

UNIT 6

GOVERNANCE, ROLE OF THE STATE, MARKET AND CIVIL SOCIETY

Governance, role of the state, market and civil society are crucial factors in every economy. This unit covers the concepts related to governance in lesson-1, role of state and market in lesson-2 and the role of the civil society in lesson-3.

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Lesson 1: Governance¹

Objectives:

After studying this lesson, you will be able to:

- Understand theoretical concepts related to governance.
- Analysis the market and Government.
- Describe the economic performance.

Introduction

The concept of governance is not easy to define. In case of an institution, it may be said that the term refers to processes through which an organisation is governed. When it is linked to a country the term relates to processes having complex historical, cultural, social and political determinants. It deals with the science of government behaviour and performance. Economic theories emphasise efficiency in explaining the role of institutions in development, while political and sociological theories emphasise the role of authority, beliefs and ideology.

Analytical Concepts: A Snapshot

Economic theories hold that institutions are created when it is efficient to create them, i.e. when the benefits of building institutions exceed the transaction costs of doing so and political theories focus on redistribution rather than efficiency and hold that policies and institutions are shaped by those in power to stay in power and to transfer resources to themselves (La Porta *et al.* 1998).

There are approaches² which examine both government and markets not only from the perspective of allocating resources through prices, voting systems or discretionary power, but also from the point of view of informational advantages, incentives and rights of control over resources. These approaches recognise that there are political as well as market failures, and are rooted in informational, transactional and political constraints on government activity. Informational constraints on organisations are channeled through moral hazard and adverse selection. Transactional constraints arise because contracts seldom provide for all contingencies, which must be specified, and need to be monitored and enforced. The more uncertain the future is, the higher transaction costs are likely to be. The type of governance structure, and in particular the ownership structure, matters in the presence of transaction costs.

¹ The section draws on J. J. Dethier: *Governance and Economic Performance: A Survey*, ZEF Discussion Papers on Development Policy No. 5, Center for Development Research, Bonn, April, 1999.

² See Note 1.

Governance structures are characterised by agency relationships. The standard model of operation of an agency is one where the principal devises a scheme of incentives or penalties, such that the agent's action is altered at least partially in the direction that favours the principal's interest. This typically requires a trade-off between efficiency and risk sharing, and the result is a second best. Agency relationships are often more complex in the political than in the economic sphere. Most important, it is not always clear who the agent is. (Dixit 1996).

In addition to informational and transactional constraints, governments face legal and political constraints. Legal and political institutions provide the rules of the game according to which individuals and organisations operate. The rules both constrain and facilitate economic conduct. Informational constraints, economic and political transaction costs and the law give rise to several forms of rents in addition to the more familiar forms of rents arising from market imperfections (monopolies, environmental externalities, etc). Incentive schemes are set up in order to overcome these constraints and maximize efficiency.

A great variety of schemes affecting both the quantitative and qualitative aspects of economic activity are available. Generally speaking, the theory of incentives shows that there is no first-best world and that every situation will involve trade-offs. Adverse selection implies a trade-off between efficiency and ex ante rent extraction. Moral hazard implies a trade-off between efficiency and ex post rent extraction.

Good development policy-making involves not only selecting the right policy instruments, but also designing appropriate incentive schemes and institutions such that credible pre-commitments are in place, and agents can realistically be expected to maximize social welfare.

Two paradigms are used to discuss incentive problems arising from informational, transactional and institutional constraints. The first is complete contracts. In this case, a government is viewed as a group of agents motivated by formal and well-defined incentive schemes. Agents are induced to choose desirable actions and to reveal information fully and truthfully. The second paradigm is incomplete contracting, reflecting the fact that contracts cannot provide for all contingencies. This latter paradigm probably corresponds more closely to the actual workings of governments than does the complete-contract paradigm. In this case, a government is viewed as having control rights over several decisions. These control rights are determined by political processes and customs, and are summarised by constitutions and laws.

There are major differences between private and public organisations. A government is not a single agent (a benevolent dictator) maximising social welfare, as is often assumed in economic models. A government is a complex organisation consisting of many officials and multiple agencies, which are often in conflict with each other. A government consists of various tiers, each having a separate mandate and authority. Inadequately coordinated decision-making can lead to costly social policies. The main prerequisites for achieving successful governmental

outcomes appear to be accurate information, credible commitment, effective monitoring and enforcement. If these prerequisites are lacking, inefficiencies arise, mutual gains disappear and opportunism prevails.

Economic outcomes are measured in terms of efficiency and welfare. The concept of efficiency has been attacked from two directions. One fundamental criticism of neoclassical economics is that 'efficiency losses' in resource allocation are usually measured against hypothetical situations involving zero information costs or zero transaction costs. Demsetz (1969) points out that traditional definitions of efficiency ignore the real scarcities and costs of information, and tend to presume that people behave differently than they do.

Government and Markets

The government-markets nexus is the "core" of the problem of economic performance. Markets and governments are interdependent in at least three ways (Drèze and Sen 1995).

- ◆ First, markets can hardly function in the absence of legal enforcement of contracts and particular rights. For instance, it is intuitively clear that one major reason why markets are weak in countries such as Somalia is the breakdown of law and order.
- ◆ Second, the government has a major role to play in facilitating market-based economic growth, whether in dealing with skill formation in the labor force, technological externalities, or economies of scale.
- ◆ Third and more controversially, the market mechanism is dependent, for its outcomes, on government action. One interpretation of the "second theorem of welfare economics" which formed the intellectual underpinning for extensive government intervention in developing or former socialist countries (Stiglitz 1994) is that government can play a major role in redistributing endowments, for instance by instituting a land reform benefiting poor peasants. Recent developments in welfare economics have shown that issues of efficiency and distribution cannot be separated.

Rodrik (1997) has put forward an interesting hypothesis about the role of institutions that serve to mitigate social risks and the complementarity of governments and markets. He makes the empirical point that countries with greater exposure to trade, and thus to external risks, have bigger governments and that the degree of openness is a good predictor of the expansion of governments. This, incidentally, is confirmed by the recent cross-country study by La Porta et al. (1998), who find that larger governments tend to perform better. Equating size and growth of government with the provision of social insurance, Rodrik argues that elaborate social safety nets and social security systems are found in fiscally responsible countries such as Chile or Germany, which are very sensitive to exposure to external risk. He considers that social risk-mitigating systems ensure social welfare and political stability by acting as a "shock absorber" in case of large external shocks in a rapidly

globalising economy, a view largely shared by social-democratic economists.

Institution and Economic Performance

Economic performance is greatly determined by the quality of institutions. Rules and regulations are required to make markets function more effectively. Countries grow more if these rules are clear, predictable, enforceable, and supportive of private enterprise. A number of recent studies have established the primacy of institutions for a well-functioning market economy (Knack and Keefer 1995, 1997a, and 1997b; Mauro 1995). Strong institutions foster economic growth by securing property rights, by enforcing commercial contracts, and by making economic policies more stable and predictable. Differences in the quality of institutions help explain the gap in economic performance between rich and poor nations. Behind the spectacular economic success of the developed countries lies a transparent framework for formulating economic policies—a framework that is guided by clear rules. Developing countries with efficient institutions are more likely to have faster economic growth than those countries without such institutions. 'A country with an initial per capita income of \$500 that has the lowest risk of contract repudiation by the government will grow 2.22 percentage points a year faster than a country with initial per capita income of \$1500' (Knack and Keefer 1997b).

There are several reasons for such links between strong institutions and economic growth: *First*, an economic activity based on clear and conducive rules diminish the arbitrary influence of powerful lobbies, reducing the costs of economic exchange (transaction costs). *Second*, the existence of copyrights, patents, and an assisting economic framework encourages new innovations that are critical for sustained economic growth. Institutions are needed both for the creation and assimilation of new investments and technology. *Third*, institutions affect how the key factors responsible for production, such as land, labour, capital, and technology, are created, used, and transferred. *Fourth*, institutions determine the efficiency with which governments formulate and implement policies. The lack of high-quality institutions can result in an inefficient and corrupt bureaucracy. *Fifth*, informal rules determine the civic behaviour of a society. A responsible civil society can better assert its basic economic and political rights. It can also forge well-developed traditions of hard work and honesty—civic traditions that have clear economic pay-offs. The more civil a society, the more able it is to realise the basic human capabilities of its people.

The Provision of Public Goods

The economic case for having some goods provided by private or by public organisations

cannot be made if one assumes a world of complete contracts since there is no difference between state and private provision of goods and services (Shleifer 1998). Coase (1988) has emphasized that the existence

of an externality does not imply that there is a prima facie case for public intervention. The Coase solution is to solve the problem without state intervention, apart from fixing property rights, but this is not always practicable. It does not generally work for education or health.

Bardhan (1997) points out, this calls for a more detailed theory of the state than is usually available from the old “market vs. state” debate. On the one hand, it is necessary to recognize the limitations of the state as an economic governance structure, arising from its lack of access to local information, its lack of local accountability and its vulnerability to wasteful rent-seeking processes. On the other hand, especially in poor countries, it is often desirable that the state play an active role, catalysing the mobilisation of people in participatory development and providing supra-local support of a financial and technical nature. In situations of high economic and political inequality where elites dominate local governance structures, benefits are not likely to percolate easily to the poorer (and weaker) segments of the population.

Should public goods be provided by the government or by the private sector? To what extent are market mechanisms better guarantors of efficiency and/or social welfare than political processes or deliberative government interventions? Theory provides guidelines, but the answers to these questions have to be given on a case-by-case basis. Hart, Shleifer and Vishny (1997) develop a model based on incomplete contracts to assess the provision of public goods by private or public firms. Private providers have stronger incentives to improve the quality of service and reduce costs than do public providers. However, private providers’ incentives to cut costs are too strong because they can ignore the adverse impact on quality. Hart, Shleifer and Vishny apply their theory to the private management of prisons, a controversial trend which, according to critics, has been driven entirely by ideology and politics and yields low economic benefits (Schlosser 1998).

Democracy, governance and growth

North (1990:109) describes the ideal political system for maximising economic performance as one in which affected parties have full information about prospective legislation, preferences are communicated to legislators who faithfully represent those preferences, votes are weighted by gains and losses with losers being compensated, and this process occurs at a low enough cost to make it all worthwhile. Although noting various reasons why democracies fall short of this ideal, North concludes: "The institutional structure most favorable to approximating such conditions is a modern democratic society with universal suffrage. Vote trading, logrolling, and the incentive of an incumbent's opponents to bring his or her *deficiencies* before constituents and hence reduce agency problems all contribute to better outcomes."

The Nobel Prize winner Amartya Sen has argued that the openness and accountability of democratic societies explains why India - despite its poverty - but not China has managed to avoid large-scale famines. A free press, in particular, increases public awareness of famine, raising its

political costs to India's leaders, who thus have a greater incentive than the Chinese leadership to adopt policies to combat hunger (Dreze and Sen, 1982).

A sizeable cross-country empirical literature, critically reviewed in Przeworski and Limongi (1993), examines the relationship between regime type and economic performance. Results are mixed, with the most recent and sophisticated analyses concluding that democracies are no more or less likely than non-democracies to grow rapidly.

Persson and Tabellini (1994) formalise this intuition in a growth model, and claim to have found supporting evidence in the cross-country data: income inequality is associated with slower growth among democracies, but not among non-democracies, where the median voter theories do not apply. However, other researchers using somewhat different data sources on inequality, and on regime types, have found that income inequality affects growth equally in democracies and non-democracies (e.g., Alesina and Rodrik, 1994). Knack and Keefer (1997) replicate the Persson and Tabellini findings, but show that when reasonable corrections are made for mis-measurement in their income inequality and regime type data, the impact of inequality on growth is just as strong or non-democracies as for democracies. Coupled with other evidence suggesting that non-democracies also face pressures to redistribute from rich to poor (e.g., through political violence; see Alesina and Perotti (1996), it remains an open question whether insecurities in property rights associated with majority-rule voting counteract some of the governance advantages of democratic regimes.

A second possible reason for the failure of democracies to systematically outperform autocracies is related to interest group pressures on the state. The political openness characteristic of democracy may also allow freer rein for the growth-slowing rent-seeking activities of special interest organisations (Olson, 1982).

Conclusion

An overwhelming body of accumulating evidence indicates that good governance and economic freedoms are crucial for attaining rapid increases in the living standards of the broad mass of people in a developing economy. Transparent, predictable governmental institutions and policies are conducive not only to rising per capita incomes but also to declines in absolute poverty.

Note

Many economists are trying to understand institutional causality. New developments in the economics of organisation, information and incentives have led to a major reformulation of welfare issues, both in microeconomics and macro-economics. Basic references are Williamson (1985), Tirole (1989), Laffont and Tirole (1993) Persson and Tabellini (1990). Hirshleifer and Riley 1992 and Salanie 1997 are theoretical overviews that are more accessible. As discussed by Tirole 1994, extending this theoretical framework to include governments as

organisations is a more recent, but growing, preoccupation. On institutions and transaction costs, the 'new institutional economics' has produced a voluminous literature. Useful surveys are Eggerston (1990), Lin and Nugent (1995) and Rutherford (1996). These two types of literature — incentive theory and institutional economics — share concerns with more traditional public finance (Jha 1998 contains a recent exposition), e.g. on the provision of public goods and on incentive problems arising from distortive taxation, and with public choice (Mueller 1989 remains the best survey), e.g. on decision-making processes relating to public goods. Recent surveys on the economic theory of politics, which has developed as a separate branch of economics and is also relevant for governance, can be found in Persson and Tabellini (1994) and Alesina & Roubini (1997).

Questions for Review

1. How do you define governance?
2. Analyse the statement that good development policy-making involves not only selecting right policy instruments, but also appropriate institutions.
3. Do you think there is correlation between democracy and economic performance?
4. What are basic characteristics of good governance? Provide specific criteria of economic and political good governance.

Further Readings

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Lesson 2 : Role of the State and Market

Objectives:

This has been one question that has constantly occupied economists since the birth of the subject. There have been a number of swings in the dominant opinion on the subject, but the two major swings that have occurred during the last half century after the Second World War. The early postwar years witnessed the world-wide rejection of the *laissez faire* doctrine. This new consensus was dramatically overturned since the mid-1970s, following the Neo-Liberal counter-offensive. Both the past praise and the current criticism of the East Asian miracle, however, have brought the question of the role of government to the forefront.

After studying this lesson, you will be able to:

- understand basic concepts relating to the role of state;
- examine concepts and assumptions arising out of the neo- liberal school of thought ; and
- comprehend critique of the mainstream view from the institutionalist point of view Introduction

Introduction³

The discussion of the role of government is vital for improving development strategy. There is a growing consensus that governments can play a vital role in successful development efforts, but wrong kind of government intervention can be highly detrimental. There has been recognition that the key issue is the scope and effectiveness of government activities, rather than simply the size of the government's budget or personnel.

