including the contradictions between policy legitimacy, ownership and participation,[28] the cost of the policy shifts, and the absence of self-correcting mechanisms in IFI policies. It seems that, under IG, failure still be blamed on the victims, and the remedy will continue to include the demand that they should try again, harder. These limitations cannot be addressed except through a considerable relaxation of the conditionalities imposed by the IFIs. Conditionality is the enemy of experimentation, without which the 'leaders' brought together by the World Bank would have no lessons to reflect upon. Conditionality is also inimical to the contextual links between general principles and local conditions which is, allegedly, at the core of IG.

Fourth, the lessons of growth reported in World Bank and CGD reports aim to present a plausible menu of 'successful' policies and, simultaneously, to legitimise the displacement of pro-poor strategies by a growth-enhanced version of the PWC. However, their conclusions are biased. Two examples should suffice. The CGD claims that '[g]rowth of 7 percent a year … is possible only because the world economy is now more open and integrated … Sustainable, high growth is catch-up growth. And the global economy is the essential resource' (CGD 2008, p.2). This is presumably an argument for free trade and free flows of capital and people.

It may be appealing, but it is also flawed because it brushes aside numerous episodes of rapid and sustained growth before neoliberal 'globalisation', for example, in Brazil, China, India, Mexico, Norway, Poland, South Africa and the USSR, not to speak of heavily selective 'global integration' in South Korea and Taiwan before the mid-1980s. The second example refers to the dog that has failed to bark: although the World Bank increasingly recognises the significance of asset ownership in its definitions of poverty (see section 3.1), IG breezily ignores the role of asset transfers in its *own* selected experiences of growth, including radical land reforms in China, Japan, South Korea and Taiwan, and the distributive implications of resource rents in Botswana and Oman.

Fifth, IG assumes that economic growth is the most powerful tool for the elimination of poverty. This conclusion ignores that growth can also *create* poverty because it brings technological changes, shifts in property or user rights and transformations in the labour markets which can dispossess and impoverish large numbers of people (see section 2.1). Many workers may be unable to find alternative productive assets or jobs with equivalent pay, or to retrain in order to seek better opportunities elsewhere. The self-employed may also find that their economic prospects are depressed because of their insufficient access to credit and markets. Even when they induce growth in selected sectors, mainstream development strategies - including IG - ignore the structural inequalities which create poverty even as the economy expands. If income and productivity growth are sufficiently rapid, most people benefit even if inequality rises (e.g., Brazil and Mexico from the 1950s to the 1970s, the Gulf economies between the early 1970s and mid-1980s, and China since the 1980s). Alternatively, GDP growth may be insufficient or erratic, leading to the stagnation or even the decline of the welfare standards of large numbers of people (e.g., Russia and other former Soviet countries since the early 1990s, and most Middle Eastern, African and poor Latin American countries since the 1980s).

Sixth, the inclusion of social safety nets in IG is primarily instrumental. They alleviate poverty, provide political legitimacy for the World Bank's preferred policies, and offer a channel for the poor to gain from growth - but they are *not* implemented in order to achieve distributive goals. Distribution is purely incidental to IG; the focus of these policies is entirely on growth and on the ensuing (primarily spontaneous but, at the margin, state-sponsored) absolute welfare gains for the poor.

4 - From Pro-Poor Growth to Pro-Poor Development Strategy

The PPG literature attempted to confront the (P)WC by claiming that equity is an ethical imperative, and that distribution as well as growth would benefit the poor. The potential tension between these statements - one about principles and the other about instruments - was exploited by the mainstream in four stages. First, by gesturally admitting that equity is good in itself. Second, by restricting the concept of equity to equality of opportunity only (in contrast with the increasingly broader definitions of poverty in World Bank publications, see section 3.1). Third, by 'operationalising' the relationship between growth and distribution through measurements of the impact of equity on growth; and, finally, concluding that poverty and inequality are mutually reinforcing, and that 'inclusive' growth is the best way to address both of them simultaneously.

