

THE GLOBAL FINANCIAL CRISIS: TURNING THREATS INTO OPPORTUNITIES

Executive Summary

The Global Financial Crisis (GFC) is a threat to poverty reduction but it has served to reveal indisputably the fault lines of neo-liberalism. It can thus be seen as an opportunity to press the case for an alternative, rights-based, approach. Such an opportunity did not exist while neo-liberalism remained dominant. Its focus on market forces provided the intellectual support needed by a powerful political movement that stood for less government and its self-selected indicators of success, emphasising economic growth, seemed to prove its incontestability.

The domination was summed up in the term “Washington Consensus”, which led to a series of policy prescriptions being imposed globally, including as the central plank of development co-operation. Failures occurred but were rationalised away. Dissent was voiced, reflecting concern about rights and broader aspects of well-being, especially of the most vulnerable. It could not however gain a proper hearing as neo-liberalism dominated. This imbalance extended to the Australian aid program, with economic growth being seen as a necessary and sufficient condition for effective development.

Disagreement over neo-liberalism divided those who might otherwise claim to share the same objectives for development co-operation. One group saw its objectives solely in economic terms; the other advocated wider objectives, reflecting different elements of human aspiration and advocated an approach based on rights to secure these aspirations. ActionAid Australia is part of this latter group and, with its strong commitment to a rights-based approach as part of ActionAid, can play a leading role in arguing for a review of the impact of neo-liberalism.

The GFC has not only placed the wisdom of neo-liberalism in doubt but has provided some points of leverage which ActionAid Australia and others can use to demand a proper review of its lessons for the future direction of Australia’s aid policy. These include the Prime Minister’s own affirmation of the need to harness and more closely manage market forces to secure intrinsic rights to human dignity, the prospects of destabilisation of some countries as a result of the GFC and the acceptance in some parts of the coalition that formed the Washington Consensus that there is no single set of policy prescriptions suited to all cases.

The suitability of neo-liberalism as a foundation for development strategies depends on the relevance of its assumptions concerning the nature of economic decision-makers and the role of prices in driving market forces. When these are shown to fundamentally misrepresent the real situation, the distortions and problems thereby created can be better understood. Key messages that should be delivered in a future debate include the impact of neo-liberalism in terms of exacerbating inequality and discounting other elements of vulnerability and applying standards of risk to developing countries that fail to register the different levels of likelihood and consequences that need to be used in managing risks in such countries. The failure to acknowledge these problems led to demands that poorer countries follow the same policies with the same sorts of institutions that were seen as appropriate for richer countries. This mindset was reinforced by being implemented through development institutions, multilateral and bilateral, that gave little hearing to alternative voices and lacked the standards of responsiveness and accountability that they demanded of recipient governments as a cornerstone of good governance.

ActionAid Australia has a range of opportunities to initiate and develop the new debate. These include existing dialogues, such as those on food security and conflict and possible new initiatives including a suggested seminar on issues of governance. It should also press for a new approach to whole-of-government approaches to development, one that ensures that other government policies are consistent with aid objectives rather than vice versa and which also opens up residual commitment to neo-liberalism on other parts of government to greater contestability in the context of development.

A. Introduction

The Global Financial Crisis (GFC) is a major threat to poverty reduction. Most developing countries have been seriously affected, reflecting the impact of globalisation. Governments have less resources to tackle poverty at a time when more people are in danger of slipping into poverty – such as those in export industries. There are serious threats to stability of some government as the growing prosperity on which they have secured popular support is eroded. Instability brings its own dividends in terms of decline in living standards, especially of the most vulnerable.

The least developed countries represent special cases, facing problems that arise from the GFC that are in some cases different but at least as serious. Many of them are less enmeshed in the global economy. They are however generally much more dependent on ODA, and the prospect of lower levels of aid as richer countries turn their attention more to their own problems will therefore have a significantly greater impact on them. Many are also very dependent on a small number of industries, such as tourism or mineral exports, which are particularly susceptible to the GFC. In some cases, a large

proportion of their national income comes from remittances by nationals who have gone elsewhere to work and who may now be forced by unemployment to return home.

The impact of the GFC is thus a major threat but it can also be an opportunity. It has given good cause to question some of the basic assumptions that underpinned the conventional wisdom as to what constitutes “good” governance. These assumptions reflected a neo-liberal economic agenda, comprising fiscal conservatism, tax reform, trade, foreign direct investment, interest rate and exchange rate liberalisation, deregulation and privatisation.

This paper considers how NGOs such as ActionAid Australia can use this opportunity. The objective is to ensure that the lessons of the GFC steer development cooperation more effectively towards helping governments and civil society in developing countries to protect the interests of the most vulnerable¹. Such a transformation is essential if future development co-operation is to be grounded in a rights-based approach.² An important theme of the paper is that the GFC has revealed the fault lines in neo-liberalism; the focus therefore should be on the record of neo-liberalism as a whole rather than simply on the causes and impact of the GFC.

The paper is at this stage intended to facilitate internal discussion. As its intended audience may have differing levels of understanding of some of the key economic issues, some additional explanation is provided, often in the form of boxes that can be skipped by those with greater familiarity with such issues. It has however been drafted with next steps in mind and some of the text could be easily adapted to provide a background paper for a wider audience, including AusAID.

The paper is structured as follows. A background section sets the scene, explaining the reasons for the ascendancy of neo-liberalism globally and in the context of Australia’s government aid program. The next section examines the standpoints of the two sides of the debate over the record of neo-liberalism. This is followed by an examination of potential points of leverage that could be used to establish a more open debate. The next and most lengthy section considers the key elements of the rights-based rejoinder to neo-liberalism, thereby trying to focus on what are the priority points to be made once the opportunity to debate the neo-liberal legacy and the consequences of the GFC has been secured. The paper then concludes with some exploration of specific activities that could be used to advance the rights-based approach.

B. Background

Neo-liberalism is not a single set of theories or policy prescriptions. Nonetheless, the term can be broadly applied to a range of economic strategies intended to maximise the reach and frequency of market transactions and to bring all human actions into the domain of the market.³ Unlike Keynesian theory, which addressed the problems caused by the unpredictability of human nature (what Keynes himself called “animal spirits”), neo-liberalism based itself squarely on the earlier neo-classical models and endeavoured to portray its theories as akin to those of natural sciences. Consequently, it pushed aside uncertainty of human behaviour in favour of assumptions that any decision would be rational, maximising and based on perfect knowledge. These decision-makers could then maximise their individual economic outcomes with no intervention from government.

Neo-liberalism’s chance to become the dominant economic setting came with the evident failure of Keynesian theory to predict or resolve the stagflation of the 1970’s, coupled with the ascendancy of a political movement that essentially saw government as the problem, not the solution. Its messages of self-correcting markets, lack of need for intensive government involvement and the advantages of leaving the private sector alone fitted neatly into this political ideology and became its intellectual justification. Its domination was further assured by its apparent success in practice. Neo-liberalism had in fact set its own measures of success, creating a process of self-justification. These measures concentrated on indicators of economic growth, with trends in inequality or concern for non-economic factors that can affect vulnerability being ignored, dismissed as inconsequential or rationalised away by shibboleths such as “a rising tide (eventually) lifts all boats”. Additionally, with the agenda being set by developed country governments who could focus on their own decades of more

¹ The term “vulnerability” is generally used here, in preference to narrower terms such as “poverty” since it more effectively encompasses what can be a wide range of economic, social, physical and other problems that undermine the well-being of people. As will be seen below, “poverty” tends to denote only the economic dimensions of vulnerability and policies that focus solely on these risks distorting the priorities of those who are most vulnerable.

² ActionAid Australia, is well placed to pursue this objective, given ActionAid’s strong advocacy of a rights-based approach, which recognizes poverty and injustice as a direct human rights violation. As a result, it approaches its work not as charity but as partnership with people as holders of rights rather than as passive beneficiaries.

