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The evolution of development economics and globalization

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Abstract *The legacy of the last 50 years of development economics is not very inspiring. In the 1960s and 1970s, instead of looking at the real causes and viable solutions to poverty and underdevelopment, development economics was preoccupied with the politically-charged debate over the superiority of either state-controlled or market systems. In the 1980s and 1990s, economists expected that globalization would come to be a panacea for all developing countries. They advocated the abandonment of traditional industries and occupations and their replacement by modern sectors modelled after or imported from the developed countries. Such policies have generally failed with few exceptions–those being countries which chose to implement their own specific policies of development. These countries skillfully combined government interventionism with market system incentives. Despite its past problems, development economics has recently evolved to better reflect the realities of developing countries. For the first time, development economics is on the verge of becoming a real social science in which analysis of traditional institutions, community life, and religious and ethnic factors is not only important but decisive in developing new social and economic growth objectives and economic policies.*

Introduction

Kindleberger wrote that a theory of economic development could not be compared to a theory of economic growth, as the latter is simple, elegant and easy to explain. In contrast, theories of economic development are general, vague and chaotic – much like the mass poverty with which they attempt to come to terms (Herrick and Kindleberger, 1988, p. 48).

The legacy of the last 50 years of development economics is not very inspiring. Twentieth-century development theories focused on the choice between the market and the state as well as individualism versus collectivism, but did not take into account the socio-cultural complexities of the world they were trying to model. Today's conflict of Western individualistic capitalism and liberal democracy with radical Islamic unifiers may symbolize a gap between economists wishful thinking that goals and methods to achieve it are universally accepted and understood (Kiriyenko, 2002). Undoubtedly, modern development economics must do better in understanding the different objectives and paths of growth. Additionally, it needs to tune in its paradigms and objectives to a world that is struggling to reconcile globalization with regionalism, as well as uniformization with national identity. For the first time

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since its inception, development economics is on the verge of becoming a valid social science, in which the analysis of traditional institutions, community life, religious and ethnic factors is not only important, but also decisive in developing new social and economic growth objectives and economic models.

The birth of "development economics" as a discipline

After the Second World War, there was widespread interest among economists in finding solutions to the poverty and underdevelopment left behind by the disintegrating colonial system. Despite controversial legacy of Stalin's economic model in Russia, faith in the benefits of planning and nationalization became common even among "Western" economists. Works on economic planning by two Polish economists, Michal Kalecki and Oskar Lange, and one Russian, Vladimir Kantorovitch, served as standard readings for many students of economic development. In the 1950s and 1960s, development economics was a breeding ground for alternative theories "to wasteful, exploitative capitalism". While it was categorized as a sub-discipline of economic science, development theory was reminiscent of "political economy" with a very distinct shift to the left. Gradually, the discipline produced more literature concerning economic development in areas outside the Western and Soviet camps. Sauvy is generally credited with coining the term "Third World", which he first used in 1952 on analogy with the so-called "third state" of the pre-Revolutionary France – that is, social groups other than clergy and aristocracy. The term fit well for developing countries that either did not want to associate with either camp or preferred to play East-West confrontation to their advantage (Roy, 1999, p. 3).

Generally, theories of development in this period originate in two theoretical and philosophical schools of eighteenth- and nineteenth-century European thought. Though both concern the wealth of nations, they differ fundamentally on how growth should be achieved and how its benefits should be distributed within a society. For classicists and neo-liberals, the interests of nations and social classes are compatible and harmonious, while for Marxists, dependists and radicals; a definite conflict of classes and interests exists, requiring either radical social engineering or revolutionary change (Black, 1999).

Thus the literature on economic development is generally categorized by different degrees of attachment to the "market" and mechanisms for creating "just prices", different approaches to the international economy, and, above all, different evaluations of the role of state in the economic life (Herrick and Kindleberger, 1988, pp. 48-61). The main groups of theories were:

- Neo-classical theories of economic development (including the work of such economists as: Peter Bauer, Theodore Schultz, James Meade, Gerald Meier, and Henry Bruton).
- Theories of structural imbalance (Hollis Chenery, Jeffrey Nugent, and others).

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- Radical and Marxist theories of economic development (Paul Baran, Gunder Frank, Vladimir Lenin, Samir Amin, Gabriel Palma, and others).