The mainstream reaction against the PPG literature was successful because the latter was *too close to the mainstream*, agreeing to an instrumental definition of PPG as *any* growth which disproportionately benefits the poor and, subsequently, becoming embroiled in a degenerating debate about the relative implications of (a disembedded process of) 'growth' and distribution on absolute poverty. This was a blunder, because disembedded growth does not exist, and there can be no valid debate about the distributional or any other impact of growth 'in general'.[29] Growth exists only concretely, and the modality of growth is inextricably bound up with its distributional (and other) outcomes.

In contrast with the narrow and gradually collapsing expectations of PPG, a *pro-poor development strategy* (PPS) is both ambitious and clearly distinct from the mainstream. A PPS needs to satisfy two conditions. First, it must explain the structures and processes underpinning the pro-poor growth process, for example, those examined in section 2. These structures and processes should include not only a positive feedback loop between growth and distribution but, more strongly, they should make distribution *essential* for growth (growth will take place *only* insofar as it benefits the poor disproportionately). *In PPS, distributional outcomes are a condition for growth, rather than the incidental outcome of growth*. Second, PPS must recognise that logical consistency is a necessary but insufficient condition for success. Implementation of PPS depends critically on the *political structures* underpinning this development strategy.

4.1 - Growth and Distribution in Pro-Poor Development Strategies

The first condition for PPS transcends the duality between growth and distribution which doomed the 'early' PPG literature. It was shown in section 3.1 that PPG was criticised by the mainstream because it left imprecise the relationship between growth and distribution. For example, the mainstream argued that, at a static level, some countries are 'too poor to redistribute' (their per capita income is so low that redistribution would have little impact on the level of poverty) and that, at a dynamic level, growth can reduce poverty more efficiently than distribution.[30] These arguments are based on an artificial separation between distribution and growth. This separation is untenable, because growth *always* redistributes income and wealth, and the distinction between static and dynamic redistribution is purely analytical. Since redistribution is inherent in the process of growth, it is appropriate that *both* growth and distribution should be subjected to policy influence.[31]

Recognition that growth and distribution are inseparable supports the case for a more expansionary pro-poor development strategy, going beyond what is permissible under the mainstream policy compact. Faster growth will generate additional resources for redistribution and promote economic resilience through employment creation, investment in productive assets and in economic diversification, and social protection and the supply of public goods, especially health and education. Unless distributive and social policies are co-ordinated with the overall expansion of the economy there may be gluts in the labour market (e.g., skilled engineers driving taxis or working in food kiosks), which would be wasteful for the economy and demoralising for the affected individuals. Insufficient investment would also make social welfare excessively vulnerable to economic volatility, which tends to affect disproportionately economies lacking basic infrastructure.

Faster growth must be supported by the redistribution of income and assets and by a shift of investment priorities, i.e., a dynamic (continuing) redistribution of productive assets, for two reasons. First, because of the significant impact of redistribution on poverty:

> Very small changes in distribution can have a large effect on poverty head counts … [For example, if] the share of national income that goes to the poorest population quintile increased from 6 to 6.25 per cent, this would represent a 4 per cent increase in their total income. Thus, a very small redistribution would have the same effect on poverty as doubling the annual growth of national income from 4 per cent … to 8 per

> cent … [Similarly,] over the 15-year forecast period a 5 per cent point change in the Gini makes as much a difference to poverty reduction as an additional 50 per cent growth in consumption per capita. On an annual basis this translates to an additional 1.3 per cent growth per capita (Naschold 2004, pp.108, 118).

Second, because 'increases in inequality are hard to reverse, and greater inequality reduces the poverty elasticity of growth' (Naschold 2004, p.118).

The state plays an essential role in the co-ordination of growth, investment and distribution. PPS requires close co-ordination between private and public sector activities, and the regulation of intersectoral and intertemporal resource allocation (including international capital flows) through industrial and financial policy. This is not because the state is either necessarily efficient or inherently 'good'. Experience with (P)WC policies shows that markets are not efficient in the abstract, and they cannot even provide the parameters to assess economic efficiency in general. Conventional perceptions of market efficiency are normally based on an idealisation of what financial or currency markets do. However, even before the current crisis these markets were very different from the markets for oil, coffee, computer programmes, air travel or health services. In each market, efficiency has to be measured and assessed in specific ways, the penalty being the application of misconceived policies at great cost.