The View from the Market: Three Conservative Propositions

Many critics of the government base their beliefs on premises that markets by themselves yield efficient outcomes, and second, efficiency is more important than, say, distribution between persons or generations. Based on these judgments, critics of government have argued:

- Government is unnecessary because anything the government can do, the private sector can do better;
- Government is ineffective because anything the government does, the private sector can and will undo;
- The incentive structures inherent in public institutions imply that government actions generally decrease societal welfare, or, at the

³ The section draws on Stiglitz, Joseph, "Redefining the Role of the State *What should it do? How Should it Do it? And How should these decisions be made?* presented on the Tenth Anniversary of MITI Research Institute, Tokyo, Japan, March 17, 1998

very least, inhibit productive economic activity by taking resources away from one group and giving them to another, often less deserving group.

According to Stiglitz (1998), the first proposition is simply not true: government has powers that the private sector does not have. The second proposition is even more obviously wrong, he adds. The third proposition, according to Stiglitz, is the most difficult to deal with. Certainly, there is no general proposition concerning the efficiency of actions which emerge from political processes. There are good reasons to believe that public and private interests are far from perfectly aligned. The principal agent problems which arise in the public sector are, in many respects, not dissimilar to those which arise in large corporations in the public (Stiglitz, 1994).⁴ In both cases, the rewards of managers are at best only loosely linked to performance.

Market failure and public failure

While market failure theories dominated thinking about the role of government in the decades following the proof of the fundamental theorems of welfare economics, public failure theories began to dominate discussions in the Reagan/Thatcher era. The public failure theories can be thought of as an elaboration of the third Conservative proposition above. It was asserted that

- Special interest groups would, without constitutional bars, seek to establish market impediments that generate rents;
- The opposing public interests were too diffuse to successfully oppose the special interests. While aggregate costs might exceed aggregate benefits for society, a public goods problem arose when costs were much more diffuse than benefits.
- Competition for rent seeking tended to dissipate the rents, but the rent dissipation simply added to the waste.

While there is plenty of evidence to suggest that rent seeking was important, these propositions do not seem to adequately describe the process. Stiglitz (1998) provides three reasons for his view. First, there is a curious intellectual inconsistency: while many conservatives seemed to argue that Coase's theorem (or what might more appropriately be called Coase's conjecture) worked well in the private sector, it seemed to have no sway in the public. Inefficiencies within that sector did not seem to get "bargained out." Second, it was simply assumed that there was perfect competition in rent seeking. In reality, however, competition in rent seeking was every bit as imperfect as competition elsewhere in the economy. There are quite general theorems which established that if there were even epsilon sunk costs, even strong potential competition was not enough for the dissipation of imperfect competition rents.

⁴ Stiglitz, J.E. 1994. *Whither Socialism?*. Cambridge, MA: MIT Press.

(Stiglitz, 1987)⁵. Third, rent-seeking activities tend to be concentrated in certain sectors, e.g. trade and agriculture, although there are clearly opportunities for significant rents elsewhere. Understanding why these are not pursued, or at least successfully pursued, may provide important new insights into the rent-seeking process.

Reading of the Lesson

The present lesson concentrates on a selection, an essay written by Dr. Ha-Joon Chang, Faculty of Economics and Politics, University of Cambridge, UK entitled *An Institutional Perspective on the Role of the State - Towards an Institutional Political Economy*.⁶

Dr. Chang critically examines some of its basic concepts and assumptions of the Neo-Liberal agenda from the institutionalist point of view. He argues that there are more than one views of what the "ideal" market can do. He opines that the Neoclassical theory is essentially a theory of the market, but capitalism, as a socio-economic system, is more than a collection of markets, and is made up of many institutions. He holds the view that the market is a fundamentally political construction. The paper reiterates the need to build a theory of politics which takes a much broader, balanced, and sophisticated view of politics than what is offered by Neo-Liberalism.

⁵ Stiglitz, J.E. 1987. "Technological Change, Sunk Costs, and Competition," *Brookings Papers on Economic Activity*, 3, 1987. (Special issue of *Microeconomics*, M.N. Baily and C. Winston (eds.), 1988, pp. 883-947.)

⁶ This is a slightly revised version of the paper presented by the author at the International Conference on "Institutions and Economic Development - Towards a Comparative Perspective on State Reform", November 12-14, 1997, Rio de Janeiro, Brazil. This is forthcoming in L. Burlamaqui, A. Castro & H-J. Chang (eds.), *Institutions and the Role of the State*, Edward Elgar). The paper is reproduced with the permission of the author.

**AN INSTITUTIONALIST PERSPECTIVE ON THE ROLE OF THE STATE -
TOWARDS AN INSTITUTIONALIST POLITICAL ECONOMY**

Ha-Joon Chang

1. Introduction

What is the appropriate role of the state? This has been one question that has constantly occupied economists for the last 2-3 centuries since the birth of the subject (for some excellent historical reviews, see Deane, 1989, and Shonfield, 1965). During this period, there have been a number of swings in the dominant opinion on the subject, but the two major swings that have occurred during the last half century after the Second World War are particularly remarkable in their scope and suddenness (see Chang & Rowthorn, 1995a, whose Spanish translation appears in Chang, 1996). The early postwar years witnessed the worldwide rejection of the *laissez faire* doctrine that failed so spectacularly during the interwar period, and the resulting emergence of a widespread consensus on state activism. By the 1960s, the end of *laissez faire* capitalism was announced in many quarters and there was a widespread consensus that we are now living in the "mixed economy" (alternatively, "modern capitalism" or "organised capitalism"). However, this new consensus was dramatically overturned since the mid-1970s, following the Neo-Liberal counter-offensive, which sought to end the mixed economy and re-introduce market principles to the extent that would have been unimaginable during the early postwar years.

The upsurge of Neo-Liberalism during the last two decades or so has fundamentally changed the terms of debate on the role of the state (for more details, see Chang, 1994a, chs. 1-2). The state is no more assumed to be an impartial, omnipotent social guardian and is now analysed either as a "predator" or as a vehicle for politically powerful groups (including the politicians and the bureaucrats themselves) to advance their sectional interests. No other motives than maximisation of material self interests are accorded to any agent even in the "public" domains of life, denouncing the role of politics as a legitimate way to correct the market outcomes according to the "collective will". The resulting "minimalist" bias in the terms of debate means that those who want to make a case for state intervention have to fight their adversaries at each and every step of their arguments, whatever the merits of their arguments may be, whereas those who want to discredit state activism can often do so with a very simplistic logic supported by, often unrepresentative, anecdotes. Although the Neo-Liberal agenda itself has a lot of intellectual limitations and biases, as we will discuss in the rest of the paper, the legacy of Neo-Liberal counter-offensive has not been entirely negative. For one thing, it exposed fundamental problems with the "technocratic" view on the role of the state that prevailed in the heyday of welfare economics ('50s and '60s) and brought politics back into economics (although it ultimately aimed to abolish politics; see section 3.4.). And more importantly, its explicit engagement in "political economy" discussions opened the door for the subsequent rise of "institutionalists" criticisms (e.g., see Evans et al. (eds.) 1985; Hall (ed.), 1989; Toye,

1991; Evans, 1995; Chang & Rowthorn, 1995b).¹ And following the institutionalist criticisms, even some proponents of Neo-Liberal doctrine have recently come to admit (but without necessarily recognising the contributions from their critics) the importance of institutional factors in understanding the role of the state (North, 1994, and World Bank, 1997, are good examples of such change). Having achieved that important, if unfairly unacknowledged, victory over the Neo-Liberals, however, I think it is fair to say that the institutionalists still lack a full-blown political economy that can replace the Neo-Liberal political economy. In this paper, I will make some suggestions as to what I think should be the building blocks of what may be called an institutionalist political economy. For this purpose, I will dissect the Neo-Liberal research agenda on the role of the state from an explicitly institutionalist perspective and identify what I think are the fundamental flaws in it, and in that process suggest what should be the elements in the institutionalist theory of state intervention that can overcome these flaws.

2. Disentangling the Neo-Liberal Agenda

The Messianic convictions with which many proponents of Neo-Liberalism have delivered their messages have created the impression that it is a very coherent doctrine with clear conclusions. However, contrary to this popular belief, the Neo-Liberal doctrine is in fact a very heterogeneous and internally inconsistent intellectual edifice. So before going into the detailed criticisms of this doctrine, it will be useful to delineate the basic fault lines in the Neo-Liberal intellectual agenda and reveal some of its obvious weaknesses.

2.1. The Unholy Alliance: Neoclassicism and the Austrian-Libertarian Tradition

The biggest contradiction in the Neo-Liberal research programme comes from the fact that it was born out of a marriage of convenience between Neoclassical economics as the source of intellectual legitimacy (given its dominance in the academia) and what maybe broadly called the Austrian-Libertarian tradition as the source of political rhetoric. The gap between these two intellectual traditions is not a minor one, as those who are familiar with, for example, Hayek's scathing criticism of Neoclassical economics would know (e.g., see essays in Hayek, 1949). However, the marriage of convenience goes on, because the Austrian-Libertarian tradition supplies the popular appeal that Neoclassical economics can never dream of supplying itself (who's going to risk their lives for "Pareto Optimality"? - but many have been willing to for "liberty" and "entrepreneurship"), while the Austrian-Libertarian tradition, given its lack of intellectual legitimacy in "respectable" circles, needs the aura of "science" that Neoclassical economics carries around.² But in return for the increased power of persuasion that they acquired by allying with the Austrian-Libertarian tradition, Neoclassical economics had to pay a heavy price. In order to maintain the alliance with the Austrian-Libertarian tradition, it has had to suppress its interventionist streak, given the strong anti-statism of the latter. So how is this done? One such method of suppression is to accept the logic of "market failure" behind

welfare economics but then not to extend it beyond the set of "politically acceptable" areas. So, for example, the externality argument is often applied to politically less controversial areas such as the environment or education, but is rarely applied to such politically more controversial areas as "selective" industrial policy a la East Asia, which can be justified by the same logic equally well. Given that there is no theoretical way in Neoclassical economics to determine what is the "correct" boundary for state intervention, it becomes necessary to argue that market failures exist as logical possibilities, but rarely occur in reality - naturally without providing much evidence (Friedman, 1962, is a good example).³ 2 This point is best illustrated by the experiences during the early days of "reform" in the former Communist countries. What captured people's imagination in those days was the Austrian-Libertarian languages of freedom and entrepreneurship, and *not* the arid Neoclassical languages of Pareto Optimality and General Equilibrium. However, when the post-Communist governments in these countries chose their foreign economic advisers, it was according, largely, to how high a standing they had in the Western academic "hierarchy", which was determined by how good they were in handling the concepts and the tools of Neoclassical economics. Friedman's list of legitimate functions of the state is as follows: maintenance of law and order; definition of property rights; service as a means whereby people modify property rights and other rules of the economic game; adjudication of disputes about the.⁶ The second method of suppressing the interventionist instinct of Neoclassical economics is to separate, partly deliberately and partly subconsciously, the "serious" academic discourse from the "popular" policy discourse and compartmentalise them. So Neoclassical economists in universities may be doing researches justifying stringent anti-trust policy, but the "lax" anti-trust policy by the government may be justified in terms of some other logic which has no place in Neoclassical economics - say, by citing the need "not to discourage entrepreneurship", etc.. The recent "reform" experiences in the former Communist countries that we just talked about is a most poignant example of such practice. The last method of suppression is to fully accept the logic of market failure and build models that may have strong interventionist conclusions, but later dismiss them on the ground that "real life" states cannot possibly be entrusted with such policies that are technically difficult (due to informational asymmetry) and politically dangerous (due to the possibility of bureaucratic abuse and/or interest group capture). Various writings by the American trade economist Krugman provide the best example, where frequently a few paragraphs, at the end of an article, of "pop political economy" analysis dismissing the integrity of the state would be used to discredit his own elaborate "strategic trade theory" model endorsing state intervention that went on in the rest of the article. To put it bluntly, the name of the game is that, a Neoclassical economist may build a model that interpretation of the rules; enforcement of contracts; promotion of competition; provision of a monetary framework; engagement in activities to counter technical monopolies and to overcome "neighbourhood effects" [his term for externality] widely regarded as sufficiently important to justify government intervention; supplementation of private charity and the private family in protecting

the irresponsible, whether madman or child (Friedman, 1962, p. 34). A well-known Neo-Liberal economist, Robert Lucas, reviewing Krugman's book with Helpmann, asked why they had written the book in the first place if they were going to say in the end that the interventionist policies that follow from their models cannot be recommended because of the political dangers that they carry. See Lucas (1990)..⁷ recommends state intervention as far as it is "technically competent", but he/she has to prove his/her political credential by rubbishing his/her own model on political grounds.

2.2. The Indeterminacy of the Neoclassical Position on State Intervention

Even when we ignore the above-mentioned tension between the Neoclassical element and the Austrian-Libertarian element in the Neo-Liberal intellectual edifice, there are still disagreements amongst the Neoclassical economists themselves on exactly what the role of the state should be, as we implicitly suggested above. As I indicated above, Neoclassical economics has a strong interventionist streak that is best manifested in welfare economics. Especially, as Baumol (1965) and others have pointed out, once we begin to follow the logic of externality faithfully, it seems doubtful whether we should have any market transaction at all. Most goods create some negative externalities in their production processes in the form of pollution, except in those few cases where proper compensation is actually made. When considering "linkage effects" (Hirschman, 1958, ch. 6) or "pecuniary externalities" (Scitovsky, 1954), many goods may additionally be classified as having positive externalities. Some economists even argue that some goods which have conventionally been treated as lacking externalities, say basic foodstuff, can be seen as creating externalities when they are not consumed in the proper amount and therefore induce crime (Schotter, 1985, pp. 68-80). Moreover, there exist interdependences between individual preferences. For example, people have what Elster (1983, ch. 2) calls counteradaptive preferences - "the grass is always greener on the other side of the fence". The psychology of luxury good consumption - part of one's pleasure derives from the very fact that one consumes what others do not - is another example of interdependent consumer preference. The list can go on, but the point here is that, even using a purely Neoclassical logic, one can justify an enormous range of state intervention. Indeed, in the 1920s and.⁸ the 1930s people like Oskar Lange were trying to justify socialist planning on the basis of essentially Neoclassical models (Lavoie, 1985; Pagano, 1985). Thus seen, whether a Neoclassical economist is an interventionist or not depends more on his/her political preference rather than the "hard" economics that he/she practices. Seen in this way, it is important to reject the myth propagated by Neoclassical economists that the boundary between "good" and "bad" intervention can be drawn according to some "scientific" rules.

2.3. Concluding Remarks

Neo-Liberalism is based on an unholy alliance between Neoclassical economics, which provides the intellectual legitimacy, and the Austrian-

Libertarian tradition, which provides the political rhetoric. This, in turn, means that the interventionist streak of Neoclassical economics has to be suppressed. Such suppression involves, we pointed out, intellectually and morally indefensible practices like drawing an "arbitrary" boundary around the state without acknowledging its arbitrariness, using different discourses for "serious" academic research and for "popular" policy discussion (again without acknowledging such compartmentalisation), and denouncing interventionist conclusions of formal models with unsubstantiated "pop" political economy. We then argued that, even Neoclassical economics itself does not provide us with any unambiguous "scientific" criterion to draw the boundary between "good" and "bad" interventions. Thus seen, despite its pretence of intellectual coherence and clear-cut messages, Neo-Liberalism is an internally heterogeneous and inconsistent intellectual doctrine with confused and confusing messages.

