Silent Consensus against the Washington Consensus

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This paper discusses the theoretical and empirical considerations related to the economic reforms. It is argued that there is no alternative to each country developing its own optimal policies, whereas in the designing of economic reforms in India a country-specific perspective has been totally missing.

I
Introduction

RECENTLY I have argued that one must design economic reforms taking the specific objectives and constraints of the country in question into account, and that it can be done best by following the operations research approach introduced to economists by Mahalanobis nearly half a century ago.[1] This approach is much different from the more popular approach known as the Washington consensus. Those who are in agreement with me and also those who are critical of my views seem to agree on one thing – that I had not given a convincing account of the theoretical and empirical support either in favour of the Washington consensus or against it. It is the main aim of this paper to fill that void. In a recent talk Justice O Chinnappa Reddy made a reference to the prevailing world economic scenario and expressed concern regarding the loud silence over the adverse impact on the poor and the poor nations of the course of world economic trends.[2] His talk, and an earlier talk by D M Nanjundappa on the lack of equity considerations in designing and measuring the impact of economic reforms, prompted me to amplify the whispering sounds silenced under louder ones.[3]

There seems to be a great deal of confusion on theoretical and empirical moorings of the widely talked about policies of economic reforms. It is the main endeavour of this paper to discuss the theoretical and empirical considerations related to these economic reforms, some in support of them and some against them. It is then argued that there is no alternative to each country developing its own optimal policies. If anyone or any agency comes forward and recommends certain policies as good or best policies for all countries it is incumbent on them to demonstrate the same using the country-specific objectives and constraints. There seems to be no country-specific perspective in our country in recent years in designing the economic reforms. There is also no proper direction to planning in recent years. It is unfortunate that it has also become fashionable these days to follow the rule of giving primacy to the market forces and to withdraw from the act of planning altogether.

Economic theories and their relevance for development planning are put in a proper perspective in this paper to highlight the importance of the scientific operations research approach or strategic approach to planning. This paper deals more with the general issues and methodology, or what may be called the technology of economic policy making. It is about the strategic approach to designing the optimal economic policies.

II
Methodology or Technology of Economic Policy

Senator Patrick Moynihan, the former US Ambassador to India, raised a provocative question about two decades ago at a conference on Social Science Policy Research organised by the Abt Associates Inc at Cambridge, Massachusetts. The question was: "The engineers put a man on the Moon, what did the social scientists do?" I consider this question to be quite relevant because what we seem to be doing is not to note the analogy between the technology and economic policy on the one hand, and not to recognise that economics is a science on the other. If economics is a science then economic policy is the technology that uses that science. In technology, science forms the basis for designing an instrument or a technique. But once the technology is in place what matters is how the technology works and how to improve it. Some times one can learn about the technology by observing how it works without much recourse to theory. In such instances what really matters is: how good one's understanding is on how the system works? It is this kind of approach to technology management that enabled the space scientists to develop the technology for putting the man on the Moon before they could derive analytically the solutions of the dynamic equations of motion of the rocket.[4]

It is also useful to recall the statement made by P C Mahalanobis that statistics, operations research, and econometrics constitute a technology useful for economic planning. It may also be noted that this technology was employed quite successfully by India in the 1950s and the 1960s, and by South Korea subsequently.

There are two specific features of an operations research approach that are quite indicative of the realistic approaches to optimal policies. One is the gradient search. This involves the choice of the right direction for the move towards the goal, and the choice of the length of the step to be taken in that direction. The direction in which one should proceed and the length of the step one should take in that direction depend on the goal that is set and also on how far one is from such a goal. To the extent that these goals and the initial conditions might differ from country to country, and from time to time for the same country, the directions and the steps one should take in those directions, ought to vary from country to country and from time to time. The second aspect is the decomposition principle under which planning should be limited to co-ordination when the information needed for planning is widely dispersed and localised, and when there are externalities and market failures. The failure of planning in the east European countries is mostly because it ignored this aspect- that information needed for planning, both regarding the goals and constraints, is available only in a decentralised fashion. But market failures and externalities do require co-ordination. Hence to assume that there is a limited role for planning is to ignore the possibilities of market failures and externalities.