³ Definition taken from Andrew Rosser, “Neo-liberalism and its discontents in Australian aid policy”, Australian Journal of International Affairs, Volume 62, Issue 3, September 2008.

or less uninterrupted strong growth, any doubts about the impact of the neo-liberal agenda on poorer countries – and especially on the most vulnerable in those countries – could be ignored or rationalised away.

This dominance is well summed up in the use of the term “Washington Consensus”. This ascendancy, together with the evident triumph of liberal democratic politics, created an irresistible force that allowed all dissent to be stifled. In fact, one of its most fervent advocates, Francis Fukuyama, was inspired to proclaim that the “end of history” had been reached.⁴

However, when the application of the Washington Consensus led to some catastrophic failures, such as in Russia, the overall strategy had to be reviewed. This led to a new paradigm, labelled the “Post Washington Consensus”. An outline of both the original strategy and the revised version is set out in Box 1.

Box 1
The Washington Consensus

The term “Washington Consensus” was coined by economist John Williamson in 1989 and was used by him to describe a specific package of economic reform measures designed to be applied to developing countries. These measures included stringent fiscal discipline (i.e. balanced budgets), tax reform (usually intended to relax the tax burden on higher income earners to provide more “incentive”), trade liberalisation, foreign direct investment liberalisation, deregulation, interest rate and exchange rate liberalisation, privatisation and secure property rights. All these measures reflected the neo-liberal economic theology and it was assumed that they could be applied equally to any situation.

Nonetheless, some drastic failures occurred – such as in the overnight shock therapy applied in Russia in the early 1990s. Responding to this failure of the WC prescriptions to deliver the expected benefits in all cases, its proponents have tended to offer two explanations – either that the medicine was not followed adequately or that something more was needed. The latter response led to the so-called “Post Washington Consensus”, an approach which acknowledged a continuing role for government in some limited key areas, notably in addressing income distribution and in providing institutional arrangements to facilitate effective market operations.

The problems with both the original Consensus and its revised versions will be considered in more detail below.

Inevitably, neo-liberalism’s ascendancy shaped the development of Australian aid policy. Alternative approaches were given scant attention. Even when the direction of aid was supposedly opened up to comprehensive re-examination, notably in the Jackson and Simons Reviews, the outcomes were largely predetermined by the predominance of orthodox economic thinking in the teams appointed to carry out the work. Additionally, Australian business used its easy access to higher levels of government to push for an agenda that promoted development in neighbouring countries of pro-market and pro-investment policies and practices. All this meant that, even when new directions were incorporated in the aid program, these were fundamentally shaped by the neo-liberal agenda. For example, as “governance” became more a focus of attention, from the 1990s, so did the presumption that “good” forms of governance necessarily involved substantial application of the “Washington Consensus”.

C. Defining the debate

The entrenched position of neo-liberal attitudes has fundamentally affected the debate on Australian aid policy. Ostensibly united by the common purpose of reducing poverty (as shown, for example, in the theme of the Simons Report – “One Clear Objective”), there emerged instead two often diametrically opposed views of how this might be achieved. It is important to understand the characteristics of these two opposing groups. For this purpose, a methodology will be used that was initially made popular by Ravi Kanbur of Cornell University. He distinguished between “Type As – archetypally from finance ministries and international financial institutions, who take a rather ‘economistic’ and analytical approach” and “Type Bs – archetypally from civil society and non-governmental organisations, who are more broadly social scientific in their thinking.”⁵ There are of course always dangers in trying to generalise about different positions in a debate but Kanbur’s categories help to demonstrate that those who press for more attention to a rights-based approach have a legitimate claim to equal attention in any debate over the legacy of neo-liberalism and of the lessons of the GFC. Kanbur identified three distinct differences in the perspectives of the two categories, which are set out below in Table 1.

⁴ Francis Fukuyama, *The End of History and the Last Man*, Free Press, 1992.

⁵ R Kanbur, “Economic Policy, Distribution and Poverty: The Nature of Disagreements”; paper presented to the Swedish Parliamentary Commission on Global Development, Stockholm, September 2000.

Type:	A	B
Issue		
1. Measuring poverty	Quantifiable measures at aggregate level	Broader, more qualitative measures, including individual and small group experiences
2. Time frame	Medium term equilibrium	Short term, with focus on adjustment costs and temporary poverty
3. Underlying assumptions	Perfect market – equal and perfect information, clear incentives etc.	Imperfect competition dominated by benefits of power etc.

Implicit in this typology is the attitude of each group to the concept of a rights-based approach. For Type A, it is beside the point. As earlier indicated, even the concessions to equity reflected in the Post Washington Consensus did not extend to any active consideration of broader rights. For Type B, a rights-based approach has become increasingly dominant as the foundations for their strategy for reducing vulnerability.

D. Breaking into the debate

Any substantial and lasting change in Australia’s aid policy will depend on the ability of Type 2 organisations such as ActionAid Australia to take two crucial steps: to gain equal status in addressing the legacy of neo-liberalism and then to make an effective case for changing direction away from the policy and practices determined by that legacy. Neither step can be assumed to be easy. Despite all that has happened, the default setting for Australian aid strategy remains market-oriented and growth focused. This may be seen as a matter of inertia, fostered by lack of clear political leadership to drive new thinking. It is however more entrenched than that, protected by the strenuous efforts of neo-liberalism’s supporters to defend their position or at least to cloud the debate. This is addressed in more detail in Box 2.

Box 2
Neo-liberalism’s fightback

Declarations that “we are all Keynesians now” are predictably met by denials from many quarters, primarily those who defend the mantra that “the government is not the solution, it is the problem.” Anyone wishing to see the range of arguments used in favour of resisting the siren call of neo-Keynesianism (which many see as socialism in disguise) should read the columns of “The Australian” or, for a particularly breathtaking effort, the analysis provided in Quadrant by Steven Kates (“The Dangerous Return to Keynesian Economics”, Quadrant, March 2009), who backed up his contention that governments should basically do nothing by arguing that “the world’s economies are not suffering from a lack of demand, and the best policy response is not a demand stimulus.”

However, whether or not fiscal stimulus packages succeed, all sides are likely to claim victory; economists have become very adept at using the facts, ex-post, to demonstrate that their theories have been vindicated. If the facts do not fit, there are a variety of excuses, starting with the claim that exogenous factors intervened. In other words, unco-operative statistics can be dismissed as irrelevant. However fast the GFC is resolved, there will be many who would argue that recovery would have been faster if only the markets had been left to work their magic without government interference.

This attachment to neo-liberalism remains deeply rooted in key parts of the Australian public service, as demonstrated for example by the continued advocacy of unqualified free trade by DFAT.⁶ As part of a whole of government approach to aid policy, the tenacity of these influences cannot be ignored.

To get a fair hearing, advocates of a rights-based approach will gain most leverage by building on existing contributions to the debate. Some examples, both domestic and international, are suggested to start such a process of identification.

The strongest domestic point of entry is the government’s own efforts to distance itself from the neo-liberal agenda, as typified most prominently by the Prime Minister’s paper in the February issue of The Monthly. This evidently signalled his return from an ideological attachment to “fiscal conservatism” in the me-too election campaign to the social democratic principle that markets need to be managed to ensure greater stability and equity. Its significance is shown by the weight of

⁶ This faith is a classic example of Type 1 thinking. It owes much to the belief that Ricardo’s doctrine of comparative advantage is universally applicable. This doctrine, which underpins most of the case for free trade, in fact holds true only under very rigorous conditions which have no equivalent in the real world. In particular, it assumes that technology remains unchanged and that there are constant returns to scale.

the invective launched against it. Despite the efforts of many commentators to characterise the paper as anti-market, it is in fact a nuanced piece; Rudd is concerned that we should not throw the baby out with the bathwater. This points to the need for care in building on his approach since it does not provide a green light for all-out attack on market forces. Even so, there is enough in Rudd's apparent Damascene (re)conversion for NGOs to claim some authoritative support in opening up the debate. An analysis of suggested key points, to aid discussion of this opportunity, is contained in Box 3.