3. Some Institutional Criticisms of the Foundations of the Neo-Liberal Analysis of Market, State, and Politics

Having pointed out the fundamental fractures in the very set-up of the Neo-Liberal doctrine, let us now make some detailed criticisms of it from an institutionalist perspective, questioning the very way they envisage the market, the state, and other institutions, as well as the relations between them.

3.1. What is a Free Market? : Defining and Measuring State Intervention

3.1.1. Defining State Intervention

The Neo-Liberal discourse on the state is basically about whether "free" markets produce socially optimal results, which it thinks is most of the time the case, and whether therefore state intervention may be able to improve the free-market outcomes, which it thinks is rarely the case. Whether or not we agree with the conclusion, the discourse seems straightforward enough, but is it? This question may look stupid. Don't we know that a "free" market is a market without state intervention? Of course, the argument may go, we may have disagreements on which is a "good" state intervention and which is a "bad" one, but don't we all know what state intervention means? I am not actually sure that we do. The trouble is that the same state action can be, and has been, considered an "intervention" in one society but not in another (which could be the same society in a different point of time). Why is this? Let me answer this question with a few examples. First, let us take the case of child labour. Few people in the OECD countries at present would consider the ban on child labour as a state intervention "artificially" restricting entry into the labour market, whereas many Third World capitalists (and indeed the capitalists in the now-OECD economies in the late 19th and the early 20th century) regard it as just that. In the advanced countries, the rights of the children not to toil but to be educated are so totally accepted, and have been incorporated into the structure of (property and other) rights and obligations underlying the labour market (as the right to self-

ownership has been, since the abolition of slavery), they are *not* a matter of policy debate (i.e., there is no debate on whether the ban on child labour is "efficient" in some sense). In contrast, in the developing countries (of today and yesterday), such rights of children are not so totally accepted, and therefore state action regarding child labour is considered an "intervention", whose impact on "efficiency" is still a *legitimate* subject of policy debate. For another example, many environmental standards, which were widely criticised as unwarranted intrusion on business and personal freedom (e.g., automobile emission standards) when they were first introduced in the OECD countries not so long ago, are these days rarely regarded as "interventions". Therefore there would be few people in the OECD countries who would say that their country's automobile market is *not* a "free" market because of these regulations. In contrast, some developing country exporters who do not accept such stringent environmental standard as "legitimate" may consider them as "invisible trade barriers" that "distort" the market. Still for another example, many Neoclassical economists who criticise minimum wages and "excessively" high labour standards in the advanced countries as unwarranted state interventions that "artificially" set up entry barrier into the labour market do not even regard the heavy restrictions on immigration that exist in these countries as a state intervention (not to speak of supporting it), although immigration control sets up an "artificial" entry barrier into the labour market as much as the above-mentioned "interventions" do. This contradictory attitude is possible only because these economists believe in the right of the existing citizens of a country to dictate the terms of the non-citizens' participation in "their" labour market, without explicitly stating their "political" position on this matter. The examples can go on, but point is that, depending on which rights and obligations are regarded as "legitimate" by the members of the society, the same action could be considered an "intervention" in one society and not in another. And once something is not even considered to be an "intervention" in a particular society at a given time (e.g., ban on child labour or slavery in the OECD countries), debating their "efficiency" becomes politically unacceptable - although here is no God-given reason why this should be the case. The corollary is that, depending on the rights-obligations structure, the same market with the same state "intervention" in the same area - for example, regarding child labour - can be seen as "free" (from state intervention) in one society and not in another. So, therefore, if we want to decide whether a particular market is "free" or not, we need to understand the underlying institutions which define the rights-obligations structure for the participants in the relevant market (and indeed certain non-participants, when it involves "externalities"). The institutions that need to be understood in this context will include, among other things: (i) the formal and informal rules that govern the way in which interests are organised and exercised (e.g., rules on political associations, rules on incorporation, rules on lobbying); (ii) the formal and informal "ideologies" relating to the notions such as "fairness" and "natural rights" that prevail in the society (e.g., rights for everyone to self-ownership, rights for children to education); (iii) the formal and informal institutions that determine how the rights-obligations structure could be changed (e.g., procedures for

legal changes, social customs about when and how some *de facto* rights/obligations can become "legitimate", if not necessarily legalised). Thus, the apparently simple exercise of defining what is a "free" market (and what constitutes "state intervention") is not so obvious any more - and this is, to repeat, even *before* we can discuss whether some markets are "failing" and therefore state intervention may make them "more efficient". From the institutionalist perspective, we may even say that defining a free market is at the deepest level a pointless exercise, because no market¹² is in the end "free", as all markets have some state regulations on who can participate in which markets and in what terms. It is only because some regulations (and the rights and the obligations that they are creating) can be so totally accepted (by those who are making the observation as well as by the participants in the market) that some markets appear to have no "intervention" and therefore be "free".

3.1.2. How do We Measure State Intervention and Why does It Matter? For the purpose of international and historical comparison, people have used some quantitative measures of state intervention. At one level, this seems a straightforward exercise. However, how good a measure of state intervention is depends on the theory (of state intervention) that underpins it. Therefore, we need to look beyond the "numbers" that are supposed to measure the extent of state intervention and analyse the theories that lie behind those numbers. Let us explain what we mean by this. Traditionally, the most popular measures of the degree of state intervention have been the total government budget as a ratio of GDP and the share of the public enterprise (PE) sector in GDP (or total investment). It may be true that these measures give us as good an idea of how "big" the state sector is but it is not true that they are good indicators of the degree of state intervention. This is because a "big" government is not necessarily a more "interventionist" government. The point is very well illustrated by the East Asian countries of Japan, Korea, and Taiwan. On the basis of these traditional measures, until recently many people believed that we could "objectively" establish that the East Asian countries are "non-interventionist" (e.g., World Bank, 1991, p. 40, Box 2.2.). And except for the (conveniently ignored) fact that Taiwan has one of the largest PE sectors in the non-socialist, non-oil-producing world, this observation does not seem to be too far from the truth - that is, as far as we accept that the "vision" of the role of the state that lies behind these measures correctly reflects the actual role of state intervention in these countries. However, the mode of state intervention in East Asia has been quite different from what is envisaged in the "vision" that lies behind these traditional measures, and thus they "wrongly" measure the extent of state intervention in East Asia. In the "traditional" vision, the state exercises its control basically through the ownership of the means of production, which is (wrongly) equated with the control over its use, and the reallocation of resources via taxes and subsidies, for example, in the manner prescribed in welfare economics. However, state intervention in East Asia has. The ratio of government expenditure to GDP for Japan in 1985 was 33%, far lower than those in other industrial nations except the US (37%). Corresponding figures include 47% for Germany, 48% for the UK, 52% for France, and 65% for Sweden (World Bank, 1991, p. 139, Table 7.4). In the case of Korea,

the ratio of *central* government expenditure to GNP in 1989 was 16.9%, a figure substantially lower than those for other semi-industrialised countries. Corresponding figures were 21.2% for Mexico, 30.6% for Brazil, 32.5% for Chile, and 33% for South Africa (World Bank, 1991, pp. 224-5, Table 11). Comparable data for Taiwan is not readily available. As of the mid-1970s (1974-77), the share of public enterprise output in GDP in Korea was around 6.4% and that in Taiwan around 13.6%. The average for developing countries was 8.6%. Korea, then, was somewhat less interventionist than the average on this account (but higher than Pakistan (6.0%), the Philippines (1.7%), Argentina (4.8%), which are all regarded to be cases of failed state intervention), and Taiwan substantially above-average interventionist. The corresponding figure for Japan is not available, but on the basis of the share of the public enterprise sector in gross fixed capital formation, Japan (11.6%) as of the mid-1970s was of about average interventionism amongst industrialised countries - the average being 11.1% (see Short, 1984, Table 1). A more recent estimate by the World Bank puts the share of public enterprise sector in GDP for the 1978-91 period at 6.9% for Taiwan and at 10.6% for Korea, when the unweighted average of the corresponding figures for 40 developing countries in the sample was 10.9% (World Bank, 1995, Table A.1.). However, in light of other qualitative evidence, the World Bank figure seems to grossly underestimate the importance of public enterprises in Taiwan. In my view, this may be due to the fact that there are many "public" enterprises that are owned by the ruling Kuomintang Party, which may be officially classified as "private" enterprises. Unfortunately, I have not been able to acquire any systematic data on this been conducted less through state ownership and budgetary outlays, but more through measures which need little state ownership or budgetary outlays. They include: (i) regulatory measures (on entry, capacity, price, technology, etc.); (ii) the state's influence on bank lending decisions (especially in Korea and Taiwan, the majority of the banks have been state-owned); and (iii) various "informal" channels of influence on the business sector (a manifestation of what Evans describes as "embeddedness" of these states; see Evans, 1995). The example does not, in fact, stop in East Asia. For example, some commentators point out that the US federal state, despite its *laissez faire* rhetoric, has strongly influenced the country's industrial evolution through defence procurement programmes and defence-related R&D contracts - especially in industries like computer, telecommunication, and aviation (Johnson, 1982). So, again, the prevailing vision of the role of the state, where "defence" is accepted as one of the "minimum" functions of the state (almost shading into "non-intervention"), makes people underestimate the importance of the US federal government in the country's industrial development. The point that we are trying to illustrate with the above examples is that how we measure state intervention matters, because the particular measures that we use embody a particular vision of the role of the state which may not be universally applicable, because the institutional assumptions behind that vision may not hold in those contexts other than the one from which that vision emerged. Unless we recognise that different measures of state intervention re based on different theories on the role of the state, which

embody different assumptions about the institutions and the political economy of state. The most recent and striking example of this comes from the aviation industry. The repeated rejections by the US federal government of applications from McDonnell Douglas for a number of critical *defence* projects have damaged the latter's profits so badly that it had to merge with its major rival, Boeing, changing the fate of the country's, and indeed the world's, *civil* aviation industry. Intervention, our empirical investigation of the role of the state will be constrained by the limitations of the theoretical perspective that lies behind the "measures" of intervention that we use.

3.2. What does Market Failure Mean and How Much does It Matter?: "Rival Views of Market Society"

3.2.1. When does the Market Fail?

The term, "market failure", refers to a situation when the market does not work like what is expected of the "ideal" market. But what is the ideal market supposed to do? Given the current domination of Neoclassical economics, the ideal market is usually equated with the "perfectly competitive market" in Neoclassical economics. However, the Neoclassical theory of the market is only *one* of the many legitimate theories of how the market works (and therefore what we can expect from the ideal market and therefore when we can say a market has "failed") - and not a particularly good one at that. In other words, there are, to borrow Hirschman's phrase, many different "rival views of market society" (Hirschman, 1982a). And therefore the same market could be seen as "failing" by some people while others regard it as "normal" or even "succeeding", depending on their respective theories of the market. Let us illustrate this point with some examples. For example, many people think that one of the biggest "failures" of the market is to generate "unacceptable" level of inequality (whatever the criteria for "acceptability" may be). However, in Neoclassical economics, this is not a market "failure", because the "ideal" Neoclassical market is not assumed to generate equitable income distribution in the first place. This is *not* to deny that many well-intentioned Neoclassical economists may dislike the income distribution prevailing in, say, Brazil, and may support some "non-distortionary" lump-sum income transfers, *but* to point out that even they would argue that an equitable income distribution is simply not something that the market should be expected to generate and therefore the issue is beyond economic "science". For another example, a "non-competitive" market is one of the most obvious examples of a "failing" market for Neoclassical economics, while the Schumpeterian theory (and before it the Marxian theory) argues that the existence of "non-competitive" (in the Neoclassical sense) markets is an inevitable, if a secondary, feature of a dynamic economy driven by technological innovation. Thus, a classic example of market failure in the Neoclassical framework, namely, the non-competitive market, is regarded as an inevitable feature of a "successful" dynamic economy, according to the Schumpeterian perspective or to put it differently, a market which is "perfect" in the Neoclassical sense (e.g., no participant in the market has any market power) may look like an absolute "failure"

to a Schumpeterian because it lacks technological dynamism. The point that we have just tried to illustrate with our examples is that, when we talk about "market failures", we need to make it clear what we think the "ideal" market is capable of doing. Otherwise, the concept of market failure can become so elastic that it means hundred different things to hundred different people. Thus, where one person sees a "perfection", another person can see a miserable "failure" of the market, and *vice versa* (the above example about monopoly illustrates this point very well). Only when we make our "theory of the market" clear, we can make what we mean by "market failure" clear.

3.2.2. How Much does the Market Failure Matter? Recall Schumpeter's famous metaphor that the relationship between the efficiency gains from competition through innovation and that from (Neoclassical) price competition was "as a bombardment is in comparison with forcing a door" (Schumpeter, 1987, p. 84). This, needless to say, does not exclude the possibility (which is often realised) that an economy may be full of monopolies but is undynamic. Now, how much does "market failure" matter, however we may define it? The short answer is that it would matter greatly for the Neoclassical economists while it may not matter so much for other people, especially the institutionalist economists. Neoclassical economics is an economics about the market (or more precisely not even that - it is really about the barter exchange economy, where, to borrow Coase's analogy, "lone individuals exchanging nuts and berries on the edge of the forest"; Coase, 1992, p. 718). In Neoclassical theory, even the firm exists only as a "production function", and not as an "institution of production". Other forms of institutions that make up the modern capitalist economy (e.g., formal producer associations, informal "networks", trade unions) figure, if they ever, only as "rigidities" that prevent the proper functioning of markets (for a criticism of the view of non-market institutions as "rigidities", see Chang, 1995, whose Spanish translation appears in Chang, 1996). Therefore, for the Neoclassical economists, for whom "the market" is essentially "the economy", if the market fails, the economy fails. And if the economy fails, the state has to step in, as no intermediate institutions or organisation have a legitimate place in their scheme. In contrast, for the institutionalist economists, who regard the market as only one of the many institutional mechanisms that make up the capitalist economic system, market failures may not matter as much, because they know that there are many institutional mechanisms other than markets through which we can organise, and have organised, our economic activities. In other words, when most economic interactions in the modern industrial economy are actually conducted *within* organisations, and not between them through the market (Simon, 1991), the fact that some (or even many) markets are "failing" according to one (that is, Neoclassical) of many possible criteria, may not really make a big difference for the performance of the capitalist system as a whole. For example, in many modern industries where there are high incidences of monopoly and oligopoly, the market is "failing" all the time according to the Neoclassical criterion, but at the same time these industries were often very "successful" in the Schumpeterian sense that they generated high productivity growth and

consequently high standards of living. Such outcome was due to the "success" of modern business organisations which enabled the coordination of a most complex division of labour - so, where Neoclassical economists see a "market failure", other economists may see an "organisational success" (Lazonick, 1991). And if this is indeed the case, state intervention in these markets, especially of the Neoclassical anti-trust variety, may not be very necessary, and indeed under circumstances may actually harm the economy. The point is not that market failures do not exist or that they do not matter at all on the contrary, the real world is full of market failures even by Neoclassical standard (see section 2.2.) and they do matter. The real point is that the market is only one of the many institutions that make up what people call "the market economy", or what we think is better to be called "capitalism". The capitalist system is made up of a range of institutions, including the markets as institutions of exchange, the firms as institutions of production, and the state as the creator and regulator of the institutions governing their relationships. Thus, focusing on the market (and market failure), as Neoclassical economics does, really gives us a wrong perspective in the sense that we lose sight of a large chunk of the economic system and concentrate on one part only.