There are two types of knowledge which one should utilise in the general problem-solving exercise, such as an operations research approach to planning for economic development. These are: (i) generalised and generalisable (basic) knowledge which is applicable to a variety of situations having some common features, and (ii) specific knowledge that is specific to the given specific situation. If one uses the general knowledge alone and ignores the knowledge that is specific to a given situation the perceived results can, and do, deviate from the real situation. Similarly, if one ignores the general knowledge that had been proven to hold good in many general situations such an omission can make one's perceptions imprecise. Many controversies in the debate on economic reforms can be resolved by noting that such controversies emphasise either the generalised knowledge that may or may not be applicable to a given situation, or that they emphasise the specific knowledge which exhibits some deviation from the general knowledge.

III
Washington Consensus

In the emerging global economic environment the most important question that developing countries such as India ask is "How should the country adapt its economic system and its economic policies to the rapidly changing and emerging economic environment?" While the economic science, both the economic theory and the empirical evidence, seems to offer no clear-cut answers to this question a particular vocal segment of the economics profession seems to hold the view that a broad set of policies, enshrined in the so-called " Washington Consensus", are the best policies for all the developing countries [Williamson 1990]. It is necessary therefore to state briefly the major ingredients of the Washington consensus. These are: (i) a balanced budget, (ii) relative price correction, including removal of subsidies and moving to a market determined exchange rate, (iii) liberalisation of trade and removal of restrictions on capital mobility between countries, (iv) privatisation, and (v) domestic market deregulation. While on the one hand it is claimed that these policies stem from classical economic theory, on the other the classical economic theory is being propped up as the mainstream theory, ignoring the other major contributions which do not necessarily support the policies enshrined in the Washington consensus. The story narrated in the appendix gives a good perspective of the Washington consensus.[5]

IV
Consensus against Washington Consensus

The syndrome exhibited by the above story is quite indicative of the conclusions one can draw regarding the beneficial effects of the policy package such as the ones suggested by the Washington consensus. The outcome would very much depend on the individual characteristics of the countries and the real intentions of the developed countries in extending the help to the developing countries. Dr Bernard's prescription is what one should consider quite seriously. One must be aware that a prescription used successfully elsewhere might generate allergies in the home country.

The state of the theory of economic development in providing some guidance on what policies a country ought to pursue is very well summarised by Stern as follows:

> The apparent swing in the profession from the whole-hearted espousal of extensive government intervention to its rubbishing seems to be an example of unbalanced intellectual growth, although perhaps development economics is no more subject to this kind of fluctuation than other parts of the subject. There are problems and virtues of both state intervention and the free market. The problem should not be viewed as one of a simple choice. There is no doubt, however, that whether one sees a very large or very small role for the market depends on how one judges the seriousness of the problems with markets and planning which we have been describing. In my judgment the problems of the market are particularly severe (relative to those of state intervention) in the areas of health, infrastructure (roads, communication, power, water and so on), education, and social security. Those of planning appear most strongly when the government gets heavily involved in production activities outside the infrastructure. Even in those areas where one might argue the balance of the argument is clear, however, we still have the crucial questions of pricing, regulation, and taxation. Thus the problem is the design of workable and incentive compatible policies which take account of the political processes of the country at hand [Stern 1989: 621-22].

Williamson (1990) notes that the Washington consensus has support from the classical economic theory. Barro (1991) substantiates Williamson's statement by gathering empirical evidence from a wide cross-section of countries. The classical theory makes certain assumptions such as constant returns to scale, the same technology being available to all the countries, no external economies, etc. The so-called "new trade theory", which is based on imperfect competition and non-constant returns to scale, is contrasted with the old theory by Dixit (1983), Brander and Spencer (1983, 1985), Helpman and Krugman (1985) and others. Dixit explained the high volumes of trade in industrial products between industrialised countries through the assumption of imperfect competition, and demonstrated the importance of recognising departures from competition and constant returns to scales in understanding the empirical findings on international trade. Ethier has demonstrated that the free trade argument will not hold if there are increasing returns to scale and external economies [Ethier 1982a, 1982b]. Brander and Spencer (1983, 1985) related industrial R and D to the issue of increasing returns to scale and to externalities and offered suggestions for strategic approach to industrial policy and trade policy.