Box 3

Building on Social Democracy – key points from Rudd's "The Monthly" paper

There are four particularly relevant aspects in the Rudd paper

- the strong links he draws between social democracy and social justice;
- his acknowledgement that human dignity is an intrinsic right, which extends beyond any opportunities provided by market forces and which also effectively negates measures of progress in reducing poverty that rely purely on economic indicators;
- the role played by the IMF in promoting the neo-liberal agenda in developing countries; and
- the absence to date of a full debate on the impact of the GFC on poverty and political stability in developing countries.

Put together, these can be distilled into two critical development-related issues:

- Social justice in terms of assurance of human dignity is a legitimate - in fact essential - objective but cannot be assured through market mechanisms; and
- The international community and its multilateral agencies need to approach diagnosis and cure of development problems with considerably more humility.

A second domestic point of entry is lies in the warnings that the GFC risks stability in many developing countries. The Government's concerns about security issues and about the implications of failing states in Australia's region points to the need to review what has hitherto been considered "good" in terms of the standards of governance promoted through the aid program. A useful point of reference for this comes from the Pacific 2020 strategy of the previous government. This stated that "without a sustained acceleration in growth, the Pacific will be unable to meet its pressing challenges". This meant in practice that aid was used to help governments of Pacific island countries to become more attractive to foreign investment.

Some the strongest warnings about the consequences of the GFC for stability in some developing countries have come from the International Financial Institutions which have to some extent acknowledged a degree of responsibility for the situation. This can be a particularly valuable point of entry since it represents admission from some of the most influential advocates of neo-liberalism that there were flaws in their approach.⁷ Noteworthy in this respect is a publication of the World Bank – "Economic Growth in the 1990s: Learning from a decade of reform".⁸ The thrust of the analysis in this book has been very succinctly described by Dani Rodrik: "There are no confident assertions here of what works and what doesn't – and no blueprints for policymakers to adopt."⁹ Significantly, this transition from faith to doubt took place before the GFC, and subsequent events will have strengthened even more the conclusion that one size certainly does not fit all. We return later to the analysis Rodrik provides in response to the new and more humble voice of the World Bank. At this stage, however, it is important to repeat the warning that any counter to neo-liberalism must leave the baby unharmed while the bathwater disappears. Credibility requires care to demonstrate that the alternative is not to abandon market-based practices altogether.

⁷ There has of course always been a wide range of attitudes to neo-liberal thinking within the multilateral community. It is not surprising that the level of scepticism has tended to increase in proportion to the level of democracy in the decision-making processes of such bodies; in those bodies where each country gets an equal say, such as UNDP, neo-liberalism has always been more emphatically disputed. The UNDP's Human Development Index, for example, tries to provide a broader perspective on elements of vulnerability than is covered by a single-minded focus on average per capita income, an approach that invites concentration only on measures that promote economic growth.

⁸ World Bank, "Economic Growth in the 1990s: Learning from a decade of reform", Washington, 2005.

⁹ Dani Rodrik, "Goodbye Washington Consensus; Hello Washington Confusion". *Journal of Economic Literature*, Vol XLIV No. 4 December 2006.

Already, some in the international development field, such as William Easterly, are warning that the GFC should not become an excuse to abandon the role of the market.¹⁰ To suggest that the pendulum should swing back too far would in any case, be at odds with what NGOs have themselves learned from the problems of excessive state control.

E. Neo-liberalism and rights-based approaches

The second question – what to argue once at the table – will require careful preparation. A credible case based on a rights-based approach will need to concentrate specifically on those aspects of neo-liberalism that have affected the process of development and, in particular, have had an impact on the well-being of the most vulnerable. There is an immediate challenge here – part of the mantra of neo-liberalism is that there is little difference between development economics and more general economic theory, as seen in the one-size-fits-all approach taken to prescriptions provided through the Washington Consensus. A key element of an effective Type 2 rejoinder is to highlight what are the differences.

Neo-liberalism is based on the classical concept of economic interaction between people, which sees people as individuals pursuing their own self-interest in markets where prices rise and fall to ensure that supply and demand will always move back towards equilibrium. By reducing the complexity of human society to such basic units, making decisions to maximise their own utility on the basis of price signals, classical economists could develop models of economic behaviour that were both value-free and had a precision that resembled the natural sciences. Just as a physicist can predict how fast a given object will fall, economists sought to predict exactly how an individual would respond to any particular choices facing them. To do this required a set of assumptions that excluded any human frailty or other factors that might introduce an element of uncertainty to their decisions. This meant creating an image of an economic actor who operated independently, sought always to maximise their utility and had access to all relevant information. Much of the current debate in the wake of the GFC is about the validity of such models and, in particular, whether the self-correcting process (Adam Smith's "invisible hand") can be relied on to correct the existing imbalances without the intervention of government. Central to this debate is the nature of the economic actors and whether they can be expected to make "rational decisions". It is essential to the belief in self-correcting markets that it can be assumed that they will. This leaves no space to contemplate the implications of what Keynes called "animal spirits." Ignoring the scope for irrational acts, including the likelihood of self-fulfilling fears of economic downturn, has a basic divergence between the neo-liberal and Keynesian approaches to the GFC. Can we just wait for market forces to kick in, returning us to equilibrium, or accept that we are in a downward spiral requiring some outside intervention to break this spiral?

In a development context, there are some very important implications of the faith in market-driven solutions. They emerge from the underlying assumptions – especially those concerning the nature of the economic actors and the role of prices in providing the signals to these actors. Considering each of these sets of assumptions in turn allows a clearer understanding of the implications of neo-liberalism for development challenges and in particular for the poorest and most vulnerable.

Homo economicus

The mythical being, able and willing to act "rationally" and in possession of all relevant information, has commonly been labelled "homo economicus". Even if we might regard belief in such a being as comparable to belief in fairies, it has been sustained for a long time. Its supporters argued that it provided enough of an approximation of reality to justify the policy decisions that resulted from the models based on its predictability; as already noted, awkward questions about the relevance of such models could be deflected by a combination of outcomes – decades of strong economic growth – and the determination of the ascendant political paradigm to believe in its message of minimal government interference.

From a Type 2 perspective, there are some very real and substantial problems with this reliance on homo economicus. These start with the **assertion of individualism**, which discourages any serious consideration of the extent to which interaction between people affects their vulnerability, positively or negatively. This has meant that economic theories of development have tended to ignore other factors that should be taken into account but which emerge from other disciplines, notably sociology and political science. The need for cross-discipline approaches to development issues is understood by some economists, such as Amartya Sen, but broader preparedness to expand beyond the economic horizons has been inhibited by the neo-liberal focus and its assumptions about the nature of economic actors. Box 4 outlines two cases where the narrow economic perspective puts effective responses to development challenges in jeopardy by ignoring the messages from other disciplines – in these cases, by ignoring the crucial links with culture and with political empowerment. Both examples highlight issues of inequity and foreshadow aspects that are taken up in more detail in a separate section below.

¹⁰ William Easterly, "The Poor Man's Burden", Foreign Policy, January/February 2009.