Until the 1980s, a score of developing nations experimented with non-market theories and concepts, but with rather limited success. Brazil, India experienced a few years of non-sustainable growth in the 1960s. Unfortunately, none of these countries could match the successes of those that chose the mixed economy and the market system in 1990s.

The crisis of "development economics" in the 1980s

By the 1980s, against many prominent economists' expectations, development had not materialized in the Third World – with the exception of the Gulf nations. Even in countries such as Qatar, Kuwait, and Saudi Arabia, where significant growth was observed, employment gains were generally unsatisfactory. Everywhere else in the developing world inequality and poverty grew. In addition, inflow of capital and Western consumption standards challenged traditional sectors and the existing power structures. As a result, tensions between modernizers and Islamic traditionalists heightened. According to various estimates only 10-25 percent of windfall revenue following the oil crises was used for development purposes. This was one of the problems that "development economics" was not prepared to solve (Bruton, 1985). Hirschman (1981) wrote that the hopes for Third World growth cherished by economists in the 1950s and 1960s had been lost. Streeten (1984, p. 121) was equally pessimistic when he wrote: "at the end of the day we must admit that we do not know what causes underdevelopment, and, what is worse, we lack a clear plan and timetable for further scientific research".

The disappointments of the mid-1980s spurred a debate between adherents of neo-classical model, such as Ian Little, Anne Krueger, Deepak Lall and others, known as "the World Bank group", and the Brandt Commission group, which included structuralists, dependists, neo-institutionalists and others. According to the World Bank group, stagnation in the Third World had to be blamed on a bad price system, misallocated investments, and wrong choices in production technology (Stewart, 1987). While the Brandt Commission group did not fully reject this neo-classical critique, they attributed the stagnation more to failure of the state's industrial and price intervention policies than to the incompleteness of the neo-liberal economic model. According to the Brandt Commission group, there was no proof that a free price system could lead to better welfare than a system based on price intervention. As Streeten (1984, p. 143) wrote, "a good price system does not mean the end of the economic development process, although it is obvious that a bad price system can totally hinder economic development". Finally, the Brandt Commission group was convinced that it was impossible to trigger development processes without state intervention. The Asian pro-export growth strategy of the late 1980s lent strong support to their claim.

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A common characteristic of development theories before the 1990s was a conviction about the advantages of industrial policy and state trade strategy. Economists and politicians praised the effects of subsidies and state-business cooperation in establishing export industries, price intervention, and protectionism. In a way, this opinion was consistent with the prevailing economic notion of the post-war era – that the nation-state was to be strong and active in promoting economic growth. The concepts of the indispensability of a powerful government and interventionism originated in the legacy of post-colonialism and the critique of the developed countries. Political and intellectual elites presented the opinion that gaining independence in early 1960s did not mean gaining economic independence, after all. The "First World" capitalist countries would not open markets to agricultural imports or provide enough capital to modernize the "Third World" struggling economies. Thus, Latin American economists, worried about the declining terms of trade, advised minimal reliance on world markets, the creation of government monopolies in banking, transport and other key industries, and import substitution. South East Asian countries, on the other hand, saw a chance to develop the export sector and open their economies to foreign investments. The theory of development focused on describing the benefits of state control over key sectors of national economy. A pro-active nation-state became the focus in India, Mexico, Chile, Argentina, Brazil, Indonesia, Malaysia, and South Korea.

A big shift in development economics started in the mid-1980s, and the Latin American debt crisis had no small role in the re-evaluation of the old developmental paradigms. After the failures of economic policies in Mexico, Brazil, and Bolivia, it was obvious that massive borrowing alone would not solve their problems; a new approach was required. In addition, development economists became more skeptical, and even cynical, in their evaluation of the motivations of politicians and the competence of bureaucrats. The politicians were criticized for being mostly concerned with their own political survival, and the governments for mainly representing the interests of small but influential pressure groups (Balasubramanyam and Lall, 1991, p. 12). Governments became a problem, rather than a solution. At the same time, more and more development economists argued for free, deregulated markets and limited interventionism (Lall, 1983, p. 109).