Murphy, Shleifer, and Vishney (1989) give additional support to the argument of Ethier and Brander and Spencer by demonstrating that market size effects can, in effect, create external economies among firms investing in industrialisation and R and D. They thus provide a theoretical rationalisation for the big-push argument of Rosenstein-Rodan and the strategic approach to industrial development followed by Japan and South Korea. Krugman (1981) uses the external economies argument and formulates a model of uneven development in which the rich and poor nations evolve endogenously through the historical accident of different types of specialisation by the two types of countries. His model justifies a set of heterodox views.[7] Harris (1994) employs the strategic trade policy approach of Helpman and Krugman to suggest the protection for the declining US steel industry. Can one justify, using the same theory or logic, protection to a declining steel industry at home and dismantling of such protection to similar industries in less industrially advanced countries?[8]

Grossman and Helpman (1989) explain the emergence of multinational corporations (MNCs) by assuming product development through R and D, increasing returns to scale due to R and D, and the need for external trade to sustain growth. Grossman and Helpman (1995) employ public choice theory and introduce political interest groups to come to the conclusion that governments are persuaded by the special interest groups to employ tariff protections. If even one country departs from the free trade, then even the classical theory suggests that there is no sanctity to adhering to the free trade principle by the other countries. This is based on the popular theory of the second best. One might entertain a wishful thinking that the policies of the Washington consensus are quite robust to changes between the initial conditions and economic structures of different developing countries, implying thereby that even if they are sub-optimal for any given country-setting they are not very far from the optimal policies. But such noble property of the policies of the Washington consensus has not been established to the best of this author's knowledge.

The theoretical literature surveyed above suggests quite clearly that there are possibly three parallel streams of reasoning to justify economic reforms. One stream of reasoning, which is based on old classical theories, is intended mainly to bluff the ignorant ones. The second stream of reasoning suggests that such reforms, which open up the markets in the third world, are a necessity for the survival and growth of the MNCs of the industrially developed countries, and for alleviating the industrially advanced countries from the problem of prolonged recession. The third stream suggests that if the reforms are carefully, selectively, and strategically employed they would lead to mutual benefit for both the industrially advanced countries and the industrially less advanced countries. The economic theory also explains why certain political pressure groups put pressure on their home countries to impose protective tariff for themselves and advocate tariff reduction for the developing countries. Similarly it is in the interests of the industrially advanced countries to persuade and coerce the developing countries to liberalise their trade regime and to remove the restrictions on capital mobility, particularly the inward capital mobility. Looking at it from an optimistic view point, the reforms can also lead to a mutually beneficial position to both the industrially developed and less developed countries, if they are selectively and strategically chosen.

To suggest that the consensus could be loaded heavily against the Washington consensus one might cite the opinions of two other well known economists, I G Patel and J E Stiglitz:[9]

> The current consensus derives it authority not so much from any advance in theory as from a better appreciation of the effects of earlier policies and a comparison of the experiences of different countries. But experience is often ambivalent and of limited value in a changing and variegated world [Patel 1993:10].
>
> I argue that much of the rationale for liberalising financial markets is based neither on a sound economic understanding of how these markets work nor on the potential scope for government intervention. Often, too, it lacks an understanding of the historical events and political forces that have led governments to assume their present role. Instead, it is based on an ideological commitment to an idealised conception of markets that is grounded neither in fact nor in economic theory. [Stiglitz 1993: 20].

One major flaw associated with the exercise of sifting through the theory and experience, comparing them, and coming up with the policy prescription that one set of policies such as the Washington consensus is superior than others, is that the yard stick used for such comparisons has always been the aggregate growth. There is, of course a tongue-in-cheek and unsubstantiated assertion that the trickle-down phenomenon holds, and that the vulnerable sections are not adversely affected by such policies. If the yardstick used comprises of both growth and equitable distribution, i e, a function of both growth and an improvement in the distribution of income, with a specified trade-off between the two goals, then the resulting conclusion would be quite different. This intuitively obvious result has also been rigorously established, theoretically and empirically by Alsina and Rodrik (1994) employing a hybrid model of neo-classical theory and public choice theory. They claim: "Policies that maximise growth are optimal only for a government that cares solely about pure "capitalists". The greater the inequality of wealth and income, the higher the rate of taxation, and lower the growth."