Box 4

Development through cultural and political perspectives

Culture, as a factor interacting with economic dimensions of development, has been generally disregarded by mainstream economists. Amartya Sen, in a contribution to a World Bank-sponsored anthology looking at the impact of culture on development, wrote that “sociologists, anthropologists, and historians have often commented on the tendency of economists to pay inadequate attention to culture in investigating the operation of societies in general and the process of development in particular”. (“Culture and Public Action”, Ed. Vijayendra Rao and Michael Walton, World Bank, Washington, 2004). There have been some significant theories of the interaction of culture and development, such as Max Weber’s “The Protestant Ethic and the Spirit of Capitalism”, but culture remains either as something that is considered irrelevant or, probably more accurately, as something that is just “too hard” to integrate. Ignoring the impact of such interaction can and does seriously inhibit effective approaches to the problems of development. For example, it prevents proper understanding of the extent to which cultural constraints can inhibit some people from achieving their potential. This can mean that two people, given supposedly equal opportunities, can achieve significantly different outcomes in terms of their well-being. An important element of this difference in taking up opportunities is what has been called by Arjun Appadurai, (a sociologist and advisor to the World Bank) “the capacity to aspire”. Ignoring the impact of such interaction can also mean failing to recognise the role of institutions, especially those in civil society, that can complement and sustain economic outcomes of importance to vulnerable people. This highlights one limitation of the concessions provided in the Post Washington Consensus; while those provide greater acknowledgement of the role of institutions, the focus has been exclusively on formal institutions whereas some of the most effective ones in practice have been informal in nature.

The interaction of the economics of development and political science has equally been inhibited by the lack of comprehensive regard for inter-disciplinary studies. The sort of triumphalism proclaimed by Fukuyama regarding the dual supremacy of neo-liberal economics and liberal democratic politics has in fact encouraged a mindset that prevents proper attention being given to the need to differentiate between the formal mechanisms of democracy and the achievement of democratic processes that genuinely serve the interests of the most vulnerable. The interaction between development and democracy is of course a complex and hotly debated subject but there should be less controversy over the basic principle that neo-liberal economics is, by its own admission, resolutely value-free on the issue of inequity. If inequality is to be addressed, therefore, as a core aspect of a rights-based approach, it will require inter alia consideration to the way in which the most vulnerable can make government more responsive and accountable as part of a political process.

The second problematic assumption about homo economicus, **perfect and equal access to information**, is also an issue of inequity. As part of a rights-based approach, access to relevant information is a core priority. In its absence, inequity may be sustained and even intensified. For example, small scale farmers can be easily exploited when they lack accurate information on the true worth of their products. Inequity in access to information has been a key tool of power for international companies, acting as monopsonies or oligopsonies in purchasing from individual farmers. A basic condition of the neo-liberal economic model has thus not been achieved but the tendency has been to proceed as though it is in fact the case. This has meant that inadequate attention has been given to important countervailing mechanisms such as producer co-operatives or other systems for information collection and dissemination.

Third, the model assumes that human utility can be measured solely in economic terms; thus decisions by individuals that reflect **non-economic priorities** are irrational and thus, by definition, excluded from consideration. This is a basic point of divergence between Types 1 and 2. For most economists, the goal of development is maximisation of economic well-being. This has some far-reaching consequences. First, it encourages a focus on economic growth as a sufficient response to development challenges, with quantifiable measures such as per capita income seen as adequate proxies for progress. This means that issues of inequality are ignored; rises in per capita income are seen to denote reductions in poverty, even if the process of economic growth creates greater divergence about the average. This is addressed further as part of the analysis of inequality below.

Furthermore, the focus on economic indicators ignores other dimensions of vulnerability that are of more concern to Type 2. As already noted, the use of the term “vulnerability” indicates recognition that the challenges of development encompass more than overcoming income poverty. Sen’s concept of capabilities is ground-breaking in this regard, reminding us that economic development must be seen not as an end in itself but as a means for achieving greater human dignity. Likewise, UNDP has done much to shift attention away from a narrow focus on economic measures to embrace more relevant

indicators of human wellbeing, notably through the breadth of coverage in its annual Human Development Report and its Human Development Index, which uses several economic and no n-economic measures.

A uni-dimensional focus can thus over-simplify the objectives of development. This can militate against serious attention to consultative processes, whereby the key target group are closely involved in determining their own priorities. If the answer is seemingly known in advance – greater economic well-being - such consultation may be seen as unnecessary.

Typically, such consultations show that the most vulnerable people will rate greater security as high in their priorities, with security covering much more than simply a reasonable level of income. Lack of such security represents the downside risks of development and is a fundamental focus of a rights-based approach but tends to be given little direct attention in a narrow economic strategy. Even if the focus moves beyond average per capita income to address issues of equity, this does not necessarily accommodate the implications of economic downturns, disasters and other risks to wellbeing. This, from the perspective of Type 2, is a major weakness of the Post Washington Consensus. While this revision of the original version acknowledged a role for government in addressing inequity, it did so with the overall assumption that the general strategy of single-minded growth orientation would continue. Thus, even if it is accepted that “a rising tide lifts all boats” and that, at the very least, some of the benefits will trickle down, there is strong evidence that downturns affect the most vulnerable far more. Amartya Sen, among others, has documented the uneven impact of the downturns that have occurred even in the middle of the neo-liberal economic miracle – notably in the Asian economic crisis of 1997-99. An important implication of this is that, alongside issues of equity in growth, a rights-based approach to development needs to take account of the way in which risk is managed in poorer countries. This is again addressed in more detail below.

The price mechanism

The neo-liberal determination to equate utility with economic outcomes extends also to the assumptions made about the reliability of the pricing mechanism. Again, the outcome can distort development strategies, reducing their effectiveness in addressing issues of concern from a rights-based perspective. In the classical economic system, the price mechanism provides the information individuals need to make decisions. Prices thereby are a fundamental dimension of a monetised economy. Three fundamental development problems arise from this.

The first is the assumption that prices accurately reflect real economic costs and benefits. There is already a good deal of debate about this, much of it generated by the often considerable divergence between private and public costs and benefits. Decisions based on private costs can fail to take proper account of the full costs of those decisions when there are other factors – known as externalities – which individuals do not need to address directly. The most prominent current example of this concerns the impact of decisions on production and consumption that fail to take account of their full environmental impact. Realisation that price signals fail to reflect the real social cost of production and consumption decisions – leading for example to the lack of measurement of the full cost of use of fuels that contribute disproportionately to global warming – has led to a vigorous debate over how to modify the market signals to ensure that such costs are properly assessed. The implications of this for a pure market system have, not surprisingly, led to a high level of correlation between those resisting the conclusions about climate change and those who support neo-liberalism.

With the most vulnerable typically being most affected by and least able to cope with environmental problems ranging from local issues of pollution through to widespread climate change, this has a particularly serious development dimension that deserves to be addressed in its own right as part of a Type 2 rejoinder to the neo-liberal paradigm. Put simply, the most vulnerable have a right to have the impact on them of decisions that affect their environment properly addressed by being reflected more accurately in costs.

The second major problem of the pricing mechanism concerns the assumption that prices reflect the outcome of interactions between individuals with equal market power. As with the issue of unequal access to information, there is already a wealth of debate about this in the general economic arena. The underlying assumptions of fully competitive markets are frequently transgressed by monopoly or oligopoly power and this has caused even some neo-liberals to accept the need for some correction process by way of regulation of markets. In a development context, these inequalities in ability to influence prices attain a higher level of significance. For a start, processes of regulation that may help to even up the balance within individual countries are generally of little use in international economic exchanges. For example, harnessing the power of major transnational buyers would require agreement on and ability to enforce international rules, something that has so far provided unattainable. In the meantime, those espousing a rights-based approach have to content themselves with advocacy, promotion of “fair trade” alternatives and, as with the efforts to improve access to information, support for development of stronger community or government support for countervailing organisations such as producer co-operatives.