3.3. "In the Beginning, There Were Markets."?: The Market Primacy Assumption

More recently, the Neoclassical economists have started to discuss the workings of non-market institutions, especially the firm (transaction cost economics; e.g., Williamson, 1975) and the state (the "government failure" literature; e.g., Krueger, 1990). However, these analyses have important shortcomings as these institutions are analysed as "quasi-markets" ultimately based on voluntary contracting (see Vira, 1997). One thing that distinguishes even the most enlightened and open-minded Neoclassical economists from the truly institutionally-conscious economists is their belief in what I call the market primacy assumption. In their view, "in the beginning, there were the markets" (Williamson, 1975, p. 20), and state intervention, organisations, and other institutions are seen as man-made substitutes which emerged only after the defects in the market ("market failure") became unbearable (Arrow, 1974, is the most sophisticated example of this view). The most obvious example of this market primacy assumption is the Contractarian "explanation" of the origin of the state. In this view, the state has emerged as a solution to the "collective action problem" of providing the "public good" of law and order (especially the security of property), which is seen as necessary (and often sufficient) for markets to function at all (Nozick, 1974; Buchanan, 1986). Thus, in this view, even the very existence of the state is explained according to the logic of "market failure" in the sense that it is seen as having emerged only after the market has failed to provide law and order due to the "public goods" problem - an explanation which is obviously contrary to the historical truth and therefore can only be seen as an "ideological" defence of an "unjust" system (for a criticism, see Chang, 1994a, ch. 1). At this point, we must emphasise that the fact that someone attributes institutional primacy to the market does *not*

necessarily mean that he/she endorses a minimal state view, as the problem here is *not* really about where the right "boundary" between the state and the market should lie. There are many who start (at least implicitly) from the market supremacy assumption but are keenly aware of the failings of the market and willingly endorse a relatively wide range of intervention. Indeed, as we pointed out earlier (section 10 Williamson defends this starting assumption on the ground of "expositional convenience", arguing that the logic of his analysis would be the same even if the starting assumption was that "in the beginning, there was central planning" (pp. 20-1). However, as we shall see below, this apparently innocuous assumption has a lot of important theoretical ramifications and policy implications.), if these open-minded Neoclassical economists began to take their own logic to the limit, they could end up endorsing all kinds of state intervention. However, they would still see state intervention, or for that matter any other solution based on non-market institutions (e.g., hierarchical organisations like firms), as "man-made" substitute for the "natural" institution called market. The point is that, in the beginning, there were *not* markets. Economic historians have repeatedly shown us that, except at the very local level (in supplying basic necessities) or at the very international level (in luxury trade), the market mechanism was *not* an important part of human economic life until recently. In fact, although even Joseph Stiglitz, one of the most enlightened Neoclassical economists of our generation, says that "markets develop naturally" (Stiglitz, 1992, p. 75), the emergence of markets was almost always deliberately engineered by the state, especially in the early stage of capitalist development. Karl Polanyi's classic work shows how even in the UK, where the market economy is supposed to have emerged "spontaneously", state intervention played a critical role in the process. He argues that "the road to the free market was opened and kept open by *an enormous increase in continuous, centrally organised and controlled interventionism* [italics added]. To make Adam Smith's 'simple and natural liberty' compatible with the needs of a human society was a most complicated affair. Witness the complexity of the provisions in the innumerable enclosure laws; the amount of bureaucratic control involved in the administration of the New Poor Laws which for the first time since Queen Elizabeth's reign were effectively supervised by central authority; Lange's defence of socialist planning may be an extreme example, but Schotter's argument for state provision of basic goods (on the ground that an inadequate amount of consumption of such goods can create "externality" in the form of crime), which we cited earlier, is a less extreme example of how the logic can be carried much beyond where most Neoclassical economists are currently willing to take it to or the increase in governmental administration entailed in the meritorious task of municipal reform" (Polanyi, 1957, p. 140). Also in the case of the US, the early intervention by the state in establishing property rights, providing critical physical infrastructure (especially railways and telegraphy), funding of agricultural research, and so on, were critical for its success in early industrialisation (Kozul-Wright, 1995; even the World Bank now recognises this –see the World Bank, 1997, p. 21, Box 1.2). Most importantly, the US was the home of the idea of infant

industry protection (Freeman, 1989), and was indeed the most heavily protected economy among the industrial countries for around a century until the Second World War (see World Bank, 1991, p. 97, Box Table 5.2; Kozul-Wright, 1995, p. 97, Table 4.8). Moving beyond the UK and the US, we realise that there is virtually no country, except Hong Kong, which achieved the status of an industrialised country without at least some periods of heavy state involvement in the developmental effort. The exact forms of intervention varied - "pre-emptive" welfare state in Bismarckian Germany, postwar French industrial policy, early Swedish state support of research and development, transformation of the Austrian manufacturing sector since World War Two And he continues: "Administrators had to be constantly on the watch to ensure the free working of the system. Thus even those who wished most ardently to free the state from all unnecessary duties, and whose whole philosophy demanded the restriction of state activities, could not but entrust the self-same state with the new powers, organs, and instruments required for the establishment of *laissez-faire* [italics original]" (p. 140) During this period, few countries had tariff autonomy either because of outright colonial rule or because of "unequal treaties" - for example, Japan got tariff autonomy only in 1899 when all its unequal treaties expired. Of the countries with tariff autonomy, the US had by far the highest tariff rates. Its average tariff rates since the 1820s was never below 25%, and usually around 40%, when those in other countries for which the data are available, such as Austria, Belgium, France, Italy, and Sweden, were rarely over 20%. For detailed figures, see World Bank (1991, p. 97, Box 5.2.) public enterprise sector, the well-known state-led developments of the East Asian countries - but the fact remains that all successful developmental efforts involved substantial state intervention. So if virtually all now-advanced countries, with the possible exceptions of Britain at certain phases and Hong Kong, developed in some "unnatural" way which involved heavy state intervention, it seems questionable whether there is any point in calling the market a "natural" phenomenon. What we have just discussed is not simply of historical interest. Whether or not we accord primacy to the market institution makes a critical difference on how we design developmental policies. For example, the severe economic crises that many former Communist countries which have opted for a "big bang" reform have experienced during the last several years is one striking example which shows how the establishment of a well-functioning market economy is impossible without a well-functioning state (see Chang & Nolan, 1995, whose Spanish translation appears as Chang & Nolan, 1996). In fact, if the markets evolve so "naturally" as the Neoclassical economists believe, these countries would not be in such trouble now. Likewise, the developmental crises that many developing countries have gone through during the last two decades or so also show how dangerous it is to assume the primacy of market institutions and believe that it will naturally develop as far as the state does not "interfere" with its evolution. The assumption of market primacy has a lot more serious implications than it first appears to have.

3.4. Can We Rid the Market of Politics?: The Disguised Revival of the Old Liberal

Politics

One major assumption behind the Neo-Liberal doctrine is the belief that politics allows "sectional" interests to "distort" the "rationality" of the market system and therefore is something that has to be purged from the market. Criticising the naivete of welfare economics which assumed the state to be the all-knowing, all-powerful social guardian, the "New Political Economy" of Neo-Liberalism tried to demonstrate how politics is an inevitably corrupting force on the economy. The Neo-Liberal political economists have argued that therefore we need to "depoliticise" the economy by restricting the scope of the state and by reducing the room for policy discretion in those few areas where it is allowed to operate, for example, by strengthening the rules on bureaucratic conduct and by setting up "politically independent" agencies bound by rigid rules (e.g., independent central bank, independent regulatory agencies). There have been many powerful criticisms of Neo-Liberal political economy, and we do not feel that this is a place to go into the details (e.g., see, in chronological order, Toye, 1987; King, 1987; Gamble, 1988; Toye, 1991; Chang, 1994a and 1994b; Evans, 1995; Chang & Rowthorn, 1995a and 1995b, both whose translation appear in Chang, 1996). However, we want to point out some basic issues in order to highlight some fundamental problems in the Neo-Liberal (and indeed Old Liberal) view of politics.

3.4.1. All Prices are "Political". First of all, the establishment and distribution of property rights and other entitlements that define the "endowments" that Neoclassical economics takes as given is a highly political exercise. The most extreme example will be the various stories of "original accumulation" such as the Great Plunder or the Enclosure in the early days of British capitalism or the "shady" deals that dominate the privatisation process in many ex-communist countries these days, but the continuous political campaigns that established environmental rights and consumer rights as legitimate rights at least in the OECD countries are less dramatic but perhaps equally important examples. Moreover, there are practically no prices in reality which do not have some "political" element in it. To begin with, two critical "prices" which affect almost every sector, namely, wages and interest rates, are politically determined to a very large degree. Wages are affected not only by minimum wage legislations, but also by various regulations regarding labour standards, welfare entitlements, and most importantly immigration control. Interest rates are also highly political prices, despite the guise of "depoliticisation" that those who support central bank independence want to give to the process of interest rates determination. The recent debate in Europe on the relationship between political sovereignty and autonomy in monetary policy, which was prompted by the approaching European Monetary Union, shows this very clearly. When we add to them those numerous regulations in the product markets regarding safety, pollution, import contents, and so on, there is virtually no price which is "free from politics". Of course, all these are not to deny that a certain degree of depoliticisation of the resource allocation process may be necessary. For

one thing, unless the resource allocation outcome is at least to a degree accepted as "objective", the political legitimacy of the market-based system itself may be threatened. Moreover, an enormous amount of "transaction costs" would be incurred on search and bargaining activities if every allocational decision is regarded as negotiable, as it was in the case of the ex-Communist countries. However, this is not to say that no price under no circumstances should be subject to political negotiations, because in the final analysis, there is no price which is really free from politics. We were reminded of this clearly in the British coal crisis in the early 1990s, where the British coal-miners were told to accept the logic of the "world market" and face mine closures with grace. However, the world market prices, which the then British government argued to be beyond political negotiation, turned out to be determined by the "political" decisions of the German government to give subsidies to their coal, of the French government to allow the export of their subsidised nuclear electricity, and of the many developing country governments to allow, at least *de facto*, child labour in their coal mines.

3.4.2. De-Politicisation: The Disguised Revival of Old Liberal Politics

If what appear to be "objective" outcomes of "impersonal" markets are in the end the results of certain (explicit and implicit) "political" decisions about property rights, entitlements, and prices, the Neo-Liberal proposal for "de-politicisation" of the economic policy-making process as a means to restore "economic rationality" also cannot be taken at its face value. One basic problem with the Neo-Liberal proposal for de-politicisation is that the "rationality" that such exercise wants to "rescue" from the corrupting influences of politics can only be meaningfully defined with reference to the existing institutional structure, which is itself a product of politics (Vira, 1997, for a further exposition of this point). So when the basic institutional parameters of the economy have been, and can only be, set through an "irrational" political process, a call for de-politicisation of the economic process on "rationality" ground rings hollow. Another problem with the Neo-Liberal proposal for de-politicisation is that its politics is *not* what it pretends to be. The call for de-politicisation is often justified in a populist rhetoric as an attempt to defend the "silent majority" from the greedy politicians and powerful interest groups. However, the diminution of the legitimate domain of politics that de-politicisation will bring only serves to further diminish what little political influence that these underprivileged people have in modifying the market outcomes, which, we repeat, are heavily influenced by politically-determined institutional parameters. Thus seen, the Neo-Liberal call for the de-politicisation of the economy aims to revive the Old Liberal politics in a disguised form (Bobbio, 1990, provides an excellent anatomy of the Old Liberal politics). Like the Neo-Liberals, the Old Liberals believed that allowing political power to those who "do not have a stake" in the existing institutional arrangements will inevitably result in the modifications of either such arrangements or of its outcomes mediated through the market. However, unlike the Old Liberals, who could openly oppose democracy, the Neo-Liberals cannot do that, so they try to do it by arguing against "politics" in general and making proposals which ostensibly seek to reduce the influence of those "untrustworthy politicians" but ultimately aims to diminish democratic control itself

(e.g., proposals for "independent" central bank or regulatory agencies). The last, but not least, problem with the call for de-politicisation is that it may not be a politically feasible recommendation. For good or bad reasons, all countries have accumulated politically organised groups and have developed certain (at least implicitly accepted) ways to "politically" modify certain market outcomes. Some of these, of course, could be easily eliminated, but others may be so entrenched that they may be eliminated only at very high political and economic costs. Hence the apparent paradox that radical economic liberalisation frequently requires harsh authoritarian politics, in order to achieve the high degree of de-politicisation that is required for such policy, as graphically exemplified by the liberalisation attempt by the Pinochet regime in Chile (also see Gamble, 1988). But the truth is that, however harsh the political regime which pursued it may have been, de-politicisation has never been, and can be, complete in practice, and even backfire.