What caused the growing dissatisfaction with the role of once omnipotent governments in the development process? The answers are many:

- In many poor countries, the governments failed to address even the most fundamental social-economic problems, such as education, illiteracy, health, water supply, and transportation. These governments came to be mistrusted as their administrations turned out to be parasitic and corrupted – that is, run by "cleptocracies".
- Foreign aid mainly benefited the ruling élite, not the poor and needy.

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- The fragile political/ethnic consensus in many African countries collapsed as the governments revealed their inability to cope with national emergencies such as drought, disease control, and ethnic strife.
- National and religious identities were revived in the poorest Asian nations in the face of governmental failure to cope with poverty, drug trade, health catastrophes, and famines.

The rise and decline of neo-liberals

The shortcomings of traditional development models were particularly obvious during Latin America's "lost decade" of the 1980s. Mounting debt, inflation, and negative growth in all but one of the region's economies sounded the final death knell for "import substitution" and the "independencia theory". On the other side of the Pacific, export-driven growth, inflow of technological foreign direct investments, and fast industrialization in Malaysia, Indonesia, and Singapore armed the liberal lobby of Washington's think-tanks and the World Bank group with new convincing arguments, and a list of liberal reform guidelines known as the "Washington consensus" was born. The "consensus" carried the unequivocal message that a free market and open economy supported development far better than any form of protectionism and state interventionism. However, not all development economists agreed, and an ideological rift ensued. While the majority seemed to accept a neo-classical model, a sizable group of "leftist" structuralists disagreed.

During most of 1990s the Washington consensus dominated the theory and practice of economic development. This entailed tough fiscal and monetary policy, deregulation, foreign trade and capital flow liberalization, elimination of government subsidies, moderate taxation, liberalization of interest rates, maintenance of low inflation, and so forth. The proponents of these comprehensive liberal reforms strongly believed that the "miracle of the market" would eventually solve the problems endemic to underdevelopment. A special role in this process was attributed to global corporations and the inflow of foreign direct investments to low-cost developing economies.

In the 1990s, the theory and practice of development economics turned to the analysis of export promotion, trade-related industrial policies and models of optimal state-business relations (Piasecki, 1998, pp. 39-51). According to the representatives of a new school of thought, economic development depended on the following conditions:

- the opening of national economies to the outside world;
- synergy with the world market in order to obtain optimal allocation of resources;
- international competition; and
- the social acceptance of the objectives and methods for the economic growth.

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The policy implications for developing countries in the area of foreign trade were truly fundamental. Governments shifted from either neutral or negative assessment of interaction with the world markets (for example, in the dependency school of the 1970s) to acceptance of free trade and unrestricted flow of capital as the most important means of overcoming structural underdevelopment.

The classic comparative advantage trade theory by David Ricardo (Ricardo, 1911) was rejuvenated as a new development paradigm. While classical trade theory advocated specialization and gainful trade between the developed and developing countries, foreign trade became, in the new paradigm, both the means to assure optimal use of land and labor resources and the source of technologically advanced industrialization. The post-Ricardian trade theories predicted that specialization in labor- and capital-intensive goods would bridge enormous wage gaps between the poor and rich countries, sparing the latter from massive labor immigration. The theories developed by Hecksher, Ohlin, Stopler, and Samuelson offered, among other things, theoretical explanation of welfare effects for displaced workers in developed countries, as well as the benefits of factor price-equalization on a global scale. At the same time, the international trade literature made strong arguments denouncing the effects of state protectionism (Gerber, 2002).

The limits of the "Washington consensus"

The second half of the 1990s, beset with financial and currency crises, proved that the openness strategy advocated by the Washington consensus had its limitations. The South East Asian currency crises of 1997-1998 showed that the combination of fixed exchange rate regimes and a large inflow of foreign investment could be very risky for macroeconomic stability. Indonesia, Malaysia, Singapore, and Thailand seemed to have gone through similar cycles of economic overheating. It started with demand-driven inflation, real currency overvaluation, current account deficit, and outflow of currency reserves, and finally ended with nominal currency devaluations and a recession. These crises might have been averted by timely currency refloating and tighter fiscal and monetary policies. Many of the liberal reformers chose to blame external causes, such as currency speculation, globalization, the IMF, and the World Bank, for their own mistakes.