The third major issue is the extent to which prices, as a dimension of a monetised economy, can provide signals for decisions on activities that lie outside that economy. In reality, a large proportion of activities take place in the informal sector and in unpaid “home” work such as child raising and cooking. This has generally tended to undervalue the contribution made by women, who typically carry out the bulk of such non-monetised activities. This has a very real and emphatic development dimension. For example, allowing market forces to determine priorities frequently leads to skewed policy decisions such as on infrastructure priorities. When those decisions are linked to what is seen as maximising economic growth potential, with growth being measured only by monetised output, higher real priorities can be ignored.

F. Identifying priority issues

Emerging from this analysis is a core message that neo-liberalism, despite its claim to be “value-free” and thus neutral as regards its impact on the rights of vulnerable people, has in fact significantly eroded those rights. By amplifying initial advantages of those with economic power and by demanding the dismantling of systems intended to offset those advantages, it has negated a good deal of what has otherwise been achieved through development co-operation.

This bleak conclusion justifies a more vigorous debate on the future direction of Australia’s aid program – a debate in which rights-based groups such as ActionAid Australia can quite legitimately now demand an equal hearing. More specifically, the analysis of what has been done by adherence to the principles of neo-liberalism has revealed some recurring issues that are of particular priority from a rights-based perspective. These issues are inequality, vulnerability and risk. They are closely linked. From a Type 2 perspective, inequality is both a cause and a symptom of vulnerability. The purpose of making a distinction is to allow critical examination of the issue of economic inequality – where the neo-liberal case might appear strongest. Both economic inequality and other aspects of vulnerability affect the way in which risk has to be addressed, especially by those who are most disadvantaged, while the consequences of risk can create even more inequality. Together, therefore, these three issues can and do exacerbate the problems of most concern from a rights-based point of view.

An associated issue is the presumption of universal application – the belief underlying the Washington Consensus that the same medicine applies in all cases – i.e. that one size fits all. A final priority issue is the nature of the decision-making processes for development co-operation, at a national and international level. The basic question is how to prevent one loud and self-confident voice again crowding out other views that, in retrospect, prove to be wiser.

Issue 1: Inequality

Neo-liberal economic theory ignores inequality, arguing that it is concerned only with efficiency and that any attempt to interfere with market forces will reduce overall efficiency and therefore economic growth. Although these market forces will tend to maintain any initial unequal distribution of economic power, there is still scope for the poorest to benefit through what has become known as “trickle-down” of the rewards of economic efficiency. Hence, any attempts to intervene will incur a cost – less efficiency and therefore lower economic growth, meaning that there is less to trickle down.

This represents a typical Type 1 view. Type 2 would see the role of economic growth somewhat differently. Few would go to the extent of contending that economic growth has no place in a strategy to reduce poverty or even vulnerability. In fact, while some progress can be made by redistribution alone, this will generally be a short term and unsustainable measure. As noted by Duncan Green of Oxfam, “countries that have reduced poverty have invariably had to grow to do so.”¹¹ They would however argue that a single-minded focus on growth will invariably jeopardise the rights of vulnerable people and that, if equality is accepted as an objective in its own right, some trade-off is needed.

This position reflects a very different perspective on the objectives of development. For a start, poverty should be seen not only in absolute but also in relative terms. While some benefits may eventually trickle down to the most vulnerable, they will tend to be left further behind and this increasing gap further erodes their dignity. Other “dividends” of the growth imperative include discounting of cultural, social and other non-economic components of the bundle of values that real people hold dear. Liberalised trade, investment, exchange rate and even labour market policies may be seen as assuring the sort of openness that will “guarantee” more rapid growth. A rights-based perspective will however focus on the tendency for the process of liberalisation to create a rush to the bottom, especially when it takes place as part of a process of globalisation. In this context, labour rights have typically been eroded, sovereignty over taxation and even territory has been surrendered, environmental degradation has been permitted, rights of indigenous people have been trampled on to allow easy access to timber and other raw materials – and the enthusiasm by governments to introduce such investment-friendly policies have often reflected a reality that the bulk of the benefits will go to a small elite; this belies claims that such

¹¹ Duncan Green, “From Poverty to Power”, Oxfam, Oxford, 2008, p. 179.

sacrifices are necessary because in the end everyone gains. Even if such outcomes of liberalisation do in some small part trickle down, the supposition that this can compensate for loss of rights and of land divides Types 1 and 2. For the former, these losses are, like the impact of relative poverty, non-economic in nature and therefore are not given any value.

So far, this case has been based on the supposition that there has to be some trade-off between efficiency and equality. It can however also be argued that the inevitability of such a trade-off is no more than a neo-liberal myth. It is certainly true that inequality of income distribution tends to rise in times of rapid economic growth. Considerable work has already been done on this, providing a strong database of evidence that the rising tide does not lift all boats evenly.¹² Yet this does not necessarily represent the result of efficient market forces. For a start, inequality of pay can represent underutilisation of some inputs – the most extreme version being unemployment. James K Galbraith has examined the empirical data for income inequality in the USA and found that it correlates most closely with unemployment – i.e. that it is most probably a by-product of market inefficiency.¹³ An important corollary of this, based on comparison between the US and countries with much greater equality of income such as Denmark, reveals that those countries with greater equality also have lower levels of unemployment while still enjoying some of the highest overall standards of living. Thus, it seems, equality creates efficiency rather than inequality being a necessary by-product of efficiency. The neo-liberal logic does not seem to hold water in terms of empirical evidence.

There is an important gender dimension to this; inequality in the earnings of men and women is endemic across the developing (and developed) world and needs to be seen for what it is – gross discrimination or, in the terms of economists, widespread underutilisation of half the world's labour-based productive capacity – rather than as an inevitable result of the drive for efficiency.

If it is recognised that inequality need not necessarily be accepted as an outcome of the growth imperative, there are implications for the claim that efforts to reduce inequality necessarily involve interventions that reduce growth. This argument generally revolves around the notion that growth relies on securing and preserving incentives. Efforts to reduce inequality are in this perspective seen as tantamount of smothering entrepreneurship. This justification provided much of the rationale for tax cuts for the richest during the George W Bush Presidency. It remains a highly suspect theory, with much of the empirical data showing little or no correlation between lower taxes at higher income levels and higher levels of productive investment by their beneficiaries. Yet it is a theory that remained as part of the prescriptions set under the Washington Consensus, with developing countries governments being pressed to reduce taxes on the supposed entrepreneurial classes (a measure many were happy to do, but for the wrong reasons – given that such governments were generally thereby reducing taxes on themselves and their friends).

The inequality/efficiency trade-off can also be called into question by examining the underlying assumptions of the classical market, which in theory rule out inequality being a result of market inefficiencies. Yet, in reality, all economic actors are not dealt equal hands. Differences in access to information, differential treatment in terms of property rights and status before the law and the sort of differences of capacity to aspire that Appadurai¹⁴ and others have identified as a sociological constraint on many people all mean that the classical assumptions about equality of all individuals at the starting point seldom reflect reality. Market mechanisms thus do not necessarily generate inequality in pursuit of efficiency - instead, they can transmit and magnify the consequences of initial inefficiencies.

If the neo-liberal contention that inequality is an inevitable outcome of the pursuit for economic efficiency is thus found wanting, there are considerable implications for the way in which the pursuit of economic growth is factored into future policy development. This can be illustrated by looking at the way in which inequality has hitherto been addressed under the Washington Consensus. The willingness of its proponents to acknowledge a need to factor in efforts to create greater equality as part of the Post Washington Consensus reflected perhaps a recognition that inequality generates social costs that market forces do not automatically take into account – or possibly it was simply a matter of bowing to the growing demands for a moral dimension to be added to the neo-liberal prescriptions. Whatever the motive, the intent has in practice been significantly undermined to the determination to maintain the rest of the package unchanged. Pro-poor taxation policies, subsidies on basic goods, protection of industries of critical importance to the poorest and other such measures have still been condemned as “anti-growth” and have in some cases had to be discarded as a condition for receipt of support from the IFIs and bilateral donors.