4. Conclusion: Towards an Institutionalist Political Economy

After pointing out some internal fault lines and indeterminacy in the Neo-Liberal intellectual agenda, we critically examined some of its basic concepts and assumptions from the institutionalist point of view. As we have repeatedly emphasised, the real point we should also note that political activities are often ends in themselves and people may derive value from the activities *per se* as well as from the products of such activities (see Hirschman, 1982b, pp. 85-6) of our criticism is *not* that Neoclassical theory is too little (or for that matter too much) interventionist. As we have pointed out repeatedly, a full-blooded Neoclassical economist can legitimately endorse anything from a minimal state to socialist planning, depending on his/her assumption about technological (and implicitly property rights) conditions. What we are really trying to argue is that the way in which the relations between the state and the market (and other institutions in those rare occasions when they feature) is envisaged in Neoclassical economics prevents an adequate understanding of some fundamental issues surrounding the role of the state. We propose that an approach which may be called "institutionalist political economy" should be the way forward, and suggest some elements of this theory. Our starting point should be to reject the assumption of market primacy that underlies Neoclassical economics. As we pointed out earlier, Neoclassical economics sees the market as a "natural" institution (if it is ever acknowledged that it is an institution) which spontaneously emerges, but sees other institutional arrangements, be they state institutions or firms (or "hierarchies"), as emerging only when the market "fails". However, saying that the market emerged as a result of the failure of "planning" (not necessarily by the state, but also by other organisations) or "hierarchy" is probably closer to the historical truth, which of course is much more complex. We should see the market as an institution which, both logically and historically, has no primacy over other institutions, and therefore as "natural" (or, for that matter, as "artificial") as other institutions. Only when we do that, will we be able to see the relations between market, state, and other institutions in a balanced and historically more accurate way. Secondly,

we should remember that there are more than one views of what the "ideal" market can do, and that the Neoclassical view is only one of many plausible views I have attempted to develop this theory in a number of my previous works. See Chang (1994), Chang (1995), Chang & Rowthorn (1995b), and Chang (1997)..28 - and not a particularly good one at that. Accordingly, it becomes possible that the same market may be seen as failing by some with one "theory of the market" and as succeeding by others with another theory. Only when an economist makes his/her own theory of the market explicit, we will be able to judge the merit of his/her view that the market is "failing" (or not) and thus to accept or reject the "solution" to the problem, whether it is some kind of state intervention or the establishment of some non-market institutions and/or organisations. Thirdly, we need to realise that the Neoclassical theory is essentially a theory of the market (and a very schematic and misleading one at that). However, capitalism, as a socio-economic system, is more than a collection of markets, and is made up of many institutions, including, among others, the firms as institutions of production, the markets as institutions of exchange, the state as an institution of politically addressing collective interests, and various producer and consumer groupings (e.g., conglomeration of firms, producer associations, trade unions, purchasing cooperatives, subcontracting networks). Thus seen, market failure becomes, somewhat paradoxically, less of a problem in the institutionalist framework than in the Neoclassical framework, because in the former framework even widespread and severe market failures would not necessarily suggest that the whole "economy" is failing, whereas the latter framework would see it as just that. Fourthly, we need to understand that the market is a fundamentally political construction. A market cannot be defined except with reference to the specific rights/obligations structure that underpins it. And since these rights and obligations are determined through a political process, and not by any "scientific" or "natural" law as Neoclassical (and other Neo-Liberal) commentators want us to believe, all markets have a fundamentally "political" origin. Therefore, it is impossible to decide whether a market is "free" or not, without specifying the position of the person(s) making that statement regarding the legitimacy of the current rights/obligations structure. Added to this are the more explicit administrations of prices that are found in many markets through price caps, price ceilings, state setting of certain prices, and quantity controls. While some prices may be more politically administered than others in a given context, ultimately no price is free from politics. This brings us to our fifth element in the institutionalist theory on the role of the state, namely, the need to build a theory of politics which takes a much more broad, balanced, and sophisticated view of politics than what is offered by Neo-Liberalism. Neo-Liberal thinkers see politics as a market-like process, where material benefits are exchanged for political supports, but as a process that ultimately corrupts the "rationality" of the market, because of the discretionary powers that it confers to those who can make and/or influence political decisions. However, this is a fundamentally jaundiced view of politics. The main problem with this view is that the "rationality" that it wants to preserve through "de-politicisation of the economy", which is in fact an

euphemism for emasculating democracy, makes sense only in relation to the underlying rights/obligations structure, which is a fundamentally political construction. Thus, we need a theory of politics which is not merely an extension of market logic. Lastly, we need to pay attention to the institutional diversity of capitalism (Albert, 1991; Berger & Dore (eds.), 1996; Chang, 1997). Unfortunately, Neoclassical economics has little to say about the issue of institutional diversity, because it is a theory of an abstract market economy, or rather of an "exchange economy" based on barter, as we have pointed out earlier. Partly for this reason, the Neo-Liberal economists have found it difficult to admit that there are many ways for the state to intervene other than through taxes/subsidies and public ownership, thus misrepresenting, although for the issue has been discussed in various areas, including: the organisation of finance (capital-market-based vs. bank-led vs. state-dominated); corporate governance (U-form vs. M-form; H-firm or A-firm vs. J-firm); wage bargaining structure (centralised vs. decentralised); union organisation (centralised vs. industrial vs. company vs. craft); mode of state intervention (Anglo-American, East Asian, Scandinavian, etc.); industrial policy (general vs. selective). For more details, see Chang (1997) somewhat different reasons, certain countries as being much less interventionist than they actually are (e.g. Japan, Korea, the USA; see section 3.1.2.). In discussing this issue of institutional diversity, understanding the role of the state is critical, not simply because the international differences in the mode of state intervention is a major source of this diversity, but also because the exact institutional forms of, say, corporate governance or labour representation, will have to be legitimatised in the eyes of the (current and prospective) market participants, either through formal legislation by the state or through informal support from the state. Constructing an institutionalist political economy which satisfied all the above criteria (and I am sure that there are more important criteria that I did not think of is surely a tall order. However, without a radical restructuring of the ways in which we conceptualise the market, the state, and politics, and the ways in which we analyse the relationships between them, we will not be able to overcome the Neo-Liberal world view, which has dominated the political and the intellectual agenda of our time, in my view with many negative consequences.

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Review Questions

1. “The state is no more assumed to be an impartial, omnipotent social guardian and is now analysed either as a “predator” or as a vehicle for politically powerful groups,” – place your own observation on the statement.
2. Do you agree with the statement that “the Neo-Liberal doctrine is in fact a very heterogeneous and internally inconsistent intellectual edifice?”
3. What is a free Market? How do we measure state intervention and Why does It Matter?
4. What does market failure mean and how much does it matter?
5. “Can we rid the market of politics?” – analyse.
6. Do you agree with view that “all prices are political”?
7. Write a criticism of “institutionalist political economy.”

Lesson 3: Role of the Civil Society

After studying this lesson, you will be able to:

- Understand the role of the 'civil society' in Bangladesh in terms of political and developmental discourse.
- Explain the gaps between promises and reality according to Rehman Sobhan.
- Make appropriate comment on the statement “a strategy of a more egalitarian development is not only socially just, it would also make Bangladesh more competitive in a fast globalizing economy”.

Introduction

The idea of 'civil society' has achieved prominence in political and developmental discourse over the past two decades. Civil society, particularly by the development partners, has been widely seen as an increasingly crucial agent for limiting authoritarian government, strengthening popular empowerment, reducing the socially atomizing and unsettling effects of market forces, enforcing political accountability, and improving the quality and inclusiveness of governance. With the end of the Cold War and the ideological rationale for aid, donor enthusiasm for civil society has been reflected in a growing number of programmes and projects aimed both at creating and strengthening an intermediary stratum of non-governmental organisations and in fostering partnerships between such organisations, government and business. Whilst the market seemed to hold its sway, the concept of civil society began to enter academic discourse to conceptualise effective challenges to oppressive state systems.

Definitions of 'civil society' are diverse and often rooted in alternative social and political philosophies. The recent conception of civil society can be traced to that of an intermediate associational realm situated between the state on the one side and the basic building blocks of society on the other (individuals, families and firms). The contribution of civil society to good governance may have been summarised in Manor (1998)⁷ under four headings: public policy and decision making; enhancing state performance; transparency and information; and social justice and the rule of law.

Public Policy and Decision Making: Civil society organizations can play a role in mobilizing particular constituencies to participate more fully in politics and public affairs. Wealthy and socially dominant groups are better able to organize themselves by virtue of superior resources while poor and socially disadvantaged groups -- marginal peasants,

⁷ The section draws on Manor, James, “Civil Society and Governance: A Concept Paper,” presented as the basis for a research project on civil society and governance, funded by the Ford Foundation, and coordinated by and held at the Institute of Development Studies, University of Sussex, England, June 1998.

sharecroppers, landless labourers, artisans, informal sector workers, urban slum dwellers, disabled people and certain categories of women -- are usually much less able to exercise influence over public policy and resource allocations.

Transparency and Information: Civil organizations are thought to contribute to better governance by improving transparency and increasing the availability of information about the making and implementation of government policy.

Enhancing State Performance: The quality and effectiveness of public services and expenditures are integral to good governance. Civil society organizations can contribute by working directly with government in shaping, financing and delivering public services in a variety of ways.

Social Justice, Rights and the Rule of Law: The fourth area where civil society can make a contribution to good governance is in the field of social justice, rights and the rule of law.

Reading for the Lesson

The present lesson concentrates on a selection, an essay written by Professor Rehman Sobhan entitled *Building a Responsible Civil Society: Challenges and Prospects*.⁹

According to Professor Rounaq Jahan¹⁰, the editor of the volume in which Professor Sobhan's article appeared, the author attempts to synthesize the major trends in the polity, society and economy and argues that building on existing political assets and past experiences, the country can recapture the goals underlying the nationalist movement - nationalism, democracy and social justice.

Sobhan counts the tradition of civil society activism, the relatively homogeneous society and the emerging two party system as major political assets. He notes the gaps between the promise and reality and highlights the challenges e.g. the need for private finance for party building and election campaign that has made the political parties captives of special interest groups, the political confrontation between the two dominant parties that has resulted in "illiberal democracy", the growing donor dependence that has driven the state to surrender ownership of its own development agenda and has increased the inequalities between the rich and the poor.

⁸ The section draws on Manor, James, "Civil Society and Governance: A Concept Paper," presented as the basis for a research project on civil society and governance, funded by the Ford Foundation, and coordinated by and held at the Institute of Development Studies, University of Sussex, England, June 1998.

⁹ Sobhan, R "Building a Responsible Civil Society: Challenges and Prospects," in Rounaq Jahan (ed) *Bangladesh: Promise and Performance*, Dhaka: University Press Limited, 2000. The essay is reproduced with the permission of the author and editor.

¹⁰ The present introduction is an excerpt of Rounaq Jahan, "Introduction: Bangladesh: Promise and Performance," in Rounaq Jahan (ed) *Bangladesh: Promise and Performance*, Dhaka: University Press Limited, 2000.

Despite these problems Rehman Sobhan believes Bangladesh can overcome its current crisis. He argues that a more proactive civil society and a reorientation of politics and priorities will set the country into a path for democratic governance and a just social order. He posits that the prevailing political practices that emphasize private interest can be challenged if a critical mass of civil society activists join political parties and attempt to change the culture of party politics from within. He underscores the importance of pursuing a strategy of incremental civil society mobilization first around social issues e.g. improving the quality of primary education and health care services and cleaner urban neighbourhoods and then move on to more difficult political issues such as challenging the politically connected muscle-men who terrorize the campuses of educational institutions, the rich businessmen who default on bank loans, powerful bureaucrats and political leaders who are personally corrupt and patronize corruption and so on.

Sobhan believes that a strategy of a more egalitarian development is not only socially just, it would also make Bangladesh more competitive in a fast globalizing economy. He identifies several priority actions, e.g. democratizing human development, upgrading technical skills of both men and women, providing health care to the poor, and creating a stake for the deprived in the development of the economy. He also emphasizes the importance of economic diplomacy and suggests building a workable pattern of relations with neighbouring countries, particularly India for better terms of trade and economic exchanges.

Rehman Sobhan concludes that the new millennium holds out an enormous promise for Bangladesh but the realization of this promise requires structural changes both in politics and society. Civil society has an important role to play in initiating these changes but it needs to first restore a sense of public purpose within itself.

BANGLADESH IN THE NEW MILLENNIUM: BUILDING

A RESPONSIBLE CIVIL SOCIETY

Rehman Sobhan

Introduction

Bangladesh was conceived in hope but born in pain. As we enter the new millennium after 29 years of independence the sense of pain appears to prevail over the sense of hope. For a generation such as ours which lived in hope that an independent Bangladesh would lay the foundations of a democratic, secular, self reliant and egalitarian society based on justice, contemporary Bangladesh remains a far cry from the aspirations of its founding fathers. Our democratic system was held captive in the cantonment for 16 years. The restoration of a pluralist democracy since 1991 has not fulfilled the promise of accountable governance. Secularism was not only eliminated as a pillar of the constitution but we have since become more communal and intolerant of the rights of minorities in our society. Over the years our commitment to nationalism has been eroded not just by our external dependence for resources to underwrite our

development but we have surrendered our autonomy over economic policymaking to our aid donors. Above all we have become less egalitarian as a society to the point where two societies appears to co-exist in one country. This growth in inequality has little to do with efficiency or merit but originates in an unjust social order which rewards malfeasant behavior and provides insufficient incentives to the creative and hardworking elements in society.

In such an environment people have tended to trade their expectation of a better future for their country for the pursuit of private agendas where the self and household delimit our aspirations so that private gain prevails over societal progress. In spite of this erosion of hope and the obsession with private gain enough people remain captivated with the vision of a better Bangladesh to ensure that the flame of hope lit by those who fought for our liberation, however dim it may appear today, remains unextinguished. In particular junctures of time, 21st February, 26 March, 15 August, 16 December, we stoke this flame through bouts of mass remembrance. But the day passes, the emotions die down and we return to our self-centered lives. Such days have thus degenerated into rituals of synthetic remembrance which generates insufficient resonance to sustain a process of renewal in our personal and public affairs throughout the rest of the year.

The real tragedy of contemporary Bangladesh lies in the fact that, viewed from a global perspective, it is a country which in its emergence as an independent state was possessed of a variety of positive assets which could have transformed it into a dynamic, democratic society. Over the years new areas of opportunity have opened up which have kept the embers still glowing in the twilight of our hopes. In the remainder of this paper I will explore some of the contemporary developments and circumstances of Bangladesh which provide some grounds for hope as well as suggest areas of action where such hopes can be translated into action for building a more liveable society. I will structure the paper around three pivotal themes associated with such an agenda for sustaining hope in -Bangladesh – democracy, nationalism and social justice.

Democracy

Bangladesh's political assets

Every major political event in the history of Bangladesh over the last 60 years originated in a process of democratic mobilisation. The liberation of Bangladesh and the more recent overthrow of the Ershad autocracy were sustained by such a process. There was therefore every expectation that the Bangladesh polity would be grounded in a working democracy underwritten by the hunger for democracy of its citizens. Today few people would have reason to feel optimistic about the state of democratic governance in Bangladesh. After a decade of democratic renewal in the 1990s which succeeded 16 years of cantonment *raj* our politics is becoming increasingly dysfunctional. The very institutions of democracy, elections, parliament, political parties show signs of degeneration in their

practises. The culture of intolerance which permeates our polity holds the nation hostage to a confrontational style of politics which is gradually making the democratic process unworkable.

Ironically this process of confrontational politics originates in what should have been the most positive asset for sustaining a democratic system in Bangladesh. Since 1991 Bangladesh has witnessed the consolidation of a viable two party system. This system is anchored by the Awami League elected to power in 1996 and the Bangladesh Nationalist Party (BNP) which was elected to office in 1991 and held office till 1996. Each party operates with a national support base and retains a credible prospect of capturing state power through the electoral process. The amendment to our constitution in 1996 has institutionalised the preconditions for holding such free and fair elections under a non-partisan, caretaker government which leaves the two parties with equal opportunities to solicit the support of the voters. During the election campaigns of 1991 and 1996 it was difficult to predict which party would capture state power. The two elections were recognised to be more free and fair than any election in the last 50 years and was seen by outside observers to compare favourably with elections in our neighbouring countries.

Bangladesh's two party system should have minimised the scope for political instability in contrast to India, Pakistan, Nepal, even some of our South East Asian neighbours. Most of our neighbours either have to cope with the uncertainties associated with a multiplicity of parties sharing state power or remain exposed to the authoritarianism associated with a single party dominated polity. As we read in the papers of ethnic and communal conflicts in India, Pakistan, Sri Lanka, Myanmar, Indonesia or Philippines, Bangladeshis can better appreciate our political good fortune in inheriting a relatively homogenous language and culture which has minimised the scope for identity politics. Whilst we have a large religious minority and a small ethnic minority of tribal people, the unifying legacy of the liberation war and the original commitment to secularism ensured that religious vote banks would not emerge as a factor in national politics. However, the constitutional assault on secularism as well as the failure to recognise the legitimate rights of tribal minorities marked a departure from the secular premise of Bangladesh's national politics. The subsequent reinduction of overtly communal forces into national politics revived the tendency of some parties to project fundamentalist ideas into the national political discourse.