From this state of affairs it is quite clear that economic theory is not able to meet the policy requirements. Economic policy has to be specific to a given country, given its initial conditions, its economic structure, and the external environment it faces. This is the kind of situation that justifies employing an operations research approach to design the economic reforms [Kumar 1996].[10]

V
Some Remarks on Planning and Economic Reforms[11]

The strategic planning type of work that was being carried out at the Planning Commission seems to have come to a grinding halt after the Fifth Five Year Plan. There is a need to revive that kind of quantitative economic policy work in the country. There is a hope of rebuilding such an endeavour only if the new reforms under way do not cut the size of the budget of the Planning Commission itself! There has been significant work on macro-economic policy models in the control theoretic framework in India. Most of it has been carried out at the Bombay School of Economics by Manohar Rao and his students and colleagues. What is needed is a major thrust to that line of work at the Planning Commission itself, which has better access to data and financial resources than university professors and their students. The most important next step to be taken regarding the economic reforms is, in this author's opinion, to derive optimal strategies and plans "endogenously" and "indigenously" by employing the optimal control theoretic methods.[12]

The type of policy research that is suggested here is much broader in scope and it will pay rich dividends for several years to come. It is quite easy to recognise that planning itself is a public good. As there are non-pecuniary externalities associated with macro level planning exercise, private organisations and agents would like to be free riders. The market fails to plan. Without the co-ordination needed to take care of externalities unco-ordinated decentralised plans yield sub-optimal solutions. Once a proper planning infrastructure is thus created as a public good it will generate the externalities whose benefits far outweigh the costs associated with creating the planning infrastructure.

Various industry groups and various regional governments can be asked to develop their own decentralised regional and sectoral plans. The planning agencies at the state and the central levels can then put together such plans and provide a co-ordinated national level plan that can serve as an indicative plan, of the type the French use. If we observe any resistance to planning in India among the private business and industry groups it is because they have been accustomed to associate planning with licences and regulations. The moment they realise that planning really means co-ordination through participative co-operation, I am sure, there will be widespread enthusiasm for planning in India.

One might wonder how the economic reforms are related to the strategic planning framework that was indicated above. Reforms may be viewed as dismantling outdated and outlived institutional mechanisms, or as introducing new institutional mechanisms, or as bringing abnormal changes in the normally employed policy instruments. The question then arises as to which of various alternate reforms constitute the best package. The criterion one must use in choosing between them must be based on the policy objectives facing the country. It cannot be based on a policy objective function chosen by another country or a multilateral agency. A simple aggregate growth oriented objective such as the one implicit in the Washington consensus will not suit the needs of developing countries that ought to worry about protecting the poor. The approach suggested above has in-built in it an objective function. While choosing between alternate reforms one must assess the impact of such reforms on the economy. The historic data can offer little evidence on what we can expect from introducing new institutional mechanisms or from dismantling the old ones. We must develop policy simulations of the control theoretic model based on certain assumed structure of the economy under such a changed regime. This is perhaps what was implicit in the quotation cited above from Patel. The econometric tools such as the Bayesian Vector Autoregression would be quite useful in tackling this kind of problems. Have we done such exercises? There is no clear indication that our government has done any such exercises before, or even after, introducing the economic reforms.

Economic history evolves in a systematic way. The rate of change of output of any sector in a country depends on six factors: (i) the initial conditions, such as the initial level of stock of capital, and the initial levels of output of that sector and related sectors, (ii) the flow of productive resources into the sector, (iii) the production technology, (iv) external trade, (v) the institutional structures under which the resources are transformed into output, employing the technology, and (vi) the demand for the output. Some of these depend on the linkages the economy has with the external world. Hence monitoring the external economy and forming informed judgments on how the external world would behave towards us are two important aspects that should receive importance in national level planning. Hence there should be a new cell within the Planning Commission that will deal with the international economy.