¹² Contributions to this include the work of the New Economics Foundation; its publication “Growth Isn’t Working; The Unbalanced Distribution of Benefits and Costs from Economic Growth” (NEF, London 2006) compiles some of the most basic evidence about trends towards greater inequality.

¹³ James K Galbraith, “The Predator State”, Free Press, New York 2008.

¹⁴ A useful starting point for understanding the nature and consequences of the capacity to aspire is provided in Appadurai’s contribution (chapter 3) in Rao and Walton op. cit.

A final issue that should also be addressed in any discussion on the neo-liberal legacy concerns the concession that market forces may need to be tweaked in order to promote “pro-poor” growth. Has this resulted in any significant changes or is it, like the acknowledgement of the need to address inequality, part of a façade to reduce the pressure for more substantial change?

Issue 2: Vulnerability

A key rights-based objective must be to counter the neo-liberal perspective on the objectives of development. This perspective, which ignores or discounts non-economic factors such as relative poverty and rights that get in the way of the drive for maximum growth, has helped to stifle efforts to broaden the debate on development policy. As well as permitting the debate to remain dominated by the growth imperative, it has inhibited efforts to introduce several other disciplines into the analysis of the role of development co-operation. Box 4 provided some examples of the need to blend economic analysis with other factors. Such examples, developed perhaps into case studies, can help to illustrate that an aid strategy that is focused narrowly on economic indicators can achieve results that achieve little in terms of the overall well-being of those who should be the main targets for help through the Australian aid program.

The Prime Minister evidently understands and supports the need for a broader concept of the objectives of development. His paper in *The Monthly* states that “the pursuit of social justice is founded on the argument that all human beings have an intrinsic right to human dignity, equality of opportunity and the ability to lead a fulfilling life”. By quoting Amartya Sen in support of this position, he has even more strongly identified himself with a view of well-being that goes well beyond economic dimensions.

AusAID is already addressing the distinction between income poverty and broader vulnerability and it should be possible to link this to the need to view the consequences of neo-liberalism in a more multi-dimensional manner. This should therefore provide more traction to ActionAid Australia’s efforts to join the debate on the implications of the GFC. The importance of issues that are already on the table, such as food security and the civil society capacity building, is better understood when the consequences of the rise and fall of neo-liberalism are factored in. For example, increased food insecurity can be legitimately argued as a consequence of pressures to favour urban development and investment friendly infrastructure at the expense of rural development as well as those pressures applied to farmers to move into cash crops and to take on debt to fund purchases of equipment, fertiliser etc. in the name of greater productivity. The lack of countervailing voices in the debate on these priorities, even within democratic states, and the imbalance in global markets between small farmers and large buyers also serve to illustrate the importance of giving adequate attention to the effectiveness of civil society.

There is however a danger that the pre-eminence of narrow economic perspectives of development in other government departments will mean that, in practice, the approach remains “business as usual”. Even if there is some acknowledgement that the ultimate objectives must extend beyond economic dimensions of well-being, it may still be argued that these can be best addressed once economic affluence has been achieved. To put it another way, money can buy anything. This contention has been surprisingly resilient and may need to be challenged by case studies that cover its weaknesses. Three specific points could be covered in that respect. First, income cannot “buy” crucial aspects of well-being such as health and education if there is systemic discrimination against certain people based on their religion, caste or other dimensions of “otherness”. Second, lack of certainty about rule of law and basic freedoms from fear of loss of property, arbitrary arrest, torture etc. can outweigh any benefits of income – and may undermine confidence that that income will continue. Third, claims that it is enough to provide resources to allow equal opportunity should be addressed by looking at cultural issues such as inequality of aspiration – outlined above in Box 4 – to illustrate that vulnerability cannot be addressed solely in economic terms.

Issue 3: Risk

Risk management via market mechanisms is a central feature of the neo-liberal model, with consequences that have become very clear. However, even before the GFC there should have been more reflection on whether the neo-liberal approach to risk management could be applied universally. Both likelihood and consequences, the two elements of risk management, need to be assessed carefully on a case by case basis. Yet, as part of the belief in the strength of markets, they tended to be treated as though the same conclusions could be applied universally – conclusions that essentially threw caution to the wind in the belief that nothing could really go wrong.

Likelihood in the neo-liberal model is based essentially on assumptions about the self-correcting nature of markets and their tendency to move always back towards equilibrium. In such circumstances, it was easy to characterise much of the caution

inherent in government regulation - such as rules preventing banks from becoming a form of casino – as risk averse, unnecessary and anti-growth. Assumptions about rational decision-making and symmetrical perfect knowledge were seen as a reasonable proxy for the real world, a conclusion that substantially influenced the assessment of risk probability in policy making and in decisions taken in the financial sector. As the GFC has shown, caution was in fact a much wiser policy. Feedback mechanisms that owe more to Keynesian “animal spirits” have amplified what might initially have been slight problems into escalating declines in confidence.

If such problems can occur in the major world economies, it should have been recognised that the risks would be much greater in developing economies. It did not require the GFC to bring home this reality. The disastrous outcome of efforts to introduce market reforms to Russia by way of “overnight shock therapy” show that, even if a neo-liberal approach might have some benefits when applied in established market economies, it cannot be automatically assumed that it is appropriate elsewhere as a basis for transition. Even when the process is more gradual, as in many of the Asian economies, the results show that the process of creating more open economies can lead to much greater risks than neo-liberal theory would acknowledge. The Asian economic crisis of the late 1990s provided early warnings of the GFC that should have been better heeded. Paul Krugman has shown that the way in which markets judged the economic fundamentals of several Asian economies reflected more prejudice and less objective evaluation than would be expected in the perfect knowledge/rational decision-making setting assumed by neo-liberalism.¹⁵ In particular, the markets tended to regard all such economies as having the same problems, even if their fundamentals were quite different. Thus, it did not save those countries which had been quite scrupulous about their economic management from being subjected to the same self-justifying panic. Furthermore, Krugman points out that Australia encountered a very different market perception. The substantial devaluation of the Australian dollar in response to the Asian crisis was accepted by investors as an adequate response; no further calamity was anticipated and investment resumed. Other countries in the region, even though they adopted similar medicine, generated only expectations of further problems, setting up a downward spiral of withdrawal of funds and self-fulfilling expectations of illiquidity and unpalatable choices between even more devaluation and growth-strangling rises in interest rates. All this points to the need to factor in very different assessments of the likelihood of risk in developing countries – a conclusion that belies the neo-liberal notion of universal applicability of the same basic principles.

Turning to the consequences, we all live with some degree of risk in our lives. Richer societies can however call on more means to manage or avoid risks. Poorer societies have less scope to do so. The consequences for them can in some cases be, quite literally, a matter of life or death. Hence there a tendency to be more risk averse should not be decried – the consequences are too great to do otherwise. Many of the risks entailed in growth-oriented strategies, such as transferring from subsistence to cash crops, make individuals more vulnerable; new crops may be susceptible to disease and there is always the risk that markets may fail, leaving them with crops they cannot use and certainly not eat. Introduction of free trade may be justified in a richer country on the basis that the inevitable “losers” – those whose jobs go elsewhere as a consequence of greater competition – can be retrained or otherwise compensated. Without such safety nets, the consequences in many developing countries are more serious and can literally be a matter of life or death.