State-led coordination of activity is necessary because the state is a fundamental tool for collective action. The state is the only social institution that is at least potentially democratically accountable and that can influence the pattern of employment, the production and distribution of goods and services and the distribution of income and assets at the level of society as a whole. Only the state can limit the power of unaccountable private interests, raise sufficient funds for democratic economic reforms, and ensure that economic activity is guided by the demands of the majority. PPS is distinctive not because the state manages individual firms or enjoys unlimited property rights, but because of the way in which the state coordinates economic activity in pursuit of distributive ends. State ownership of specific assets is a secondary issue; what really matters are the objectives of government policy, and how state institutions interact with one another and with private concerns.

This is an argument for specificity in PPS. The diversity of country experiences and over time suggests that the state and its economic policies cannot be selected or analysed in the abstract.

Similarly, it was shown in sections 2.2 and 3.2 that there can be no expectation that policies can be replicated from one country to another with the same effects. Historical instances of success and failure must be assessed in context, recognising that their outcomes are specific to both country and time. This is not an argument against learning from experience, but a claim that empirical developments do not offer ahistorical lessons. Finally, recognition of the significance of specificity and the importance of context for the evaluation economic policy is not the same thing as the deployment of induction in World Bank arguments for IG. It was shown in section 3.5 that the latter are logically muddled up, offering evidence drawn up selectively and filtered by criteria which remain implicit but that are, invariably, based on neoclassical economics.

4.2 - The Politics of Pro-Poor Development Strategies

The second condition for PPS concerns the significance of politics, at two levels. First, political co-operation is essential for the manageent of contradictions between sectional interests and the public good, which are intrinsic to a market economy. This includes the destructive implications of competition, for example, the unco-ordinated destruction of jobs and skills through market power, technological change or because of narrow or sectoral economic imperatives.

Second, PPS recognises that collective action always has a political content, and it should be steered to promote equality, inclusiveness and democratic accountability rather than, for example, social exclusion. The expression of the interests of the poor in a capitalist economy is intrinsically conflictual both because the distribution of income and assets and the direction of growth are always contested and, at a deeper level, because the structures of social and economic reproduction are, necessarily, based on conflicts between individuals and groups. The economic weakness of the poor can be overcome, and a politically supportive environment can be created, only through their political mobilisation.

The mobilisation of poor people should be welcomed within democratic institutional structures in order to help balance the political biases introduced by entrenched inequalities. Mobilisation will also offer the poor avenues for the expression of their perceived needs (see, for example, Wignaraja et al 2009), and it will give political leverage to governments committed to PPS. It was also shown above (see section 3.1) that, for the mainstream, PPG can trigger political reactions which may destabilise the economy and paralyse policy-making.

This is correct, and it also applies to PPS. However, successful examples of growth and distribution in Chile, Cuba, India (especially in Kerala State), Sri Lanka, Venezuela, Vietnam and other countries demonstrate that these adverse outcomes are avoidable. In sum, PPS must be underpinned by sufficient political will to confront the conventional wisdom and the neoliberal hegemony, and to build alternatives based on the joint efforts of governments, heterodox economists and civil society:

> Political costs (namely, losses for the rich) are usually cited as a rationale for avoiding redistributive policies. We would emphasize, in stark contrast, that the majority of the working population need to mobilize themselves politically so that the 'political costs' of not undertaking redistribution become prohibitively high (McKinley 2009, p.19).

Naturally, the demands of the poor will not always be achievable, which invites negotiation and compromise around the stages of PPS; but they will at least be the legitimate expression of the felt needs of large numbers of citizens. This is far from being a novelty. Political mobilisations by the poor in the UK in the late 19th Century helped to reduce inequality in the country, and mobilisations in Western Europe and East Asia in the post-WW2 period helped to achieve significant distributive gains. In the West, broad-based social mobilisation also made the expansion of the Welfare State possible and sustainable over time.