This erosion of Bangladesh's secular tradition has contributed to the suppression of minority identities and diminished opportunities for their political participation. The 1997 Peace Agreement with the *Jumma* or hill people of the *Chittagong Hill Tracts* (CHT) could have emerged as a move to reaffirm Bangladesh's non-communal tradition. But the treaty has been used as a vehicle by opposition political parties to activate communal forces in the polity by focussing on the communal divide between tribals and Bangali settlers in the CHT. This intrusion of communalism could open up fissures in our political landscape which

could in the future expose us to the destabilising tensions afflicting our neighbours.

The crisis of democracy

Unless our principal political parties are willing to practise tolerance in their dealings with their opponents parliamentary democracy will become a constraint rather than a resource for stimulating good governance. A workable two-party democratic system demands tolerance for each others positions, respect for the democratic rights of the opposition and a regular process of consultation both in the functioning of the democratic system as well as in the design of national policy. A majority party, commanding less than 50% of the national vote has to constantly consult with the opposition parties who represent more than 50% of the voters, if the political system is to remain effective. The practise of ‘illiberal’ democracy based on a *winner take all* philosophy may be legally correct but remains politically unsustainable. Where this culture of intolerance amongst the political parties is further aggravated by deep personal antagonism between the leaders of the two principal parties in Bangladesh politics, to the point where minimal political dialogue is not possible, then the system of democracy in Bangladesh could become unworkable.

Already this practise of ‘illiberal’ democracy has contributed to the proliferation of a breed of politicians exclusively preoccupied with private gain where money and arms rather than democratic consent is seen as the route to power. This new breed of politicians are now evolving from the role of foot soldiers into field commanders, in the confrontational environment of contemporary politics, where corruption, violence, mendacity, slander and incendiary rhetoric pollute the vocabulary of politics. It is small wonder that parliament is no longer seen as an arena for intelligent, even coherent discussion of national problems and policies. Nor is there any evidence that our principal political parties are unduly preoccupied with finding solutions to the myriad problems which oppress the ordinary people in Bangladesh.

It is now recognised not just in Bangladesh’s but also by our so-called development partners that a transformation of Bangladesh’s developmental landscape would be unrealisable without a transformation in our political culture. Current producers as well as prospective investors need social and political stability to sustain their entrepreneurship. A visibly malfunctioning democratic system which carries the threat of constantly imploding is not an ideal environment to optimise productivity or initiate long term investment.

Adversarial politics is also aggravating the misgovernance of the economy. Such politics breeds a politicised bureaucracy and a malfeasant system of law and order. These instruments of governance, operating without accountability or transparency, leads to the machinery of state being used as a political resource rather than an instrument of governance. In such a polity the state can neither discharge its regulatory

or its operational role with integrity, impartiality or efficiency and misgovernance is perpetuated.

In such a malfunctioning system decentralised government degenerates into a cliché where local institutions remain powerless because national politicians and bureaucrats remain unwilling to surrender the power and patronage associated with the exercise of centralised power. What passes for local government remains a miniaturised extension of national governance, politicised and corrupted in its incidence because local power remains delegated rather than derived from a system built upon local accountability and resources.

Transforming the political culture

Can anything be done about transforming our political culture and reforming our governance? We have to live with the reality of a two-party political system and should seek to draw upon its advantages rather than live with its liabilities. This recognition of the dominance of two major parties in the polity remains without prejudice to the need for at least two ideologically motivated parties since both our parties, whilst divided by their historical inheritance, remain parties of the political centre. However, within the prevailing bipolar polity in Bangladesh democracy could be well-served by some ideologically inspired diversity. Thus, a unified party of the left committed to the concerns of the deprived segments of the population could present some genuine alternatives to the voters. Such a party could address, within a coherent, workable political agenda, many of the concerns largely espoused today by the NGO community. Such a party, operating as part of a unified political movement shorn of ideological posturings, should find a place in parliament and emerge as the conscience-keeper of the political system. It may also be feasible for a party of the right to emerge which is thereby given space to project the fundamentalist political agenda within the norms of democratic politics rather than as a terrorist conspiracy.

Given the reality of our two-party dominated system major efforts at reform must be focussed on the two principal parties. The prospect of these two political parties reinventing themselves does not, however, appear to hold much promise. Pressure for political change in these parties must, therefore, in large measure originate from civil society. However, those in civil society who would seek genuine political change for better governance in Bangladesh will have to expose themselves to the inconvenience and hazards of political involvement in sufficient numbers to make a difference. Such people will have to join political parties and from within demand a reconstruction of its political culture, including the democratisation of the party. Such a commitment by civil society will not come easily because it involves, effort, risk and above all time, which are more difficult to come by than sitting in seminars, giving statements to the newspapers or even participating in the occasional demonstration. Such an attempt to upgrade the quality of representation in our political parties will generate resistance from enhanced vested interests in the parties. But it is arguable that if such newcomers demonstrate patience, humility and dedication in their commitment to

political work, there remain large numbers of uncompromised political workers and leaders who would be able to draw upon these newcomers as allies in building a modern political party.

Reforming political finances

A major source of the degeneration in our political culture originates in the need for mobilising private funds for financing party and electoral activities. This pursuit of private finance for underwriting party activity makes both parties and their leaders hostage to special interest groups. Much of the corruption and malfeasance in decision-making originates in the need to do favours to such political financiers. These same financiers are now directly entering politics whilst political activists are gradually evolving into businessmen. A peculiar symbiosis now binds politicians, businessmen and bureaucrats together in a collusive relationship which has infected the entire system of governance. Such a system of political financing by its nature, remains devoid of transparency and contributes to the retention of disproportionate power in the hands of party leaders which further weakens the process of inner-party democracy.

Any effort to reform politics from within thus needs to reduce the dependence of the political process on private financiers. One way to break the hold of such financiers is to introduce public funding to underwrite democratic politics through allocations in the national budget. For example, a fixed percentage, say one percent of the total annual revenue, could be allocated every year to both finance the political party organisations as well as their participation in elections. This could put at the disposal of the political parties a sizeable annual budget of around Tk. 2 billion. Through a process of political consultation it would need to be decided how such funds should be disbursed into the political system and who should be eligible for such funds. The arrangement would have to ensure that frivolous claims are not made on this fund by private entrepreneurs or adventurers with no political following. Thus, for example, budgetary allocations could be limited to those parties with enough popular support to ensure their representation in parliament. Budgetary resources could thereby be distributed to the parties in parliament on the basis of their share of the vote in the elections to the national parliament.

Since financing of political activity would originate from the public exchequer its utilisation by a party would demand transparency in the administration and accounting of the funds. This may involve audit of party finances and greater inner party democracy in the disposition of such funds. Such an institutionalised mechanism of political finance need not eliminate the need for private financing of politics but this too should be kept within a ceiling. Disposition of such private funds should also remain fully transparent and governed by law as is the practice in most mature democracies.

The role of civil society

Upgrading the quality of political participation would need to move in tandem with pressures for political reform emanating from a more pro-active civil society. Trade unions, peasant organisations, women's groups, human rights and environmental activists, professional organisation as well as business associations have all become increasingly active in Bangladesh in recent years in seeking remedial action from the government or in pursuit of particularist agendas. Such efforts, whilst realising some gains, have tended to be episodic and have thereby failed to build-up a critical mass to realise substantive change. Such organisations, acting both individually and collectively will, thus, have to commit themselves to civic involvement and advocacy as a full time exercise. Such a surge in civic enterprise involves leadership, entrepreneurship, creative imagination and above all cooperation rather than a quest for private or institutional aggrandisement or as an initiative sustained by donor patronage. Such civil society organisations also need to be made more democratic within themselves, kept accountable to their constituents and transparent in their transactions.

Since the business community is also a part of civil society they must engage themselves not just in the pursuit of their sectoral agendas but concern themselves with the broader aspects of governance. This involves both responsibility to help the community where they do business as well as accountability and transparency in their practises. Thus, the business sector needs to remain more accountable to all its shareholders as well as its workers, to depositors who use private banking services, to local communities where they operate and to the public at large. Where the private sector draws upon public resources or benefits from public policies such a process of public accountability becomes all the more important because such resources have a high opportunity cost. For example, the amount of defaulted loans to the nationalised commercial banks (NCB) could comfortably meet the entire demand for micro-credit in Bangladesh and also finance a corporate stake for the deprived. Misuse of such funds is thus not a private affair of the borrower and the lender but need to be accounted to the public, most of whom do not have access to such funds from the NCBs.

A pro-active civil society means that Bangladeshis will need to come out of their drawing rooms, seminars and coffee shops in increasing numbers to assert their rights as voters and citizens. Parents of children in government primary schools and users of primary health care centres must come forward to demand effective service. Citizens in every locality of Bangladesh must challenge the police to provide honest and effective law enforcement. Municipalities must be pressured to provide clean neighbourhoods. This exercise of civic power will need to be escalated to make ministers, parliamentarians and bureaucracy accountable for their every action or inaction so as to make them count the political costs of malgovernance. If our citizens cannot make the effort to demand better governance as a matter of right, then we must be prepared to live in a misgoverned polity.

Nationalism

Coping with globalisation

In this day and age of globalisation an exclusively national agenda is no longer meaningful. Whether we like it or not Bangladesh will have to participate in the process of globalisation and will have to interact more closely with our neighbours in order to better equip ourselves to cope with this process. Bangladesh, over the last two decades has already been exposed to a process of external dependence because of the dominant role of aid donors in underwriting our development finance and influencing our policy agendas. Donors are, today, much more assertive as a price for committing their aid to Bangladesh. Not only have donors sought to use aid conditionality so as to impose policy reforms on Bangladesh but they are now becoming more exigent in their demands for better governance. This tendency of the donors to intrude from the economic to the political domain in their attempt to influence Bangladesh's policy agendas indicates that two decades of donor driven policy reform have yielded only modest returns.

In contrast to the increasing trend by donors to influence both policy and governance the share of aid as a resource for development has declined from around 10% of GDP in the early 1980s to 2 or 3% at the end of this century. This decline in aid dependence in Bangladesh reflects both an improved capacity for domestic resource mobilisation as well as an expansion in our export earnings over the last decade. At the same time the 1990s witnessed an absolute stagnation and decline in the share of aid resources in total public expenditure. The tendency for donors to seek to influence our national policy agendas appears to have risen inversely to their contribution to our public finances, as a result their ability to exercise leverage over our public finances today compared to a decade ago has also weakened. The emerging policy vacuum in Bangladesh has not been readily filled by the government of Bangladesh who still look to our aid donors to set the policy agenda.

This decline in the importance of aid in Bangladesh is part of a changing global scenario where donors are limiting their aid commitments and countries such as Bangladesh are being propelled by their donors to seek foreign direct investment (FDI). In this process Bangladesh is being asked to use FDI to underwrite the development of its infrastructure in areas where aid was once the dominant source of finance. Investment in energy development, power, telecommunications, even highways and bridges, once the core of the aid programme, are today viewed by donors as part of the domain of FDI. Over the decade of the 90's neither the World Bank nor the Asian Development Bank committed any loans for expansion or even upgradation of Bangladesh's public sector power generation facilities. Any funds on offer in this area by these agencies is to be used as risk guarantee funds for prospective private power producers. Bangladesh, therefore, has to not only make itself receptive to donor advice but to make itself attractive to prospective private foreign investors. In contrast to aid where access originates in the specific relationship of Bangladesh with its aid donors, to attract FDI

Bangladesh has to compete with other developing countries throughout the world. Thus, today there is much less assurance available to Bangladesh that a sufficiency of external resources needed to support its development programmes will be realisable.

Today US and European Union (EU) policy in relation to the *multifibre arrangement* (MFA) and import of RMG from Bangladesh is a far more important factor in influencing our economic fortunes than their aid commitment to us. As we enter the new millennium, the immigration policies of Saudi Arabia, UAE, Malaysia, Pakistan or India are also no less important to our future than World Bank loans to finance economic reforms. Bangladesh thus needs to adjust its external economic relations to make the best use of trading opportunities on offer under the process of globalisation. However, as a beneficiary of such export opportunities Bangladesh has to compete for such markets with many other developing countries (DC) and less developed countries (LDC). Such a process of globalisation will, therefore tend to favour those countries who can equip themselves to compete in a harsh and unpredictable external environment. What Bangladesh needs to do is to put in place an agenda for coping with globalisation so that we can exercise some influence over the terms on which we participate in the process rather than remain as helpless victims of the vicissitudes of this process.

Whilst the process of globalisation is impacting on Bangladesh in a wide variety of areas we limit our attention in this paper to those aspects which remain likely to impact on our external earning capacity. The new global trading system which will emerge out of the Seattle Round of negotiations could have far reaching implications for Bangladesh. At the top of our agenda we will, therefore, need to carefully review Bangladesh's role in the WTO. This review will demand that we analyse our options and improve our negotiating capacity in order to obtain the best terms which we can hope to extract from the Seattle negotiations. We will need to study the agendas of our bilateral economic partners to identify where export opportunities may open up for Bangladesh. We should draw upon such assessments so as to enhance our diplomatic capacities to enable us to exploit opportunities on offer to us. At the same time we need to develop our supply side capacity to create and exploit new opportunities available to us in the markets of these countries. For example, we should equip ourselves to exploit the enlarged export quotas on offer by the USA and Europe under the MFA and GSP. We should also exploit emerging opportunities for exports of semi-skilled labour to Japan, Korea, Malaysia, India, Pakistan, Europe and North America. We should study their future market needs, invest in training our workers to respond to such needs and negotiate globally and bilaterally to facilitate competitive access of our workers to their labour markets. Bangladesh's future should not depend on the enterprise of our illegal emigrants but on our capacity to ensure that free export of labour services becomes a legitimate part of the process of globalisation.

Bangladesh will need to invest in equipping ourselves to participate in the globalisation of information both as users of knowledge as well as providers of information services. We already lag far behind our neighbour, India, which is moving rapidly to avail of global opportunities on offer in the software market and newer areas of information services. The growth in training schools for informatics and software in Bangladesh is an indication of the enterprise of our youth to participate in the information revolution. Such private initiatives should now be backed by the state as part of a major strategic effort.

We will further need to diversify our production and export capacities. Bangladesh is in danger of being trapped into a highly concentrated export structure where RMG today accounts for 75% of our exports. We may begin this process by moving to add value to the RMG sector which has already carved out a market niche in the *global* trading system. Value addition to our RMG sector may be realised through investing in backward linkages through domestic manufacture of yarn as well as fabrics and forward linkages in the area of design and marketing of the RMG. If we play our cards right Bangladesh has a capacity to expand our aggregate export earnings from RMG 10 fold in the next decade. We may or may not be able to realise these goals but it is important to recognise that such opportunities are open to us because we have already established that we can export RMG and labour services on competitive terms. The same areas of comparative advantage enjoyed by Bangladesh in the RMG sector can be exploited in the area of leather products, consumer electronics, toys, or other labour intensive economic activities.