The Washington consensus was critiqued in the post-communist countries of East Central Europe as well. After the market reforms and four to five years of rapid growth in early 1990s, Poland, the Czech Republic, Hungary, and Slovakia experienced an unexpectedly hard landing in the second half of the decade. Rising unemployment, currency devaluation in the Czech Republic, and growing budgetary and current account deficits encouraged criticism of "foreign capital" in the banking, financial services, retail and power generation sectors. Notably, however, none of the ruling post-communist coalitions had ever advocated deconstruction of their market economies, and instead they all

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continued with privatization and vigorous pursuit of membership in the European Union.

Several authors who evaluated the relevance of the Washington consensus to the realities of economic development in Asia, Central Europe, and Latin America in the 1990s were convinced that it had some significant omissions. One of the fundamental lessons learned by the countries pursuing large-scale privatizations in 1990s was the issue of competition. In countries where liberal reforms were limited to the exchange of state monopolies for private monopolies, market reforms failed. This was because many small- and medium-sized businesses either disappeared or were not given a chance to grow during the large scale privatizations. Decontrolled prices quickly rose and popular support for the reformers waned. Before any positive effects of reforms were felt, the reformers had to step down. In Argentina, Chile, and Bolivia, new private monopolies in trade, transportation, and banking first eliminated competition, then raised prices, then reduced their tax payments to the government. Stiglitz (1998) observed that the neo-classical concentration on creating "just prices" is not sufficient to support a functionally sound market economy. The insufficient emphasis on competition in the Washington consensus may be one of its main weaknesses.

Another significant criticism of the Washington consensus concerned its lack of attention to effective legal-institutional infrastructures. The problems encountered in Poland, Russia, and the Czech Republic proved that, in addition to political will, large scale privatization requires a clear and transparent body of laws: land deeds registry, stock registry, tenant-owner laws, consistent contract laws, a valuation system of loan collaterals, and so forth. These laws and institutions make the true difference between successes and failures of market economies and influence broad popular support for liberal reform-minded governments.

For example, Hernando de Soto argued that the root cause of Latin American underdevelopment is the absence of land deeds and legal titles to property. Since the squatters of poor Latin American *favelas* could not collateralize their houses and businesses, they could not take advantage of the banking system, which requires proof of ownership. Consequently, the poorest of the poor were unable to obtain bank loans to expand their businesses and raise their income no matter how hard-working they might be. Billions of *reals'* worth of potential value was not created in Brazil and millions of houses were not mortgaged or built because the most fundamental bank service was not available to the poor. Moreover, poverty became endemic because family members inherited undocumented property (de Soto, 1991).

Less-than-perfect information represents even a bigger problem in applying a market system in developing countries than in developed ones. Since access to information in poor countries is limited by cost considerations and communication technology, price transparency and rationality cannot be assumed as given. Not surprisingly, some neo-liberal economists outside these

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countries could not agree on many aspects of micro- and macro-management in developing countries, such as:

- the use of capital controls;
- the need to target the current account;
- anti-inflationary measures in the fast developing market;
- the use of income policies and indexation;
- the level of the tax burden and the degree to which governments should be involved in the redistribution of income;
- the use of industrial policies;
- the priority of population control; and
- the priority of environmental conservation.

Globalization and economic development

By the mid-1990s, the advances in international trade and investment looked like undisputable proof of the validity of neo-liberal model. It seemed no wonder that the concepts of "openness" and development through "globalization" and "regional integration" became new development paradigms. Economists studied the opportunities offered by "outsourcing", "special economic zones", free trade agreements, and regional integration. NAFTA was intended to become a model solution for the Americas. Emblematic of that period was the ministerial session of UNCTAD in Midrand, South Africa in 1996. Globalization was equated with "democratization" of world economic growth, a historic opportunity, which converged the interests of the poor and the rich nations. This new optimism contrasted with the pessimism of the 1980s, when only one-eighth of the developing countries could report some economic and social growth.

The shift in development economists' opinion on "globalization" came around the time of the currency crises in South East Asia in 1997 and 1998. These crises particularly influenced opinion because countries that were rather well integrated into the world economy, such as Indonesia, Malaysia, Singapore, and Thailand, suffered most. Devaluations, interest rate hikes, and stock price crashes turned the average 6-7 percent annual GDP growth of the early 1990s into a deep social and economic crisis. In Indonesia, for example, unemployment and poverty grew to levels not experienced in two decades, health conditions worsened, and the natural environment degraded.