VI
Global Planning Models

The global economy is now characterised by extensive global linkages. These extensive global linkages have resulted in massive opportunities for international trade. These trade opportunities also generated opportunities for competition as well as co-operation. The global economic evolution can therefore be regarded as an evolutionary n-person competitive game, where the number of players in the game, viz, n, has to be determined on the basis of a co-operative game to be played by all the nations, the co-operation giving rise to the formation of coalitions such as the customs unions or free trading areas, or common currency areas, etc. As a result of the evolutionary nature of economic environment the players must come to an agreement on the rules of the game, viz, the institutional mechanism under which such game is to be played. GATT, along with the international financial system and the international legal system constituted such an institutional system until recently. These institutions had to undergo a reform through the formation of the World Trade Organisation. A nation playing an evolutionary game of this nature should not only choose a strategy at any given instant, but it should also pay attention to choosing its strategies in shaping the rules of the game, so that in a competitive environment the rules actually chosen turn out to be more beneficial to it than several other feasible rules. The nation also should reassess, from time to time, to which coalition it should belong, basing its decision on the changing global scenario.

The international economic order now allows capital mobility between nations and it permits the exchange rates to be flexible. Capital mobility depends on the real interest rate differentials and the exchange rate depends on the domestic and world inflation rates. The fiscal and monetary policies of each country affect its own real interest rates and inflation rates and also those of other countries with which it has strong trade links. Hence, if all the nations wish to make the best use of this international economic order it is absolutely necessary to bring about a policy co-ordination. Such macro-economics policy co-ordination is already taking place in the European union and it is also needed at a much larger scale between all nations that are major participants in the world trade. The existing institutional set up does not permit a fruitful policy co-ordination. There is thus a need for creating a new international institutional mechanism for macro-economic policy co-ordination. This is particularly so if we wish to avoid exchange rate volatility and to avoid transmission of depression from one country to another.

The IMF, the World Bank, the United Nations and a group of dedicated international scholars must develop alternate global planning models, such as the ones Mahalanobis developed for a single country.[13] These global models must be dynamic and interactive general equilibrium models. In such a model the economic growth of any country depends on factors, both domestic and external, some of which affecting growth positively, while others affecting it negatively. It should be the objective of global planning to increase the growth of all nations as much as possible. Nations compete with each other for resources and growth. The problem should be examined as a problem that comes under the so-called Nash programme. Under this programme first a non-cooperative n-person game problem must be solved assuming that all the n countries are pursuing their individual interests competitively. The solution of such non-cooperative game provides a clear picture of the potential threats and also of the opportunities for co-operation. Then a co-operative game must be solved that would improve the welfare of at least one country without reducing the welfare of other countries. The global growth equilibrium must be chosen, therefore, first as a Nash equilibrium, a well known equilibrium concept in n-person non-cooperative game theory. In such an equilibrium each country's growth strategy is the best alternative to the best alternative chosen by all the other countries.

This calls for an extension of the strategic approach described in the previous section. The control theoretic problem described there must be taken as a part of a larger differential game problem [Basar and Olsder 1982]. One would assume that the other countries with which we have major interactions have their own control theoretic policy models and assume that such country specific control theoretic policy models are "common knowledge", at least in aggregate and broad details, and then solve a differential game problem.[14]

Appendix
"Girls in a Boys' Party" Syndrome: The Tale of Twin Cities

This is a syndrome that explains how good the policies enshrined in the Washington consensus are for economic growth and development of developing countries in the emerging global economic environment. This syndrome can be explained best by narrating a story, The Tale of Twin Cities, from which this syndrome is derived.

The city of "Eagle Grove" had two segregated settlements, the "North City" and the "South City". The people in the North City were quite affluent as they were either well-qualified professionals or they were persons who had accumulated enormous wealth. The people in the South City, on the other hand, were much poorer and they were supplying low-cost essential goods and household services to the people in the North City. Except for this linkage there was little interaction between the people of the North City and the South City.

Over the years the North City grew, making the best use of their professional skills and the accumulated wealth. They were selling their products both in the North City as well as in the South City. Then a time came when the North City people found that investment opportunities had diminished as the demand for goods they produce reached a saturation point both in the North City, and in the South City. The North City's demand saturated because people had become so busy either doing work or enjoying leisure that they could not consume any more. The demographic factors prevailing in the North City also resulted in low population growth which put constraints on growth in demand. The South City's residents' demand also reached a saturation level but for a different reason.

Their incomes became quite limiting, at prices that were pulled up by the rich residents of the North City. The rapid growth in population of the South City resulted in a concern among its residents to have a more equitable distribution of their consumption than to have more aggregate consumption. The people from the North City were prohibited from investing in the South City. But the South City realised the importance of having more investment in their part of the city. Realising this, some enterprising entrepreneurs of the North City had joined hands and created two new institutions, which were strategically located between the two settlements, a hotel and a bank. It was the main purpose of the hotel to provide a meeting ground for the people from both the North City and the South City. The bank was supposed to take the excess savings of the North City and make it available to the South City for investment.