In recognising that our future lies in trade not aid Bangladesh should redefine its relations with our donors. Our diplomatic initiatives should move away from soliciting aid to securing and sustaining access to global markets as well to that of our immediate neighbours. Whatever aid is likely to be available to us should be focussed on enhancing our capacity to participate in the global trading system. This enhancement of our competitive capacities will demand investments in both basic education as well as skill upgradation and in development of our information linkages to the international system. This will also require investments in physical infrastructure where aid should be used to reduce our exclusive dependence on foreign private investors to meet this need.

Recapturing ownership over the development agenda

Bangladesh's need to cope with globalisation should not leave us exclusively preoccupied with enhancing our export capacity. Bangladesh is possessed of a population approaching 130 million who provide a large and growing demand for goods and services. Such a domestic market is an important resource of Bangladesh not available to countries with smaller populations. We need to gear our production systems to service this demand rather than surrender our local market to foreign suppliers in the name of globalisation. To this end we must refocus both policy and political attention to meeting local needs even if this means some challenge to the process of globalisation. Neither our neighbour

India, or China or the US are so casual about surrendering their large domestic market. We therefore need to invest as much attention on ensuring more competitive local production of goods and services for the local market as we do to export promotion. Promoting local production capacity will be particularly beneficial to small scale and rural producers who cater largely to local needs. Stimulating demand for small industries has the further advantage of widening domestic development opportunities because of the greater use by this sector for intermediate inputs derived from local resources and skills. Since the small scale sector has always been neglected as regards both policy and resources a major thrust area for Bangladesh in the millennium should therefore be towards promoting this sector by helping to upgrade their technology and improve their competitiveness. At the same time we need to take lessons from Japan, China and Republic of Korea who, as part of their high growth strategy, attached an absolute value to using local capacities. Such a perspective serves to restore a sense of pride in local producers as well as to disseminate growth opportunities across the domestic economy.

Our diminished need for aid should also be used as an opportunity to resume ownership over our policy agendas. A move towards restoration of ownership coincides with the now universal recognition amongst donors that weak local ownership diminishes aid effectiveness and neutralises the impact of externally driven reforms. Such a resumption of ownership demands a credible effort within Bangladesh to develop our own vision, commitment and capacity to design as well as implement policy.

This demonstration of vision and commitments must largely originate from our political leadership. In this respect the capacity of the state to design policy has diminished as the machinery of state has lost confidence in its ability to design policy. However, policy design and implementation is no longer the exclusive monopoly of the state. Civil society also needs to have its own vision and to demonstrate a commitment and capacity to realise this vision. In Bangladesh there is no shortage of professional resources to design and implement such a vision nor do we lack the skills to build a political consensus behind such agendas. The efforts of the caretaker government of President Shahabuddin Ahmad in 1991 to commission 255 of our best experts assembled in 29 Task Forces to advise the incoming elected government on policy options, demonstrated the worth of our local professionals. The incumbent Awami League government has also drawn upon such indigenous skills to service a variety of National Commissions on policy reform in such areas as Administration, Banking, Local Government, Industry, Agriculture, Health, Media and other vital issues. Such exercises have thrown up valuable policy advice but have not always been operationalised into legislation or policy. Nor has much effort been invested in building a broad political consensus behind the recommendations of these National Commissions. Thus, even where the government has moved to assume some ownership over policy design it has not made the best possible use of these initiatives. This suggests that

the government of Bangladesh remains disinclined to rely on domestic professional skills in preference to advice originating from its donors. Such a response by the government has a demoralising effect on Bangladesh's own professionals who thereby tend to fall back on donor-driven consultancy work. This externally owned work is seen by our professionals as a practical route to influence public policy whilst also providing more lucrative compensation.

In the light of experiences over the last 25 years of Bangladesh's history nationalism for the 21st century implies a capacity to think as well as act for ourselves. Such an autonomous process of policy thinking, thus, needs to be backed by policy commitment as well as the development of operational capacity to realise our own vision. We will, therefore, need to build supportive political constituencies to sustain such a process of national self-assertion. Acquiring these skills will not enable us to resist globalisation but will better equip us to participate in the process. Rhetorical protestations about national sovereignty emanating from political practitioners who have over two decades abdicated sovereignty over all aspects of development policy remains neither politically credible or operationally meaningful. At the end of the day we have to demonstrate to our development partners that resumption of policy ownership is more than a slogan. We will have to demonstrate a capacity to mobilise local resources, use local skills as well as enhance local productivity and above all improve governance if the concept of ownership is to graduate from rhetoric to reality.

Justice and Equity

The emergence of two societies

Our goals of democracy, secularism and nationalism will all remain unsustainable if we cannot establish a more equitable society permeated by a spirit of social justice. Whilst the constitutional commitment to socialism meant different things to different people, this goal was premised on the commitment to democratise economic opportunities for the deprived majority of the population. Bangladesh did not attain its independence through the goodwill of its masters but through protracted struggle, sustained by the sacrifices of common people. A democratic Bangladesh was thus, honour bound to build a social order which gave common people a stake in the development process.

Unlike many countries, including some in South Asia, at the time of our liberation Bangladesh did not inherit an elite class of feudal lords or a super-rich bourgeoisie. The emergence of extreme social and economic disparities which characterises Bangladesh today was a post-liberation phenomena driven by the externally driven policy agendas which guided our economic policy. Such policy advice did little to accelerate development or eliminate poverty but it did contribute to a process of social polarization which has invested Bangladesh with a new elite, many of whom have earned their wealth more by political access and patronage than by their entrepreneurial skills. A society which

maldistributes the rewards of development to a rentier elite will promote neither growth nor equity. More important such a system perpetuates a sense of unjust relative deprivation. Such a social order lacks popular legitimacy and thus remains inherently unstable. Much of the social anarchy which is permeating Bangladesh today derives from the feeling in all segments of society that the fruits of independence have been unjustly distributed.

Bangladesh's unequal social structure is now perpetuating a process of undemocratic politics where the deprived majority have little chance of entering parliament and remain largely excluded from the tiers of local government. Politics is increasingly becoming a rich man's game played with the objective of enhancing private wealth rather than to serve a public purpose. A political system which effectively disenfranchises two-thirds of the population remains fundamentally unstable because it denies a political stake to those very classes who remain the ultimate defenders of democratic institutions. No usurper could hope to seize state power if they know that half-a-million working people would occupy the streets of Dhaka and Chittagong to protect democratic institutions in which they have a direct stake.

Building a just social order

To build a more just society we need to make our development agenda more inclusive so as to widen the opportunities for the deprived to participate in the development process and the market as both producers and consumers. Such an agenda will serve to eradicate the moral crime of poverty and stimulate as well as sustain growth because it will widen the domestic market for indigenous producers. Such a redirection in Bangladesh's development agenda is a challenging professional and political task which merits fuller discussion in another paper. To provide a flavour of some of the issues which demand address in a more inclusive development agenda we present below a selective rather than comprehensive agenda for social reform:

Democratising human development

The emergence of two societies built around unequal access to education and health care needs to be arrested. It is not enough to spend more public money on primary education and health care if a small elite monopolises access to superior private education or health care facilities. A dualistic education system institutionalises disparities in lifetime opportunities for upward mobility. Such a system ensures that those privileged to receive an expensive private education will perpetuate themselves as a ruling class whilst those who depend on public education will always remain an underclass.

Europe's social revolution after World War II was founded on democratisation of education and health care built around public provision of quality education and health care to all citizens irrespective of income or social background. Bangladesh needs to follow this path. It

would be unrealistic at this stage, perhaps unwise, to eliminate private education. However, such institutions should be encouraged to provide scholarships to the underprivileged so as to democratise access to these institutions. Private resources may be supplemented by public funds for financing scholarships for the deprived.

However, the main thrust in the democratisation of education should be carried forward through an exponential improvement in the quality of public education and health care from the primary to the tertiary level. Such a public initiative will need to ensure that disparities in the quality of public and private education are minimised. Such a democratisation of education will not only demand more expenditure on public provision of education but an upgradation of its governance which remains a much more scarce resource than money. As a beginning the government may target 100 rural primary schools every year and invest in raising their academic standards at least to the level of the private schools in Dhaka. Such a programme is already, in some form, under implementation by the Ministry of Education. It is to be seen whether such an upgradation of rural primary education can be sustained within the prevailing environment of weak governance. Better governance of education cannot, however, substitute for poor motivation of our school teachers and the lack of collective initiative by parents to enforce accountability from the teachers. Thus, the quest for better education will need to extend beyond the state and activate civil society to exercise their rights as parents and citizens.

In upgrading our education system we cannot afford to neglect university education. We must restore the opportunity for the children of poor families to at least have access to our public universities to enable them to compete for the best jobs on offer in society. Regretably Bangladesh's universities, once the cradle of our professional and political elite, have been infected by all the maladies which have plagued the polity. Universities have been politicised and factionalised at the level of both teachers and students. Armed hoodlums occupy the halls of residence, intrude into the development activities of the universities and have destabilised the campus as organised gangs fight their turf wars for private gain. Politics for these elements in the campus is a mercenary activity used to serve private political and commercial agendas rather than to serve a public purposes. The use of student muscle power as an instrument of politics buys immunity from the forces of law and order for these hoodlum. It is not surprising that the quality of public university education in Bangladesh has deteriorated and parents who can afford to do so are either sending their children abroad or into the proliferating private universities. The crisis of our universities is thus part of our crisis of governance and unless this is rectified this educationally driven process of social disparity will be perpetuated into the future generation.

Upgrading technical skills

As the base of our public education expands and upgrades itself we should aim to provide institutional facilities to enable youth graduating out of rural schools who have limited opportunity to acquire marketable

skills to broaden their employment horizons. The Bangladesh government may intervene to consciously promote upward mobility by setting up technical schools in every *upazilla* on the lines of such schools in Germany, Japan and Republic of Korea. These proposed technical schools should each aim to graduate perhaps 500 boys and 500 girls every year, drawn from the poorer segments of society, who will be equipped by the schools to operate a rapidly changing economy in the 21st century. Such technical schools should be well-equipped, staffed with the best available professional skills and should calibrate their courses to the needs of both the global and local market. This system should widen and diversify economic opportunities for the poor, deprived by both class and gender, to enable them to benefit from the globalisation process.

Today in the age of the information revolution not every villager needs to send their offspring to Dhaka for a better education. Enhancement in the capacity of distance learning can provide village students with the same knowledge base available to students in Dhaka. But this will require a major investment in the telecommunications infrastructure as well as a transformation in the techniques and institutions of education in Bangladesh. This will need to not only train teachers to use the resources of the information age but a transformation in the system of management and motivation of public education.

Upgrading health care

Bangladesh has registered some gains in health. Its immunisation programme has registered promising results. Its family planning programme has raised the contraceptive prevalence rate (CPR) from around 10% in the 1970s to 50% today which has helped to halve its fertility rate in 20 years from 6.4 to 3.2. The absolute as well as relative share of public expenditure going to health care has also increased in the last decade. However all such gains stand to be neutralised by the degeneration in the quality of our curative health care due to its poor governance. It is this poor quality of care which is opening up major social disparities in access to health care.

As in the case of education, primary health care should, therefore, be provided at a level which is comparable to facilities on offer in the private sector. It is clear that the better-off sections of society have come to depend on private health care whilst the elite seek such care abroad in India, Thailand, Singapore and in the West. This means that public health care is exclusively used by those who cannot afford private care. However, the public system carries heavy private costs paid to functionaries within the public system. The public health system is poorly governed which encourages rent-seeking and perpetuates a system which is overloaded as well as poorly administered and maintained. Under this system the quality of public care is so poor that it drives even the deprived to seek more expensive private care. In such a system the *real* costs of health care contribute to impoverish the borderline poor and pauperise the hard core poor.

Bangladesh thus needs a system of quality care for the deprived which builds upon the comparative successes of the immunisation and family planning programme. Such a system needs to ensure the effective implementation of the new health care policy based on community participation, prioritisation of preventative care and improved governance of the system of curative care. This requires bigger investments in public health as well as effective management.

The test of the new system at the village level will be measured by whether the poor in rural Bangladesh are kept waiting long hours by the doctor, can expect to be treated with respect in the local primary health care centre, are not made to pay rents for realising health services; if admitted to a upazilla hospital such patients should expect to sleep on clean sheets, eat decent food and use clean toilets.

An upgraded health care system needs to be backed up by a system of health insurance which provides both security and choice for the entire population in Bangladesh. The development of a contributory health care system based on insurance will serve to provide some stake to the users in the operation of the system whilst reducing the fiscal claims on the public exchequer. The insurance system pioneered by *Gono Shasto Kendro* and other such insurance systems may be studied with a view to designing a national system.

A stake for the deprived

Human development is important in its own right because it enhances the capabilities of the deprived to both fulfil themselves and participate in the market. If opportunities for the poor are to be enhanced we would, however, need to move beyond enhancing their human development to enable them to realise the full benefits which could be derived from improved human capabilities. To this end we need to re-engineer our institutions to provide the deprived with a stake in the development of the economy. This involves taking the micro-credit revolution to its logical conclusion by ensuring that every person eligible for such credit has access to credit. This goal will demand not just the extension of lending by micro-credit institutions but that our commercial banks should also equip themselves to provide micro-credit to anyone who needs it. Micro-credit will thus need to be integrated into the formulation of monetary policy so that it can be served by the mainstream banking system. Redirection of the lending practises of our commercial banks should be backed by policy and institutional arrangements to relocate credit from large defaulters to the commercial banking system to the more creditworthy micro-borrowers. Such a relocation of credit would be consistent with both market efficiency as well as the goals of national policy where credit to the deprived need not remain the exclusive concern of Grameen Bank or the NGOs. To redirect commercial bank credit to the deprived will, however, need more than a change in monetary policy and will have to address the crucial problem of misgovernance and weak regulation which has compromised the viability of our banking system.

Our financial system will also need to be reconstructed to mobilise the savings of the poor to finance investments both in the corporate sector and in corporatising the rural economy. Savings of these segments, mobilised by the micro-credit sector alone would be in the range of Tk. 5 billion. Part of these savings should be put to work, leveraged by commercial bank financing to be used to buy a corporate stake for the deprived in the modern production and export sector. Furthermore, since the assets of micro-credit institutions have in large measure proven to be relatively secure income generating assets, this credit could be securitised and marketed in the domestic as well as international capital markets. Such a prospective exercise is already under review in the Grameen Bank which thereby hopes to tap a wider resource base at the national and global level to underwrite the expansion of its micro-credit operations in Bangladesh.

As the rural poor are integrated as stake holders, producers and consumers into the corporate sector, the rural economy needs to develop its own unique corporate bodies, such as *Grameenphone*, designed to use local savings and attract outside capital. This will need corporate entities which link micro-producers using micro-credit with national and even global markets. This approach could both build corporate marketing entities for small producers as well as invest in value addition for primary producers as has been done by BRAC in setting up the *Aarong* milk processing facility.