According to the Secretary General of UNCTAD, the two causes of the South East Asian crises were: "excessive openness to the world economy" and "inability to manage this openness" on the part of the South East Asian governments. Rucipero recounts that, after the liberalization the 1990s, the trade deficit of those countries was three percentage points of GNP higher than it was in the 1970s, while their average economic development growth rate was lower by two percentage points. In his opinion, globalization failed to assure

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sustainable economic growth in the developing countries (Rucipero, UNCTAD, 1999). Others simply blamed globalization for deepening vertical and horizontal income inequalities. Special criticism was reserved for those neo-classical economists who talked about wealth "trickle down" effects.

From the beginning, the term "globalization" meant quite different things to different people (Streeten, 2001). The 1998 winner of the Nobel Prize in Economics, Amartya Sen, defined it as the "intensification of the process of interaction involving trade, migration and dissemination of knowledge that has shaped the progress of the world over millennia" (Gerber, 2002, p.33). Globalization, understood as international economic integration, did not give rise to much emotional reaction among development anti-internationalists. However, the "collateral dependency" that this process has brought has definitely became an issue for "globalization". First, the number of nations dependent on trade, foreign capital, and the world financial markets increased greatly. Second, multinational corporations increased their bargaining power *vis-à-vis* nation-states. Third, global and intercultural communication resulted in challenges to tribal, theocratic, and non-democratic systems to provide more individual and economic freedoms. Fourth, the World Trade Organization emerged as a powerful multilateral organization capable of effectively influencing individual governments to follow international trade rules, copyrights, policies on subsidies, taxes, and tariffs. Nation-states could not break the rules without facing economic consequences. Fifth, widespread use of computers, faxes and mobile phones, introduction of the internet and e-commerce, and quicker and cheaper means of transportation in some cases offered opportunities to developing countries, but in many cases deepened the gap between global firms and traditional industries (UNCTAD, 1999, p. 30).

The opinion on globalization among the development lobby shifted from euphoria to ardent criticism. Violent anti-globalist protests during the December 1999 Seattle World Trade Organization meeting and again in April 2000 in Washington provided evidence of a growing and vocal international lobby demanding the reform of the International Monetary Fund and the World Bank.

The facts were hard to dispute. The world economic system, which 80 percent of countries regarded as failing to give them a fair chance to improve living standards, was no longer viable. It is estimated that only 20-25 percent of the world population directly benefits from globalization, and for the rest the benefits are marginal or nonexistent. Only 1.8 billion people out of six billion can afford the goods and services available on the world market. Only half of those lucky ones are within the reach of the banking system (de Rivero, 2001, p. 82).

The real issue is how to ensure jobs and a better quality of life for the almost three billion people today earning less than two dollars per day and for the two to three billion people to be added to the world's population over the next 30 to 50 years. Reaching this goal, while taking better care of our environmental and social assets, requires a different global development strategy than the one

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followed in the past (World Development Report, 2003). Is globalization, as we know it, offering a chance to achieve these developmental goals?

Critique of globalization theories

The relations between globalization and development are neither straightforward nor palpable. A good illustration of its complex make-up is the relation of a nation-state and a global corporation:

- In theory, developing countries can use general or specific industrial and trade policies to be more or less "welcoming" to foreign direct investments, capital, foreign tourist services, and so forth. They can directly and indirectly shape their participation in the global economic system. In practice, however, with few notable exceptions, developing countries were passive in structuring their own participation in international trade and finance. In practice, the end decision and the net economic effect of their "openness" to globalization was beyond their control. During the negotiation of costs and benefits between the nation-state and a global corporation, the first was often in a weaker bargaining position.
- In theory, the nation-state and a global corporation should cooperate in addressing social and environmental challenges that directly affect their foreign direct investments. In some cases, the divergent goals of multinationals and local governments were successfully brought together to solve the educational, housing, environmental and health problems of a local community. In practice, however, the recent experience in Latin America has been that many such open-handed multinationals moved their operations to, for example, China or South East Asia because of cost and market considerations.
- In theory, globalization opened up new opportunities for developing countries to create jobs and expand exports. In practice, many developing countries competing for foreign investors offered longer tax holidays, costly subsidies, and various incentives for multinationals. The competition among developing nations reduced positive net effects of globalization or, at best, delayed them.