Issue 4: One Size Fits All

The triumphal assertion of the superiority of neo-liberal economics has generated a sort of missionary fervour with its exponents vigorously promoting market-based reforms globally. Despite setbacks such as the catastrophic impact of the reform program in Russia, faith in the principles remained largely intact. For example, William Easterly wrote in 2007 about Jeffrey Sachs that, in his book “the End of Poverty”, he was “recycling his theories of overnight shock therapy, which failed so miserably in Russia, into promises of overnight global poverty reduction.”¹⁶ Yet, Easterly himself is committed to market based solutions without explaining how these can empower people who lack the economic power to make markets work for them.¹⁷

The Post Washington Consensus can likewise be seen as an attempt to address criticisms of neo-liberalism while leaving its basic principles intact. What its supporters share with most advocates of neo-liberalism is the firm belief that these principles can be applied universally; what works in one country can be expected to work anywhere. Recognition of the danger of this approach has however come from within the heart of the neo-liberal establishment. Francis Fukuyama, who famously proclaimed the end of history in 1989 with the apparent final victory of liberal democracy and neo-liberal

¹⁵ The Krugman analysis is taken from his book, *The Return of Depression Economics*, pp. 93-94, Paul Krugman, Penguin, London 2008

¹⁶ William Easterly “The Ideology of Development”, *Foreign Policy*, July/August 2007.

¹⁷ *The White Man's Burden: Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good*. William Easterly. Penguin Press, 2007

economics, was by 2004 accepting that there remained many loose ends to be tied up.¹⁸ These included the nature of state-building. This might seem surprising from someone who had been associated with the ideology of state reduction but Fukuyama had been forced to contemplate the lessons of disastrous experiments such as the shock therapy applied in Russia and had concluded that state reduction must proceed in conjunction with a process of strengthening whatever functions the state had to continue to perform. In his book “State-Building”, Fukuyama cites the work of Lant Pritchett and Michael Woolcock, who argued that many problems are caused by seeking to establish in developing countries the same sort of Weberian bureaucratic structures that exist in most developed countries – which they describe as “Denmark”, this being a euphemism for the “common core of the structure of the workings of the public sector in countries usually called ‘developed’.”¹⁹ A key conclusion of their work is that this strategy – which they call “skipping straight to Weber” – has been a root cause of many of the problems experienced in developing countries seeking to deliver better services to their population. This particularly applies to many of the very poorest countries, including the least developed countries. For such countries, where governance can be so problematic that the most basic of first steps are required, attempts to introduce sophisticated forms of bureaucracy can be not only futile but can divert scarce resources that should be used instead to address urgent humanitarian concerns that can mean the difference between life and death for many.

Subsequent analysis has reinforced the conclusions by Pritchett and Woolcock. For example, Dani Rodrik’s review of the World Bank evaluation of the record of economic growth in the 1990s points out that there has been no link found between any particular approach to institutional design and economic growth. Citing China, he concluded that it is more important to ensure that institutional design accommodates cultural factors and existing power structures than to try to impose a set design – as had been done with much less success in Russia.²⁰ In fact, comparisons between countries that conscientiously followed the Washington Consensus programs and those that did not repeatedly throw up evidence that contradicts the claims that the Consensus provides a standard and superior approach to development. Box 5 provides some of this evidence.

Box 5
Performance under the Washington Consensus – the awkward facts

Dani Rodrik’s paper “Goodbye Washington Consensus: Hello Washington Confusion?” provides several examples where countries closely following the prescriptions of the Consensus have performed poorly by comparison with otherwise comparable countries that have taken other approaches. The comparison of China and Russia, noted in the body of the text above, is made in the context of the capacity of each to mobilise private investment. China used a system of state ownership (township and village enterprises) whereas Russia implemented a more orthodox western-style structure of purely private ownership. China achieved much greater success, which Rodrik attributes to the greater sense of security felt by investors when allying themselves with local governments with residual claims on the stream of profits. In Russia, investors evidently feared having to entrust their assets to private contracts that would have to be enforced by incompetent and corrupt courts.

Rodrik also cites the great progress made by both China and India in achieving economic growth in the 1990s despite following programs that contained only a few elements of the Washington Consensus. He acknowledges that both increased their reliance on market forces, but both otherwise adopted highly unconventional policies. “With high levels of trade protection, lack of privatization, extensive industrial policies, and lax fiscal and financial policies through the 1990s, these two economies hardly looked like exemplars of the Washington Consensus. Indeed, had they been dismal failures instead of the successes they turned out to be, they would have arguably presented stronger evidence in support of Washington Consensus policies.”

Another high profile critic of the Washington Consensus, Joseph Stiglitz, has often compared the performance of Latin America under its regimen, and the East Asian countries that followed their own unorthodox approaches. These included slow progress in liberalising capital markets and trade and adherence to government involvement in industrial development, including establishment of some very successful government enterprises. Not only did their economic performance far outstrip that of Latin America in the 1990s, when the Consensus approach was most dominant, but Latin America itself performed worse in that decade than in prior decades when it followed looser economic policies.

Despite the strong evidence for these conclusions, the Australian aid program has for some time been locked into a supposition that the best approach is to help poorer countries become more like Australia. Reservations about the suitability of Australian models may have been held by many within AusAID but as part of a whole of government approach they tended to be outgunned by experts from other departments. AusAID’s ability to influence the process of identifying suitable

¹⁸ Francis Fukuyama, *State-building: Governance and World Order in the 21st Century*. Cornell University Press, Ithica, 2004.

¹⁹ Pritchett and Woolcock, “Solutions when the solution is the problem”, *World Development*, Vol 32 No 2, 2004, p. 192.

²⁰ Rodrik, *op. cit.*

approaches to technical cooperation and capacity building, key aspects of the process of helping to strengthen governance in partner countries, has been further eroded by the growing trend for aid money to be spent through and by other government departments. It is such departments that most confidently proclaim that their experience of economic management in Australia makes them well qualified to know what is needed elsewhere. This is an assumption that should now be more aggressively challenged as part of the general review of the neo-liberal legacy.

Issue 5: Improved governance in development co-operation

While much of the focus of development co-operation has in recent years been on efforts to make governments of partner countries more responsive and accountable, the same level of scrutiny has not been applied to the quality of governance in the organisations that plan and implement development co-operation. The most obvious examples are the International Financial Institutions (IFIs), where decision-making reflects the size of the stake by each donor country. Furthermore, the heads of the IMF and World Bank are not appointed by open competition but are nominated by the EU and the US government respectively. This has meant that protests by recipient countries about the requirements set for access to IFI funding can be ignored. This has in turn tended to influence the debate within developing countries. Even in countries with democratic processes, governments that want – or need – IFI funding have frequently connived to stifle open debate on the wisdom of the conditions set for such funding. This has undermined even the processes set up by the IFIs themselves to promote greater participation by civil society in the development of the plans that are to govern the provision of their support. The best known of these processes is that supposedly undertaken in the preparation of Bank Poverty Reduction Strategy Papers (PRSPs). Oxfam carried out a comprehensive evaluation of the nature of the participatory exercises undertaken prior to finalisation of over 30 PRSPs and concluded that it would at best be possible to describe them as consultations rather than participation. There was widespread failure to involve key stakeholders and control of the policy content was firmly held by the World Bank and other donors.²¹

Processes that pay lip service to participation while ensuring that pre-determined outcomes remain largely unaffected do little to promote proper accountability of governments in partner countries. They also reinforce the lack of accountability of those within the IFIs for the quality of the outcomes. There has been a similar lack of accountability in donor governments. Their official development agencies are staffed by public servants who are accountable to their own governments rather than to the primary stakeholders – the poorest. Their incentives therefore are distorted. Furthermore, with staff in donor agencies generally moving on well before the impact of their decisions can be measured, no-one is ever likely to be called to account for specific failures.

Problems of poor accountability and skewed incentives can also apply to International NGOs, which can easily become paternalistic and push their own agendas rather than necessarily reflect the genuine interests of the most vulnerable.