Over time the young residents, particularly the boys, of the North City realised that nature made no distinction between the North City and the South City and that there were more pretty and intelligent girls in the South City than in the North City. They wanted to get to know the South City girls with even the possibility of marrying them. But how to go about this difficult task, given the segregated nature of the twin cities? There was no dearth of good and productive ideas among the youth of the North City. They enlisted the support of Sheila who worked in the hotel's beauty parlour. This beauty parlour was frequently visited by the girls from the South City. Sheila was to invite some of the prospective girls from the South City to a party in the hotel, to be hosted and fully financed by the boys of the North City.

Sheila herself was originally from the South City but settled and well integrated into the North City culture. She was often confused to be from the South City.

There were altogether five girls who attended the party, of whom Sheila was one and all the other four were from the South City. When Sheila invited her South City clients for the party there was considerable hesitation from the South City girls. They were quite apprehensive of the intentions of Sheila and of the boys from the North City. "Do the boys have questionable bad intentions of misbehaving with them and exploit them? Or, are they gentlemen with genuine and noble intentions?" The four girls who decided to go to the party were mainly of two types. Anne and Mary were quite adventurous in their nature because of their upbringing. They came from families with a relatively better economic background within the South City. Carol and Nancy, on the other hand, came from very poor and very vulnerable families. For them any positive chance, however small, of becoming at least slightly better off, was not worth missing.

Anne was quite smart and she was brought up by her parents on the principles of encouragement and guidance, with only limited restraint. She had a good world view of things. She had developed the habit of making independent and calculated decisions. Mary was brought up under a different and a disciplinary environment. She developed the habit of taking others' opinions and guidance to take her decisions.

Carol was also brought up like Anne in an enabling environment with freedom and guidance with only limited restraint. But she was not as smart as Anne in taking independent decisions. On occasions she took wrong decisions. Nancy was brought up under a bad environment. There was neither encouragement or restriction, nor guidance. Her upbringing did not develop in her a set of good moral values.

These five girls, including Sheila, developed sustained friendship with seven boys from the North City. Anne was quite thoughtful in choosing Bob as her friend, because in him she saw certain virtues such as being honest, understanding, and intelligent. Their friendship developed into a successful marriage. Mary had been persuaded by Sheila to befriend David. David was also interested in Mary as she was the prettiest of all the five girls. David was the richest of the boys who gathered at the party. David and Mary also married each other. But their marriage lasted only for a few years as Mary realised that David was not honest, as she expected him to be. She felt sorry for taking Sheila's advice in the early stages. Carol was also quite pretty, although not as pretty as Mary. Carol and Karl became quite friendly. Karl helped Carol with her education, and later in her business. But they remained as good friends only and led their independent lives later. There was no doubt that Carol benefited immensely from her friendship with Karl. There were three boys, all of them hailing from very rich families in the North City. They were after Nancy and Nancy was also after them. Nancy took advantage of the friendship. There was no doubt that Nancy felt benefited from the friendship with the three boys, but this friendship did not materially improve the social and economic status of Nancy. Sheila married John, the son of the most popular businessman-cum-politician. John himself became, like his father, a famous politician with a good economic base.

There was considerable interest among the people of Eagle Grove on the outcome of the boys' party, and how the party had changed the lives of the five South City girls. Four out of the five had benefited from the party, although what kind of benefit Nancy got was a matter of debate, and it is not clear whether one should consider Sheila as a South City girl.

But when someone asked Mary and her parents about the party their response was quite different. They said it would have been better if Mary did not attend that fateful party which ruined her life. They cited the instances of some other South City girls who did not attend the boys' party but who led contended and reasonably decent lives. But Mary and her parents had the right attitude not to blame the party as such for their misfortune. They attributed the problems Mary faced to a wrong assessment of David and his intentions. They felt that if Mary could have chosen someone like Bob, Mary's fortunes would have been like that of Anne. It was their view that the party was only a catalyst. How that catalyst worked depended on the nature and character of both the boys and girls who used it. The statistical evidence, such as per cent of cases in which the party had a beneficial effect on the girls in general – however large that percentage is, has very little wisdom in it to have an overwhelming faith in the party.[6]

Notes

[This paper is based on a paper presented at a seminar 'Economic Reforms – The Next Step' organised by the Rajiv Gandhi Foundation and the Rajiv Gandhi Institute for Contemporary Studies at New Delhi on October 2-4, 1996.]