According to critics such as de Rivero, the key problem for the global economy is, on the one hand, the deepening of the gap between the more dynamic and complex world of international finance and investment, and, on the other hand, the absence of a relevant institutional system capable of management and effective control over those processes.

What was the role of international organizations in solving developmental problems? Most of the critics are quite unforgiving. The development experts, they claim, have wrongly assumed that it was enough to put a correct program into practice and poor countries would, not now but "eventually", catch up with industrialized countries. Many of the worlds' most influential economists

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reinforced this rather simplistic approach. As a result, many poor countries espoused unrealistic expectations and demands only to end up deeply disillusioned. This type of wishful thinking is evident in numerous UN resolutions on "the right to development", interpreted as the right of poor countries to obtain the standards and models of consumption of the industrialized countries. These resolutions, which were also important for political propaganda, were not just divorced from reality, but unfeasible. If all developing countries reached today's level of consumption in the industrialized world, global environmental catastrophe would be imminent (de Rivero, 2001, pp. 110-14). For example, since 1982, the UN tried to implement 162 adaptation programs in Africa and 126 programs in other developing countries. After twenty years of subsequent developmental experiments, Africa entered the new millennium as the continent with the most highly dysfunctional and marginal national economies lingering outside the global economy (UNCTAD, 1993, pp. 163-7).

Severine Rugumamu concludes that in the twenty-first century the position of the African continent in the world economic system will probably continue to worsen in the short- and middle-range perspectives. Its economic growth will be slow and sometimes even negative; terms of trade and debt crisis will worsen; areas of poverty will increase. Simultaneously, the population will grow and deadly diseases will spread (Rugumamu, 2001, p. 77).

The "misery" of a traditional development economics and the opportunities for a modern development economics

What caused the "misery" of traditional development economics? We think that the main reasons are as follows.

First, "development economics" limited the scope of its research mainly or exclusively to economic factors. It is accepted nowadays that development economics, in particular, should cover the whole range of both economic and non-economic developmental factors.

Second, many economists applied economic concepts that were totally inadequate to the realities of developing countries, such as industrial unemployment, skill levels measured by years of formal education, or naively adopted biased or inaccurate statistical data in their research.

Third, "development economics" did not do enough to grasp country-specific developmental factors. Instead, it excelled in advocating sweeping replacements of a traditional sectors with the modern, more efficient ones. The process of sector replacement was supported by propagating foreign cultural models in media, educating the elite abroad and yielding to demonstration effects. Development strategies recommended costly, modern solutions, abandoning long-established less costly production methods and market structures. Thus, lack of domestic and foreign capital was considered to be the main obstacle to growth and the "capital shortage" hypothesis dominated development economics for many years.

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Fourth, in recent decades, development economics held a simplistic view of the fundamentals that govern the theory and practice of development. This view holds that growth requires two things: foreign technology and good institutions. Failure to grow can be attributed to either (or both) of two pathologies: the "protection" pathology, in which governments stymied progress by reducing access to foreign investment and technology, and the "corruption" pathology, where political leaders failed to respect property rights and the rule of law (Rodrik, 2002).

Traditional development economics failed to resolve a number of important issues for developing countries. For example, what effects does specialization have on economic growth in the long run? The resolution of this issue is vital in discussions of globalization effects on developing countries. Advocates of deep specialization argue that it does not matter whether a given country specializes in raw materials, agriculture, or electronic production. The developmental impact would be equally positive in all cases. However, the empirical evidence has been that the spillover effects may vary significantly depending on the type of specialization. Generally, the levels of technology used make all the difference. What is more, the world demands different types of exports; for example, raw material, agricultural and electronic production grow at different rates. Thus, overly narrow specialization in some developing nations (for example, mono-cultural ones) can lead to high levels of dependence on weather cycles or demand in major import markets. The issue of specialization risks requires particularly careful analysis in the context of recommending an export-driven growth model for developing countries.