Working people in the urban areas, particularly working women in the RMG sector, should also be given a stake in the enterprises where they work. A more just society would need to recognise the contribution of these rural women, drawn from deprived families, who through the value added by their labours, provide most of the net foreign exchange earnings accruing to Bangladesh's export sector. This recognition of the contribution of working women should be provided by accepting them as partners in the development process through giving them an equity stake in the factories where they work. This stake could be funded by bank loans in the same way that commercial banks finance share purchases by the elite of Bangladesh. Such a move to broaden the ownership of corporate wealth need not limit itself to the RMG sector but should be extended to other sectors of the economy. In a society where public credit is a critical factor in facilitating participation in the market the state exercises responsibility to use its own resources to widen the ownership of wealth so as to substantially democratise opportunities for access to the market.

The Government of Bangladesh should also recognise the contribution of these RMG workers in stimulating our exports by ensuring that the working conditions in all RMG units is at least in conformity with the provisions of the prevailing laws of the land. Since the concerns of working women extend outside their work place the government should recognise the societal contribution of these women and invest in the provision of improved housing, transport facilities and the security of these women. Such measures to provide security and an improved quality of life for these women would stimulate both their will and

capacity to improve productivity in the RMG sector which could thereby expect to enhance Bangladesh's export competitiveness. In Bangladesh justice and efficiency are not only fully compatible but remain symbiotically linked.

In the final analysis the quest for justice in Bangladesh in the next millennium should aspire to gradually erase the dividing line between labour and capital. A sustainable democratic system demands a cohesive social order which does not divide a society into haves and have nots. If we aspire to build a more inclusive society in Bangladesh we need to give every household a stake in the development of the economy whether it is through title to land or permanence of tenancy rights or as partners in corporate enterprises. The fruits of growth need to be shared and incentives provided not just to a small class of property owners but to all segments of society. Such a system of incentives will help to tap the creativity and work potential of a much broader segment of the population, will widen their income earning opportunities and graduate them from recipients of public largesse into full partners in the development process. Within a more just framework of development which integrates issues of asset ownership with market access, production growth and poverty eradication, equity and economic growth can be made part of a holistic agenda for both sustainable development and sustainable democracy.

External relations

In building a sustainable domestic order our leaders will have to also build a workable pattern of relations with our neighbours through the framework of SAARC. Both geography and history have linked Bangladesh's prosperity and security to the nature of its relations with its neighbours. Bangladesh's future agricultural development, depends in considerable measure on the enhancement of water resources inputs and in its capacity to cope with floods. This degree of water security can, in the long run, only be realised through cooperation with India and Nepal from where our principal rivers originate. Our energy needs will also demand an integrated solution which links the energy production capacity of Bangladesh with its immediate neighbours and even beyond to the energy resources of West and Central Asia through a shared distribution network. Furthermore, Bangladesh's transport system will need to be integrated not just with our South Asia neighbours but with South East Asia and China through the Asian Highway and Railway network. In order to enhance and develop Bangladesh's production potential we will need to have access to the wider South Asian market particularly to India, through the mechanism of the *South Asian Free Trade Area* (SAFTA). At the same time we will have to equip ourselves to cope with the gradual integration of our economy into a South Asian economic community.

Bangladesh's principal external policy challenge will therefore be to develop our relations with our neighbours, particularly India, into an area of opportunity rather than conflict, on the basis of mutual self interest. Such an agenda will be immeasurably facilitated by a dynamic well-

functioning economy and a working democracy which sees politics as a positive sum game where our relations with our principal neighbour are not treated as an extension of our dysfunctional domestic political process. Bangladesh will therefore need to directly address the issue of external relations particularly with India, as part of a national debate where such a relationship can be seen to originate out of a political consensus rather than serve to aggravate domestic political divisions.

Conclusion

Building upon our assets

This paper is designed to demonstrate that Bangladesh does indeed command the potential to build a sustainable development process and democratic order for the 21st century. In identifying possibilities for the new millennium the approach was to focus on the art of the possible. Thus in each area of discussion I have attempted to anchor the opportunities for change on assets or initiatives already in place to which some value addition was deemed possible. The prospects for the consolidation of democratic and secular politics derive from the objective reality of a two-party system located in a relatively homogenous society. Scope for a reassertion of nationalism derive from our visible strengths in export growth and domestic resource mobilization which have contributed to the decline in aid dependence. The new opportunities offered by the globalization process, are likely to sustain our export growth. The quest for social justice is grounded in the positive gains registered in micro-credit, widening of educational opportunities, the successes of the immunization as well as the family planning programs but above all in the resilience, industry and enterprise of the common people of Bangladesh. The visible production potential as well as credit worthiness of the deprived, the contribution of rural women to the dynamism of the RMG sector and the emergence of a number of globally recognized institutions targeting the deprived demonstrates both institutional commitment as well as capacity to mobilise these constituencies of the underprivileged.

In seeking to build our future upon our revealed capacities and experience we need to take account of the possibility that such gains can also be undone mostly on account of Bangladesh's dysfunctional political processes, persistent malgovernance and increasingly unjust social order. The prevailing political practises appear to emphasise private and party needs over the public interest, as a result the machinery of state is becoming increasingly anarchic and predatory. The progressive degeneration in the social commitment of the state has led to a configuration of social power which has elevated a small, affluent elite into positions of political influence which has empowered them to monopolise resources and remain immune from both the laws of the land as well as of the market.

The dominance of the two party system in the Bangladesh polity insulates the two parties from electoral challenge so that their dysfunctional politics can perpetuate itself over successive regimes. At the same time the power of Bangladesh's new elite has enabled them to use their resources to consolidate their dominance of our electoral institutions at the expense of excluding the more resource-deprived segments of society. This incestuous link between power and wealth is compromising the representative character of the democratic system in Bangladesh. At the same time, women remain underrepresented in Parliament even though they are now better represented at the local level. Successive parliaments have thus remained increasingly alienated from their constituents, including the deprived as well as women.

Mobilising civil society

Can a more enlightened and pro-active civil society help to reconstruct our political parties and contribute to empowering the deprived to challenge the social dominance of the elite? Those with both power and resources at their command have the capacity to deter, often by not very democratic means, any challenge to their authority. This means that the costs of such a civic mobilisation remain high whilst the returns are far from assured. Much will depend here on the sense of outrage which will serve to raise the threshold of risk and pain willing to be borne by the citizens of Bangladesh. Whilst civic activism has increased in recent years it is far from clear that the sense of outrage has reached a point where issue-focussed activists are willing to expose themselves to a more intensive involvement in advocacy by joining a major political party and challenging the authority of its power brokers.

Some civil society activists have indeed evolved from social activists to party political activists. But such persons tended to be in a minority so that their social motivation tends to be eroded by compromises forced on them by the realities of party politics. Their experience discourages more such persons from entering politics when in fact politics needs a larger proportion of such social activists who can generate enough critical mass to influence the culture of party politics.

Under the circumstances feasible politics suggests a strategy of incremental mobilisation. This may begin with issues of urgent public concern where the capacity for resistance is relatively weaker. Civil society mobilisation around such issues as improving the quality of primary education and health care services or cleaner urban neighbourhoods could yield high returns because no strong social forces are likely to strongly resist these agendas. Resistance from unions of primary school teachers and health sector employees may be forthcoming if these employees are to be made accountable to local citizens. But such unions are only powerful when mobilised to challenge administrative authority in Dhaka. Their capacity to resist the mobilisation of parents of school children in a union in Gaibandha or of citizens seeking health care in rural Comilla is likely to be much weaker particularly if the local elected government and the national government do not give these public employees their political backing. Such civic

mobilisation will need to be reinforced by a countervailing capacity of citizens to take over schools and health care centres and run it themselves or to organise themselves to clean the street in their neighbourhood. It is not to be ruled out that a future regime in office may be persuaded to politically back and even to institutionalise such interventions. Such local initiatives can also be escalated to wider mobilisations at the *upazilla*, district and even national level.

In other areas such as protecting the environment against polluting autorickshaw owners or shrimp cultivators damaging the environment for paddy farmers, where private financial interests are involved, the stakes will be higher and the capacity for resistance stronger. Such mobilisations would need to be more willing to take risks and accept some pain. However, I cannot see the political or business elite of Bangladesh opposing a sustained citizen's mobilisation to take two-stroke autorickshaws off the street or to compel Eastern Refinery to de-lead the petrol it produces or to enforce some discipline in the flow of traffic in our urban areas.

If we move upscale to challenge toll collectors and those hoodlums who terrorise our campuses the risk quotient increases largely because the challenged parties are often equipped with arms and better integrated to the mainstream political parties so that they can use such arms with relative immunity from the law enforcement agencies. However, as and when citizens have rallied to protest against weak law enforcement the government of the day has had to demonstrate some willingness to enforce the law. Unfortunately, such citizen's coalitions disperse after an initial mobilisation thereby relaxing pressure on the government enabling the criminals to resurface after a short period of hibernation. Thus, for example, a credible civic mobilisation to restore order in our universities would demand the emergence of a coalition of parents, students, teachers and leading citizens, working in collaboration with the university administration, which works together on a sustained basis until all the hoodlums are not only driven out of the halls of residence and campuses of the universities but are kept out on a long term basis. Such a mobilisation will demand political skill to build and sustain a non-partisan coalition, demonstrate high risk taking capacity and above all perseverance to see the fight through to the finish.

Can similar mobilisations challenge bank defaulters, energy thieves, corrupt senior bureaucrats and politically influential persons? As the issues become more complex and the political influence of the affected party increases the risks to citizens leading a mobilisation increases as does the time which needs to be invested in taking the exercise through to a positive conclusion.

A politics of the feasible

The nature of the problems indicated above suggest that particularist coalitions of citizens focussing on specific issues need to be assembled around people willing to invest time and to effort to see the mobilisation through to its eventual conclusion. In each such coalition a smaller

number of people would need to commit themselves on a full time basis to sustain such struggles. Do we have such dedicated citizens who feel so strongly about particular issues to take leave of their vocations, even if necessary, of their families, to embark on such a risk prone enterprise? Thus far, there is little evidence of such persons willing to commit themselves to the finish though a much larger constituency is likely to be available to support episodic mobilisations demanding small doses of effort and involving moderate risk. If civil society is to take itself seriously it will have to demonstrate a capacity to produce even a small number of such coalitions committed to see a particular mobilisation through to its final outcome.

Whilst issue-based mobilisations remain a feasible option political activism by civil society remains much more problematic. The time and risk involved is infinitely higher if one aspires to join a mainstream political party and engage oneself in an endeavour to upgrade the quality of the party. To be effective any such effort would demand that enough people join a party to exercise some weight in the party. Those entering politics should appreciate that they are not entering politics in a vacuum but have to interact with political workers who have been in the field a long time whilst such civil society members were comfortably engaged in their profession. Many of these workers have long records of party loyalty, material sacrifice and persecution by autocratic regimes. These workers have, over the years, earned the loyalty of not just their party associates but also the trust of their constituents who look to them in moments of need. Whilst some of those workers could be categorised as corrupt and/or as musclemen they too retain a degree of credibility in the local community through their dependability in moments of the crisis and cannot, therefore, be disregarded as political liabilities. Any newcomer to local politics, no matter how professionally eminent or morally upright they be should not therefore aspire to displace party cadres active in local politics but should learn to work with them. If politics is to be seen as the art of the possible we will have to recognise the coexistence of the good and the bad elements in the politics of Bangladesh with such qualities often co-existing in the same person. The real task of political reconstruction in Bangladesh is to see that the good more often prevails over the bad in influencing the course of politics.

As with all other professions political novices will have to prove their own credentials to the people through work at the constituency level. It is arguable that such newcomers, will contribute to the preponderance of better influences in politics by bringing in new ideas, demonstrating commitment, patience, humility and a capacity to work with no expectation of immediate national advancement from their presence in politics. Such newcomers would hope to thereby earn the confidence of local people as well as party workers. Through such service they should be able to build up loyalty amongst the party cadres, earn the respect of senior workers and may even influence the leadership by demonstrating their use value to the party. Few people in mainstream politics in Bangladesh today demonstrate the qualities indicated above so that such a qualitative change in political activity, even if originating from

newcomers, would not go unrecognised. Political leaders are not totally devoid of good sense in failing to recognise a political asset when they see one. *Gresham's Law*, whereby bad people drive away good people from politics may be at work in Bangladesh but its applicability originates in no small measure from tendency of those with something to offer to treat politics as a spectator sport to be shunned by decent people.

Individual political enterprise will however not be enough. The point at issue is to impact on the culture of politics where entrenched forces at all levels remain strong, have a high political stake and material interests to defend. Here individuals who join political parties will need to draw upon the backing of a mobilised civil society who are willing to engage in the high risk task of influencing political action. These new political activists are needed to serve as a bridge between civil society and party politics where the concerns of the citizens can be brought to bear on the agenda and behavior of political activists. The problem with involving civil society in politics will, however, have to address the reality that civil society organisations of teachers, lawyers, doctors and engineers, themselves remain divided along the faultlines of Bangladesh's bipolar political system. As a result few people command the credentials to reach across the political divide and assemble a consensual coalition of citizens committed to a public cause rather than a partisan agenda. In such a context if civil society is to command sufficient authority in the polity political identities will periodically need to be subsumed in the service of a bigger cause and will need to build their own issue-based consensus in the same way that politicians are expected to do so. There is something absurd if not tragic about professional colleagues, with no real ideological contradictions to divide them, becoming even more rabid in their mutual antagonisms than the political parties who patronise them. Such political contradictions do more than immobilise civil society, they also undermine professional institutions. Thus, dysfunctional politics tends to perpetuate dysfunctional institutions.

Towards a just society

Whilst improving the quality of politics is important the more vital task remains to democratise politics as well as access to resources in a milieu where strong vested interests with much to lose occupy positions of power and influence at all levels. To challenge these forces in national or even local government elections is costly as well as fraught with risk. In contrast, assembling coalitions of the deprived, many of whom remain captive to vertical patron-client relations with the powerful, is time consuming and hazardous to the deprived who may lose what crumbs are on offer by their patrons for demonstrating the temerity to challenge the existing social order. Thus, the agenda for building a more just society needs to reach out to a much broader constituency built up through empowering the deprived, including women, who must be politically mobilised to struggle for their rights. In this task civil society can be the ally of the deprived but it cannot be their proxy. A discussion on the processes and implications of empowering the deprived is a major exercise which merits independent address in another paper.

This paper has argued that the new millennium holds out enormous promise for Bangladesh. But to realise this promise will demand structural adjustment not just for the economy but in our politics and society. Such a process of structural change is beyond the capacity of any donor and will have to be an indigenous exercise. In seeking such political change civil society will have to play a much more active role than before and will have to move beyond social issues to address political concerns. In playing a more pro-active role in the polity civil society will have to increasingly demonstrate its commitment to prioritise societal over personal concerns. Over the years Bangladesh has paid a heavy price for the privatisation of our sense of public purpose. If Bangladesh is to establish itself as a dynamic and just nation state in the next decade a restoration of a sense of public purpose within civil society remains indispensable.

Review Questions

- What are the gaps between promises and reality, according to Sobhan? Do you agree with his line of analysis?
- “A more proactive civil society and a reorientation of politics and priorities will set the country into a path for democratic governance and a just social order” – analyse the statement.
- Do you subscribe to the view that a strategy of a more egalitarian development is not only socially just, it would also make Bangladesh more competitive in a fast globalizing economy?