1 See Kumar (1996).

2 Justice K Narayana Rao Memorial lecture delivered by Justice O Chinnappa Reddy on 'Courts and the Constitution, 1950 to 1996: Peaks and Depths', National Law School of India University, December 13, 1996.

3 One such loud pronouncement with a rhetorical exaggeration comes from a senior World Bank economist as follows: "The design of structural adjustment programmes directed at the four '... ations' – stabilisation, liberalisation, deregulation, privatisation – has become a cottage industry" [see Summers and Pritchet 1993: 383].

4 Those who are familiar with the developments in the numerical computation of optimal control paths, such as those advanced by Kalman and others in early 1960s, will easily recognise this fact.

5 This is a fictitious story developed by the author to relate Dr Bernard's prescription (to be cited later) to the reforms package offered as a prescription to bring about sustainable economic stability and growth to a large number of developing countries which are facing severe balance of payment crises.

6 The prescription Dr Claude Bernard gave is perhaps quite appropriate here. "A great surgeon performs operations for stones by a single method; later he makes a statistical summary of deaths and recoveries, and he concludes from these statistics that the mortality law for this operation is two out of five. Well, I say that this ratio means literally nothing scientifically and gives no certainty in performing the next operation. What should really be done, instead of gathering facts empirically, is to study them more accurately, each in its special determinism..." [Bernard 1927, cited in Cornfield 1975].

7 In a subsequent paper Krugman shows that the introduction of increasing returns to scale assumption leads to multiple equilibria [Krugman 1991]. He argues that the choice between alternate equilibria is made either by historical initial conditions or by self-fulfilling strategies. This author had also suggested the importance of initial conditions and the self-fulfilling strategies in explaining the varieties of reform experience [Kumar 1994a].

8 The book edited by Krugman and Smith (1994) has several interesting articles, such as Harris's article cited above, on empirical aspects of strategic trade policy.

9 When these views were presented at a seminar one of the participants remarked that the references cited by this author were selectively chosen to present a biased view. That statement proves this author's point that by not citing some of the references that are cited here the other unconditional advocates of the Washington Consensus provide a biased view! The main thrust of this paper is not to depend on the general opinions based on theory and empirical evidence adduced by the others but to develop one's own strategy based on country-specific conditions.

10 It must be said that the main proponents of the Washington consensus had realised, after examining carefully the reasons for the Miracle of the East Asian Tigers, the importance of designing economic policies that are country specific (see the foreword by the president of the World Bank to its report on the East Asian Miracle (1993)).

11 Many participants at the seminar where this paper was presented were apparently up at arms with the author for what seemed to them as a suggestion to return to the old planning regime of licences and controls, as they mistook strategic planning approach of Mahalanobis with the planning strategies of the Nehru-Mahalanobis era. It may therefore be stressed that what is being suggested here

is that while dispensing with licensing and controls one should not throw the baby with the bath waters. One must realise that indicative planning and strategic planning have important roles to play to co-ordinate and direct the individual plans in a liberalised economic environment. While it is true that India's planning experience shows excessive doses of licensing and controls India's planning cannot be treated as centralised planning of the type used by the Soviet Union. India's planning has been mostly indicative planning, as the agricultural sector and the private industrial sector in India have sufficient leverage in making independent decisions. Under the licence control Raj this leverage was much less.

12 One may see Rao (1987), Rao and Karnik (1994), and Rao and Singh (1995) for control theoretic modelling of the Indian economy.

13 What is being suggested is an extension of the type of work that is already underway on the empirical open macro-economic models. One may see, for example, Hamada (1976, 1979, 1985, 1986), Buiter and Marston (1985), Miller and Salmon (1985), Bryant et al (1988), Mckibbin and Sachs (1991), Bryant, Hooper, and Mann (1993).

14 One may see Hamada (1979) and Miller and Salmon (1985) for more details on such formulation of global policy conflicts and global policy co-ordination.

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