Modern development economics needs to address the issue of rational decision-making process and human psychology. Explaining underdevelopment as the absence of rational market behavior, as some development theories did, was simply incorrect. What seemed irrational to some economists could have been explained by lack of information, high costs of entry into a given market (transaction costs), problems with obtaining loans, insurance costs, new technologies acquisition, lack of marketing skills, lack of access to markets, and so on. A comprehensive analysis of human behavior, underlying religious beliefs, ethical standards, and ethnic traditions in developing countries may prove to be very significant for putting the theory of development to a new, higher level than it is at today.

Another key point for development economics is that all development models are, by necessity, country-specific and nation-specific. Discovering what works and what does not in any one country requires experimentation. After all, what may succeed in one setting may perform poorly or fail completely in others. It seems that this simple truth took decades for development economists to acknowledge. Such specificity helps explain why successful countries – China, India, South Korea and Taiwan, among others – usually combined unorthodox elements with orthodox policies. It also accounts for why important institutional differences persist among the advanced countries of North America, Western Europe, and Japan in areas such as the

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role of the public sector, the legal system, corporate governance, financial markets, labor markets, and social insurance.

Conclusions

Development economics is trying to take a broader and longer-term view of development processes – happily, no one is proposing quick fixes. Remarkably, "globalization", which in the past was regarded as a universal panacea for the poor nations, is not even once mentioned in the World Bank's World Development Report (2003). Contemporary development studies more often include interaction between economic, social and environmental problems to identify that could be handled locally, internationally or globally. This is because the solutions to specific problems are in inclusive societies and institutions that promote growth by encouraging creativity, initiative, and learning. These initiatives may come from the public sector, the private sector, or the civil society. The objective of fighting poverty is not to wait for the creation of a brand new sector, but to modify the traditional sector so that it becomes naturally viable, dynamic, and flexible, suited to the needs and ambitions of the traditional environment.

Quite often the past failures of "development economics" were attributed to the blind imposition of "Western" modernization schemes on the societies, whose traditions, values, habits, social strata, and concepts of economic activity were fundamentally different. This type of mismatched modernization scheme proved to be costly, unsustainable, or both. Unsuitable economic models rekindled ethnic and political conflicts and contributed to regional destabilization. "Western" institutions replicated in developing countries were ineffective and the resources used to create them often wasted. Theories on import substitution, nationalization, collective farming, subsistence production, and central planning were revealed to be divorced from the realities of developing countries – culturally alien and economically unviable. Many of these theories reigned too long only because of bureaucratic and corruptive manipulation. In the final analysis, the development theories that either totally abandoned neo-liberal paradigms or tried to transplant them fully to developing countries contributed little or nothing to the development of poor countries.

Is then the neo-classic "development model" proposed by the developed countries moribund? We believe that the neo-classical hopes for the poor countries have not been fulfilled yet. The limited success of the Washington consensus is enlightens us more about its implementation processes than its relevance for developing countries (Fine *et al.*, 2001). How, then, should the Washington consensus be modified and restated? We propose following amendments:

- A more sustainable development path is possible only in a socially inclusive society. It enables the society to transform and solve collective action problems. The neoclassical dimension of this process is the

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formulation of policies to stimulate local initiatives and local responsibility for job creation, environment, and education.

- The civic society and the local institutions should be very sensitive to removing impediments to the creation of markets and supporting legal and financial institutions.
- The approach should focus on the issues and processes that underpin human life and the nation's wellbeing, improve the quality of the environment, strengthen the social fabric, and improve educational standards. In particular, the investments in human capital have fundamental importance to successful development in the long term.
- The development will be sustainable only if there is a flow information and mechanisms assuring absorption of such information. The market system requires informed participants.
- Wherever there are market imperfections, state intervention should be market- and competition-friendly.

Finally, we believe that the neo-liberal economic model of global market openness, if not distorted to serve selected interest groups, is basically culturally and politically neutral: it is not Western or Eastern, American or European. Even though globalization is often presented as the source of inequality, alienation and interference in the traditional social fabric, it is, *de facto*, the most inclusive system there is. Any type of internationalization of production, distribution, and consumption will affect the way in which people live or strive today in the poor countries of the world. The debate about the globalization pros and cons and different growth models will continue among development economists, but a true verification of any policy choices they offer will be whether or not the lives of three billion people improve in the future.

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