Conclusion

A cursory reading of the debates about growth and distribution in the early 2000s would suggest that pro-poor growth was becoming the new consensus economic policy. Evidence that the concentration of income was increasing both between and within countries under neoliberal globalisation was increasingly difficult to reject;[32] and the UN declarations of the right to development and the MDGs seemed to signal the defeat of the 'pro-market' claims associated with the (P)WC. Nevertheless, rhetorical convergence around a pro-poor discourse concealed a significant undercurrent, as the mainstream sought to capture the moral and conceptual high ground. The 'inclusive growth' paradigm is the outcome of this effort.[33]

Critical assessment of IG should depart from the recognition that it belongs squarely within the (P)WC traditions of the mainstream, and that it has been obvious for many years that the policy prescriptions of the (P)WC are successful only exceptionally. But this is insufficient. For the critical issue is *neither* the comparison between the growth rates achieved by

economies with or without adjustment programmes, or before and after such programmes, *nor* the evaluation of the implications of these programmes (including IG) on absolute poverty.

The principles of global justice offer an indispensible moral compass for the assessment of alternative economic policies. For the main problem for the majority concerns the *type* of growth promoted by different versions of neoliberalism. This growth pattern - whether it is inspired by the WC, the PWC or IG - is undesirable because it achieves *less* than what is possible for the poor, given the resources and technologies available, and because it concentrates income and power, perpetuates deprivation and prevents the realisation of human potential. Today, failure is not due to the lack of resources or to ignorance. It is due to perverse policy choices.

The limitations and insufficiencies of mainstream development strategies make it essential for the poor majority, which has hardly benefited from economic development for an entire generation, to consider alternative development strategies. These strategies should respond to the imperatives of equality, democracy and social justice, and foster economic growth, mass employment, social inclusion, the satisfaction of basic needs and the provision of welfare for the vast majority of the population. Experience shows that these objectives can be achieved only through the deployment of centrally co-ordinated industrial and investment policy, informed by the democratic mobilisation of the majority of the population.

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Endnotes:

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[1] I am grateful to Muhammad Ali Jan and Trudy Rebert for their superb research assistance.
[2] This paper treats the terms 'poor' and 'developing' countries as synonyms. These countries are disaggregated, when necessary, into 'very poor' and 'middle-income' countries.
[3] 'It is not necessarily the case that shocks affect the poor disproportionately, but it is clearly the case that they are more vulnerable, since their economic margin is slim' (Bigsten and Levin 2004, p. 269).
[4] See Fine, Lapavitsas and Pincus (2001), and van Waeyenberge (2007).
[5] For a taste of the literature, see Bird (2001), Buira (2003), IMF and IDA (1999), Pender (2001), UNCTAD (2000, ch. 5 and 2002, ch. 5), and World Bank and IMF (2004).
[6] For an overview of the pro-poor policy literature, see Dagdeviren et al. (2002), Kakwani (2001, 2002), Kakwani and Pernia (2000), McCulloch and Baulch (1999), McKinley (2001, 2003), Osmani (2001), Palanivel (2003), Pasha and Palanivel (2004), Rao (2002), Saad-Filho (2007), UNDP (2002), Vandemoortele (2004) and Winters (2002).
[7] This aim is not only important in itself; it is also mandated by the United Nations through the Universal Declaration of Human Rights (UDHR), the Declaration on the Right to Development (UNDRD), and the MDG.
[8] The expansion of the economy always helps to alleviate poverty, except in a small number of perverse cases. This is hardly sufficient: the point is how to maximise the impact of growth on poverty over the long-term (see Dagdeviren et al, 2002, p.391).
[9] See, for example, Amsden (1997, 2001), Chang and Grabel (2004), McKinley (2003), Osmani (2001) and Pasha (2002).
[10] These examples are merely indicative. The impact of growth on poverty depends on the initial distribution of income and, especially, its distribution near the poverty line, as well as the occupational composition, skills and other features of the workforce.
[11] Pro-poor fiscal policy is reviewed by Kakwani and Son (2001) and Roy and Weeks (2003).
[12] See, for example, Chang (2003), Chang and Grabel (2004, ch. 9), Eichengreen (2003), Epstein, Grabel and Jomo (2003), Grabel (2004), Helleiner (1996), Kaplan and Rodrik (2001) and MacEwan (2003).
[13] Moderate exchange rate undervaluation finds strong support in the literature on trade and industrial policy; see Agosín and Tussie (1993), Chang (1994) and Gereffi and Wyman (1990).
[14] See, for example, Levine (1997), Palma (1998), Sikorski (1996) and Studart (2005)
[15] Universal basic income (UBI) is the only type of non-targeted cash transfer. However, it is unaffordable for most very poor countries, and this is hardly the best use for the scarce resources of the middle-income countries. UBI is also vulnerable to most criticisms of cash transfers listed above.
[16] For example, Vandemoortele (2004, p. 12) notes that user fees can 'aggravate gender discrimination ... Since the mid-1990s, school fees have been abolished in Malawi and Uganda and more recently in Kenya. That pro-poor policy was followed by a surge in enrolment in all three countries – with girls being the prime beneficiaries. These positive experiences illustrate that even a small nominal fee can be a formidable obstacle for poor families.'
[17] 'By focusing on inequality, the relative definition could lead to sub-optimal outcomes for both poor and non-poor households. For example, a society attempting to achieve pro-poor growth under the relative definition would favor an outcome characterized by average income growth of 2 percent where the income of poor households grew by 3 percent, over an outcome where average growth was 6 percent, but the incomes of poor households grew by only 4 percent. While the distributional pattern of growth favors poor households in the first scenario, both poor and non-poor households are better off in the second scenario. *There is broad recognition that when poverty reduction is the objective, then the absolute definition of pro-poor growth is the most relevant* … Using the absolute definition, the aim is to increase the rate of growth to achieve the greatest pace of poverty reduction (World Bank 2009, p.3).
[18] For an overview, see Bowman (1997), Cornia (2004), Cramer (2000), Kanbur (1998), Niggle (1998) and Persson and Tabellini (1994).
[19] The 'Commission on Growth and Development [is] an independent group of policy makers, business leaders, and scholars, supported by the World Bank, the Hewlett Foundation, and the governments of Australia, Netherlands, Sweden, and the United Kingdom' (CGD 2008, p.13).
[20] The CGD (2008, p.7) pointedly remarks that 'Governments in the high-growth economies were not free-market purists. They tried a variety of policies to help diversify exports or sustain competitiveness'.
[21] See Besley and Cord (2007, pp.14, 17), CGD (2008, pp.5, 15, 21), and World Bank (2009, p.7).
[22] Three caveats are immediately added (ibid.): 'First, labor market regulations are only one of a set of factors that affect the investment climate and the willingness of a firm to formalize … Second, loosening labor market regulations in some regions … may have little impact on labor markets, especially if employment is mainly in agriculture … Third, labor market regulations … constitute a form of social protection'.
[23] 'Yes, capital controls are leaky, but so are taxes, and that does not stop governments from trying to tax their citizens' (Pedro Pablo Kuczynski, in CGD 2008, p.52).
[24] See, for example, McKinnon (1982) and Milanovic (2005).
[25] The case of Zambia is especially revealing; see Weeks (2007).