The lack of direct accountability of those responsible for developing development policy made it easier for the neo-liberal paradigm to remain dominant for so long, even when there was growing evidence that it was failing. A critical issue at this point, therefore, is to create more contestable and accountable processes of policy making that will prevent future domination by single mindsets.

At the multilateral level, the sort of open-mindedness already demonstrated by the more “democratic” bodies such as UNDP may now be emerging. The World Bank, at least, now accepts that there is no single set of rules as to what works. Its paper “Economic Growth in the 1990s: Learning from a decade of reform” represents acknowledgement from within the heartland of neo-liberal orthodoxy that it is no longer acceptable to be dogmatic. This sort of agnosticism may not necessarily have yet fully spread across Nineteenth Street in Washington but, with the IMF now unable to focus obsessively on inflation-beating as the cornerstone of sound economic practice, there are signs of greater contestability in determining what represents good economics.

The bilateral donors have generally taken their lead from the IFIs. In many cases, agreement between the Bank and partner governments was a condition for bilateral funding to proceed. It might therefore be hoped that the Bank’s now-found “humbleness” might permeate through to bilateral decision-making processes. For those pressing for a rights-based approach, however, this cannot be left to chance. It is one thing for the Bank to accept that there are different ways of achieving specific development objectives; that does not necessarily mean that those objectives will be themselves be revised to reflect more priority for rights-based outcomes. The economists’ views remain largely uncontested and, if the objectives of development are to be broadened to encompass the sort of issues of vulnerability championed by Type 1, the starting point will have to be a change of mindset at the level of bilateral donors, hopefully permeating upwards to changing approaches in the organisations those donors still control.

²¹ “From Donorship to Ownership”, Oxfam International, 2004

In the context of Australia's aid program, the challenge will be to create a more contestable environment in the bodies that develop overall policy. An important target in this respect is the way in which aid is considered in whole-of-government processes. For example, with free trade orthodoxy still uncontested in DFAT and DAFF, aid policy has remained constrained by the need to fit in with policy parameters that remain focused on the ability of markets to solve problems such as food security and unequal power. Similarly, the belief that governance problems can be solved by helping partner countries to become more like Australia is likely to remain generally unchallenged.

G. Taking the opportunities – options for promoting a rights-based approach

Based on the foregoing analysis, there is a compelling case for fundamental review of the neo-liberal domination of development co-operation strategy and to promote greater understanding of and active support for a rights-based approach at the core of what replaces that strategy. What follows are some specific steps that could be undertaken to open up such a review and to promote a rights-based approach.

1. Incorporating the message in existing dialogues

Many of the conclusions about the impact of neo-liberalism fit easily into existing work plans. For example, ActionAid Australia's work on food security should highlight many of the problems created by a neo-liberal approach – e.g. the impact of pressures on farmers to move into cash crops, the temptations for governing elites to acquire land to sell or lease to large scale multinational producer organisations to supply retail needs in richer countries and/or produce bio-fuel, the unequal business relationships between small farmers and large buyers, the pressure from IFIs on governments to remove subsidies, dismantle organisations designed to manage agricultural production, the business driven shift of government investment and aid from agriculture and other aspects of rural development to urban development and creation of infrastructure designed to facilitate greater integration into global markets.

In the area of conflict, an obvious dimension to be further emphasised is the growth of market-driven opportunities for corruption and appropriation as part of market-driven resource allocation. Conflict economics, with its models of appropriation as an alternative to production, should be given a central place in analysing the causes of and solutions to actual and potential conflict situation; this will in turn allow far more focus on the perils created by allowing market forces to reign without any restraint.

2. New initiatives

A potentially useful initiative that has already been discussed by ActionAid Australia informally with AusAID is for a workshop/seminar to be held on issues of governance. Discussed in the context of AusAID's need to follow the government's signals of its unease with the doctrine established under the Howard government, such an activity could provide a valuable platform to discuss what needs to be learned from the domination of neo-liberalism and how this should influence the future shape of Australian development co-operation.

Preliminary thinking on the agenda for such an exercise suggests that it might cover several dimensions of government activity as well as the role to be played by civil society. The approach to the role of government should be developed within the parameters of a return to the appreciation of the role that government should play in regulating market forces and in ensuring that rights-based objectives are given adequate attention. Within these parameters, specific areas of governance that could be covered include service delivery, overall economic management, regulation and safety nets. In each case, it would be possible to raise cross-cutting issues of concern from a rights-based perspective – including gender, non-economic aspects of vulnerability and, most basically, what is meant by a rights-based approach. Box 6 provides a more detailed analysis of what might be covered in addressing service delivery, as an example of how rights-based approaches can be introduced logically and without creating a confrontation.

Box 6

The role of government in service delivery – towards greater understanding of a rights-based approach

Service delivery is a particularly potent area for review of neo-liberal principles. Wholesale privatisation, as practiced in many countries, led to a variety of problems such as predatory pricing by newly privatised monopoly service providers (and, at the other extreme, inability of private operators to make a reasonable economic return due to populist policies adopted by regulators), continuation of the poor delivery records of the pre-privatised providers because the supposed “magic” of the market failed to emerge due to very imperfect competition and failure to respond to the needs of the poorest. These problems both expose the myths of neo-liberalism’s magic bullets and make it easier to understand that a rights-based approach is an essential aspect of an effective policy on governance. It should thereby be possible to foster a better understanding of the value of a rights-based approach. This is probably not properly understood yet in government and is possibly seen either as a vague concept that has no practical application or as something that represents demands that may create legal complications for the Australian government. When considered in the context of service delivery, it provides a clear standard of what constitutes good delivery. When those providing services argue that they have no obligation to extend those services to the poorest or that it is not economically viable to do so, a rights-based approach provides a solid counter-argument that is firmly bedded in notions of equity that the Australian government should not be able to dismiss.

Review of service delivery also provides an opportunity to address some of the worst examples of the one-size-fits-all assumptions. For example, the mantra of privatisation ignored the available evidence that demonstrated that the operating environment is more important than ownership. Australia’s own example of provision of services such as water was often ignored; rather than privatise, the generally followed model in Australia was one of corporatisation – i.e. government-owned bodies required to operate in a competitive environment with a bottom line of adequate return on investment and, where competition could not be naturally created, development of benchmarks of performance to be monitored by independent regulators alongside decisions on pricing.

Including economic management as an agenda item might be considered risky - AusAID’s economists may be inclined still to defend the Washington consensus doctrines. It is however a vital area to address; the problems of inappropriate risk management strategies have made a major impact on vulnerability. A legitimate basis for open discussion is provided by the acknowledgement of the Bank that there is no longer a single unique set of rules to be applied in all circumstances. In fact, the Bank publication “Economic Growth in the 1990s” and/or Dani Rodrik’s analysis of its implications would provide an authoritative starting point for such a discussion.

3. Redefining whole of government approaches.

For many donors, notably the British government, whole of government approaches have generally meant that other aspects of government policy that may have an impact on development objectives must be reviewed in the light of that impact. This meant, for example, that arms exports to developing countries were subject to DFID review both to assess the human rights and conflict implications but also to assess whether the purchases could be seen as consistent with pro-poor spending priorities being discussed by DFID with partner governments.

In the case of Australia, the interaction has generally been reversed. The aid budget is subject to scrutiny to see how it can best promote other national interests. This has, as already noted, allowed the business community to exert undue influence to facilitate their interests in partner countries. This process has also led to steadily increasing proportions of the aid budget being controlled by other government departments. A key issue in this respect is technical assistance for capacity building in government which, as already noted, has led to efforts to make partner country governments “more like Australia”.

There should be more scope now to propose that, alongside the development of a new debate with the community based on better balance between Types 1 and 2, whole of government processes should also be reviewed to ensure a similar balance and to afford recognition to the importance of avoiding decisions that undermine aid objectives that reflect priorities that extend beyond economic growth.

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May 2009