[26] This includes both the speed of growth and its distributional implications. For example, 'pro-poor growth, even over sustained periods of time, can occur in a variety of contexts, including very unfavorable initial conditions' (Besley and Cord 2007, p.20). However, '[t]he difficulty of creating pro-growth environments in these more challenging areas may particularly explain the rise in inequality that these [very poor] countries experienced in the 1990s (Besley and Cord 2007, p.4).
[27] For a similar argument, see Cling et al (2002, p. 9).
[28] The World Bank could never resolve such conundrums as this: '[r]esearch of the World Bank … suggests that the aspiration of the African poor is not the development of private property rights per se, but rather land reform (UNCTAD 2002, p.40). In these cases, the poor need not be listened to.
[29] In other words, the growth-distribution dichotomy is false, and it is wrong to decompose poverty changes into its growth and distribution components, because the interaction between these elements is not simply additive: the impact of growth on inequality, and the growth-elasticity of poverty, vary with the degree of inequality, the level of development of the country, and so on (see Heltberg 2004, pp.82, 90).
[30] '[A] key difference between the poverty projections for LDCs and those for other developing countries is the relative importance of income inequality for reducing poverty. For developing countries as a whole the growth effect dominates the inequality effect' (Naschold 2004, p.118).
[31] For a similar argument, see Dagdeviren et al (2002) and Heltberg (2004).
[32] See, for example, Milanovic (2002, 2003).
[33] There is a close resemblance between the mainstream confrontation, taming and subordination of PPG and the much earlier subordination of the radical implications of Keynesianism by the mainstream through the neoclassical synthesis.